

Extra Space Storage Inc.
Form 10-Q
November 04, 2013
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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2013

or

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

For the transition period from _____ to _____.

Commission File Number: 001-32269

EXTRA SPACE STORAGE INC.

(Exact name of registrant as specified in its charter)

Maryland

(State or other jurisdiction of incorporation or organization)

20-1076777

(I.R.S. Employer Identification No.)

2795 East Cottonwood Parkway, Suite 400

Salt Lake City, Utah 84121

(Address of principal executive offices)

Registrant's telephone number, including area code: **(801) 365-4600**

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 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

Accelerated filer

Non-accelerated filer

Smaller reporting company

(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 No

The number of shares outstanding of the registrant's common stock, par value \$0.01 per share, as of October 31, 2013, was 111,253,494.

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EXTRA SPACE STORAGE INC.

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STATEMENT ON FORWARD-LOOKING INFORMATION

Certain information presented in this report contains forward-looking statements within the meaning of the federal securities laws. Forward-looking statements include statements concerning our plans, objectives, goals, strategies, future events, future revenues or performance, capital expenditures, financing needs, plans or intentions relating to acquisitions and other information that is not historical information. In some cases, forward-looking statements can be identified by terminology such as believes, expects, estimates, may, will, should, anticipates, intends, or the negative of such terms or other comparable terminology, or by discussions of strategy. We may also make additional forward-looking statements from time to time. All such subsequent forward-looking statements, whether written or oral, by us or on our behalf, are also expressly qualified by these cautionary statements.

All forward-looking statements, including without limitation, management's examination of historical operating trends and estimate of future earnings, are based upon our current expectations and various assumptions. Our expectations, beliefs and projections are expressed in good faith and we believe there is a reasonable basis for them, but there can be no assurance that management's expectations, beliefs and projections will result or be achieved. All forward-looking statements apply only as of the date made. We undertake no obligation to publicly update or revise forward-looking statements which may be made to reflect events or circumstances after the date made or to reflect the occurrence of unanticipated events.

There are a number of risks and uncertainties that could cause our actual results to differ materially from the forward-looking statements contained in or contemplated by this report. Any forward-looking statements should be considered in light of the risks referenced in Part II. Item 1A. Risk Factors below and in Part I. Item 1A. Risk Factors included in our most recent Annual Report on Form 10-K. Such factors include, but are not limited to:

- adverse changes in general economic conditions, the real estate industry and the markets in which we operate;
- failure to close pending acquisitions on expected terms, or at all;
- the effect of competition from new and existing self-storage facilities or other storage alternatives, which could cause rents and occupancy rates to decline;
- difficulties in our ability to evaluate, finance, complete and integrate acquisitions and developments successfully and to lease up those properties, which could adversely affect our profitability;
- potential liability for uninsured losses and environmental contamination;

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- the impact of the regulatory environment as well as national, state and local laws and regulations including, without limitation, those governing real estate investment trusts (REITs), tenant reinsurance and other aspects of our business, which could adversely affect our results;
- disruptions in credit and financial markets and resulting difficulties in raising capital or obtaining credit at reasonable rates or at all, which could impede our ability to grow;
- increased interest rates and operating costs;
- reductions in asset valuations and related impairment charges;
- the failure of our joint venture partners to fulfill their obligations to us or their pursuit of actions that are inconsistent with our objectives;
- the failure to maintain our REIT status for federal income tax purposes;
- economic uncertainty due to the impact of war or terrorism, which could adversely affect our business plan; and
- difficulties in our ability to attract and retain qualified personnel and management members.

Table of Contents**PART I. FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****Extra Space Storage Inc.****Condensed Consolidated Balance Sheets**

(amounts in thousands, except share data)

	September 30, 2013 (Unaudited)	December 31, 2012
Assets:		
Real estate assets, net	\$ 3,223,672	\$ 2,991,722
Investments in unconsolidated real estate ventures	100,455	106,313
Cash and cash equivalents	81,699	30,785
Restricted cash	22,803	16,976
Receivables from related parties and affiliated real estate joint ventures	7,928	11,078
Other assets, net	81,682	66,603
Total assets	\$ 3,518,239	\$ 3,223,477
Liabilities, Noncontrolling Interests and Equity:		
Notes payable	\$ 1,402,432	\$ 1,369,690
Premium on notes payable	2,336	3,319
Exchangeable senior notes	250,000	
Discount on exchangeable senior notes	(17,299)	
Notes payable to trusts	119,590	119,590
Lines of credit		85,000
Accounts payable and accrued expenses	58,248	52,299
Other liabilities	34,052	48,248
Total liabilities	1,849,359	1,678,146
Commitments and contingencies		
Noncontrolling interest represented by Series B Preferred Operating Partnership units	33,713	
Noncontrolling Interests and Equity:		
Extra Space Storage Inc. stockholders' equity:		
Preferred stock, \$0.01 par value, 50,000,000 shares authorized, no shares issued or outstanding		
Common stock, \$0.01 par value, 300,000,000 shares authorized, 111,236,044 and 110,737,205 shares issued and outstanding at September 30, 2013 and December 31, 2012, respectively		
	1,112	1,107
Paid-in capital	1,766,691	1,740,037
Accumulated other comprehensive income (deficit)	3,146	(14,273)
Accumulated deficit	(256,640)	(235,064)
Total Extra Space Storage Inc. stockholders' equity	1,514,309	1,491,807

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Noncontrolling interest represented by Series A Preferred Operating Partnership units, net of \$100,000 note receivable	29,880	29,918
Noncontrolling interests in Operating Partnership	90,504	22,492
Other noncontrolling interests	474	1,114
Total noncontrolling interests and equity	1,635,167	1,545,331
Total liabilities, noncontrolling interests and equity	\$ 3,518,239	\$ 3,223,477

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents**Extra Space Storage Inc.****Condensed Consolidated Statements of Operations**

(amounts in thousands, except share data)

(unaudited)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2013	2012	2013	2012
Revenues:				
Property rental	\$ 113,881	\$ 94,065	\$ 324,144	\$ 249,193
Tenant reinsurance	12,294	9,495	34,625	27,060
Management fees	6,936	6,231	19,910	19,476
Total revenues	133,111	109,791	378,679	295,729
Expenses:				
Property operations	34,376	30,115	102,275	82,723
Tenant reinsurance	2,873	1,379	6,985	4,651
Acquisition related costs	2,427	2,486	3,562	3,564
General and administrative	13,943	12,559	40,451	37,744
Depreciation and amortization	23,428	19,768	69,238	52,918
Total expenses	77,047	66,307	222,511	181,600
Income from operations	56,064	43,484	156,168	114,129
Gain on sale of real estate assets			800	
Loss on extinguishment of debt related to portfolio acquisition	(9,153)		(9,153)	
Interest expense	(16,264)	(18,423)	(51,992)	(52,348)
Non-cash interest expense related to amortization of discount on equity component of exchangeable senior notes	(834)		(947)	(444)
Interest income	202	461	519	1,184
Interest income on note receivable from Preferred Operating Partnership unit holder	1,213	1,213	3,638	3,638
Income before equity in earnings of unconsolidated real estate ventures and income tax expense	31,228	26,735	99,033	66,159
Equity in earnings of unconsolidated real estate ventures	3,405	2,854	8,942	7,848
Equity in earnings of unconsolidated real estate ventures - gain on sale of real estate assets and purchase of joint venture partners' interests		13,620	2,556	19,049
Income tax expense	(2,281)	(1,656)	(7,147)	(4,240)
Net income	32,352	41,553	103,384	88,816
Net income allocated to Preferred Operating Partnership noncontrolling interests	(2,033)	(1,805)	(5,495)	(5,108)

