Commercial Vehicle Group, Inc.
Form S-3/A
January 08, 2010

Table of Contents

As filed with the Securities and Exchange Commission on January 8, 2010

Registration No. 333-163276

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Amendment No. 2
to

Form S-3
REGISTRATION STATEMENT
UNDER THE SECURITIES ACT OF 1933

Commercial Vehicle Group, Inc.*
(Exact name of registrant as specified in its charter)

Delaware	**41-1990662**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*

7800 Walton Parkway
New Albany, Ohio 43054
(614) 289-5360
(Address, including zip code, and telephone number, including area code, of registrant s principal executive offices)

Chad M. Utrup
Chief Financial Officer
Commercial Vehicle Group, Inc.
7800 Walton Parkway
New Albany, Ohio 43054
Tel.: (614) 289-5360
Fax: (614) 289-5361
(Name, address, including zip code, and telephone number, including area code, of agent for service)

Copies of all communications, including communications sent to agent for service, should be sent to:
Dennis M. Myers, P.C.
Kirkland & Ellis LLP
300 North LaSalle
Chicago, IL 60654
Fax: (312) 862-2200

* The co-registrants listed on the next page are also included in this Form S-3 Registration Statement as additional registrants.

Approximate date of commencement of proposed sale to the public: From time to time on or after the effective date of this Registration Statement.

If the only securities being registered on this Form are being offered pursuant to dividend or interest reinvestment plans, please check the following box. o

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box. þ

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. o

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. o

If this Form is a registration statement pursuant to General Instruction I.D. or a post-effective amendment thereto that shall become effective upon filing with the Commission pursuant to Rule 462(e) under the Securities Act, check the following box. o

If this Form is a post-effective amendment to a registration statement filed pursuant to General Instruction I.D. filed to register additional securities or additional classes of securities pursuant to Rule 413(b) under the Securities Act, check the following box. 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 o	Accelerated filer þ	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to be Registered(1)	**Amount to be Registered(1)(2)**	**Proposed Maximum Offering Price Per Share(1)(2)**	**Maximum Aggregate Offering Price(1)(2)(3)**	**Amount of Registration Fee**
Primary Offering by Commercial Vehicle Group, Inc.:				
Common Stock, par value $0.01 per share (5)				
Debt Securities (6)				
Guarantees of Debt Securities (7)				

Total Primary Offering			$200,000,000	$11,160(4)
Secondary Offering by Selling Stockholders:				
Common Stock, par value $0.01 per share, underlying Warrants to Purchase Common Stock (5)	344,014(8)	$5.41(9)	$1,861,116(9)	$104
Total Primary and Secondary Offerings			$201,861,116	$11,264(10)

Table of Contents

(1) Pursuant to General Instruction II.D of Form S-3, not specified as to each class of securities to be registered. There is being registered hereby such indeterminate number or amount, as the case may be, of the securities of each identified class as may from time to time be issued at indeterminate prices. Securities registered hereby may be offered for U.S. dollars or the equivalent thereof in foreign currencies. Securities registered hereby may be sold separately, together or in units with other securities registered hereby.

(2) The securities being registered hereby may be convertible into or exchangeable or exercisable for other securities of any identified class. In addition to the securities that may be issued directly under this registration statement, there is being registered hereunder such indeterminate aggregate number or amount, as the case may be, of the securities of each identified class as may from time to time be issued upon the conversion, exchange, settlement or exercise of other securities offered hereby. Separate consideration may or may not be received for securities that are issued upon the conversion or exercise of, or in exchange for, other securities offered hereby. If any debt securities are issued at an original issue discount, then the offering price of such debt securities shall be such greater amount as shall result in an aggregate initial offering price not to exceed $200,000,000, less the aggregate dollar amount of all securities previously issued hereunder.

(3) Estimated solely for the purpose of computing the registration fee pursuant to Rule 457(o) under the Securities Act, and exclusive of accrued interest, distributions and dividends, if any. The proposed maximum offering price will be determined from time to time in connection with the issuance of the securities registered hereunder.

(4) Calculated pursuant to Rule 457(o) under the Securities Act.

(5) Includes the rights attached to each share of common stock pursuant to the stockholder rights plan adopted on May 21, 2009, which rights are not currently separable from the shares of common stock and are not currently exercisable.

(6) The debt securities may be issued without guarantees or may be guaranteed by one or more of the registrants named below under Table of Additional Registrants.

(7) The guarantees of debt securities will be issued by one or more of the registrants named below under Table of Additional Registrants and will be issued without additional consideration. Pursuant to Rule 457(n), no registration fee is payable with respect to any such guarantees.

(8) These shares were included in the initial filing of this registration statement filed on November 20, 2009.

(9) Estimated solely for purposes of calculating the registration fee pursuant to Rule 457(c) under the Securities Act based upon the average high and low per share sale price as reported on The NASDAQ Global Select Market on November 18, 2009.

(10) Previously paid.

Table of Additional Registrants

Exact Name of Additional	Primary Standard Industrial Classification	I.R.S. Employer

Registrants*	Number	Jurisdiction of Formation	Identification No.
Cabarrus Plastics, Inc.	3714	North Carolina	56-1621055
CVG CS LLC	3714	Delaware	26-1459567
CVG European Holdings, LLC	3714	Delaware	20-5764995
CVG Logistics, LLC	3714	Delaware	20-1869535
CVG Management Corporation	3714	Delaware	20-2012737
CVG Oregon, LLC	3714	Delaware	26-1148839
CVS Holdings, Inc.	3714	Delaware	41-1967792
Mayflower Vehicle Systems, LLC	3714	Delaware	20-1895930
Monona Corporation	3714	Delaware	71-0944690
Monona (Mexico) Holdings LLC	3714	Illinois	36-4376683
Monona Wire Corporation	3714	Iowa	42-0945022
National Seating Company	3714	Delaware	36-2932300
Sprague Devices, Inc.	3714	Delaware	35-2104052
Trim Systems, Inc.	3714	Delaware	41-1887687
Trim Systems Operating Corp.	3714	Delaware	41-1921605

* The address for each of the Additional Registrants is c/o Commercial Vehicle Group, Inc., 7800 Walton Parkway, New Albany, Ohio 43054, telephone: (614) 289-5360. The name, address, including zip code of the agent for service for each of the Additional Registrants is Chad M. Utrup, Chief Financial Officer of Commercial Vehicle Group, Inc., 7800 Walton Parkway, New Albany, Ohio 43054, telephone: (614) 289-5360

The registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, as amended, or until this registration statement shall become effective on such date as the Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.

Table of Contents

The information contained in this prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and it is not the solicitation of an offer to buy these securities in any state where the offer or sale is not permitted.

SUBJECT TO COMPLETION, DATED JANUARY 8, 2010

PROSPECTUS

Commercial Vehicle Group, Inc.

Common Stock
Debt Securities

We may offer and sell, from time to time, in one or more offerings, any combination of debt and equity securities which we describe in this prospectus having a total initial offering price not exceeding $200,000,000. The selling stockholders may offer and sell up to 344,014 shares of our common stock from time to time under this prospectus, which shares are issuable upon exercise of warrants held by selling stockholders. We will not receive any proceeds from the sale of common stock by the selling stockholders.

This prospectus describes some of the general terms that may apply to these securities and the general manner in which they may be offered. Each time we offer securities, we will provide one or more supplements to this prospectus that contains specific information about the offering and the terms of any securities being sold. Before investing, you should carefully read this prospectus and any related prospectus supplement. The prospectus supplements may also add, update or change information contained in this prospectus.

Our common stock is traded on The NASDAQ Global Select Market under the symbol CVGI. On January 7, 2010, the last reported sale price of our common stock on The NASDAQ Global Select Market was $5.67 per share.

Investing in our common stock involves risks. See Risk Factors on page 5.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.

The date of this prospectus is , 2010.

TABLE OF CONTENTS

ABOUT THIS PROSPECTUS

This prospectus is a part of a registration statement that we filed with the Securities and Exchange Commission (the SEC) utilizing a shelf registration process. Under this shelf registration process, we may sell any combination of the securities described in this prospectus in one or more offerings from time to time. This prospectus provides you with a general description of the securities we may offer. Each time we sell securities under this shelf registration, we will provide a prospectus supplement that will contain specific information about the terms of that offering. The prospectus supplement may also add, update or change information contained in this prospectus. Therefore, if there is any inconsistency between the information in this prospectus and the prospectus supplement, you should rely on the information in the prospectus supplement. You should read both this prospectus and any prospectus supplement together with additional information described under the heading Where You Can Find More Information.

The selling stockholders also may use the shelf registration statement to sell up to an aggregate of 344,014 shares of our common stock from time to time in the public market. We will not receive any proceeds from the sale of common stock by the selling shareholders. The selling shareholders will deliver a supplement with this prospectus, to the extent appropriate, to update the information contained in this prospectus. The selling stockholders may sell their shares of common stock through any means described in the section entitled Plan of Distribution.

We and the selling stockholders have not authorized any dealer, salesman or other person to give any information or to make any representation other than those contained or incorporated by reference in this prospectus and the accompanying supplement to this prospectus. You must not rely upon any information or representation not contained or incorporated by reference in this prospectus or the accompanying prospectus supplement. This prospectus and the accompanying prospectus supplement do not constitute an offer to sell or the solicitation of an offer to buy any securities other than the registered securities to which they relate, nor do this prospectus and the accompanying prospectus supplement constitute an offer to sell or the solicitation of an offer to buy securities in any jurisdiction to any person to whom it is unlawful to make such offer or solicitation in such jurisdiction. You should not assume that the information contained in this prospectus and the accompanying prospectus supplement is accurate on any date subsequent to the date set forth on the front of the document or that any information we have incorporated by reference is correct on any date subsequent to the date of the document incorporated by reference, even though this prospectus and any accompanying prospectus supplement is delivered or securities are sold on a later date.

Unless the context otherwise requires or as otherwise expressly stated, references in this prospectus to the Company, we, us and our and similar terms refer to Commercial Vehicle Group, Inc. and its direct and indirect subsidiaries on a consolidated basis. References to our common stock refer to the common stock of Commercial Vehicle Group, Inc.

Table of Contents

WHERE YOU CAN FIND MORE INFORMATION

We are currently subject to the information requirements of the Securities Exchange Act of 1934, as amended (the Exchange Act) and in accordance therewith file periodic reports, proxy statements and other information with the Securities and Exchange Commission. You may read and copy (at prescribed rates) any such reports, proxy statements and other information at the SEC s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the operation of the public reference room. Our SEC filings will also be available to you on the SEC s website at http://www.sec.gov and in the Investor Relations section of our website at http://www.cvgrp.com. Our website and the information contained on that site, or connected to that site, are not incorporated into and are not a part of this prospectus.

We have filed with the SEC a registration statement on Form S-3 with respect to the shares of common stock offered hereby. This prospectus does not contain all the information set forth in the registration statement, parts of which are omitted in accordance with the rules and regulations of the SEC. For further information with respect to us and the common stock offered hereby, reference is made to the registration statement.

INCORPORATION OF CERTAIN INFORMATION BY REFERENCE

The SEC allows us to incorporate by reference information into this prospectus, which means that we can disclose important information about us by referring you to another document filed separately with the SEC. The information incorporated by reference is considered to be a part of this prospectus. This prospectus incorporates by reference the documents and reports listed below (other than portions of these documents that are either (1) described in paragraph (e) of Item 201 of Registration S-K or paragraphs (d)(1)-(3) and (e)(5) of Item 407 of Regulation S-K promulgated by the SEC or (2) furnished under Item 2.02 or Item 7.01 of a Current Report on Form 8-K):

our Annual Report on Form 10-K/A for the fiscal year ended December 31, 2008 filed with the SEC on November 20, 2009 (which amends and supercedes our Annual Report on Form 10-K for the fiscal year ended December 31, 2008 filed with the SEC on March 16, 2009);

our Quarterly Report on Form 10-Q/A for the quarter ended March 31, 2009 filed with the SEC on November 20, 2009 (which amends and supercedes our Quarterly Report on Form 10-Q for the quarter ended March 31, 2009 filed with the SEC on May 8, 2009);

our Quarterly Report on Form 10-Q/A for the quarter ended June 30, 2009 filed with the SEC on November 20, 2009 (which amends and supercedes our Quarterly Report on Form 10-Q for the quarter ended June 30, 2009 filed with the SEC on August 10, 2009);

our Quarterly Report on Form 10-Q for the quarter ended September 30, 2009 filed with the SEC on November 6, 2009;

our Current Reports on Form 8-K filed with the SEC on March 16, 2009, April 30, 2009, May 18, 2009, May 22, 2009, August 5, 2009 and December 11, 2009; and

The description of the Company s common stock, par value $0.01 per share, included under the caption Description of Capital Stock in the Prospectus forming a part of the Company s Registration Statement on Form S-1, initially filed with the Commission on May 21, 2004 (Registration No. 333-115708), including exhibits, and as may be subsequently amended from time to time, which description has been incorporated by reference in Item 1 of the Company s Registration Statement on Form 8-A, filed pursuant to Section 12 of the Exchange Act on August 5, 2004 (Registration No. 000-50890); and the description of the Company s stockholder rights plan contained in the registration statement on Form 8-A, filed pursuant to Section 12 of the Exchange Act on May 22, 2009 (Registration No. 001-34365).

We also incorporate by reference the information contained in all other documents we file with the SEC pursuant to Sections 13(a), 13(c), 14 or 15(d) of the Exchange Act (other than portions of these documents that are either (1) described in paragraph (e) of Item 201 of Registration S-K or paragraphs (d)(1)-(3) and (e)(5) of Item 407 of Regulation S-K promulgated by the SEC or (2) furnished under Item 2.02 or Item 7.01 of a Current Report on

Form 8-K, unless otherwise indicated therein) after the date of this prospectus and prior to the termination of this offering. The information contained in any such document will be considered part of this prospectus from the date the document is filed with the SEC.

Any statement contained in a document incorporated or deemed to be incorporated by reference in this prospectus will be deemed to be modified or superseded to the extent that a statement contained herein or in any other subsequently filed document which also is or is deemed to be incorporated by reference in this prospectus modifies or supersedes that statement. Any statement so modified or superseded will not be deemed, except as so modified or superseded, to constitute a part of this prospectus.