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Net income allocated to Operating Partnership and other noncontrolling interests		(1,074)		(1,142)		(2,753)		(2,475)
Net income attributable to common stockholders	\$	29,245	\$	38,606	\$	95,136	\$	81,233
Net income per common share								
Basic	\$	0.26	\$	0.37	\$	0.86	\$	0.81
Diluted	\$	0.26	\$	0.37	\$	0.84	\$	0.80
Weighted average number of shares								
Basic		111,231,452		104,252,227		111,060,997		100,429,840
Diluted		117,604,515		108,755,316		117,483,010		104,981,176
Cash dividends paid per common share	\$	0.40	\$	0.20	\$	1.05	\$	0.60

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents**Extra Space Storage Inc.****Condensed Consolidated Statements of Comprehensive Income**

(amounts in thousands)

(unaudited)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2013	2012	2013	2012
Net income	\$ 32,352	\$ 41,553	\$ 103,384	\$ 88,816
Other comprehensive income (loss):				
Change in fair value of interest rate swaps	(2,073)	(3,564)	17,967	(7,296)
Total comprehensive income	30,279	37,989	121,351	81,520
Less: comprehensive income attributable to noncontrolling interests	2,996	2,814	8,796	7,307
Comprehensive income attributable to common stockholders	\$ 27,283	\$ 35,175	\$ 112,555	\$ 74,213

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents**Extra Space Storage Inc.****Condensed Consolidated Statement of Equity**

(amounts in thousands, except share data)

(unaudited)

	Noncontrolling Interests				Extra Space Storage Inc. Stockholders			Equity		Total Equity
	Series B Preferred Operating Partnership	Series A Preferred Operating Partnership	Operating Partnership	Other	Shares	Par Value	Paid-in Capital	Accumulated Other Comprehensive Income (Deficit)	Accumulated Deficit	
Balances at December 31, 2012	\$	\$ 29,918	\$ 22,492	\$ 1,114	110,737,205	\$ 1,107	\$ 1,740,037	\$ (14,273)	\$ (235,064)	\$ 1,545,331
Issuance of common stock upon the exercise of options					387,393	4	5,872			5,876
Restricted stock grants issued					132,802	1				1
Restricted stock grants cancelled					(21,356)					
Compensation expense related to stock-based awards							3,654			3,654
Purchase of additional equity interests in existing consolidated joint ventures				(635)			(515)			(1,150)
Issuance of exchangeable senior notes - equity component							14,496			14,496
Issuance of Operating Partnership units in conjunction with portfolio acquisition	33,568		68,471							68,471
Redemption of Operating Partnership units for cash			(41)							(41)
Net income	335	5,160	2,715	38					95,136	103,049
Other comprehensive income	(22)	153	417					17,419		17,989
Tax effect from vesting of restricted stock grants and stock option exercises							3,147			3,147
Distributions to Operating Partnership units held by noncontrolling interests	(168)	(5,351)	(3,550)							(8,901)
Distributions to other noncontrolling interests				(43)						(43)
Dividends paid on common stock at \$1.05 per share									(116,712)	(116,712)
Balances at September 30, 2013	\$ 33,713	\$ 29,880	\$ 90,504	\$ 474	111,236,044	\$ 1,112	\$ 1,766,691	\$ 3,146	\$ (256,640)	\$ 1,635,167

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See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents**Extra Space Storage Inc.****Condensed Consolidated Statements of Cash Flows**

(amounts in thousands)

(unaudited)

For the Nine Months Ended September 30,
2013 2012

Cash flows from operating activities:			
Net income	\$	103,384	\$ 88,816
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization		69,238	52,918
Amortization of deferred financing costs		4,198	5,016
Loss on extinguishment of debt related to portfolio acquisition		9,153	
Non-cash interest expense related to amortization of discount on exchangeable senior notes		947	444
Non-cash interest expense related to amortization of premium on notes payable		(983)	(951)
Compensation expense related to stock-based awards		3,654	3,318
Gain on purchase of joint venture partners' interests		(2,556)	(13,499)
Distributions from unconsolidated real estate ventures in excess of earnings		3,538	1,642
Changes in operating assets and liabilities:			
Receivables from related parties and affiliated real estate joint ventures		891	7,587
Other assets, net		(1,303)	4,866
Accounts payable and accrued expenses		5,949	4,530
Other liabilities		2,474	(1,726)
Net cash provided by operating activities		198,584	152,961
Cash flows from investing activities:			
Acquisition, development and redevelopment of real estate assets		(86,890)	(368,753)
Proceeds from sale of real estate assets		889	
Investments in unconsolidated real estate ventures		(1,126)	(1,053)
Return of investment in unconsolidated real estate ventures			1,848
Change in restricted cash		(5,827)	2,384
Issuance of notes receivable		(5,000)	(7,875)
Purchase of equipment and fixtures		(2,349)	(1,620)
Net cash used in investing activities		(100,303)	(375,069)
Cash flows from financing activities:			
Proceeds from the sale of common stock, net of offering costs			226,692
Net proceeds from issuance of exchangeable senior notes		246,250	
Repurchase of exchangeable senior notes			(87,663)
Proceeds from notes payable and lines of credit		364,855	640,655
Principal payments on notes payable and lines of credit, including defeasance		(532,348)	(473,349)
Deferred financing costs		(6,135)	(8,427)
Redemption of Operating Partnership units held by noncontrolling interest		(41)	(155)
Net proceeds from exercise of stock options		5,876	8,931
Dividends paid on common stock		(116,712)	(60,693)
Distributions to noncontrolling interests		(9,112)	(6,759)
Net cash provided by (used in) financing activities		(47,367)	239,232
Net increase in cash and cash equivalents		50,914	17,124

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Cash and cash equivalents, beginning of the period		30,785		26,484
Cash and cash equivalents, end of the period	\$	81,699	\$	43,608

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents**Extra Space Storage Inc.****Condensed Consolidated Statements of Cash Flows**

(amounts in thousands)

(unaudited)

	For the Nine Months Ended September 30,	
	2013	2012
Supplemental schedule of cash flow information		
Interest paid	\$ 46,360	\$ 47,816
Income taxes paid	1,626	473
Supplemental schedule of noncash investing and financing activities:		
Tax effect from vesting of restricted stock grants and stock option exercises:		
Other assets	\$ 3,147	\$ 3,099
Paid-in capital	(3,147)	(3,099)
Acquisitions of real estate assets		
Real estate assets, net	\$ 210,372	\$ 148,021
Notes payable assumed	(7,122)	(147,592)
Notes payable assumed and immediately defeased	(98,960)	
Value of Operating Partnership units issued	(102,039)	(429)
Receivables from related parties and affiliated real estate joint ventures	(2,251)	
Receivable from sale of interest in real estate ventures		
Other assets	\$	\$ 3,349
Investments in unconsolidated real estate ventures	\$	\$ (3,349)

See accompanying notes to unaudited condensed consolidated financial statements.