If you make a request for such information in writing or by telephone, we will provide you, without charge, a copy of any or all of the information incorporated by reference into this prospectus. Any such request should be directed to:

Commercial Vehicle Group, Inc.
7800 Walton Parkway
New Albany, Ohio 43054
(614) 289-5360
Attention: Secretary

FORWARD-LOOKING STATEMENTS

This prospectus, any accompanying prospectus supplement and the documents incorporated by reference herein and therein may contain forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. The words believes, projects, anticipates, plans, expects, intends, estimat similar expressions, as well as future or conditional verbs such as will, should, would, and could, are intended to identify forward-looking statements. These forward-looking statements represent management s current reasonable expectations and involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance and achievements, or industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. These factors, risks, and uncertainties include but are not limited to the factors described under Forward-Looking Statements and Risk Factors in our most recent Annual Report on Form 10-K/A and any subsequently filed Quarterly Reports on Form 10-Q or Form 10-Q/A, and the following:

- the continued severe downturn in the U.S. and global economies;
- continued disruptions in the credit and financial markets;
- volatility and cyclicality in the commercial vehicle market;
- production volumes for our customers vehicles;
- the ability of our major original equipment manufacturer (OEM) customers to exert influence over us;
- our inability to successfully implement our business strategy;
- our inability to obtain raw materials at favorable prices;
- our inability to complete additional strategic acquisitions;

the occurrence of labor strikes or work stoppages;

changes in statutory environmental and safety regulations or violations of applicable laws and regulations;

the impact of government regulations (foreign and domestic) on our OEM customers;

the concentration of our customer base or the discontinuation of a particular commercial vehicle platform;

currency exchange rate fluctuations;

risks associated with our foreign operations;

competition in the commercial vehicle component supply industry;

changes in competitive technologies;

our inability to recruit or retain skilled personnel, or the loss of services of any of our key management personnel;

our inability to protect our intellectual property rights;

claims by third parties that our products infringe upon their proprietary rights;

product liability claims, recalls or warranty claims;

equipment failures, delays in deliveries or catastrophic loss at any of our facilities leading to production or service curtailments or shutdowns;

our inability to comply with covenants in agreements governing our indebtedness;

our inability to implement our business strategy due to restrictions contained in our debt documents;

our inability to successfully execute any planned cost reductions, restructuring initiatives or the achievement of operational efficiencies; and

additional impairment charges.

There may be other factors that may cause our actual results to differ materially from the forward-looking statements. Our actual results, performance or achievements could differ materially from those expressed in, or implied by, the forward-looking statements. We can give no assurances that any of the events anticipated by the forward-looking statements will occur or, if any of them does, what impact they will have on our results of operations and financial condition. You should carefully read the factors described in the Risk Factors section of this prospectus and the documents incorporated by reference into this prospectus for a description of certain risks that could, among other things, cause our actual results to differ from these forward-looking statements.

Forward-looking statements speak only as of the date they were made. We undertake no obligation to update or revise forward-looking statements to reflect events or circumstances that arise after the date made or to reflect the occurrence of unanticipated events, other than as required by law.

OUR COMPANY

We are a leading supplier of fully integrated system solutions for the global commercial vehicle market, including the heavy-duty truck market, the construction and agricultural markets, and the specialty and military transportation markets. Our products include static and suspension seat systems, electronic wire harness assemblies, controls and switches, cab structures and components, interior trim systems (including instrument panels, door panels, headliners, cabinetry and floor systems), mirrors and wiper systems specifically designed for applications in commercial vehicles.

We are differentiated from suppliers to the automotive industry by our ability to manufacture low volume customized products on a sequenced basis to meet the requirements of our customers. We believe that we have the number one or two position in most of our major markets and that we are the only supplier in the North American commercial vehicle market that can offer complete cab systems including cab body assemblies, sleeper boxes, seats, interior trim, flooring, wire harnesses, panel assemblies and other structural components. We believe our products are used by virtually every major North American commercial vehicle OEM, which we believe creates an opportunity to cross-sell our products and offer a fully integrated system solution.

Demand for our products is generally dependent on the number of new commercial vehicles manufactured, which in turn is a function of general economic conditions, interest rates, changes in governmental regulations, consumer spending, fuel costs and our customers inventory levels and production rates.

New commercial vehicle demand in the North American Class 8 truck market has historically been cyclical and is particularly sensitive to the industrial sector of the economy, which generates a significant portion of the freight tonnage hauled by commercial vehicles. Production of Class 8 heavy trucks in North America initially peaked in 1999 and experienced a downturn from 2000 to 2003 that was due to a weak economy, an oversupply of

Table of Contents

new and used vehicle inventory and lower spending on commercial vehicles and equipment. Demand for commercial vehicles improved from 2004 to 2006 due to broad economic recovery in North America, corresponding growth in the movement of goods, the growing need to replace aging truck fleets and OEMs receiving larger than expected pre-orders in anticipation of the new EPA emissions standards becoming effective in 2007. During 2007 and 2008, the demand for North American Class 8 heavy trucks experienced a downturn as a result of pre-orders in 2006 and weakness in the North American economy and corresponding decline in the need for commercial vehicles to haul freight tonnage in North America as well as a global decline in demand for heavy and medium duty construction vehicles.

New commercial vehicle demand in the global construction equipment market generally follows certain economic conditions around the world. Within the construction market, there are two classes of construction equipment, the medium/heavy equipment market (weighing over 12 metric tons) and the light construction equipment market (weighing below 12 metric tons). Demand in the medium/heavy construction equipment market is typically related to the level of larger scale infrastructure development projects such as highways, dams, harbors, hospitals, airports and industrial development as well as activity in the mining, forestry and other raw material based industries. Demand in the light construction equipment market is typically related to certain economic conditions such as the level of housing construction and other smaller-scale developments and projects. Our products are primarily used in the medium/heavy construction equipment markets.

Our principal executive offices are located at 7800 Walton Parkway, New Albany, Ohio, 43054, and our telephone number is (614) 289-5360. Our website address is www.cvgrp.com. The information found on our website is not part of this prospectus.

Table of Contents

RISK FACTORS

Our business is subject to uncertainties and risks. You should carefully consider and evaluate all of the information included and incorporated by reference in this prospectus, including the risk factors incorporated by reference from our most recent annual report on Form 10-K/A, as updated by our quarterly reports on Form 10-Q/A for the quarters ended March 31, 2009 and June 30, 2009 and on Form 10-Q for the quarter ended September 30, 2009 and other filings we make with the SEC. Our business, financial condition, liquidity or results of operations could be materially adversely affected by any of these risks.

USE OF PROCEEDS

Unless otherwise indicated in the applicable prospectus supplement, we will use the net proceeds from the sale of our securities offered by this prospectus for the repayment of indebtedness and/or for general corporate and working capital purposes.

We will not receive any proceeds from the sale of shares of common stock by the selling stockholders.

RATIO OF EARNINGS TO FIXED CHARGES

The following table sets forth our historical ratio of earnings to fixed charges and ratio of earnings to combined fixed charges and preference dividends for the periods indicated. This information should be read in conjunction with the consolidated financial statements and the accompanying notes incorporated by reference in this prospectus.

	Nine Months Ended September 30,	Year Ended December 31,				
	2009	2008	2007	2006	2005	2004
Ratio of Earnings to Fixed Charges	(2.84)x	(10.76)x	0.71x	6.08x	5.79x	3.40x

For purposes of calculating the ratio of earnings to fixed charges, earnings are defined as income from continuing operations before income taxes and cumulative effect of change in accounting principles plus fixed charges. Fixed charges include interest expense (including amortization of deferred financing costs) and an estimate of operating rental expense, approximately 20%, which management believes is representative of the interest component.

Earnings before fixed charges were inadequate to cover fixed charges by $56.7 million, $220.7 million and $4.8 million for the nine months ended September 30, 2009, the year ended December 31, 2008 and the year ended December 31, 2007, respectively.

DESCRIPTION OF DEBT SECURITIES AND GUARANTEES

General

We may issue senior or subordinated debt securities, which will be direct, general obligations of Commercial Vehicle Group, Inc. that may be secured or unsecured.

The senior debt securities will constitute part of our senior debt, will be issued under the senior debt indenture described below and will rank equally with all of our other unsecured and unsubordinated debt.

The subordinated debt securities will constitute part of our subordinated debt, will be issued under the subordinated debt indenture described below and will be subordinate in right of payment to all of our senior debt, as defined in the indenture with respect to subordinated debt securities. The prospectus supplement for any series of subordinated debt securities or the information incorporated in this prospectus by reference will indicate the approximate amount of senior debt outstanding as of the end of our most recent fiscal quarter. Neither indenture limits our ability to incur additional senior debt or other indebtedness.

When we refer to debt securities in this prospectus, we mean both the senior debt securities and the subordinated debt securities.

Table of Contents

The debt securities may have the benefit of guarantees (each, a guarantee) by one or more of our subsidiaries (each, a guarantor) on a senior or subordinated basis. Unless otherwise expressly stated or the context otherwise requires, as used in this section, the term guaranteed debt securities means debt securities that, as described in the prospectus supplement relating thereto, are guaranteed by one or more guarantors pursuant to the applicable indenture.

The senior debt securities and subordinated debt securities will be governed by an indenture between us and one or more trustees selected by us. We will file the forms of indentures with the SEC as exhibits to our registration statement, of which this prospectus is a part. See Where You Can Find More Information above for information on how to obtain copies of them. The indentures are substantially identical, except for certain provisions including those relating to subordination, which are included only in the indenture related to subordinated debt securities. When we refer to the indenture or the trustee with respect to any debt securities, we mean the indenture under which those debt securities are issued and the trustee under that indenture.

Series of Debt Securities

We may issue multiple debt securities or series of debt securities under either indenture. This section summarizes terms of the securities that apply generally to all debt securities and series of debt securities. The provisions of each indenture allow us not only to issue debt securities with terms different from those of debt securities previously issued under that indenture, but also to reopen a previously issued series of debt securities and issue additional debt securities of that series. We will describe most of the financial and other specific terms of a particular series, whether it be a series of the senior debt securities or subordinated debt securities, in the prospectus supplement for that series. Those terms may vary from the terms described here.

Amounts of Issuances

The indentures do not limit the amount of debt securities that may be issued under them. We may issue the debt securities from time to time in one or more series. We are not required to issue all of the debt securities of one series at the same time and, unless otherwise provided in the applicable indenture or prospectus supplement, we may reopen a series and issue additional debt securities of that series without the consent of the holders of the outstanding debt securities of that series.

Principal Amount, Stated Maturity and Maturity

Unless otherwise stated, the principal amount of a debt security means the principal amount payable at its stated maturity, unless that amount is not determinable, in which case the principal amount of a debt security is its face amount.

The term stated maturity with respect to any debt security means the day on which the principal amount of the debt security is scheduled to become due. The principal may become due sooner, by reason of redemption or acceleration after a default or otherwise in accordance with the terms of the debt security. The day on which the principal actually becomes due, whether at the stated maturity or earlier, is called the maturity of the principal.

We also use the terms stated maturity and maturity to refer to the days when other payments become due. For example, we may refer to a regular interest payment date when an installment of interest is scheduled to become due as the stated maturity of that installment. When we refer to the stated maturity or the maturity of a debt security without specifying a particular payment, we mean the stated maturity or maturity, as the case may be, of the principal.

Specific Terms of Debt Securities

The applicable prospectus supplement will describe the specific terms of the debt securities, which will include some or all of the following:

- the title of the series and whether it is a senior debt security or a subordinated debt security;
- any limit on the total principal amount of the debt securities of the same series;

Table of Contents

the stated maturity;

the currency or currencies for principal and interest, if not U.S. dollars;

the price at which we originally issue the debt security, expressed as a percentage of the principal amount, and the original issue date;

whether the debt security is a fixed rate debt security, a floating rate debt security or an indexed debt security;

if the debt security is a fixed rate debt security, the yearly rate at which the debt security will bear interest, if any, and the interest payment dates;

if the debt security is a floating rate debt security, the interest rate basis; any applicable index currency or index maturity, spread or spread multiplier or initial base rate, maximum rate or minimum rate; the interest reset, determination, calculation and payment dates; the day count convention used to calculate interest payments for any period; the business day convention; and the calculation agent;

if the debt security is an indexed debt security, the principal amount, if any, we will pay at maturity, interest payment dates, the amount of interest, if any, we will pay on an interest payment date or the formula we will use to calculate these amounts, if any, and the terms on which the debt security will be exchangeable for or payable in cash, securities or other property;

if the debt security may be converted into or exercised or exchanged for common or preferred stock or other securities of the Company or debt or equity securities of one or more third parties, the terms on which conversion, exercise or exchange may occur, including whether conversion, exercise or exchange is mandatory, at the option of the holder or at our option, the period during which conversion, exercise or exchange may occur, the initial conversion, exercise or exchange price or rate and the circumstances or manner in which the amount of common or preferred stock or other securities issuable upon conversion, exercise or exchange may be adjusted;

if the debt security is also an original issue discount debt security, the yield to maturity;

if applicable, the circumstances under which the debt security may be redeemed at our option or repaid at the holder s option before the stated maturity, including any redemption commencement date, repayment date(s), redemption price(s) and redemption period(s);

the authorized denominations, if other than $1,000 and integral multiples of $1,000;

the depositary for the debt security, if other than The Depository Trust Company (DTC), and any circumstances under which the holder may request securities in non-global form, if we choose not to issue the debt security in book-entry form only;

if applicable, the circumstances under which we will pay additional amounts on any debt securities held by a person who is not a United States person for tax purposes and under which we can redeem the debt securities if we have to pay additional amounts;

whether the debt security will be guaranteed by any guarantors and, if so, the identity of the guarantors and, to the extent the terms thereof differ from those described in this prospectus, a description of the terms of the guarantees;

the assets, if any that will be pledged as security for the payment of the debt security;

the names and duties of any co-trustees, depositaries, authenticating agents, paying agents, transfer agents or registrars for the debt security, as applicable; and

any other terms of the debt security and any guarantees of the debt security, which could be different from those described in this prospectus.

Governing Law

The indentures and the debt securities (and any guarantees thereof) will be governed by New York law, without regard to conflicts of laws principles thereof.

Form of Debt Securities

We will issue each debt security only in registered form, without coupons, unless we specify otherwise in the applicable prospectus supplement. In addition, we will issue each debt security in global *i.e.,* book-entry form only, unless we specify otherwise in the applicable prospectus supplement. Debt securities in book-entry form will be represented by a global security registered in the name of a depositary, which will be the holder of all the debt securities represented by the global security. Those who own beneficial interests in a global debt security will do so through participants in the depositary s securities clearance system, and the rights of these indirect owners will be governed solely by the applicable procedures of the depositary and its participants. References to holders in this section mean those who own debt securities registered in their own names, on the books that we or the trustee maintain for this purpose, and not those who own beneficial interests in debt securities registered in street name or in debt securities issued in book-entry form through one or more depositaries.

Unless otherwise indicated in the prospectus supplement, the following is a summary of the depositary arrangements applicable to debt securities issued in global form and for which DTC acts as depositary.

Each global debt security will be deposited with, or on behalf of, DTC, as depositary, or its nominee, and registered in the name of a nominee of DTC. Except under the limited circumstances described below, global debt securities are not exchangeable for definitive certificated debt securities.

Ownership of beneficial interests in a global debt security is limited to institutions that have accounts with DTC or its nominee, or persons that may hold interests through those participants. In addition, ownership of beneficial interests by participants in a global debt security will be evidenced only by, and the transfer of that ownership interest will be effected only through, records maintained by DTC or its nominee for a global debt security. Ownership of beneficial interests in a global debt security by persons that hold those interests through participants will be evidenced only by, and the transfer of that ownership interest within that participant will be effected only through, records maintained by that participant. DTC has no knowledge of the actual beneficial owners of the debt securities. Beneficial owners will not receive written confirmation from DTC of their purchase, but beneficial owners are expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the participants through which the beneficial owners entered the transaction. The laws of some jurisdictions require that certain purchasers of securities take physical delivery of securities they purchase in definitive form. These laws may impair a holder s ability to transfer beneficial interests in a global debt security.

We will make payment of principal of, and interest on, debt securities represented by a global debt security registered in the name of or held by DTC or its nominee to DTC or its nominee, as the case may be, as the registered owner and holder of the global debt security representing those debt securities. DTC has advised us that upon receipt of any payment of principal of, or interest on, a global debt security, DTC immediately will credit accounts of participants on its book-entry registration and transfer system with payments in amounts proportionate to their respective interests in the principal amount of that global debt security, as shown in the records of DTC. Payments by participants to owners of beneficial interests in a global debt security held through those participants will be governed by standing instructions and customary practices, as is now the case with securities held for the accounts of customers in bearer form or registered in street name, and will be the sole responsibility of those participants, subject to any statutory or regulatory requirements that may be in effect from time to time.

Neither we, any trustee nor any of our respective agents will be responsible for any aspect of the records of DTC, any nominee or any participant relating to, or payments made on account of, beneficial interests in a permanent global debt security or for maintaining, supervising or reviewing any of the records of DTC, any nominee or any participant relating to such beneficial interests.

Table of Contents

A global debt security is exchangeable for definitive debt securities registered in the name of, and a transfer of a global debt security may be registered to, any person other than DTC or its nominee, only if:

DTC notifies us that it is unwilling or unable to continue as depositary for that global security or has ceased to be a registered clearing agency and we do not appoint another institution to act as depositary within 90 days; or

we notify the trustee that we wish to terminate that global security.

Any global debt security that is exchangeable pursuant to the preceding sentence will be exchangeable in whole for definitive debt securities in registered form, of like tenor and of an equal aggregate principal amount as the global debt security, in denominations specified in the applicable prospectus supplement, if other than $1,000 and multiples of $1,000. The definitive debt securities will be registered by the registrar in the name or names instructed by DTC. We expect that these instructions may be based upon directions received by DTC from its participants with respect to ownership of beneficial interests in the global debt security.

Except as provided above, owners of the beneficial interests in a global debt security will not be entitled to receive physical delivery of debt securities in definitive form and will not be considered the holders of debt securities for any purpose under the indentures. No global debt security shall be exchangeable except for another global debt security of like denomination and tenor to be registered in the name of DTC or its nominee. Accordingly, each person owning a beneficial interest in a global debt security must rely on the procedures of DTC and, if that person is not a participant, on the procedures of the participant through which that person owns its interest, to exercise any rights of a holder under the global debt security or the indentures.

We understand that, under existing industry practices, in the event that we request any action of holders, or an owner of a beneficial interest in a global debt security desires to give or take any action that a holder is entitled to give or take under the debt securities or the indentures, DTC would authorize the participants holding the relevant beneficial interests to give or take that action. Additionally, those participants would authorize beneficial owners owning through those participants to give or take that action or would otherwise act upon the instructions of beneficial owners owning through them.

DTC has advised us as follows:

DTC is:

a limited-purpose trust company organized under the New York Banking Law,

a banking organization within the meaning of the New York Banking Law,

a member of the Federal Reserve System,

a clearing corporation within the meaning of the New York Uniform Commercial Code, and

a clearing agency registered under Section 17A of the Securities Exchange Act of 1934.

DTC was created to hold securities of its participants and to facilitate the clearance and settlement of securities transactions among its participants in those securities through electronic book-entry changes in accounts of the participants, thereby eliminating the need for physical movement of securities certificates.

DTC s participants include securities brokers and dealers, banks, trust companies, clearing corporations and certain other organizations.

DTC is owned by a number of its participants and by the New York Stock Exchange, Inc., the NYSE Amex LLC and the Financial Industry Regulatory Authority, Inc.

Access to DTC s book-entry system is also available to others, such as banks, brokers, dealers and trust companies, that clear through or maintain a custodial relationship with a participant, either directly or indirectly.

The rules applicable to DTC and its participants are on file with the SEC.

Table of Contents

Investors may hold interests in the debt securities outside the United States through the Euroclear System (Euroclear) or Clearstream Banking (Clearstream) if they are participants in those systems, or indirectly through organizations which are participants in those systems. Euroclear and Clearstream will hold interests on behalf of their participants through customers securities accounts in Euroclear s and Clearstream s names on the books of their respective depositaries which in turn will hold such positions in customers securities accounts in the names of the nominees of the depositaries on the books of DTC. At the present time, JPMorgan Chase Bank, National Association will act as U.S. depositary for Euroclear, and Citibank, N.A. will act as U.S. depositary for Clearstream. All securities in Euroclear or Clearstream are held on a fungible basis without attribution of specific certificates to specific securities clearance accounts.

The following is based on information furnished by Euroclear or Clearstream, as the case may be.

Euroclear has advised us that:

It was created in 1968 to hold securities for participants of Euroclear and to clear and settle transactions between Euroclear participants through simultaneous electronic book-entry delivery against payment, thereby eliminating the need for physical movement of certificates and any risk from lack of simultaneous transfers of securities and cash;

Euroclear includes various other services, including securities lending and borrowing and interfaces with domestic markets in several countries;

Euroclear is operated by Euroclear Bank S.A./ N.V., as operator of the Euroclear System (the Euroclear Operator), under contract with Euroclear Clearance Systems S.C., a Belgian cooperative corporation (the Cooperative);

The Euroclear Operator conducts all operations, and all Euroclear securities clearance accounts and Euroclear cash accounts are accounts with the Euroclear Operator, not the Cooperative. The Cooperative establishes policy for Euroclear on behalf of Euroclear participants. Euroclear participants include banks (including central banks), securities brokers and dealers and other professional financial intermediaries and may include underwriters of debt securities offered by this prospectus;

Indirect access to Euroclear is also available to other firms that clear through or maintain a custodial relationship with a Euroclear participant, either directly or indirectly;

Securities clearance accounts and cash accounts with the Euroclear Operator are governed by the Terms and Conditions Governing Use of Euroclear and the related Operating Procedures of the Euroclear System, and applicable Belgian law (collectively, the Terms and Conditions);

The Terms and Conditions govern transfers of securities and cash within Euroclear, withdrawals of securities and cash from Euroclear, and receipts of payments with respect to securities in Euroclear. The Euroclear Operator acts under the Terms and Conditions only on behalf of Euroclear participants, and has no record of or relationship with persons holding through Euroclear participants; and

Distributions with respect to debt securities held beneficially through Euroclear will be credited to the cash accounts of Euroclear participants in accordance with the Terms and Conditions, to the extent received by the U.S. depositary for Euroclear.

Clearstream has advised us that:

It is incorporated under the laws of Luxembourg as a professional depositary and holds securities for its participating organizations and facilitates the clearance and settlement of securities transactions between Clearstream participants through electronic book-entry changes in accounts of Clearstream participants, thereby eliminating the need for physical movement of certificates;

Clearstream provides to Clearstream participants, among other things, services for safekeeping, administration, clearance and settlement of internationally traded securities and securities lending and borrowing. Clearstream interfaces with domestic markets in several countries;

As a professional depositary, Clearstream is subject to regulation by the Luxembourg Monetary Institute;

Clearstream participants are recognized financial institutions around the world, including underwriters, securities brokers and dealers, banks, trust companies, clearing corporations and certain other organizations and may include underwriters of debt securities offered by this prospectus;

Indirect access to Clearstream is also available to others, such as banks, brokers, dealers and trust companies that clear through or maintain a custodial relationship with a Clearstream participant either directly or indirectly; and

Distributions with respect to the debt securities held beneficially through Clearstream will be credited to cash accounts of Clearstream participants in accordance with its rules and procedures, to the extent received by the U.S. depositary for Clearstream.

We have provided the descriptions herein of the operations and procedures of Euroclear and Clearstream solely as a matter of convenience. These operations and procedures are solely within the control of Euroclear and Clearstream and are subject to change by them from time to time. Neither we, any underwriters nor the trustee takes any responsibility for these operations or procedures, and you are urged to contact Euroclear or Clearstream or their respective participants directly to discuss these matters.

Secondary market trading between Euroclear participants and Clearstream participants will occur in the ordinary way in accordance with the applicable rules and operating procedures of Euroclear and Clearstream and will be settled using the procedures applicable to conventional eurobonds in immediately available funds.

Cross-market transfers between persons holding directly or indirectly through DTC, on the one hand, and directly or indirectly through Euroclear or Clearstream participants, on the other, will be effected within DTC in accordance with DTC s rules on behalf of the relevant European international clearing system by its U.S. depositary; however, such cross-market transactions will require delivery of instructions to the relevant European international clearing system by the counterparty in such system in accordance with its rules and procedures and within its established deadlines (European time). The relevant European international clearing system will, if the transaction meets its settlement requirements, deliver instructions to its U.S. depositary to take action to effect final settlement on its behalf by delivering or receiving debt securities in DTC, and making or receiving payment in accordance with normal procedures. Euroclear participants and Clearstream participants may not deliver instructions directly to their respective U.S. depositaries.

Because of time-zone differences, credits of securities received in Euroclear or Clearstream as a result of a transaction with a DTC participant will be made during subsequent securities settlement processing and dated the business day following the DTC settlement date. Such credits, or any transactions in the securities settled during such processing, will be reported to the relevant Euroclear participants or Clearstream participants on that business day. Cash received in Euroclear or Clearstream as a result of sales of securities by or through a Euroclear participant or a Clearstream participant to a DTC participant will be received with value on the business day of settlement in DTC but will be available in the relevant Euroclear or Clearstream cash account only as of the business day following settlement in DTC.

Although DTC, Euroclear and Clearstream have agreed to the foregoing procedures in order to facilitate transfers of debt securities among participants of DTC, Euroclear and Clearstream, they are under no obligation to perform or continue to perform such procedures and they may discontinue the procedures at any time.

Redemption or Repayment

If there are any provisions regarding redemption or repayment applicable to a debt security, we will describe them in a prospectus supplement.

We or our affiliates may purchase debt securities from investors who are willing to sell from time to time, either in the open market at prevailing prices or in private transactions at negotiated prices. Debt securities that we or they purchase may, at our discretion, be held, resold or canceled.

Table of Contents

Mergers and Similar Transactions

We are generally permitted under the indenture for the relevant series to merge or consolidate with another corporation or other entity. We are also permitted under the indenture for the relevant series to sell all or substantially all of our assets to another corporation or other entity. With regard to any series of debt securities, however, we may not take any of these actions unless all the following conditions, among other things, are met:

If the successor entity in the transaction is not the Company, the successor entity must expressly assume our obligations under the debt securities of that series and the indenture with respect to that series. The successor entity may be organized and existing under the laws of the United States, any State thereof or the District of Columbia.

Immediately after the transaction, no default under the debt securities of that series has occurred and is continuing. For this purpose, default under the debt securities of that series means an event of default with respect to that series or any event that would be an event of default with respect to that series if the requirements for giving us default notice and for our default having to continue for a specific period of time were disregarded. We describe these matters below under Default, Remedies and Waiver of Default.

If the conditions described above are satisfied with respect to the debt securities of any series, we will not need to obtain the approval of the holders of those debt securities in order to merge or consolidate or to sell our assets. Also, these conditions will apply only if we wish to merge or consolidate with another entity or sell all or substantially all of our assets to another entity. We will not need to satisfy these conditions if we enter into other types of transactions, including any transaction in which we acquire the stock or assets of another entity, any transaction that involves a change of control of the Company but in which we do not merge or consolidate and any transaction in which we sell less than substantially all our assets.

If we sell all or substantially all of our assets, we will be released from all our liabilities and obligations under the debt securities of any series and the indenture with respect to that series.

Subordination Provisions

Holders of subordinated debt securities should recognize that contractual provisions in the subordinated debt indenture may prohibit us from making payments on those securities. Subordinated debt securities are subordinate and junior in right of payment, to the extent and in the manner stated in the subordinated debt indenture, to all of our senior debt, as defined in the subordinated debt indenture, including all debt securities we have issued and will issue under the senior debt indenture.

The subordinated debt indenture defines senior debt as:

our indebtedness under or in respect of our credit agreement, whether for principal, interest (including interest accruing after the filing of a petition initiating any proceeding pursuant to any bankruptcy law, whether or not the claim for such interest is allowed as a claim in such proceeding), capital lease obligations, deferred purchase price of property obligations, reimbursement obligations, fees, commissions, expenses, indemnities, dividends, hedging obligations or other amounts; and

any other indebtedness permitted under the terms of that indenture, unless the instrument under which such indebtedness is incurred expressly provides that it is on a parity with or subordinated in right of payment to the subordinated debt securities.

Notwithstanding the foregoing, senior debt will not include: (i) equity interests; (ii) any liability for taxes; (iii) any trade payables; (iv) any indebtedness subordinated or junior to other indebtedness or other obligation; or (v) any indebtedness incurred in violation of the subordinated debt indenture.

We may modify the subordination provisions, including the definition of senior debt, with respect to one or more series of subordinated debt securities. Such modifications will be set forth in the applicable prospectus supplement.

Table of Contents

The subordinated debt indenture provides that, unless all principal of and any premium or interest on the senior debt has been paid in full, no payment or other distribution may be made in respect of any subordinated debt securities in the following circumstances:

- in the event of any insolvency or bankruptcy proceedings, or any receivership, liquidation, reorganization, assignment for creditors or other similar proceedings or events involving us or our assets;

- (a) in the event and during the continuation of any default in the payment of principal, premium or interest on any senior debt beyond any applicable grace period or (b) in the event that any event of default with respect to any senior debt has occurred and is continuing, permitting the holders of that senior debt (or a trustee) to accelerate the maturity of that senior debt, whether or not the maturity is in fact accelerated (unless, in the case of (a) or (b), the payment default or event of default has been cured or waived or ceased to exist and any related acceleration has been rescinded) or (c) in the event that any judicial proceeding is pending with respect to a payment default or event of default described in (a) or (b); or

- in the event that any subordinated debt securities have been declared due and payable before their stated maturity.

If the trustee under the subordinated debt indenture or any holders of the subordinated debt securities receive any payment or distribution that is prohibited under the subordination provisions, then the trustee or the holders will have to repay that money to the holders of the senior debt.

Even if the subordination provisions prevent us from making any payment when due on the subordinated debt securities of any series, we will be in default on our obligations under that series if we do not make the payment when due. This means that the trustee under the subordinated debt indenture and the holders of that series can take action against us, but they will not receive any money until the claims of the holders of senior debt have been fully satisfied.

The subordinated debt indenture allows the holders of senior debt to obtain a court order requiring us and any holder of subordinated debt securities to comply with the subordination provisions.

Defeasance, Covenant Defeasance and Satisfaction and Discharge

When we use the term defeasance, we mean discharge from some or all of our obligations under the indenture. If we deposit with the trustee funds or government securities, or if so provided in the applicable prospectus supplement, obligations other than government securities, sufficient to make payments on any series of debt securities on the dates those payments are due and payable and other specified conditions are satisfied, then, at our option, either of the following will occur:

- we will be discharged from our obligations with respect to the debt securities of such series and all obligations of any guarantors of such debt securities will also be discharged with respect to the guarantees of such debt securities (legal defeasance); or

- we will be discharged from any covenants we make in the applicable indenture for the benefit of such series and the related events of default will no longer apply to us (covenant defeasance).