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EXTRA SPACE STORAGE INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

Amounts in thousands, except property and share data

1. ORGANIZATION

Extra Space Storage Inc. (the Company) is a fully-integrated, self-administered and self-managed real estate investment trust (REIT), formed as a Maryland corporation on April 30, 2004, to own, operate, manage, acquire, develop and redevelop professionally managed self-storage facilities located throughout the United States. The Company continues the business of Extra Space Storage LLC and its subsidiaries, which had engaged in the self-storage business since 1977. The Company's interest in its properties is held through its operating partnership, Extra Space Storage LP (the Operating Partnership), which was formed on May 5, 2004. The Company's primary assets are general partner and limited partner interests in the Operating Partnership. This structure is commonly referred to as an umbrella partnership REIT, or UPREIT. The Company has elected to be taxed as a REIT under the Internal Revenue Code of 1986, as amended. To the extent the Company continues to qualify as a REIT, it will not be subject to tax, with certain limited exceptions, on the taxable income that is distributed to its stockholders.

The Company invests in self-storage facilities by acquiring wholly-owned facilities or by acquiring an equity interest in real estate entities. At September 30, 2013, the Company had direct and indirect equity interests in 754 operating storage facilities. In addition, the Company managed 253 properties for third parties, bringing the total number of operating properties which it owns and/or manages to 1,007. These properties are located in 35 states, Washington, D.C. and Puerto Rico.

The Company operates in three distinct segments: (1) rental operations; (2) tenant reinsurance; and (3) property management, acquisition and development. The rental operations activities include rental operations of self-storage facilities in which we have an ownership interest. No single tenant accounts for more than 5% of rental income. Tenant reinsurance activities include the reinsurance of risks relating to the loss of goods stored by tenants in the Company's self-storage facilities. The Company's property management, acquisition and development activities include managing, acquiring, developing and selling self-storage facilities.

2. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements of the Company are presented on the accrual basis of accounting in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information, and in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they may not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (including normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine months ended September 30, 2013, are not necessarily indicative of results that may be expected for the year ending December 31, 2013. The condensed consolidated balance sheet as of December 31, 2012 has been derived from the Company's audited financial statements as of that date, but does not include all of the information and footnotes required by GAAP for complete financial statements. For further information refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2012, as filed with the Securities and Exchange Commission.

Certain amounts in the 2012 financial statements and supporting note disclosures have been reclassified to conform to the current period presentation. Such reclassifications did not impact previously reported net income or accumulated deficit.

Recently Issued Accounting Standards

In February 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2013-02 *Comprehensive Income - Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*, which supersedes and replaces the presentation requirements for reclassifications out of accumulated other comprehensive income in ASUs 2011-05 and 2011-12. The amendment requires an entity to report the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in net income if the amount being reclassified is required under GAAP. For other amounts that are not required under GAAP to be reclassified in their entirety to net income in the same reporting period, an entity is required to cross-reference other disclosures required under GAAP that provide additional detail about those amounts. ASU 2013-02 was effective for fiscal years, and interim periods within those years, beginning on or after December 15, 2012. The Company adopted the amended standards beginning January 1, 2013 and presents accumulated other comprehensive income in accordance with the requirements of the standard.

Table of Contents**3. FAIR VALUE DISCLOSURES***Derivative Financial Instruments*

Currently, the Company uses interest rate swaps to manage its interest rate risk. The valuation of these instruments is determined using widely accepted valuation techniques, including discounted cash flow analysis on the expected cash flows of each derivative. This analysis reflects the contractual terms of the derivatives, including the period to maturity, and uses observable market-based inputs, including interest rate curves. The fair values of interest rate swaps are determined using the market standard methodology of netting the discounted future fixed cash payments and the discounted expected variable cash receipts. The variable cash receipts are based on an expectation of future interest rates (forward curves) derived from observable market interest rate forward curves.

The Company incorporates credit valuation adjustments to appropriately reflect both its own nonperformance risk and the respective counterparty's nonperformance risk in the fair value measurements. In adjusting the fair value of its derivative contracts for the effect of nonperformance risk, the Company has considered the impact of netting and any applicable credit enhancements, such as collateral postings, thresholds, mutual puts, and guarantees. In conjunction with the FASB's fair value measurement guidance, the Company made an accounting policy election to measure the credit risk of its derivative financial instruments that are subject to master netting agreements on a net basis by counterparty portfolio.

Although the Company has determined that the majority of the inputs used to value its derivatives fall within Level 2 of the fair value hierarchy, the credit valuation adjustments associated with its derivatives utilize Level 3 inputs, such as estimates of current credit spreads to evaluate the likelihood of default by the Company and its counterparties. However, as of September 30, 2013, the Company had assessed the significance of the impact of the credit valuation adjustments on the overall valuation of its derivative positions and determined that the credit valuation adjustments were not significant to the overall valuation of its derivatives. As a result, the Company determined that its derivative valuations in their entirety were classified in Level 2 of the fair value hierarchy.

The table below presents the Company's assets and liabilities measured at fair value on a recurring basis as of September 30, 2013, aggregated by the level in the fair value hierarchy within which those measurements fall.

Description	September 30, 2013	Fair Value Measurements at Reporting Date Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Other assets - Cash Flow Hedge Swap Agreements	\$ 7,530	\$	\$ 7,530	\$
Other liabilities - Cash Flow Hedge Swap Agreements	\$ (4,953)	\$	\$ (4,953)	\$

There were no transfers of assets and liabilities between Level 1 and Level 2 during the nine months ended September 30, 2013. The Company did not have any significant assets or liabilities that are re-measured on a recurring basis using significant unobservable inputs (Level 3) for the nine months ended September 30, 2013.

Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis

Long-lived assets held for use are evaluated for impairment when events or circumstances indicate there may be impairment. The Company reviews each self-storage facility at least annually to determine if any such events or circumstances have occurred or exist. The Company focuses on facilities where occupancy and/or rental income have decreased by a significant amount. For these facilities, the Company determines whether the decrease is temporary or permanent, and whether the facility will likely recover the lost occupancy and/or revenue in the short term. In addition, the Company carefully reviews facilities in the lease-up stage and compares actual operating results to original projections.

When the Company determines that an event that may indicate impairment has occurred, the Company compares the carrying value of the related long-lived assets to the undiscounted future net operating cash flows attributable to the assets. An impairment loss is recorded if the net carrying value of the assets exceeds the undiscounted future net operating cash flows attributable to the assets. The impairment loss recognized equals the excess of net carrying value over the related fair value of the assets.

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When real estate assets are identified by management as held for sale, the Company discontinues depreciating the assets and estimates the fair value of the assets, net of selling costs. If the estimated fair value, net of selling costs, of the assets that have been identified as held for sale is less than the net carrying value of the assets, then a valuation allowance is established. The operations of assets held for sale or sold during the period are generally presented as discontinued operations for all periods presented.

The Company assesses whether there are any indicators that the value of its investments in unconsolidated real estate ventures may be impaired annually and when events or circumstances indicate there may be impairment. An investment is impaired if management's estimate of the fair value of the investment is less than its carrying value. To the extent impairment has occurred, and is considered to be other than temporary, the loss is measured as the excess of the carrying amount over the fair value of the investment.