If we defease any series of debt securities, the holders of such securities will not be entitled to the benefits of the indenture, except for our obligations to register the transfer or exchange of such securities, replace stolen, lost or mutilated securities or maintain paying agencies and hold moneys for payment in trust. In case of covenant defeasance, our obligation to pay principal, premium and interest on the applicable series of debt securities will also survive.

We will be required to deliver to the trustee an opinion of counsel that the deposit and related defeasance would not cause the holders of the applicable series of debt securities to recognize gain or loss for federal income tax purposes. If we elect legal defeasance, that opinion of counsel must be based upon a ruling from the United States Internal Revenue Service or a change in law to that effect.

Upon the effectiveness of defeasance with respect to any series of guaranteed debt securities, each guarantor of the debt securities of such series shall be automatically and unconditionally released and discharged from all of its

Table of Contents

obligations under its guarantee of the debt securities of such series and all of its other obligations under the applicable indenture in respect of the debt securities of that series, without any action by the Company, any guarantor or the trustee and without the consent of the holders of any debt securities.

Default, Remedies and Waiver of Default

Unless otherwise specified in the applicable prospectus supplement, when we refer to an event of default with respect to any series of debt securities, we mean any of the following:

- we do not pay the principal or any premium on any debt security of that series when due at its stated maturity, upon optional redemption, upon required purchase, upon declaration of acceleration or otherwise;
- we do not pay interest on any debt security of that series within 30 days after the due date;
- we or any subsidiary guarantor remain in breach of our covenants regarding mergers or sales of substantially all of our assets or any other covenant we make in the indenture for the benefit of the relevant series, for a period of 60 days after we receive a notice of default stating that we are in breach and requiring us to remedy the breach within a specified time after receipt of such notice. The notice must be sent by the trustee or the holders of at least 25% in principal amount of the relevant series of debt securities;
- we file for bankruptcy or other events of bankruptcy, insolvency or reorganization relating to the Company occur;
- if the debt securities of that series are guaranteed debt securities, the guarantee of the debt securities of that series by any guarantor shall for any reason cease to be, or shall for any reason be asserted in writing by such guarantor or the Company, not to be, in full force and effect and enforceable in accordance with its terms, except to the extent contemplated or permitted by the indenture or the debt securities of that series; or
- if the applicable prospectus supplement states that any additional event of default applies to the series, that event of default occurs.

We may change, eliminate, or add to the events of default with respect to any particular series or any particular debt security or debt securities within a series, as indicated in the applicable prospectus supplement.

If you are the holder of a subordinated debt security, all the remedies available upon the occurrence of an event of default under the subordinated debt indenture will be subject to the restrictions on the subordinated debt securities described above under Subordination Provisions.

Except as otherwise specified in the applicable prospectus supplement, if an event of default has occurred with respect to any series of debt securities and has not been cured or waived, the trustee or the holders of not less than 25% in principal amount of all debt securities of that series then outstanding may declare the entire principal amount of the debt securities of that series to be due immediately. Except as otherwise specified in the applicable prospectus supplement, if the event of default occurs because of events in bankruptcy, insolvency or reorganization relating to the Company, the entire principal amount of the debt securities of that series will be automatically accelerated, without any action by the trustee or any holder.

Each of the situations described above is called an acceleration of the stated maturity of the affected series of debt securities. Except as otherwise specified in the applicable prospectus supplement, if the stated maturity of any series is accelerated and a judgment for payment has not yet been obtained, the holders of a majority in principal amount of the debt securities of that series may cancel the acceleration for the entire series.

If an event of default occurs, the trustee will have special duties. In that situation, the trustee will be obligated to use those of its rights and powers under the relevant indenture, and to use the same degree of care and skill in doing so, that a prudent person would use in that situation in conducting his or her own affairs.

Except as described in the prior paragraph, the trustee is not required to take any action under the relevant indenture at the request of any holders unless the holders offer the trustee protection satisfactory to it from loss, liability or expense. These majority holders may also direct the trustee in performing any other action under the relevant indenture with respect to the debt securities of that series.

Table of Contents

Before a holder may take steps to enforce its rights or protect its interests relating to any debt security, all of the following must occur:

- the holder must give the trustee written notice that an event of default has occurred with respect to the debt securities of the series, and the event of default must not have been cured or waived;
- the holders of at least 25% in principal amount of all debt securities of the series must request that the trustee take action because of the default, and they or other holders must offer to the trustee indemnity reasonably satisfactory to the trustee against the cost and other liabilities of taking that action;
- the trustee must not have taken action for 60 days after the above steps have been taken; and
- during those 60 days, the holders of a majority in principal amount of the debt securities of the series must not have given the trustee directions that are inconsistent with such request.

Book-entry and other indirect owners should consult their banks or brokers for information on how to give notice or direction to or make a request of the trustee and how to declare or cancel an acceleration of the maturity.

Waiver of Default

The holders of a majority in principal amount of the debt securities of any series may by notice to the trustee waive an existing default and its consequences for all debt securities of that series except (i) a default in the payment of the principal of or interest on a debt security (ii) a default arising from the failure to redeem or purchase any debt security when required pursuant to the indenture or (iii) a default in respect of a provision that under the indenture cannot be amended without the consent of each securityholder affected. If this happens, the default is deemed cured, but no such waiver shall extend to any subsequent or other default or impair any consequent right.

Annual Information about Defaults to the Trustee

We will furnish each trustee within 120 days after the end of each fiscal year a certificate indicating whether the signers thereof know of any default that occurred in the previous year.

Modifications and Waivers

Changes Requiring Each Holder s Approval

We, along with the subsidiary guarantors and the trustee, may amend the indentures or the debt securities with the written consent of the holders of at least a majority in principal amount of the debt securities then outstanding. However, without the consent of each securityholder affected thereby, an amendment or waiver may not:

- reduce the amount of debt securities whose holders must consent to an amendment;
- reduce the rate of or extend the time for payment of the interest on any debt security;
- reduce the principal of or change the stated maturity on any debt security;
- reduce the amount payable upon redemption of any debt security or change the time at which any debt security may be redeemed as described in the applicable indenture;

permit redemption of a debt security if not previously permitted;

change the currency of any payment on a debt security;

impair the right of any holder of a debt security to receive payment of principal of and interest on such holder s debt security on or after the due dates thereof or to institute suit for the enforcement of any payment on or with respect to such holder s debt security;

change the amendment provisions which require each holder s consent or in the waiver provisions;

Table of Contents

change the ranking or priority of any debt security that would adversely affect the securityholders; or

change or release other than in accordance with the indenture, any subsidiary guaranty that would adversely affect the securityholders.

Changes Not Requiring Approval

We, along with the subsidiary guarantors and the trustee, may amend the indentures or the debt securities without notice to or consent of any securityholder:

to cure any ambiguity, omission, defect or inconsistency;

to provide for the assumption by a successor corporation of the obligations of the Company, or any subsidiary guarantor under the indenture;

to provide for uncertificated debt securities in addition to or in place of certificated debt securities;

to add guarantees with respect to the debt securities, including any subsidiary guaranties, or to secure the debt securities;

to add to the covenants of the Company or a subsidiary guarantor for the benefit of the holders of the debt securities or to surrender any right or power conferred upon the Company or a subsidiary guarantor;

to make any change that does not adversely affect the rights of any holder of the debt securities;

to comply with any requirement of the SEC in connection with the qualification of the indenture under the Trust Indenture Act; or

to make any amendment to the provisions of the indenture relating to the transfer and legending of debt securities; provided, however, that (a) compliance with the indenture as so amended would not result in debt securities being transferred in violation of the Securities Act or any other applicable securities law and (b) such amendment does not materially and adversely affect the rights of holders to transfer debt securities.

Modification of Subordination Provisions

We may not amend the indenture related to subordinated debt securities to adversely affect the interests of any holder of senior debt then outstanding in any material respect without the written consent of each holder of senior debt then outstanding who would be adversely affected (or the group or representative thereof authorized or required to consent thereto pursuant to the instrument creating or evidencing, or pursuant to which there is outstanding, such senior debt). In addition, we may not modify the subordination provisions of the indenture related to subordinated debt securities in a manner that would adversely affect the subordinated debt securities of any one or more series then outstanding in any material respect, without the consent of the holders of a majority in aggregate principal amount of all affected series then outstanding, voting together as one class (and also of any affected series that by its terms is entitled to vote separately as a series, as described below).

Book-entry and other indirect owners should consult their banks or brokers for information on how approval may be granted or denied if we seek to change an indenture or any debt securities or request a waiver.

Changes Requiring Majority Approval

Any other change to a particular indenture and the debt securities issued under that indenture would require the following approval:

- If the change affects only particular debt securities within a series issued under the applicable indenture, it must be approved by the holders of a majority in principal amount of such particular debt securities; or

- If the change affects debt securities of more than one series issued under the applicable indenture, it must be approved by the holders of a majority in principal amount of all debt securities of all such series affected by the change, with all such affected debt securities voting together as one class for this purpose and such affected debt securities of any series potentially comprising fewer than all debt securities of such series, in each case, except as may otherwise be provided pursuant to such indenture for all or any particular debt securities of any series. This means that modification of terms with respect to certain securities of a series could be effectuated without obtaining the consent of the holders of a majority in principal amount of other securities of such series that are not affected by such modification.

Special Rules for Action by Holders

Only holders of outstanding debt securities of the applicable series will be eligible to take any action under the applicable indenture, such as giving a notice of default, declaring an acceleration, approving any change or waiver or giving the trustee an instruction with respect to debt securities of that series. Also, we will count only outstanding debt securities in determining whether the various percentage requirements for taking action have been met. Any debt securities owned by us or any of our affiliates or surrendered for cancellation or for payment or redemption of which money has been set aside in trust are not deemed to be outstanding. Any required approval or waiver must be given by written consent.

In some situations, we may follow special rules in calculating the principal amount of debt securities that are to be treated as outstanding for the purposes described above. This may happen, for example, if the principal amount is payable in a non-U.S. dollar currency, increases over time or is not to be fixed until maturity.

We will generally be entitled to set any day as a record date for the purpose of determining the holders that are entitled to take action under either indenture. In certain limited circumstances, only the trustee will be entitled to set a record date for action by holders. If we or the trustee sets a record date for an approval or other action to be taken by holders, that vote or action may be taken only by persons or entities who are holders on the record date and must be taken during the period that we specify for this purpose, or that the trustee specifies if it sets the record date. We or the trustee, as applicable, may shorten or lengthen this period from time to time. This period, however, may not extend beyond the 180th day after the record date for the action. In addition, record dates for any global debt security may be set in accordance with procedures established by the depositary from time to time. Accordingly, record dates for global debt securities may differ from those for other debt securities.

Form, Exchange and Transfer

If any debt securities cease to be issued in registered global form, they will be issued:

- only in fully registered form;
- without interest coupons; and
- unless we indicate otherwise in the applicable prospectus supplement, in denominations of $1,000 and integral multiples of $1,000.

Holders may exchange their debt securities for debt securities of smaller denominations or combined into fewer debt securities of larger denominations, as long as the total principal amount is not changed. Holders may not exchange debt securities for securities of a different series or having different terms, unless permitted by the terms of that series and described in the applicable prospectus supplement.

Holders may exchange or transfer their debt securities at the office of the trustee. They may also replace lost, stolen, destroyed or mutilated debt securities at that office. We have appointed the trustee to act as our agent for registering debt securities in the names of holders and transferring and replacing debt securities. We may appoint another entity to perform these functions or perform them ourselves.

Holders will not be required to pay a service charge to transfer or exchange their debt securities, but they may be required to pay for any tax or other governmental charge associated with the exchange or transfer. The transfer or exchange, and any replacement, will be made only if our transfer agent is satisfied with the holder s proof of legal ownership. The transfer agent may require an indemnity before replacing any debt securities.

If we have designated additional transfer agents for a debt security, they will be named in the applicable prospectus supplement. We may appoint additional transfer agents or cancel the appointment of any particular transfer agent. We may also approve a change in the office through which any transfer agent acts.

Table of Contents

If the debt securities of any series are redeemable and we redeem less than all those debt securities, we may block the transfer or exchange of those debt securities during the period beginning 15 days before the day we mail the notice of redemption and ending on the day of that mailing, in order to freeze the list of holders to prepare the mailing. We may also refuse to register transfers of or exchange any debt security selected for redemption, except that we will continue to permit transfers and exchanges of the unredeemed portion of any debt security being partially redeemed.

If a debt security is issued as a global debt security, only DTC or other depositary will be entitled to transfer and exchange the debt security as described in this subsection, since the depositary will be the sole holder of the debt security.

The rules for exchange described above apply to exchange of debt securities for other debt securities of the same series and kind. If a debt security is convertible, exercisable or exchangeable into or for a different kind of security, such as one that we have not issued, or for other property, the rules governing that type of conversion, exercise or exchange will be described in the applicable prospectus supplement.

Payments

We will pay interest, principal and other amounts payable with respect to the debt securities of any series to the holders of record of those debt securities as of the record dates and otherwise in the manner specified below or in the prospectus supplement for that series.

We will make payments on a global debt security in accordance with the applicable policies of the depositary as in effect from time to time. Under those policies, we will pay directly to the depositary, or its nominee, and not to any indirect owners who own beneficial interests in the global debt security. An indirect owner s right to receive those payments will be governed by the rules and practices of the depositary and its participants.

We will make payments on a debt security in non-global, registered form as follows. We will pay interest that is due on an interest payment date by check mailed on the interest payment date to the holder at his or her address shown on the trustee s records as of the close of business on the regular record date. We will make all other payments by check at the paying agent described below, against surrender of the debt security. All payments by check will be made in next-day funds i.e., funds that become available on the day after the check is cashed.

Alternatively, if a non-global debt security has a face amount of at least $1,000,000 and the holder asks us to do so, we will pay any amount that becomes due on the debt security by wire transfer of immediately available funds to an account at a bank in New York City, on the due date. To request wire payment, the holder must give the paying agent appropriate wire transfer instructions at least five business days before the requested wire payment is due. In the case of any interest payment due on an interest payment date, the instructions must be given by the person or entity who is the holder on the relevant regular record date. In the case of any other payment, payment will be made only after the debt security is surrendered to the paying agent. Any wire instructions, once properly given, will remain in effect unless and until new instructions are given in the manner described above.

Book-entry and other indirect owners should consult their banks or brokers for information on how they will receive payments on their debt securities.

Regardless of who acts as paying agent, all money paid by us to a paying agent that remains unclaimed at the end of two years after the amount is due to a holder will be repaid to us. After that two-year period, the holder may look only to us for payment and not to the trustee, any other paying agent or anyone else.

Guarantees

The debt securities of any series may be guaranteed by one or more of our subsidiaries. However, the applicable indenture governing the debt securities will not require that any of our subsidiaries be a guarantor of any series of debt securities and will permit the guarantors for any series of guaranteed debt securities to be different from any of the subsidiaries listed herein. As a result, a series of debt securities may not have any guarantors and the guarantors of any series of guaranteed debt securities may differ from the guarantors of any other series of guaranteed debt securities. If the Company issues a series of guaranteed debt securities, the identity of the specific guarantors of the debt securities of that series will be identified in the applicable prospectus supplement.