In connection with the Company's acquisition of self-storage facilities, the purchase price is allocated to the tangible and intangible assets and liabilities acquired based on their fair values, which are estimated using significant unobservable inputs. The value of the tangible assets, consisting of land and buildings, is determined as if vacant. Intangible assets, which represent the value of existing tenant relationships, are recorded at their fair values based on the avoided cost to replace the current leases. The Company measures the value of tenant relationships based on the rent lost due to the amount of time required to replace existing customers, which is based on the Company's historical experience with turnover in its facilities. Debt assumed as part of an acquisition is recorded at fair value based on current interest rates compared to contractual rates. Acquisition-related transaction costs are expensed as incurred.

Fair Value of Financial Instruments

The carrying values of cash and cash equivalents, restricted cash, receivables, other financial instruments included in other assets, accounts payable and accrued expenses, variable-rate notes payable, lines of credit and other liabilities reflected in the condensed consolidated balance sheets at September 30, 2013 and December 31, 2012 approximate fair value.

The fair value of the Company's note receivable from Preferred Operating Partnership unit holder was based on the discounted estimated future cash flows of the note (categorized within Level 3 of the fair value hierarchy); the discount rate used approximated the current market rate for loans with similar maturities and credit quality. The fair values of the Company's fixed-rate notes payable and notes payable to trusts were estimated using the discounted estimated future cash payments to be made on such debt (categorized within Level 3 of the fair value hierarchy); the discount rates used approximated current market rates for loans, or groups of loans, with similar maturities and credit quality. The fair value of the Company's exchangeable senior notes was estimated using an average market price obtained from a third party.

The fair values of the Company's fixed-rate assets and liabilities were as follows for the periods indicated:

	September 30, 2013		December 31, 2012	
	Fair Value	Carrying Value	Fair Value	Carrying Value
Note receivable from Preferred Operating Partnership unit holder	\$ 104,299	\$ 100,000	\$ 108,138	\$ 100,000
Fixed rate notes payable and notes payable to trusts	\$ 1,272,278	\$ 1,269,205	\$ 1,342,957	\$ 1,275,605

Exchangeable senior notes	\$	253,500	\$	250,000	\$	\$
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4. NET INCOME PER COMMON SHARE

Basic net income per common share is computed by dividing net income by the weighted average common shares outstanding, including unvested share-based payment awards that contain a non-forfeitable right to dividends or dividend equivalents. Diluted earnings per common share measures the performance of the Company over the reporting period while giving effect to all potential common shares that were dilutive and outstanding during the period. The denominator includes the weighted average number of basic shares and the number of additional common shares that would have been outstanding if the potential common shares that were dilutive had been issued, and is calculated using either the treasury stock or as if-converted method. Potential common shares are securities (such as options, convertible debt, exchangeable Series A Participating Redeemable Preferred Units (Series A Units) and Series B Redeemable Preferred Units (Series B Units) (together, Preferred OP Units) and exchangeable Operating Partnership units (OP Units)) that do not have a current right to participate in earnings but could do so in the future by virtue of their option or conversion right. In computing the dilutive effect of convertible securities, net income is adjusted to add back any changes in earnings in the period associated with the

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convertible security. The numerator also is adjusted for the effects of any other non-discretionary changes in income or loss that would result from the assumed conversion of those potential common shares. In computing diluted earnings per share, only potential common shares that are dilutive (those that reduce earnings per share) are included.

The Operating Partnership had \$250,000 of its 2.375% Exchangeable Senior Notes due 2033 (the Notes) issued and outstanding as of September 30, 2013. The Notes could potentially have a dilutive effect on the Company's earnings per share calculations. The Notes are exchangeable by holders into shares of the Company's common stock under certain circumstances per the terms of the indenture governing the Notes. The exchange price of the Notes was \$55.69 per share as of September 30, 2013, and could change over time as described in the indenture. The Company has irrevocably agreed to pay only cash for the accreted principal amount of the Notes relative to its exchange obligations, but retained the right to satisfy the exchange obligation in excess of the accreted principal amount in cash and/or common stock. Though the Company has retained that right, Accounting Standards Codification (ASC) 260, *Earnings per Share*, requires an assumption that shares would be used to pay the exchange obligation in excess of the accreted principal amount, and requires that those shares be included in the Company's calculation of weighted average common shares outstanding for the diluted earnings per share computation. For the three and nine months ended September 30, 2013 no shares related to the Notes were included in the computation for diluted earnings per share as the per share price of the Company's common stock during this period did not exceed the exchange price.

For the purposes of computing the diluted impact on earnings per share of the potential conversion of Series A Units into common shares, where the Company has the option to redeem in cash or shares and where the Company has stated the positive intent and ability to settle at least \$115,000 of the instrument in cash (or net settle a portion of the Series A Units against the related outstanding note receivable), only the amount of the instrument in excess of \$115,000 is considered in the calculation of shares contingently issuable for the purposes of computing diluted earnings per share as allowed by ASC 260-10-45-46.

For the purposes of computing the diluted impact on earnings per share of the potential conversion of Series B Units into common shares, where the Company has the option to redeem in cash or shares and where the Company has stated the intent and ability to settle the redemption in shares, the Company divided the total value of the Series B Units outstanding at September 30, 2013, or \$33,568, by the closing price of \$45.75 per share at September 30, 2013. Assuming full conversion to common shares as of September 30, 2013, 733,731 shares would have been issued to holders of the Series B units.

For the three months ended September 30, 2013 and 2012, options to purchase 51,036 and 15,223 shares of common stock, respectively, and for the nine months ended September 30, 2013 and 2012, options to purchase 43,273 and 54,959 shares of common stock, respectively, were excluded from the computation of earnings per share as their effect would have been anti-dilutive. All restricted stock grants have been included in basic and diluted shares outstanding because such shares earn a non-forfeitable dividend and carry voting rights.

The computation of net income per common share was as follows for the periods indicated:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2013	2012	2013	2012
Net income attributable to common stockholders	\$ 29,245	\$ 38,606	\$ 95,136	\$ 81,233
Add: Income allocated to noncontrolling interest - Preferred Operating Partnership and Operating Partnership	3,092	2,938	8,210	7,563

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Subtract: Fixed component of income allocated to noncontrolling interest - Preferred Operating Partnership	(1,438)	(1,438)	(4,313)	(4,313)
Net income for diluted computations	\$ 30,899	\$ 40,106	\$ 99,033	\$ 84,483

Weighted average common shares outstanding:

Average number of common shares outstanding - basic	111,231,452	104,252,227	111,060,997	100,429,840
Operating Partnership units	4,346,618	3,060,467	4,346,618	3,060,467
Series A Preferred Operating Partnership units	989,980	989,980	989,980	989,980
Series B Preferred Operating Partnership units	733,731		733,731	
Shares related to dilutive and cancelled stock options	302,734	452,642	351,684	500,889
Average number of common shares outstanding - diluted	117,604,515	108,755,316	117,483,010	104,981,176

Net income per common share

Basic	\$ 0.26	\$ 0.37	\$ 0.86	\$ 0.81
Diluted	\$ 0.26	\$ 0.37	\$ 0.84	\$ 0.80

Table of Contents**5. PROPERTY ACQUISITIONS AND DISPOSITIONS**

The following table summarizes the Company's acquisitions of operating properties for the nine months ended September 30, 2013, and does not include purchases of land, purchases of additional equity interests in existing consolidated joint ventures or improvements made to existing assets:

Property Location	Number of Properties	Date of Acquisition	Consideration Paid						Acquisition Date Fair Value				Closing costs - Notes			
			Total	Cash Paid (1)	Loans Assumed (1)	Non-cash gain	Notes Issued to/from Seller	Net Liabilities from equity (Assets)	Value of OP Units Issued	Number of OP Units Issued	Land	Building		Intangible		
Maryland	1	2/13/2013	\$ 12,321	\$ 8,029	\$	\$ 2,215	\$ 2,273	\$ (196)				\$ 1,266	\$ 10,789	\$ 260	\$ 6	(2)
Illinois	1	2/13/2013	11,083	7,592		341	2,251	1,173	(274)			1,318	9,485	190	90	(2)
Hawaii	2	5/3/2013	27,560	27,648					(88)			5,991	20,976	438	155	
Texas	1	5/8/2013	7,104	7,057					47			1,374	5,636	86	8	
Maryland	1	6/10/2013	13,688	500	7,122				(64)	6,130	143,860	2,160	11,340		188	
Arizona	2	7/25/2013	9,313	9,183					130			2,001	7,110	192	10	
California	19	8/29/2013	186,427	96,085					519	89,823	2,613,728	100,446	81,830	2,997	1,154	
California	1	9/26/2013	10,928	4,791					51	6,086	177,107	3,138	7,429	181	180	
2013 Totals	28		\$ 278,424	\$ 160,885	\$ 7,122	\$ 2,556	\$ 2,251	\$ 3,446	\$ 125	\$ 102,039	2,934,695	\$ 117,694	\$ 154,595	\$ 4,344	\$ 1,791	

(1) Loans assumed and immediately defeased at closing are excluded from loans assumed and included in cash paid.

(2) Acquired from an affiliated joint venture

On August 29, 2013, the Operating Partnership completed the purchase of 19 out of 20 self-storage facilities affiliated with All Aboard Mini Storage, all of which are located in California. On September 26, 2013, the Operating Partnership completed the purchase of the remaining facility. These properties were acquired in exchange for \$100,876 in cash (including \$98,960 of debt assumed and immediately defeased at closing), 1,342,727 Series B Units valued at \$33,568 and 1,448,108 common OP Units valued at \$62,341. In accordance with ASC 805,

Business Combinations, the assumed debt was recorded at its fair value as of the closing date. The difference between the price paid to extinguish the debt, which included \$9,153 of defeasance costs, and the carrying value of the debt was recorded as loss on extinguishment of debt related to portfolio acquisition on the Company's Condensed Consolidated Statement of Operations.

In June 2013, the Company recorded a gain of \$800 due to the condemnation of a portion of land at one self-storage property in California that resulted from eminent domain.

On May 16, 2013, the Company sold a property located in New York for \$950. No gain or loss was recorded as a result of the sale.

6. VARIABLE INTERESTS

The Company has an interest in one unconsolidated joint venture with an unrelated third party which is a variable interest entity (VIE). The Company holds an 18% equity interest and a 50% profit interest in the VIE joint venture (VIE JV), and has 50% of the voting rights in the VIE JV. Qualification as a VIE was based on the determination that the equity investment at risk for this joint venture was not sufficient based on a qualitative and quantitative analysis performed by the Company. The Company performed a qualitative analysis for this joint venture to determine which party was the primary beneficiary. The Company determined that, since the powers to direct the activities most significant to the economic performance of this entity are shared equally by the Company and its joint venture partner, there is no primary beneficiary. Accordingly, this interest is recorded using the equity method.

The VIE JV owns a single self-storage property. This joint venture is financed through a combination of (1) equity contributions from the Company and its joint venture partner, (2) a primary mortgage note payable and (3) amounts payable to the Company. The amounts payable to the Company consist of expenses paid on behalf of the joint venture by the Company as manager and a secondary mortgage note payable to the Company. The Company performs management services for the VIE JV in exchange for a management fee of approximately 6% of cash collected by the property. Except as disclosed, the Company has not provided financial or other support during the periods presented to the VIE JV that it was not previously contractually obligated to provide.

The Company guarantees the primary mortgage note payable for the VIE JV. The Company's maximum exposure to loss for this joint venture as of September 30, 2013 is the total of the guaranteed loan balance, amounts payable to the Company and the Company's investment balance in the joint venture. The Company believes that the risk of incurring a material loss as a result of having to perform on the loan guarantee is unlikely and, therefore, no liability has been recorded related to this guarantee. Additionally, repossessing and/or selling the self-storage facility and land that collateralize the loan could provide funds sufficient to reimburse the Company.

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The following table compares the Company's liability balance to the VIE JV and the maximum exposure to loss as of September 30, 2013:

	Liability Balance	Investment Balance	Balance of Guaranteed Loan	Amounts Payable to the Company	Maximum Exposure to Loss	Difference
Extra Space of Sacramento One LLC	\$	\$ (1,077)	\$ 4,307	\$ 6,033	\$ 9,263	\$ (9,263)

The Operating Partnership has three wholly-owned unconsolidated subsidiaries (Trust, Trust II and Trust III, together, the Trusts) that have issued trust preferred securities to third parties and common securities to the Operating Partnership. The proceeds from the sale of the preferred and common securities were loaned in the form of notes to the Operating Partnership. The Trusts are VIEs because the holders of the equity investment at risk (the trust preferred securities) do not have the power to direct the activities of the entities that most significantly affect the entities' economic performance because of their lack of voting or similar rights. Because the Operating Partnership's investment in the Trusts common securities was financed directly by the Trusts as a result of its loan of the proceeds to the Operating Partnership, that investment is not considered an equity investment at risk. The Operating Partnership's investment in the Trusts is not a variable interest because equity interests are variable interests only to the extent that the investment is considered to be at risk, and therefore the Operating Partnership cannot be the primary beneficiary of the Trusts. Since the Company is not the primary beneficiary of the Trusts, they have not been consolidated. A debt obligation has been recorded in the form of notes for the proceeds as discussed above, which are owed to the Trusts. The Company has also included its investment in the Trusts' common securities in other assets on the condensed consolidated balance sheets.

The Company has not provided financing or other support during the periods presented to the Trusts that it was not previously contractually obligated to provide. The Company's maximum exposure to loss as a result of its involvement with the Trusts is equal to the total amount of the notes discussed above less the amounts of the Company's investments in the Trusts' common securities. The net amount is the notes payable that the Trusts owe to third parties for their investments in the Trusts' preferred securities.

The following is a tabular comparison of the liabilities the Company has recorded as a result of its involvement with the Trusts to the maximum exposure to loss the Company is subject to as a result of such involvement as of September 30, 2013:

	Notes payable to Trusts	Investment Balance	Maximum exposure to loss	Difference
Trust	\$ 36,083	\$ 1,083	\$ 35,000	\$
Trust II	42,269	1,269	41,000	\$
Trust III	41,238	1,238	40,000	\$
	\$ 119,590	\$ 3,590	\$ 116,000	\$

The Company had no consolidated VIEs during the nine months ended September 30, 2013 or 2012.