If the Company issues a series of guaranteed debt securities, a description of some of the terms of guarantees of those debt securities will be set forth in the applicable prospectus supplement. Unless otherwise provided in the prospectus supplement relating to a series of guaranteed debt securities, each guarantor of the debt securities of such series will unconditionally guarantee the due and punctual payment of the principal of, and premium, if any, and interest, if any, on each debt security of such series, all in accordance with the terms of such debt securities and the applicable indenture.

Notwithstanding the foregoing, unless otherwise provided in the prospectus supplement relating to a series of guaranteed debt securities, the applicable indenture will contain provisions to the effect that the obligations of each guarantor under its guarantees and such indenture shall be limited to the maximum amount as will, after giving effect to all other contingent and fixed liabilities of such guarantor, result in the obligations of such guarantor under such guarantees and such indenture not constituting a fraudulent conveyance or fraudulent transfer under applicable law. However, there can be no assurance that, notwithstanding such limitation, a court would not determine that a guarantee constituted a fraudulent conveyance or fraudulent transfer under applicable law. If that were to occur, the court could void the applicable guarantor s obligations under that guarantee, subordinate that guarantee to other debt and other liabilities of that guarantor or take other action detrimental to holders of the debt securities of the applicable series, including directing the holders to return any payments received from the applicable guarantor.

Unless otherwise provided in the prospectus supplement relating to a series of guaranteed debt securities, the applicable indenture will (i) provide that, upon the sale or disposition (by merger or otherwise) of any guarantor, (x) if the transferee is not an affiliate of the Company, such guarantor will automatically be released from all obligations under its guarantee of such debt securities or (y) otherwise, the transferee (if other than the Company or another guarantor) will assume the guarantor s obligations under its guarantee of such debt securities and (ii) permit us to cause the guarantee of any guarantor of such debt securities to be released at any time if we satisfy such conditions, if any, as are specified in the prospectus supplement for such debt securities.

The applicable prospectus supplement relating to any series of guaranteed debt securities will specify other terms of the applicable guarantees.

If the applicable prospectus supplement relating to a series of our senior debt securities provides that those senior debt securities will have the benefit of a guarantee by any or all of our subsidiaries, unless otherwise provided in the applicable prospectus supplement, each such guarantee will be the unsubordinated and unsecured obligation of the applicable guarantor and will rank equally in right of payment with all of the unsecured and unsubordinated indebtedness of such guarantor.

Any guarantee of any debt securities will be effectively subordinated to all existing and future secured indebtedness of the applicable guarantor, including any secured guarantees of other Company debt, to the extent of the value of the collateral securing that indebtedness. Consequently, in the event of a bankruptcy, or similar proceeding with respect to any guarantor that has provided a guarantee of any debt securities, the holders of that guarantor s secured indebtedness will be entitled to proceed directly against the collateral that secures that secured indebtedness and such collateral will not be available for satisfaction of any amount owed by such guarantor under its unsecured indebtedness, including its guarantees of any debt securities, until that secured debt is satisfied in full. Unless otherwise provided in the applicable prospectus supplement, the indenture will not limit the ability of any guarantor to incur secured indebtedness.

If the applicable prospectus supplement relating to a series of our subordinated debt securities provides that those subordinated debt securities will have the benefit of a guarantee by any or all of our subsidiaries, unless otherwise provided in the applicable prospectus supplement, each such guarantee will be the subordinated and unsecured obligation of the applicable guarantor and, in addition to being effectively subordinated to secured debt of such guarantor, will be subordinated in right of payment to all of such guarantor s existing and future senior indebtedness, including any guarantee of the senior debt securities, to the same extent and in the same manner as the subordinated debt securities are subordinated to our senior debt. See Subordination Provisions above.

Table of Contents

Paying Agents

We may appoint one or more financial institutions to act as our paying agents, at whose designated offices debt securities in non-global entry form may be surrendered for payment at their maturity. We call each of those offices a paying agent. We may add, replace or terminate paying agents from time to time. We may also choose to act as our own paying agent. We will specify in the prospectus supplement for the debt security the initial location of each paying agent for that debt security. We must notify the trustee of changes in the paying agents.

Notices

Notices to be given to holders of a global debt security will be given only to the depositary, in accordance with its applicable policies as in effect from time to time. Notices to be given to holders of debt securities not in global form will be sent by mail to the respective addresses of the holders as they appear in the trustee s records, and will be deemed given when mailed. Neither the failure to give any notice to a particular holder, nor any defect in a notice given to a particular holder, will affect the sufficiency of any notice given to another holder.

Book-entry and other indirect owners should consult their banks or brokers for information on how they will receive notices.

Our Relationship With the Trustee

The prospectus supplement for the debt security will describe any material relationships we may have with the trustee with respect to that debt security.

The same financial institution may initially serve as the trustee for our senior debt securities and subordinated debt securities. Consequently, if an actual or potential event of default occurs with respect to any of these securities, the trustee may be considered to have a conflicting interest for purposes of the Trust Indenture Act of 1939. In that case, the trustee may be required to resign under one or more of the indentures, and we would be required to appoint a successor trustee. For this purpose, a potential event of default means an event that would be an event of default if the requirements for giving us default notice or for the default having to exist for a specific period of time were disregarded.

DESCRIPTION OF CAPITAL STOCK

General Matters

Our total amount of authorized capital stock is 30,000,000 shares of common stock, par value $0.01 per share, and 5,000,000 shares of preferred stock, par value $0.01 per share. As of January 6, 2010, 23,297,050 shares of common stock were issued and outstanding and no shares of preferred stock were issued or outstanding. The following summary of certain provisions of our capital stock describes all material provisions of, but does not purport to be complete and is subject to, and qualified in its entirety by, our certificate of incorporation and by-laws and by the provisions of applicable law.

Common Stock

All of our existing common stock is, and the shares of common stock being offered by us in the offering will be, upon payment therefor, validly issued, fully paid and nonassessable. Set forth below is a brief discussion of the principal terms of our common stock.

Dividend Rights. Subject to preferences that may apply to shares of preferred stock outstanding at the time, holders of outstanding shares of common stock are entitled to receive dividends out of assets legally available at the times and in the amounts as the board of directors may from time to time determine.

Voting Rights. Each outstanding share of common stock is entitled to one vote on all matters submitted to a vote of stockholders.

Preemptive or Similar Rights. Our common stock is not entitled to preemptive or other similar subscription rights to purchase any of our securities.

Conversion Rights. Our common stock is not convertible.

Stockholder Rights Plan. On May 21, 2009, our board of directors adopted a Stockholder Rights Plan set forth in a Rights Agreement (the Rights Agreement) with Computershare Trust Company, N.A., and, in connection therewith, declared a dividend of one preferred share purchase right (a Right) for each share of common stock. Generally, the Rights would become exercisable upon the earlier of (i) ten business days following the public announcement that a person or group of affiliated or associated persons has acquired beneficial ownership of 20% or more of the then outstanding shares of common stock or (ii) ten business days following the commencement of a tender offer or exchange offer that would result in a person or group of affiliated or associated persons acquiring 20% or more of our common stock. If such a triggering event occurs, unless the Rights are redeemed or have expired, our stockholders, other than the acquirer, will generally have the right to receive that number of shares of common stock (or, in certain circumstances, preferred stock) having a mttom:2px;padding-right:2px;">

$
(14,341
)

$
(4,518
)
Improvements of existing real estate

(2,169
)

(6,796
)
Proceeds from sale of real estate

10,773

25,290

Receipts from lenders for funds held in escrow

1,097

3,320

Payments to lenders for funds held in escrow

(1,248
)

(1,119
)
Receipts from tenants for reserves

1,544

1,349

Payments to tenants from reserves

(1,175
)

(1,255
)
Deposits on future acquisitions

(340
)

(1,650
)
Deposits applied against acquisition of real estate investments

300

—

Net cash (used in) provided by investing activities

$
(5,559
)

$
14,621

Cash flows from financing activities:

Proceeds from issuance of equity

$
5,779

$

25,178

Offering costs paid

(94
)

(422
)
Retirement of senior common stock

(34
)

—

Borrowings under mortgage notes payable

9,380

6,700

Payments for deferred financing costs

(253
)

(414
)
Principal repayments on mortgage notes payable

(21,998
)

(40,573
)
Borrowings from revolving credit facility

50,400

50,000

Repayments on revolving credit facility

(38,400
)

(51,900
)

Decrease in security deposits	(26)	(348)
Distributions paid for common, senior common and preferred stock	(26,980)	(24,159)
Net cash used in financing activities	$ (22,226)	$ (35,938)
Net (decrease) increase in cash, cash equivalents, and restricted cash	$ (1,790)	$ 103
Cash, cash equivalents, and restricted cash at beginning of period	$ 9,080	$ 7,688
Cash, cash equivalents, and restricted cash at end of period	$ 7,290	$ 7,791

6

Table of Contents

NON-CASH INVESTING AND FINANCING INFORMATION		
Tenant funded fixed asset improvements	$27	$1,571
Assumed mortgage in connection with acquisition	$—	$11,179
Assumed interest rate swap fair market value	$—	$42
Unrealized gain related to interest rate hedging instruments, net	$783	$179
Capital improvements included in accounts payable and accrued expenses	$31	$2,031

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

	For the six months ended June 30,	
	2018	2017
Cash and cash equivalents	$4,552	$5,014
Restricted cash	2,738	2,777
Total cash, cash equivalents, and restricted cash shown in the condensed consolidated statement of cash flows	$7,290	$7,791

Restricted cash consists of security deposits and receipts from tenants for reserves. These funds will be released to the tenants upon completion of agreed upon tasks, as specified in the lease agreements, mainly consisting of maintenance and repairs on the buildings and upon receipt by us of evidence of insurance and tax payments.

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

7

Table of Contents

Gladstone Commercial Corporation
Notes to Condensed Consolidated Financial Statements (Unaudited)

1. Organization, Basis of Presentation and Significant Accounting Policies

Gladstone Commercial Corporation is a real estate investment trust ("REIT") that was incorporated under the General Corporation Law of the State of Maryland on February 14, 2003. We focus on acquiring, owning and managing primarily office and industrial properties. On a selective basis, we may make long term industrial and commercial mortgage loans; however, we do not have any mortgage loans currently outstanding. Subject to certain restrictions and limitations, our business is managed by Gladstone Management Corporation, a Delaware corporation (the "Adviser"), and administrative services are provided by Gladstone Administration, LLC, a Delaware limited liability company (the "Administrator"), each pursuant to a contractual arrangement with us. Our Adviser and Administrator collectively employ all of our personnel and pay their salaries, benefits, and general expenses directly. Gladstone Commercial Corporation conducts substantially all of its operations through a subsidiary, Gladstone Commercial Limited Partnership, a Delaware limited partnership (the "Operating Partnership").

All further references herein to "we," "our," "us" and the "Company" mean Gladstone Commercial Corporation and its consolidated subsidiaries, except where it is made clear that the term means only Gladstone Commercial Corporation.

Interim Financial Information

Our interim financial statements are prepared in accordance with generally accepted accounting principles ("GAAP") for interim financial information and pursuant to the requirements for reporting on Form 10-Q and in accordance with Article 10 of Regulation S-X. Accordingly, certain disclosures accompanying annual financial statements prepared in accordance with GAAP are omitted. The year-end balance sheet data presented herein was derived from audited financial statements, but does not include all disclosures required by GAAP. In the opinion of our management, all adjustments, consisting solely of normal recurring accruals, necessary for the fair statement of financial statements for the interim period, have been included. The interim financial statements and notes thereto should be read in conjunction with the financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2017, as filed with the U.S. Securities and Exchange Commission on February 14, 2018. The results of operations for the three and six months ended June 30, 2018 are not necessarily indicative of the results that may be expected for other interim periods or for the full fiscal year.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could materially differ from those estimates.

Critical Accounting Policies

In preparation of our financial statements in accordance with GAAP, we apply certain critical accounting policies which require management to make judgments that are subjective in nature to make certain estimates and assumptions. Application of our accounting policies involves the exercise of judgment regarding the use of assumptions as to future uncertainties, and as a result, actual results could materially differ from these estimates. A summary of all of our significant accounting policies is provided in Note 1 to our consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2017. There were no material changes to our critical accounting policies during the three and six months ended June 30, 2018.

8

Table of Contents

Recently Issued Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued guidance regarding the recognition of revenue from contracts with customers. Under this guidance, an entity will recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This guidance also requires improved disclosures regarding the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. We adopted this guidance for our annual and interim periods beginning January 1, 2018 and will use the modified retrospective method, under which the cumulative effect of initially applying the guidance is recognized at the date of initial application. Our adoption of this guidance did not have a material impact on our consolidated financial statements. Further, as discussed below, once the new guidance regarding the principles for the recognition measurement, presentation and disclosure of leases goes into effect on January 1, 2019, we expect the new revenue standard will apply to executory costs and other components of revenue due under leases that are deemed to be non-lease components (examples include common area maintenance and provision of utilities), even when the revenue for such activities is not separately stipulated in the lease. Revenue from these non-lease components, which were previously recognized on a straight-line basis under current lease guidance, would be recognized under the new revenue guidance as the related services are delivered. As a result, while our total revenue recognized over the lease term would not differ under the new guidance, the revenue recognition pattern could be different. We are currently evaluating the impact of revenue recognition from the adoption of the lease standard on our consolidated financial statements.

In February 2016, the FASB issued Accounting Standards Update ("ASU") 2016-02, "Leases: Amendments to the FASB Accounting Standards Codification" ("ASU 2016-02"). The new standard requires lessees to apply a dual approach, classifying leases as either finance or operating leases based on the principle of whether or not the lease is effectively a financed purchase of the leased asset by the lessee. This classification will determine whether lease expense is recognized based on an effective interest method or on a straight line basis over the term of the lease, respectively. A lessee is also required to record a right-of-use asset and a lease liability for all leases with a term of greater than 12 months regardless of their classification. Leases with a term of 12 months or less will be accounted for similar to existing guidance for operating leases today. The new standard requires lessors to account for leases using an approach that is substantially equivalent to existing guidance for sales-type leases, direct financing leases and operating leases. We are evaluating the adoption of ASU 2016-02, but we expect the standard to minimally impact our consolidated financial statements as we currently have four operating ground lease arrangements with terms greater than one year for which we are the lessee, and we don't expect the purchase of properties with ground leases to be crucial to our acquisition strategy. We also expect our general and administrative expense to increase as the new standard requires us to expense non-incremental leasing costs that were previously capitalized to leasing commissions. ASU 2016-02 supersedes the previous leases standard, ASC 840 "Leases." The standard is effective on January 1, 2019, with early adoption permitted. We will adopt using the modified retrospective method, under which the cumulative effect of initially applying the guidance is recognized at the date of initial application.

In August 2016, the FASB issued ASU 2016-15, "Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (a consensus of the Emerging Issues Task Force)," which clarifies how entities should classify certain cash receipts and cash payments on the statement of cash flows with the objective of reducing the existing diversity in practice related to eight specific cash flow issues. The areas addressed in the new guidance relate to debt prepayment costs, settlement of zero-coupon debt instruments, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, proceeds from the settlement of corporate-owned and bank-owned life insurance policies, distributions received from equity method investments, beneficial interest in securitization transactions and separately identifiable cash flows and application of the predominance principle. We adopted this guidance for the calendar year beginning January 1, 2018, and the standard requires retrospective adoption. Our adoption of this guidance did not have a material impact on our consolidated financial statements, as we have not historically completed transactions contemplated in this update.