7. DERIVATIVES

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The Company is exposed to certain risks arising from both its business operations and economic conditions. The Company principally manages its exposures to a wide variety of business and operational risks through management of its core business activities. The Company manages economic risks, including interest rate, liquidity, and credit risk primarily by managing the amount, sources and duration of its debt funding and by using derivative financial instruments. Specifically, the Company enters into derivative financial instruments to manage exposure that arises from business activities that result in the receipt or payment of future known and uncertain cash amounts, the value of which are determined by interest rates. The Company's derivative financial instruments are used to manage differences in the amount, timing and duration of the Company's known or expected cash receipts and its known or expected cash payments principally related to the Company's investments and borrowings.

Cash Flow Hedges of Interest Rate Risk

The Company's objectives in using interest rate derivatives are to add stability to interest expense and to manage its exposure to interest rate movements. To accomplish these objectives, the Company primarily uses interest rate swaps as part of its interest rate risk management strategy. Interest rate swaps designated as cash flow hedges involve the receipt of variable

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amounts from a counterparty in exchange for the Company making fixed-rate payments over the life of the agreements without exchange of the underlying notional amount.

The effective portion of changes in the fair value of derivatives designated and that qualify as cash flow hedges is recorded in accumulated other comprehensive income and is subsequently reclassified into earnings in the period that the hedged forecasted transaction affects earnings. A portion of these changes is excluded from accumulated other comprehensive income as it is allocated to noncontrolling interests. During the nine months ended September 30, 2013 and 2012, such derivatives were used to hedge the variable cash flows associated with existing variable-rate debt.

The following table summarizes the terms of the Company's 21 derivative financial instruments as of September 30, 2013:

Hedge Product	Current Notional Amounts	Strike	Effective Dates	Maturity Dates
Swap Agreements	\$4,873 - \$97,211	2.79% - 6.32%	7/1/2009 - 7/25/2013	7/1/2014 - 4/1/2021

Fair Values of Derivative Instruments

The table below presents the fair value of the Company's derivative financial instruments as well as their classification on the condensed consolidated balance sheets:

Derivatives Designated as Hedging Instruments:	Asset (Liability) Derivatives			
	September 30, 2013		December 31, 2012	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Swap Agreements	Other assets	\$ 7,530	Other assets	\$
Swap Agreements	Other liabilities	\$ (4,953)	Other liabilities	\$ (15,228)

Effect of Derivative Instruments

The tables below present the effect of the Company's derivative financial instruments on the condensed consolidated statements of operations for the periods presented. No tax effect has been presented as the derivative instruments are held by the REIT:

Type	Classification of Income (Expense)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
		2013	2012	2013	2012
Swap Agreements	Interest expense	\$ (2,307)	\$ (1,876)	\$ (6,589)	\$ (4,429)

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Type	Gain (loss) recognized in OCI September 30, 2013	Location of amounts reclassified from OCI into income	Gain (loss) reclassified from OCI For the Nine Months Ended September 30, 2013
Swap Agreements	\$ 10,837	Interest expense	\$ (6,589)

Credit-risk-related Contingent Features

The Company has agreements with some of its derivative counterparties that contain provisions pursuant to which, the Company could be declared in default of its derivative obligations if the Company defaults on any of its indebtedness, including default where repayment of the indebtedness has not been accelerated by the lender.

The Company also has an agreement with some of its derivative counterparties that incorporates the loan covenant provisions of the Company's indebtedness with a lender affiliate of the derivative counterparty. Failure to comply with the loan covenant provisions would result in the Company being in default on any derivative instrument obligations covered by the agreement.

As of September 30, 2013, the fair value of derivatives in a net liability position, which includes accrued interest but excludes any adjustment for nonperformance risk related to these agreements, was \$5,162. As of September 30, 2013, the Company

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had not posted any collateral related to these agreements. If the Company had breached any of these provisions as of September 30, 2013, it could have been required to settle its obligations under the agreements at their termination value of \$5,162.

8. EXCHANGEABLE SENIOR NOTES

On June 21, 2013, the Operating Partnership issued \$250,000 of its 2.375% Exchangeable Senior Notes due 2033 at a 1.5% discount, or \$3,750. Costs incurred to issue the Notes were approximately \$1,672. These costs are being amortized as an adjustment to interest expense over five years, which represents the estimated term based on the first available redemption date, and are included in other assets in the condensed consolidated balance sheet. The Notes are general unsecured senior obligations of the Operating Partnership and are fully guaranteed by the Company. Interest is payable on January 1 and July 1 of each year beginning January 1, 2014, until the maturity date of July 1, 2033. The Notes bear interest at 2.375% per annum and contain an exchange settlement feature, which provides that the Notes may, under certain circumstances, be exchangeable for cash (for the principal amount of the Notes) and, with respect to any excess exchange value, for cash, shares of the Company's common stock or a combination of cash and shares of the Company's common stock at the Company's option. The initial exchange rate of the Notes is approximately 17.96 shares of the Company's common stock per \$1,000 principal amount of the Notes.

The Operating Partnership may redeem the Notes at any time to preserve the Company's status as a REIT. In addition, on or after July 5, 2018, the Operating Partnership may redeem the Notes for cash, in whole or in part, at 100% of the principal amount plus accrued and unpaid interest, upon at least 30 days but not more than 60 days prior written notice to the holders of the Notes. The holders of the Notes have the right to require the Operating Partnership to repurchase the Notes for cash, in whole or in part, on July 1 of the years 2018, 2023, and 2028, and upon the occurrence of certain designated events, in each case for a repurchase price equal to 100% of the principal amount of the Notes plus accrued and unpaid interest. Certain events are considered Events of Default, as defined in the indenture governing the Notes, which may result in the accelerated maturity of the Notes.

GAAP requires entities with convertible debt instruments that may be settled entirely or partially in cash upon conversion to separately account for the liability and equity components of the instrument in a manner that reflects the issuer's economic interest cost. The Company therefore accounts for the liability and equity components of the Notes separately. The equity component is included in paid-in capital in stockholders equity in the condensed consolidated balance sheet, and the value of the equity component is treated as original issue discount for purposes of accounting for the debt component. The discount is being amortized as interest expense over the remaining period of the debt through its first redemption date, July 1, 2018. The effective interest rate on the liability component is 4.0%.

Information about the carrying amount of the equity component, the principal amount of the liability component, its unamortized discount and its net carrying amount were as follows for the periods indicated:

	September 30, 2013	December 31, 2012
Carrying amount of equity component	\$ 14,496	\$
Principal amount of liability component	\$ 250,000	\$
Unamortized discount - equity component	(13,720)	
Unamortized cash discount	(3,579)	
Net carrying amount of liability component	\$ 232,701	\$

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\$87,663 of the Operating Partnership's 3.625% Exchangeable Senior Notes due 2027 (the 2007 Notes) were issued and outstanding prior to April 2012, when all of the outstanding 2007 Notes were surrendered for exchange.

The amount of interest cost recognized relating to the contractual interest rate and the amortization of the discount on the liability component of the Notes and the 2007 Notes was as follows for the periods indicated:

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	For the Nine Months Ended September 30,			
	2013		2012	
Contractual interest	\$	1,632	\$	794
Amortization of discount on equity component		834		444
Total interest expense recognized	\$	2,466	\$	1,238

9. NONCONTROLLING INTEREST REPRESENTED BY PREFERRED OPERATING PARTNERSHIP UNITS*Classification of Noncontrolling Interests*

GAAP requires a company to present ownership interests in subsidiaries held by parties other than the company in the consolidated financial statements within the equity section, but separate from the company's equity. It also requires the amount of consolidated net income attributable to the parent and to the noncontrolling interest to be clearly identified and presented on the face of the consolidated statement of operations and requires changes in ownership interest to be accounted for similarly as equity transactions. If noncontrolling interests are determined to be redeemable, they are to be carried at their redemption value as of the balance sheet date and reported as temporary equity.

The Company has evaluated the terms of the Preferred OP Units and classifies the noncontrolling interest represented by the Preferred OP units as stockholders' equity in the accompanying condensed consolidated balance sheets. The Company will periodically evaluate individual noncontrolling interests for the ability to continue to recognize the noncontrolling amount as permanent equity in the condensed consolidated balance sheets. Any noncontrolling interests that fail to qualify as permanent equity will be reclassified as temporary equity and adjusted to the greater of (1) the carrying amount, or (2) its redemption value as of the end of the period in which the determination is made.

Series A Participating Redeemable Preferred Units

On June 15, 2007, the Operating Partnership entered into a Contribution Agreement with various limited partnerships affiliated with AAAA Rent-A-Space to acquire ten self-storage facilities (the Properties) in exchange for 989,980 Series A Units of the Operating Partnership. The self-storage facilities are located in California and Hawaii.

On June 25, 2007, the Operating Partnership loaned the holders of the Series A Units \$100,000. The note receivable bears interest at 4.85% and is due September 1, 2017. The loan is secured by the borrower's Series A Units. The holders of the Series A Units can convert up to 114,500 Series A Units prior to the maturity date of the loan. If any redemption in excess of 114,500 Series A Units occurs prior to the maturity date, the holder of the Series A Units is required to repay the loan as of the date of that redemption. Preferred OP Units are shown on the balance sheet net of the \$100,000 loan because the borrower under the loan receivable is also the holder of the Series A Units.

The Operating Partnership entered into a Second Amended and Restated Agreement of Limited Partnership (as subsequently amended, the Partnership Agreement) which provides for the designation and issuance of the Series A Units. The Series A Units will have priority over all other partnership interests of the Operating Partnership with respect to distributions and liquidation.

Under the Partnership Agreement, Series A Units in the amount of \$115,000 bear a fixed priority return of 5% and have a fixed liquidation value of \$115,000. The remaining balance participates in distributions with, and has a liquidation value equal to, that of the common OP units. The Series A Units became redeemable at the option of the holder on September 1, 2008, which redemption obligation may be satisfied, at the Company's option, in cash or shares of its common stock.

Series B Redeemable Preferred Units

On August 29, 2013, the Operating Partnership completed the purchase of 19 out of 20 self-storage facilities affiliated with All Aboard Mini Storage, all of which are located in California. On September 26, 2013, the Operating Partnership completed the purchase of the remaining facility. These properties were acquired in exchange for \$100,876 in cash (including \$98,960 of debt assumed and immediately defeased at closing), 1,342,727 Series B Units valued at \$33,568, and 1,448,108 common OP Units valued at \$62,341.

The Operating Partnership entered into a Third Amended and Restated Agreement of Limited Partnership which provides for the designation and issuance of Series B Units. The Series B Units rank junior to Series A Units but will have priority over all other partnership interests of the Operating Partnership with respect to distribution and liquidation.

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The Series B Units have a fixed value of \$25 per unit for a fixed liquidation value of \$33,568, and have limited voting rights. Holders of the Series B Units receive distributions at an annual rate of 6%. These distributions are cumulative and accrue each quarter regardless of the declaration of dividends or distributions. The Series B Units will become redeemable at the option of the holder on August 29, 2014, which redemption obligation may be satisfied at the Company's option in cash or shares of its common stock.

As of September 30, 2013, the Company's ability to issue stock upon redemption of the Series B Units was not solely within its control. Therefore, the Company reported the Series B Units in temporary equity on the Condensed Consolidated Balance Sheet, as required by GAAP.

10. NONCONTROLLING INTEREST IN OPERATING PARTNERSHIP

The Company's interest in its properties is held through the Operating Partnership. ESS Holding Business Trust I, a wholly-owned subsidiary of the Company, is the sole general partner of the Operating Partnership. The Company, through ESS Holding Business Trust II, a wholly-owned subsidiary of the Company, is also a limited partner of the Operating Partnership. Between its general partner and limited partner interests, the Company held a 94.3% majority ownership interest therein as of September 30, 2013. The remaining ownership interests in the Operating Partnership (including Preferred OP units) of 5.7% are held by certain former owners of assets acquired by the Operating Partnership. As of September 30, 2013, the Operating Partnership had 4,346,618 common OP units outstanding.

The noncontrolling interest in the Operating Partnership represents common OP Units that are not owned by the Company. In conjunction with the formation of the Company, and as a result of subsequent acquisitions, certain persons and entities contributing interests in properties to the Operating Partnership received limited partnership units in the form of OP Units. Limited partners who received OP Units in the formation transactions or in exchange for contributions for interests in properties have the right to require the Operating Partnership to redeem part or all of their common OP units for cash based upon the fair market value of an equivalent number of shares of the Company's common stock (ten-day average) at the time of the redemption. Alternatively, the Company may, at its option, elect to acquire those OP Units in exchange for shares of its common stock on a one-for-one basis, subject to anti-dilution adjustments provided in the Partnership Agreement. The ten-day average closing stock price at September 30, 2013, was \$46.02 and there were 4,346,618 common OP Units outstanding that were not owned by the Company. Assuming that all of the noncontrolling members exercised their right to redeem all of their common OP Units on September 30, 2013, and the Company elected to pay the noncontrolling members cash, the Company would have paid \$200,031 in cash consideration to redeem the OP Units.

GAAP requires a company to present ownership interests in subsidiaries held by parties other than the company in the consolidated financial statements within the equity section, but separate from the company's equity. It also requires the amount of consolidated net income attributable to the parent and to the noncontrolling interest to be clearly identified and presented on the face of the consolidated statement of operations, and requires changes in ownership interest to be accounted for similarly as equity transactions. If noncontrolling interests are determined to be redeemable, they are to be carried at their redemption value as of the balance sheet date and reported as temporary equity.

The Company has evaluated the terms of the common OP Units and classifies the noncontrolling interest in the Operating Partnership as stockholders' equity in the accompanying condensed consolidated balance sheets. The Company will periodically evaluate individual noncontrolling interests for the ability to continue to recognize the noncontrolling amount as permanent equity in the condensed consolidated balance sheets. Any noncontrolling interests that fail to qualify as permanent equity will be reclassified as temporary equity and adjusted to the greater of (1) the carrying amount, or (2) the redemption value as of the end of the period in which the determination is made.