In November 2016, the FASB issued ASU 2016-18, "Statement of Cash Flows (Topic 230): Restricted Cash (a consensus of the FASB Emerging Issues Task Force)," which requires the statement of cash flows to explain the change during the period in the total of cash, cash equivalents and amounts described as restricted cash or restricted cash equivalents. Under the new guidance, amounts described as restricted cash and restricted cash equivalents will be included with cash and cash equivalents when reconciling the beginning of period and end of period total amounts shown on the statement of cash flows. We adopted this guidance for the calendar year beginning January 1, 2018, and the standard requires retrospective adoption. Our adoption of this guidance did not have a material impact on our consolidated financial statements.

In February 2017, the FASB issued ASU 2017-05 to provide guidance for recognizing gains and losses from the transfer of nonfinancial assets and in-substance non-financial assets in contracts with non-customers, unless other specific guidance applies. The standard requires a company to de-recognize nonfinancial assets once it transfers control of a distinct nonfinancial asset or distinct in substance nonfinancial asset. Additionally, when a company transfers its controlling interest in a nonfinancial asset, but retains a noncontrolling ownership interest, the company is required to measure any non-controlling interest it receives or retains at fair value. The guidance requires companies to recognize a full gain or loss on the transaction. As a result of the new guidance, the guidance specific to real estate sales in ASC 360-20 will be eliminated, and partial sales of real estate assets will now be subject to the same de-recognition model as all other nonfinancial assets. We adopted this guidance for the calendar year beginning January 1, 2018, and the standard requires retrospective adoption. Our adoption of this guidance will not have a material impact on our consolidated financial statements, as we typically complete fee simple sales, with no continuing involvement.

2. Related-Party Transactions

Gladstone Management and Gladstone Administration

We are externally managed pursuant to contractual arrangements with our Adviser and our Administrator, which collectively employ all of our personnel and pay their salaries, benefits, and general expenses directly. Both our Adviser and Administrator are affiliates of ours, as their parent company is owned and controlled by Mr. David Gladstone, our chairman and chief executive officer. Two of our executive officers, Mr. Gladstone and Mr. Terry Lee Brubaker (our vice chairman and chief operating officer) serve as directors and executive officers of our Adviser and our Administrator. Our president, Mr. Robert Cutlip, is an executive managing director of our Adviser. Mr. Michael LiCalsi, our general counsel and secretary, serves as our Administrator's president, general counsel and secretary. We have entered into an advisory agreement with our Adviser, as amended from time to time (the "Advisory Agreement"), and an administration agreement with our Administrator (the "Administration Agreement"). The services and fees under the Advisory Agreement and Administration Agreement are described below. As of June 30, 2018 and December 31, 2017, $2.4 million and $2.3 million, respectively, were collectively due to our Adviser and Administrator.

Base Management Fee

On January 10, 2017, we entered into a Fourth Amended and Restated Investment Advisory Agreement with the Adviser, effective as of October 1, 2016. Our original entrance into the Advisory Agreement and each subsequent amendment thereof (including the fourth amendment completed in January of 2017) was approved unanimously by our Board of Directors. Our Board of Directors also reviews and considers renewing the Advisory Agreement each July. During its July 2018 meeting, our Board of Directors reviewed and renewed the Advisory Agreement for an additional year, through August 31, 2019.

Under the Advisory Agreement, the calculation of the annual base management fee equals 1.5% of our adjusted total stockholders' equity, which is our total stockholders' equity plus total mezzanine equity (before giving effect to the base management fee and incentive fee), adjusted to exclude the effect of any unrealized gains or losses that do not affect realized net income (including impairment charges) and adjusted for any one-time events and certain non-cash items (the later to occur for a given quarter only upon the approval of our Compensation Committee). The fee is calculated and accrued quarterly as 0.375% per quarter of such adjusted total stockholders' equity figure. Our Adviser does not charge acquisition or disposition fees when we acquire or dispose of properties, as is common in other externally managed REITs. Our Adviser may earn fee income from our borrowers, tenants or other sources.

For the three and six months ended June 30, 2018, we recorded a base management fee of $1.3 million and $2.6 million, respectively. For the three and six months ended June 30, 2017, we recorded a base management fee of $1.2

million and $2.4 million, respectively.

Incentive Fee

Pursuant to the Advisory Agreement, the calculation of the incentive fee rewards the Adviser in circumstances where our quarterly Core FFO (defined at the end of this paragraph), before giving effect to any incentive fee, or pre-incentive fee Core FFO, exceeds 2.0% quarterly, or 8.0% annualized, of adjusted total stockholders' equity (after giving effect to the base management fee but before giving effect to the incentive fee). We refer to this as the hurdle rate. The Adviser will receive 15.0% of the amount of our pre-incentive fee Core FFO that exceeds the hurdle rate. However, in no event shall the incentive fee for a particular quarter exceed by 15.0% (the cap) the average quarterly incentive fee paid by us for the previous four quarters (excluding quarters for which no incentive fee was paid). Core FFO (as defined in the Advisory Agreement) is GAAP net income (loss) available to common stockholders, excluding the incentive fee, depreciation and amortization, any realized and unrealized gains, losses or other non-cash items recorded in net income (loss) available to common stockholders for the period, and one-time events pursuant to changes in GAAP.

Table of Contents

For the three and six months ended June 30, 2018, we recorded an incentive fee of $0.7 million and $1.4 million, respectively. For the three and six months ended June 30, 2017, we recorded an incentive fee of $0.6 million and $1.1 million, respectively. The Adviser did not waive any portion of the incentive fee for the three and six months ended June 30, 2018 or 2017, respectively.

Capital Gain Fee

Under the Advisory Agreement, we will pay to the Adviser a capital gains-based incentive fee that will be calculated and payable in arrears as of the end of each fiscal year (or upon termination of the Advisory Agreement). In determining the capital gain fee, we will calculate aggregate realized capital gains and aggregate realized capital losses for the applicable time period. For this purpose, aggregate realized capital gains and losses, if any, equals the realized gain or loss calculated by the difference between the sales price of the property, less any costs to sell the property and the current gross value of the property (which is calculated as the original acquisition price plus any subsequent non-reimbursed capital improvements). At the end of the fiscal year, if this number is positive, then the capital gain fee payable for such time period shall equal 15.0% of such amount. No capital gain fee was recognized during the three and six months ended June 30, 2018 or 2017.

Termination Fee

The Advisory Agreement includes a termination fee whereby, in the event of our termination thereof without cause (with 120 days' prior written notice and the vote of at least two-thirds of our independent directors), a termination fee would be payable to the Adviser equal to two times the sum of the average annual base management fee and incentive fee earned by the Adviser during the 24-month period prior to such termination. A termination fee is also payable if the Adviser terminates the Advisory Agreement after we have defaulted and applicable cure periods have expired. The Advisory Agreement may also be terminated for cause by us (with 30 days' prior written notice and the vote of at least two-thirds of our independent directors), with no termination fee payable. Cause is defined in the agreement to include if the Adviser breaches any material provisions thereof, the bankruptcy or insolvency of the Adviser, dissolution of the Adviser and fraud or misappropriation of funds.

Administration Agreement

Under the terms of the Administration Agreement, we pay separately for our allocable portion of the Administrator's overhead expenses in performing its obligations to us including, but not limited to, rent and our allocable portion of the salaries and benefits expenses of our Administrator's employees, including, but not limited to, our chief financial officer, treasurer, chief compliance officer, general counsel and secretary (who also serves as our Administrator's president, general counsel and secretary), and their respective staffs. Our allocable portion of the Administrator's expenses are generally derived by multiplying our Administrator's total expenses by the approximate percentage of time the Administrator's employees perform services for us in relation to their time spent performing services for all companies serviced by our Administrator under contractual agreements. For the three and six months ended June 30, 2018, we recorded an administration fee of $0.4 million and $0.7 million, respectively. For the three and six months ended June 30, 2017, we recorded an administration fee of $0.3 million and $0.7 million, respectively.

Gladstone Securities

Gladstone Securities, LLC, ("Gladstone Securities"), is a privately held broker dealer registered with the Financial Industry Regulatory Authority and insured by the Securities Investor Protection Corporation. Gladstone Securities is an affiliate of ours, as its parent company is owned and controlled by Mr. David Gladstone, our chairman and chief executive officer. Mr. Gladstone also serves on the board of managers of Gladstone Securities.

11

Table of Contents

Mortgage Financing Arrangement Agreement

We entered into an agreement with Gladstone Securities, effective June 18, 2013, for it to act as our non-exclusive agent to assist us with arranging mortgage financing for properties we own (the “Financing Arrangement Agreement”). In connection with this engagement, Gladstone Securities will, from time to time, continue to solicit the interest of various commercial real estate lenders or recommend to us third party lenders offering credit products or packages that are responsive to our needs. We pay Gladstone Securities a financing fee in connection with the services it provides to us for securing mortgage financing on any of our properties. The amount of these financing fees, which are payable upon closing of the financing, are based on a percentage of the amount of the mortgage, generally ranging from 0.15% to a maximum of 1.0% of the mortgage obtained. The amount of the financing fees may be reduced or eliminated, as determined by us and Gladstone Securities, after taking into consideration various factors, including, but not limited to, the involvement of any third party brokers and market conditions. We paid financing fees to Gladstone Securities of $0.001 million and $0.02 million during the three and six months ended June 30, 2018, respectively, which are included in mortgage notes payable, net, in the condensed consolidated balance sheets, or 0.01% and 0.11%, respectively, of the mortgage principal secured. We paid financing fees to Gladstone Securities of $0.06 million during both the three and six months ended June 30, 2017, which are included in mortgage notes payable, net, in the condensed consolidated balance sheets, or 0.31% of the mortgage principal secured. Our Board of Directors renewed the Financing Arrangement Agreement for an additional year, through August 31, 2019, at its July 2018 meeting.

3. (Loss) earnings per Share of Common Stock

The following tables set forth the computation of basic and diluted (loss) earnings per share of common stock for the three and six months ended June 30, 2018 and 2017. We computed basic (loss) earnings per share for the three and six months ended June 30, 2018 and 2017 using the weighted average number of shares outstanding during the periods. Diluted (loss) earnings per share for the three and six months ended June 30, 2018 and 2017 reflects additional shares of common stock related to our convertible senior common stock (the “Senior Common Stock”), if the effect would be dilutive, that would have been outstanding if dilutive potential shares of common stock had been issued, as well as an adjustment to net income available to common stockholders as applicable to common stockholders that would result from their assumed issuance (dollars in thousands, except per share amounts).

	For the three months ended June 30,		For the six months ended June 30,	
	2018	2017	2018	2017
Calculation of basic (loss) earnings per share of common stock:				
Net (loss) income (attributable) available to common stockholders	$(317)	$(2,025)	$1,474	$(287)
Denominator for basic weighted average shares of common stock	28,437,855	25,276,824	28,429,475	25,121,239
Basic (loss) earnings per share of common stock	$(0.01)	$(0.08)	$0.05	$(0.01)
Calculation of diluted (loss) earnings per share of common stock:				
Net (loss) income (attributable) available to common stockholders	$(317)	$(2,025)	$1,474	$(287)
Add: income impact of assumed conversion of senior common stock (1)	—	—	—	—
Net (loss) income (attributable) available to common stockholders plus assumed conversions (1)	$(317)	$(2,025)	$1,474	$(287)
Denominator for basic weighted average shares of common stock	28,437,855	25,276,824	28,429,475	25,121,239
Effect of convertible Senior Common Stock (1)	—	—	—	—
Denominator for diluted weighted average shares of common stock (1)	28,437,855	25,276,824	28,429,475	25,121,239
Diluted (loss) earnings per share of common stock	$(0.01)	$(0.08)	$0.05	$(0.01)

(1) We excluded shares of Senior Common Stock that are convertible into shares of our common stock in the amount of 744,327 and 783,236 from the calculation of diluted (loss) earnings per share for the three and six months ended June 30, 2018 and 2017, respectively, because it was anti-dilutive.

Table of Contents

4. Real Estate and Intangible Assets

Real Estate

The following table sets forth the components of our investments in real estate as of June 30, 2018 and December 31, 2017, excluding real estate held for sale as of June 30, 2018 and December 31, 2017 (dollars in thousands):

	June 30, 2018	December 31, 2017
Real estate:		
Land	$122,010	$121,783
Building and improvements	719,603	708,948
Tenant improvements	63,736	63,122
Accumulated depreciation	(163,349)	(149,417)
Real estate, net	$742,000	$744,436

Real estate depreciation expense on building and tenant improvements was $7.5 million and $14.8 million for the three and six months ended June 30, 2018, respectively, and $6.4 million and $12.8 million for the three and six months ended June 30, 2017, respectively.

Acquisitions

We acquired one property during the six months ended June 30, 2018, and one property during the six months ended June 30, 2017. Both acquisitions are summarized below (dollars in thousands):

Six Months Ended		Square Footage	Lease Term	Purchase Price	Acquisition Expenses		Annualized GAAP Rent	Debt Issued or Assumed	
June 30, 2018	(1)	127,444	9.8 Years	$14,341	$ 91	(3)	$ 1,087	$ —	
June 30, 2017	(2)	60,016	8.5 Years	15,697	247	(3)	1,680	11,179	(4)

(1) On March 9, 2018, we acquired a 127,444 square foot property in Vance, Alabama for $14.3 million. The annualized GAAP rent on the 9.8 year lease is $1.1 million.

(2) On June 22, 2017, we acquired a 60,016 square foot property in Conshohocken, Pennsylvania for $15.7 million. We assumed $11.2 million of mortgage debt. The annualized GAAP rent on the 8.5 year lease is $1.7 million.

(3) We accounted for this transaction under ASU 2017-01, “Clarifying the Definition of a Business.” As a result, we treated our acquisitions during the six months ended June 30, 2018 and 2017 as asset acquisitions rather than business combinations. As a result of this treatment, we capitalized $0.1 million and $0.2 million, respectively, of acquisition costs that would otherwise have been expensed under business combination treatment.

(4) We assumed an interest rate swap in connection with $11.2 million of assumed debt on our Conshohocken, Pennsylvania acquisition, pursuant to which we will pay our counterparty a fixed interest rate of 1.80%, and receive a variable interest rate of one month LIBOR from our counterparty. Our total interest rate on this debt is fixed at 3.55%. The interest rate swap had a fair value of $0.04 million upon the date of assumption, and subsequently increased in value to $0.7 million at June 30, 2018. We have elected to treat this interest rate swap as a cash flow hedge, and all changes in fair market value will be recorded to accumulated other comprehensive income on the consolidated balance sheets.