11. OTHER NONCONTROLLING INTERESTS

Other noncontrolling interests represent the ownership interests of various third parties in two consolidated self-storage properties as of September 30, 2013. One of these consolidated properties was undeveloped at September 30, 2013. The ownership interests of the third-party owners range from 3.3% to 10.0%. Other noncontrolling interests are included in the stockholders' equity section of the Company's condensed consolidated balance sheet. The income or losses attributable to these third-party owners based on percentages outlined in the related agreements are reflected in net income allocated to Operating Partnership and other noncontrolling interests in the condensed consolidated statement of operations.

In February 2013, the Company purchased one of its joint venture partner's 1.7% capital interest and 17% profit interest in one of these consolidated properties for \$200. As a result, the Company's capital interest percentage in this joint venture increased from 95% to 96.7%. Since the Company retained its controlling financial interest in the subsidiary, this transaction was accounted for as an equity transaction. The carrying amount of the noncontrolling interest was reduced to reflect the

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purchase and the difference between the price paid by the Company and the adjustment to the carrying value of the noncontrolling interest was recorded as an adjustment to equity attributable to the parent.

In May 2013, the Company purchased one of its joint venture partner's 27.65% capital interest and 35% profit interest in a previously unconsolidated joint venture for \$950. The partner's interest was reported in other noncontrolling interests prior to the purchase. As a result of the acquisition, the property became wholly-owned by the Company. Since the Company retained its controlling financial interest in the subsidiary, this transaction was accounted for as an equity transaction. The carrying amount of the noncontrolling interest was reduced to zero to reflect the purchase and the difference between the price paid by the Company and the carrying value of the noncontrolling interest was recorded as an adjustment to equity attributable to the parent.

12. EQUITY IN EARNINGS OF UNCONSOLIDATED REAL ESTATE VENTURES GAIN ON SALE OF REAL ESTATE ASSETS AND PURCHASE OF JOINT VENTURE PARTNERS' INTERESTS

On February 13, 2013, the Company acquired its joint venture partner's 48% equity interest in Extra Space of Eastern Avenue LLC (Eastern Avenue), which owned one self-storage property located in Maryland, for approximately \$5,979. Prior to the acquisition, the remaining 52% interest was owned by the Company, which accounted for its investment in Eastern Avenue using the equity method. The Company recorded a non-cash gain of \$2,215 related to this transaction, which represents the increase in fair value of the Company's interest in Eastern Avenue from its formation to the acquisition date.

On February 13, 2013, the Company acquired its joint venture partner's 61% equity interest in Extra Space of Montrose Avenue LLC (Montrose), which owned one self-storage property located in Illinois, for approximately \$6,878. Prior to the acquisition, the remaining 39% interest was owned by the Company, which accounted for its investment in Montrose using the equity method. The Company recorded a non-cash gain of \$341 related to this transaction, which represents the increase in fair value of the Company's interest in the joint venture from its formation to the acquisition date.

On July 2, 2012, the Company completed the acquisition of Prudential Real Estate Investors' 94.9% interest in the ESS PRISA III LLC joint venture (PRISA III). PRISA III was formed in 2005 and owned 36 properties located in 18 states. Prior to the acquisition, the remaining 5.1% interest was owned by the Company, which accounted for its investment in PRISA III using the equity method. Subsequent to the acquisition, the Company had full ownership of PRISA III. GAAP requires an entity that completes a business combination in stages to remeasure its previously held equity interest in the acquiree at its acquisition date fair value and recognize the resulting gain or loss, if any, in earnings. The Company recorded a non-cash gain of \$13,499 related to this transaction, which represents the increase in fair value of the Company's 5.1% interest in PRISA III from the formation of the joint venture to the acquisition date.

On February 17, 2012, a joint venture in which the Company held a 40% equity interest sold its only self-storage property, which was located in New York. As a result of the sale, the joint venture was dissolved, and the Company received proceeds which resulted in a cash gain of \$5,550.

On January 15, 2012, the Company sold its 40% equity interest in U-Storage de Mexico S.A. and related entities to its joint venture partners for \$4,841. The Company received cash of \$1,492 and a note receivable of \$3,349. No gain or loss was recorded on the sale. At September 30, 2013, the balance of the note receivable was \$1,500. The note receivable is due December 31, 2014.

13. SEGMENT INFORMATION

The Company operates in three distinct segments: (1) rental operations; (2) tenant reinsurance; and (3) property management, acquisition and development. Management fees collected for wholly-owned properties are eliminated in consolidation. Financial information for the Company's business segments is presented below:

	September 30, 2013	December 31, 2012
Balance Sheet		
Investment in unconsolidated real estate ventures		
Rental operations	\$ 100,455	\$ 106,313
Total assets		
Rental operations	\$ 3,209,347	\$ 2,981,927
Tenant reinsurance	30,057	27,645
Property management, acquisition and development	278,835	213,905
	\$ 3,518,239	\$ 3,223,477

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	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2013	2012	2013	2012
Statement of Operations				
Total revenues				
Rental operations	\$ 113,881	\$ 94,065	\$ 324,144	\$ 249,193
Tenant reinsurance	12,294	9,495	34,625	27,060
Property management, acquisition and development	6,936	6,231	19,910	19,476
	133,111	109,791	378,679	295,729
Operating expenses, including depreciation and amortization				
Rental operations	56,428	48,920	167,300	132,746
Tenant reinsurance	2,873	1,379	6,985	4,651
Property management, acquisition and development	17,746	16,008	48,226	44,203
	77,047	66,307	222,511	181,600
Income (loss) from operations				
Rental operations	57,453	45,145	156,844	116,447
Tenant reinsurance	9,421	8,116	27,640	22,409
Property management, acquisition and development	(10,810)	(9,777)	(28,316)	(24,727)
	56,064	43,484	156,168	114,129
Gain on sale of real estate assets				
Rental operations			800	
Loss on extinguishment of debt related to portfolio acquisition				
Property management, acquisition and development	(9,153)		(9,153)	
Interest expense				
Rental operations	(15,608)	(17,575)	(50,657)	(50,949)
Property management, acquisition and development	(656)	(848)	(1,335)	(1,399)
	(16,264)	(18,423)	(51,992)	(52,348)
Non-cash interest expense related to amortization of discount on equity component of exchangeable senior notes				
Property management, acquisition and development	(834)		(947)	(444)
	(834)		(947)	(444)
Interest income				
Tenant reinsurance	5	2	13	8
Property management, acquisition and development	197	459	506	1,176
	202	461	519	1,184
Interest income on note receivable from Preferred Operating Partnership unit holder				
Property management, acquisition and development	1,213	1,213	3,638	3,638

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Equity in earnings of unconsolidated real estate ventures				
Rental operations	3,405	2,854	8,942	7,848
Equity in earnings of unconsolidated real estate ventures - gain on sale of real estate assets and purchase of partners' interests				
Rental operations		13,620	2,556	19,049
Income tax expense				
Rental operations		(169)		(491)
Tenant reinsurance	(3,300)	(2,841)	(12,545)	(7,845)
Property management, acquisition and development	1,019	1,354	5,398	4,096
	(2,281)	(1,656)	(7,147)	(4,240)
Net income (loss)				
Rental operations	45,250	43,875	118,485	91,904
Tenant reinsurance	6,126	5,277	15,108	14,572
Property management, acquisition and development	(19,024)	(7,599)	(30,209)	(17,660)
	\$			