Table of Contents

We determined the fair value of assets acquired and liabilities assumed related to the properties acquired during the six months ended June 30, 2018 and 2017 as follows (dollars in thousands):

Acquired assets and liabilities	Six months ended June 30, 2018 Purchase price	Six months ended June 30, 2017 Purchase price
Land	$459	$1,996
Building	11,609	9,975
Tenant Improvements	615	905
In-place Leases	509	1,690
Leasing Costs	534	464
Customer Relationships	566	1,256
Above Market Leases	49	—
Below Market Leases	—	(1,030)
Discount on Assumed Debt	—	399
Fair Value of Interest Rate Swap Assumed	—	42
Total Purchase Price	$14,341	$15,697

Significant Real Estate Activity on Existing Assets

During the six months ended June 30, 2018 and 2017, we executed one and one new lease, respectively, which are summarized below (dollars in thousands):

Six Months Ended	Aggregate Square Footage	Weighted Average Lease Term	Aggregate Annualized GAAP Rent	Aggregate Tenant Improvement	Aggregate Leasing Commissions
June 30, 2018	34,441	3.6 years	$ 97	$ —	$ 14
June 30, 2017	83,662	11.3 years	1,683	1,020	445

Intangible Assets

The following table summarizes the carrying value of intangible assets, liabilities and the accumulated amortization for each intangible asset and liability class as of June 30, 2018 and December 31, 2017, excluding real estate held for sale, as of June 30, 2018 and December 31, 2017 (dollars in thousands):

	June 30, 2018		December 31, 2017	
	Lease Intangibles	Accumulated Amortization	Lease Intangibles	Accumulated Amortization
In-place leases	$80,638	$ (36,834)	$80,355	$ (33,201)
Leasing costs	56,147	(25,458)	55,695	(23,016)
Customer relationships	59,276	(21,791)	58,892	(19,798)
	$196,061	$ (84,083)	$194,942	$ (76,015)
	Deferred Rent	Accumulated (Amortization)/Accretion	Deferred Rent	Accumulated (Amortization)/Accretion

	Receivable/(Liability)		Receivable/(Liability)	
Above market leases	$ 14,511	$ (8,439)	$ 14,425	$ (7,962)
Below market leases and deferred revenue	(26,752)	11,474	(26,725)	10,475
	$ (12,241)	$ 3,035	$ (12,300)	$ 2,513

14

Total amortization expense related to in-place leases, leasing costs and customer relationship lease intangible assets was $4.3 million and $8.6 million for the three and six months ended June 30, 2018, respectively, and $3.5 million and $7.0 million for the three and six months ended June 30, 2017, respectively, and is included in depreciation and amortization expense in the condensed consolidated statements of operations and comprehensive income.

Total amortization related to above-market lease values was $0.2 million and $0.5 million for the three and six months ended June 30, 2018, respectively, and $0.1 million and $0.3 million for the three and six months ended June 30, 2017, respectively, and is included in rental revenue in the condensed consolidated statements of operations and comprehensive income. Total amortization related to below-market lease values was $0.5 million and $1.0 million for the three and six months ended June 30, 2018, respectively, and $0.3 million and $0.7 million for the three and six months ended June 30, 2017, respectively, and is included in rental revenue in the condensed consolidated statements of operations and comprehensive income.

The weighted average amortization periods in years for the intangible assets acquired during the six months ended June 30, 2018 and 2017 were as follows:

Intangible Assets & Liabilities	2018	2017
In-place leases	9.8	8.5
Leasing costs	9.8	8.5
Customer relationships	14.8	13.5
Above market leases	9.8	0.0
Below market leases	0.0	8.5
All intangible assets & liabilities	11.1	9.8

5. Real Estate Dispositions, Held for Sale and Impairment Charges

Real Estate Dispositions

During the six months ended June 30, 2018, we continued to execute our capital recycling program, whereby we sold non-core properties and redeployed proceeds to fund property acquisitions in our target secondary growth markets, as well as repay outstanding debt. During the six months ended June 30, 2018, we sold two non-core properties, located in Arlington, Texas and Tewksbury, Massachusetts, which are summarized in the table below (dollars in thousands):

Aggregate Square Footage Sold	Aggregate Sales Price	Aggregate Sales Costs	Aggregate Gain on Sale of Real Estate, net
166,200	$ 11,100	$ 327	$ 1,844

Our dispositions during the six months ended June 30, 2018 were not classified as discontinued operations because they did not represent a strategic shift in operations, nor will they have a major effect on our operations and financial results. Accordingly, the operating results of these properties are included within continuing operations for all periods reported.

The table below summarizes the components of operating income from the real estate and related assets disposed of during the three and six months ended June 30, 2018, and 2017 (dollars in thousands):

	For the three months ended June 30,		For the six months ended June 30,	
	2018	2017	2018	2017
Operating revenue	$—	$245	$93	$525
Operating expense	12	174	161	316
Other income, net	—	—	1,844 (1)	—
(Expense) income from real estate and related assets sold	$(12)	$71	$1,776	$209

(1) Includes a $1.8 million gain on sale of real estate, net on two properties.

15

Table of Contents

Real Estate Held for Sale

At June 30, 2018, we had one property classified as held for sale, located in South Hadley, Massachusetts. We have identified a prospective buyer for this property, and we are currently negotiating a purchase and sale agreement. At December 31, 2017, we had two properties classified as held for sale, located in Arlington, Texas and Tewksbury, Massachusetts. Both of these properties were sold during the six months ended June 30, 2018.

The table below summarizes the components of the assets and liabilities held for sale reflected on the accompanying condensed consolidated balance sheets (dollars in thousands):

	June 30, 2018	December 31, 2017
Assets Held for Sale		
Real estate, at cost	$2,287	$ 12,997
Less: accumulated depreciation	857	3,970
Total real estate held for sale, net	1,430	9,027
Lease intangibles, net	6	9
Deferred rent receivable, net	—	10
Total Assets Held for Sale	$1,436	$ 9,046
Liabilities Held for Sale		
Asset retirement obligation	$297	$ 114
Total Liabilities Held for Sale	$297	$ 114

Impairment Charges

We evaluated our portfolio for triggering events to determine if any of our held and used assets were impaired during the six months ended June 30, 2018 and did not identify any held and used assets which were impaired.

We classified one property as held for sale at June 30, 2018. We performed an analysis of the property classified as held for sale, and compared the fair market value of the asset less selling costs against the carrying value of assets available for sale. We did not record an impairment charge during the three and six months ended June 30, 2018, as the fair market value was greater than the carrying value.

Fair market value for this asset was calculated using Level 3 inputs (defined in Note 6 “Mortgage Notes Payable and Credit Facility”), which were determined using comparable asset sale data from the respective asset location as well as negotiations with a prospective buyer. We continue to evaluate our properties on a quarterly basis for changes that could create the need to record impairment. Future impairment losses may result, and could be significant, should market conditions deteriorate in the markets in which we hold our assets or we are unable to secure leases at terms that are favorable to us, which could impact the estimated cash flow of our properties over the period in which we plan to hold our properties. Additionally, changes in management’s decisions to either own and lease long-term or sell a particular asset will have an impact on this analysis.

We recognized $4.0 million of impairment charges on two properties during the six months ended June 30, 2017. These properties were impaired through our held for sale carrying value analysis, during the three and six months ended June 30, 2017, and we concluded that the fair market value less selling costs was below the carrying value of the respective properties. We sold both of these properties during the year ended December 31, 2017.

16

Table of Contents

6. Mortgage Notes Payable and Credit Facility

Our mortgage notes payable and Credit Facility as of June 30, 2018 and December 31, 2017 are summarized below (dollars in thousands):

	Encumbered properties at		Carrying Value at		Stated Interest Rates at	Scheduled Maturity Dates at
	June 30, 2018		June 30, 2018	December 31, 2017	June 30, 2018	June 30, 2018
Mortgage and other secured loans:						
Fixed rate mortgage loans	48		$378,287	$383,189	(1)	(2)
Variable rate mortgage loans	18		61,590	69,302	(3)	(2)
Premiums and discounts, net	-		(334)	(281)	N/A	N/A
Deferred financing costs, mortgage loans, net	-		(4,470)	(4,830)	N/A	N/A
Total mortgage notes payable, net	66		$435,073	$447,380	(4)	
Variable rate revolving credit facility	32	(6)	$33,400	$21,400	LIBOR + 1.75%	10/27/2021
Deferred financing costs, revolving credit facility	-		(592)	(685)	N/A	N/A
Total revolver, net	32		$32,808	$20,715		
Variable rate term loan facility	-	(6)	$75,000	$75,000	LIBOR + 1.70%	10/27/2022
Deferred financing costs, term loan facility	-		(420)	(468)	N/A	N/A
Total term loan, net	N/A		$74,580	$74,532		
Total mortgage notes payable and credit facility	98		$542,461	$542,627	(5)	

(1) Interest rates on our fixed rate mortgage notes payable vary from 3.55% to 6.63%.
(2) We have 45 mortgage notes payable with maturity dates ranging from 9/30/2018 through 7/1/2045.
(3) Interest rates on our variable rate mortgage notes payable vary from one month LIBOR + 2.25% to one month LIBOR + 2.75%. At June 30, 2018, one month LIBOR was approximately 2.09%.
(4) The weighted average interest rate on the mortgage notes outstanding at June 30, 2018 was approximately 4.63%.
(5) The weighted average interest rate on all debt outstanding at June 30, 2018 was approximately 4.46%.
(6) The amount we may draw under our senior unsecured revolving credit facility and term loan facility is based on a percentage of the fair value of a combined pool of 32 unencumbered properties as of June 30, 2018.
N/A - Not Applicable

Mortgage Notes Payable

As of June 30, 2018, we had 45 mortgage notes payable, collateralized by a total of 66 properties with a net book value of $639.4 million. We have limited recourse liabilities that could result from any one or more of the following circumstances: a borrower voluntarily filing for bankruptcy, improper conveyance of a property, fraud or material misrepresentation, misapplication or misappropriation of rents, security deposits, insurance proceeds or condemnation proceeds, or physical waste or damage to the property resulting from a borrower's gross negligence or willful misconduct. We have full recourse for $10.2 million of the mortgages notes payable, net or 2.3% of the outstanding balance. We will also indemnify lenders against claims resulting from the presence of hazardous substances or activity involving hazardous substances in violation of environmental laws on a property.

Table of Contents

During the six months ended June 30, 2018, we repaid one mortgage collateralized by one property and partially repaid one mortgage collateralized by two properties, releasing one of the collateralized properties, which are summarized below (dollars in thousands):

Variable Rate Debt Repaid	Interest Rate on Variable Rate Debt Repaid	Fixed Rate Debt Repaid	Interest Rate on Fixed Rate Debt Repaid
$6,738	LIBOR + 2.25%	$9,444	5.75 %

During the six months ended June 30, 2018, we issued one mortgage, collateralized by one property, which is summarized in the table below (dollars in thousands):

Debt Issued	Interest Rate on Debt
$9,380(1)	4.58% (2)

(1) We issued $9.4 million of swapped to fixed rate debt in connection with one property with a maturity date of March 1, 2023.
(2) We entered into an interest rate swap and will be paying an all in fixed rate of 4.58%.

On April 18, 2018, we extended the maturity dates on two existing variable rate mortgage notes totaling $13.0 million from July 2018 to July 2020.

We made payments of $0.03 million and $0.2 million for deferred financing costs during the three and six months ended June 30, 2018, respectively, and $0.4 million for deferred financing costs during both the three and six months ended June 30, 2017.

Scheduled principal payments of mortgage notes payable for the six months ending 2018, and each of the five succeeding fiscal years and thereafter are as follows (dollars in thousands):

Year	Scheduled Principal Payments
Six Months Ending December 31, 2018	$20,695
2019	48,038
2020	31,772
2021	33,506
2022	97,333
2023	69,225
Thereafter	139,308
Total	$439,877 (1)

(1) This figure does not include $0.3 million of premiums and discounts, net, and $4.5 million of deferred financing costs, which are reflected in mortgage notes payable, net on the condensed consolidated balance sheets.

We believe we will be able to address all mortgage notes payable maturing over the next 12 months through a combination of refinancing our existing indebtedness, cash from operations, proceeds from one or more equity offerings and availability on our Credit Facility.

Interest Rate Cap and Interest Rate Swap Agreements

We have entered into interest rate cap agreements that cap the interest rate on certain of our variable-rate debt and we have assumed or entered into interest rate swap agreements in which we hedged our exposure to variable interest rates by agreeing to pay fixed interest rates to our respective counterparty. We have adopted the fair value measurement provisions for our financial instruments recorded at fair value. The fair value guidance establishes a three-tier value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions. Generally, we will estimate the fair value of our interest rate caps and interest rate swaps, in the absence of observable market data, using estimates of value including estimated remaining life, counterparty credit risk, current market yield and interest rate spreads of similar securities as of the measurement date. At June 30, 2018 and December 31, 2017, our interest rate cap agreements and interest rate swap were valued using Level 2 inputs.

The fair value of the interest rate cap agreements is recorded in Other assets on our accompanying condensed consolidated balance sheets. We record changes in the fair value of the interest rate cap agreements quarterly based on the current market valuations at quarter end. If the interest rate cap qualifies for hedge accounting, the change in the estimated fair value is recorded to accumulated other comprehensive income to the extent that it is effective, with any ineffective portion recorded to interest expense in our condensed consolidated statements of operations and comprehensive income. If the interest rate cap does not qualify for hedge accounting, or if it is determined the hedge is ineffective, any change in the fair value is recognized in interest expense in our consolidated statements of operations and comprehensive income. The following table summarizes the interest rate caps at June 30, 2018 and December 31, 2017 (dollars in thousands):

	June 30, 2018		December 31, 2017	
Aggregate Cost	Aggregate Notional Amount	Aggregate Fair Value	Aggregate Notional Amount	Aggregate Fair Value
$1,111(1)	$135,671	$ 1,115	$143,512	$ 504

(1) We have entered into various interest rate cap agreements on variable rate debt with LIBOR caps ranging from 2.25% to 3.25%.

We assumed an interest rate swap agreement in connection with our June 22, 2017 acquisition, whereby we will pay our counterparty an interest rate equivalent to 1.80% on a monthly basis, and receive payments from our counterparty equivalent to one month LIBOR. The fair value of our interest rate swap agreement is recorded in Other assets on our accompanying condensed consolidated balance sheets. We have designated our interest rate swap as a cash flow hedge, and we record changes in the fair value of the interest rate swap agreement to accumulated other comprehensive income on the condensed consolidated balance sheets. We record changes in fair value on a quarterly basis, using current market valuations at quarter end. We assumed our interest rate swap with a value of $0.04 million on the date of assumption, and the fair market value increased to $0.7 million at June 30, 2018. The swap had an original notional value equal to the debt we assumed of $11.2 million, and has a termination date of April 1, 2026, which is also the maturity date of the assumed debt.

We entered into an interest rate swap agreement in connection with a mortgage obtained on a Columbus, Ohio property, whereby we will pay our counterparty an interest rate equivalent to 2.83% on a monthly basis, and receive payments from our counterparty equivalent to one month LIBOR. The fair value of our interest rate swap agreement is recorded in Other assets on our accompanying condensed consolidated balance sheets. We have designated our interest rate swap as a cash flow hedge, and we record changes in the fair value of the interest rate swap agreement to accumulated other comprehensive income on the condensed consolidated balance sheets. We record changes in fair value on a quarterly basis, using current market valuations at quarter end. The fair market value at June 30, 2018 was a $0.1 million liability. The swap has a notional value equal to the debt we issued of $9.4 million, and has a termination date of March 1, 2023, which is also the maturity date of the issued debt.

Table of Contents

The following tables present the impact of our derivative instruments in the condensed consolidated financial statements (dollars in thousands):

	Amount of Gain recognized in Comprehensive Income			
	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Derivatives in cash flow hedging relationships				
Interest rate caps	$97	$—	$470	$—
Interest rate swap	192	179	313	179
Total	$289	$179	$783	$179

The following table sets forth certain information regarding our derivative instruments (dollars in thousands):

		Asset Derivatives Fair Value at	
Derivatives Designated as Hedging Instruments	Balance Sheet Location	June 30, 2018	December 31, 2017
Interest rate caps	Other assets	$920	$ 450
Derivatives Not Designated as Hedging Instruments			
Interest rate caps	Other assets	$195	$ 54
Total derivatives		$1,115	$ 504

The fair value of all mortgage notes payable outstanding as of June 30, 2018 was $435.1 million, as compared to the carrying value stated above of $439.9 million. The fair value is calculated based on a discounted cash flow analysis, using management’s estimate of market interest rates on long-term debt with comparable terms and loan to value ratios. The fair value was calculated using Level 3 inputs of the hierarchy established by ASC 820, “Fair Value Measurements and Disclosures.”

Credit Facility

On August 7, 2013, we procured our senior unsecured revolving credit facility (“Revolver”) with KeyBank National Association (“KeyBank”) (serving as revolving lender, a letter of credit issuer and an administrative agent). In October 2015, we expanded our Revolver to $85.0 million and entered into a term loan facility (“Term Loan”) whereby we added a $25.0 million, five-year Term Loan subject to the same leverage tiers as the Revolver, with the interest rate at each leverage tier being five basis points lower than that of the Revolver. We have the option to repay the Term Loan in full, or in part, at any time without penalty or premium prior to the maturity date. We refer to the Revolver and Term Loan collectively herein as the Credit Facility. On October 27, 2017, we amended our Credit Facility, increasing the Term Loan from $25.0 million, to $75.0 million, with the Revolver commitment remaining at $85.0 million. The Term Loan has a new five-year term, with a maturity date of October 27, 2022, and the Revolver has a new four-year term, with a maturity date of October 27, 2021. The interest rate for the Credit Facility was reduced by 25 basis points at each of the leverage tiers. We entered into interest rate cap agreements on the amended Term Loan, which cap LIBOR at 2.75%. We used the net proceeds of the amended Credit Facility to repay all previously existing borrowings under the Revolver. We incurred fees of approximately $0.9 million in connection with the Credit Facility amendment. The bank syndicate is now comprised of KeyBank, Fifth Third Bank, US Bank National Association and The Huntington National Bank.

As of June 30, 2018, there was $108.4 million outstanding under our Credit Facility at a weighted average interest rate of approximately 3.81% and $1.0 million outstanding under letters of credit at a weighted average interest rate of 1.75%. As of June 30, 2018, the maximum additional amount we could draw under the Revolver was $46.1 million. We were in compliance with all covenants under the Credit Facility as of June 30, 2018.

The amount outstanding under the Credit Facility approximates fair value as of June 30, 2018.

Table of Contents

7. Commitments and Contingencies

Ground Leases

We are obligated as lessee under four ground leases. Future minimum rental payments due under the terms of these leases as of June 30, 2018 are as follows (dollars in thousands):

Year	Minimum Rental Payments Due
Six Months Ending December 31, 2018	$ 233
2019	465
2020	466
2021	392
2022	319
2023	322
Thereafter	3,914
Total	$ 6,111

Rental expense incurred for properties with ground lease obligations during the three and six months ended June 30, 2018 was $0.1 million and $0.2 million, respectively, and during the three and six months ended June 30, 2017 was $0.1 million and $0.2 million, respectively. Rental expenses are reflected in property operating expenses on the condensed consolidated statements of operations and comprehensive income.

Letters of Credit

As of June 30, 2018, there was $1.0 million outstanding under letters of credit. These letters of credit are not reflected on our condensed consolidated balance sheets.

21

Table of Contents

8. Stockholders’ and Mezzanine Equity

Stockholders’ Equity

The following table summarizes the changes in our stockholders’ equity for the six months ended June 30, 2018 (dollars in thousands):

	Series A and B Preferred Stock	Common Stock	Senior Common Stock	Series A and B Preferred Stock	Senior Common Stock	Common Stock	Additional Paid in Capital	Accumulated Other Comprehensive Income	Distributions in Excess of Accumulated Earnings	Total Stockholders' Equity
Balance at December 31, 2017	2,264,000	28,384,016	904,819	$ 2	$ 1	$ 28	$ 534,790	$ 35	$ (268,058)	$ 266,798
Issuance of Series A and B preferred stock and common stock, net	—	185,084	—	—	—	1	3,520	—	—	3,521
Conversion of senior common stock to common stock	—	9,554	(11,435)	—	—	—	—	—	—	—
Retirement of senior common stock, net	—	—	(2,266)	—	—	—	(34)	—	—	(34)
Distributions declared to common, senior common and preferred stockholders	—	—	—	—	—	—	—	—	(26,982)	(26,982)
Comprehensive income	—	—	—	—	—	—	—	783	—	783
Net income	—	—	—	—	—	—	—	—	7,130	7,130
Balance at June 30, 2018	2,264,000	28,578,654	891,118	$ 2	$ 1	$ 29	$ 538,276	$ 818	$ (287,910)	$ 251,216

Distributions

We paid the following distributions per share for the three and six months ended June 30, 2018 and 2017:

	For the three months ended June 30,		For the six months ended June 30,	
	2018	2017	2018	2017
Common Stock	$ 0.375	$ 0.375	$ 0.750	$ 0.750
Senior Common Stock	0.2625	0.2625	0.5250	0.5250
Series A Preferred Stock	0.4843749	0.4843749	0.9687498	0.9687498

Series B Preferred Stock	0.46875	0.46875	0.9375	0.9375
Series D Preferred Stock	0.4374999	0.4374999	0.8749998	0.8749998

Recent Activity

Common Stock ATM Program

During the six months ended June 30, 2018, we sold 0.2 million shares of common stock, raising $3.5 million in net proceeds under our open market sales agreement with Cantor Fitzgerald (the “Common Stock ATM Program”). As of June 30, 2018, we had remaining capacity to sell up to $82.7 million of common stock under the Common Stock ATM Program.

Table of Contents

Series A and B Preferred Stock ATM Programs

Under another open market sales agreement with Cantor Fitzgerald (the "Series A and B Preferred ATM Program"), we may, from time to time, offer to sell (i) shares of our 7.75% Series A Cumulative Redeemable Preferred Stock ("Series A Preferred"), and (ii) shares of our 7.50% Series B Cumulative Redeemable Preferred Stock ("Series B Preferred"), having an aggregate offering price of up to $40.0 million, through Cantor Fitzgerald, acting as sales agent and/or principal. We did not sell any shares of our Series A Preferred or Series B Preferred during the six months ended June 30, 2018. As of June 30, 2018, we had remaining capacity to sell up to $37.2 million of preferred stock under the Series A and B Preferred ATM Program.

Mezzanine Equity

Our 7.00% Series D Cumulative Redeemable Preferred Stock ("Series D Preferred"), is classified as mezzanine equity in our condensed consolidated balance sheets because it is redeemable at the option of the shareholder upon a change of control of greater than 50% in accordance with ASC 480-10-S99 "Distinguishing Liabilities from Equity," which requires mezzanine equity classification for preferred stock issuances with redemption features which are outside of the control of the issuer. A change in control of our company, outside of our control, is only possible if a tender offer is accepted by over 90% of our shareholders. All other change in control situations would require input from our Board of Directors. We will periodically evaluate the likelihood that a change of control greater than 50% will take place, and if we deem this probable, we would adjust the Series D Preferred presented in mezzanine equity to their redemption value, with the offset to gain (loss) on extinguishment. We currently believe the likelihood of a change of control greater than 50% is remote.

Under a third open market sales agreement with Cantor Fitzgerald (the "Series D Preferred ATM Program"), we may, from time to time, offer to sell shares of our Series D Preferred, having an aggregate offering price of up to $50.0 million, through Cantor Fitzgerald, acting as sales agent and/or principal. During the six months ended June 30, 2018, we sold approximately 0.1 million shares of our Series D Preferred for net proceeds of $2.2 million. As of June 30, 2018, we had remaining capacity to sell up to $18.6 million of Series D Preferred under the Series D Preferred ATM Program.

Amendment to Articles of Incorporation

On April 11, 2018, we filed with the Maryland State Department of Assessments and Taxation an Articles Supplementary reclassifying 3,500,000 authorized but unissued shares of our convertible senior common stock (the "Senior Common Stock"), as authorized but unissued shares of our common stock. As a result of the reclassification, there were 57,969 authorized but unissued shares of Senior Common Stock.

On April 11, 2018, we also filed with the Maryland State Department of Assessments and Taxation an Articles of Amendment to increase the number of shares of capital stock we have authority to issue to 100,000,000 and authorized common stock to 87,700,000 shares.

9. Subsequent Events

Distributions

On July 10, 2018, our Board of Directors declared the following monthly distributions for the months of July, August and September of 2018:

Record Date	Payment Date	Common Stock Distributions per Share	Series A Preferred Distributions per Share	Series B Preferred Distributions per Share	Series D Preferred Distributions per Share
July 20, 2018	July 31, 2018	$ 0.125	$ 0.1614583	$ 0.15625	$ 0.1458333
August 21, 2018	August 31, 2018	0.125	0.1614583	0.15625	0.1458333
September 19, 2018	September 28, 2018	0.125	0.1614583	0.15625	0.1458333
		$ 0.375	$ 0.4843749	$ 0.46875	$ 0.4374999

Table of Contents

Senior Common Stock Distributions

Payable to the Holders of Record During the Month of:	Payment Date	Distribution per Share
July	August 7, 2018	$ 0.0875
August	September 10, 2018	0.0875
September	October 5, 2018	0.0875
		$ 0.2625

ATM Equity Activity

Subsequent to June 30, 2018 and through July 30, 2018, we raised $1.6 million in net proceeds from the sale of 83,430 shares of Common Stock under our Common Stock ATM Program. We made no sales under our Series D Preferred ATM Program or Series A and B Preferred Stock ATM Program subsequent to June 30, 2018 and through July 30, 2018.

Second Amended and Restated Agreement of Limited Partnership

On July 11, 2018, the Company, GCLP Business Trust I, and GCLP Business Trust II entered into the Second Amended and Restated Agreement of Limited Partnership of the Operating Partnership. The Second Amended and Restated Partnership Agreement consolidates the previous amendments to the First Amended and Restated Agreement of Limited Partnership of the Operating Partnership and reflects certain updates to applicable law.

Financing Activity

On July 23, 2018, we extended the maturity date on one variable rate mortgage note totaling $4.0 million from September 2018 to September 2019.

Table of Contents

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

All statements contained herein, other than historical facts, may constitute "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). These statements may relate to, among other things, future events or our future performance or financial condition. In some cases, you can identify forward-looking statements by terminology such as "may," "might," "believe," "will," "provided," "anticipate," "future," "could," "growth," "plan," "intend," "expect," "should "possible," "potential," "likely" or the negative of such terms or comparable terminology. These forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our business, financial condition, liquidity, results of operations, funds from operations or prospects to be materially different from any future business, financial condition, liquidity, results of operations, funds from operations or prospects expressed or implied by such forward-looking statements. For further information about these and other factors that could affect our future results, please see the captions titled "Forward-Looking Statements" and "Risk Factors" in this report and in our Annual Report on Form 10-K for the year ended December 31, 2017. We caution readers not to place undue reliance on any such forward-looking statements, which are made pursuant to the Private Securities Litigation Reform Act of 1995 and, as such, speak only as of the date made. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, after the date of this Quarterly Report on Form 10-Q.

All references to "we," "our," "us" and the "Company" in this Report mean Gladstone Commercial Corporation and its consolidated subsidiaries, except where otherwise noted or where the context indicates that the term means only Gladstone Commercial Corporation.

General

We are an externally-advised real estate investment trust ("REIT") that was incorporated under the General Corporation Law of the State of Maryland on February 14, 2003. We focus on acquiring, owning, and managing primarily office and industrial properties. On a selective basis, we may make long term industrial and commercial mortgage loans; however, we do not have any mortgage loans currently outstanding. Our properties are geographically diversified and our tenants cover a broad cross section of business sectors and range in size from small to very large private and public companies. We actively communicate with buyout funds, real estate brokers and other third parties to locate properties for potential acquisition or to provide mortgage financing in an effort to build our portfolio. We target secondary growth markets that possess favorable economic growth trends, diversified industries, and growing population and employment.

We have historically entered into, and intend in the future to enter into, purchase agreements primarily for real estate having net leases with remaining terms of approximately 7 to 15 years and built in rental rate increases. Under a net lease, the tenant is required to pay most or all operating, maintenance, repair and insurance costs and real estate taxes with respect to the leased property.

All references to annualized generally accepted accounting principles ("GAAP") rent are rents that each tenant pays in accordance with the terms of its respective lease reported evenly over the non-cancelable term of the lease.

As of July 30, 2018:

- we owned 98 properties totaling 11.4 million square feet in 24 states;
- our occupancy rate was 99.1%;
- the weighted average remaining term of our mortgage debt was 6.2 years and the weighted average interest rate was 4.62%; and

• the average remaining lease term of the portfolio was 7.1 years.

25

Business Environment

In the United States, vacancy rates have decreased for both office and industrial properties in most markets, as increased user demand has led to improved conditions. Vacancy rates in many markets have been reduced to levels seen at the peak before the most recent U.S. recession and rental rates have increased in most primary and secondary markets. This condition has led to a rise in construction activity for both office and industrial properties in many markets. Reports from many national research firms reflect that the industrial supply and demand relationship still appears to be in equilibrium, but that office supply and demand in select markets may be moving toward a slight increase in vacancy. Interest rates have been volatile and although interest rates are still relatively low, lenders have varied on their required spreads over the last several quarters and overall financing costs for fixed rate mortgages appear to be on the rise. The 2017 year-end statistics from national research firms indicate that total investment sales volume was approximately 8-10% less than the volume recorded in 2016. The recorded Q1 2018 investment volume was lower than Q1 2017, and we believe that the Q2 2018 investment volume for net lease properties may be lower than Q2 2017 volume as well, based on our market observations; however, industry publications containing this data have not yet been released. These statistics, once confirmed by industry reports, reflect that investment sales volumes have dropped for the past two years compared to the preceding year.

From a more macro-economic perspective, the strength of the global economy and U.S. economy continue to be uncertain with increased volatility due to the 2016 vote in the United Kingdom to exit the European Union, and an apparent continuing global economic slowdown. The long-term impact of the recent passage of tax reform in the United States is unknown at this time, although the lowering of the corporate tax rate is generally expected be beneficial. Finally, the continuing uncertainty surrounding the ability of the federal government to address its fiscal condition in both the near and long term as well as other geo-political issues has increased domestic and global instability. These developments could cause interest rates and borrowing costs to rise, which may adversely affect our ability to access both the equity and debt markets and could have an adverse effect on our tenants as well.

We continue to focus on re-leasing vacant space, renewing upcoming lease expirations, re-financing upcoming loan maturities, and acquiring additional properties with associated long-term leases. Currently, we only have two partially vacant buildings.

We have zero leases expiring during the remainder of 2018, six leases expiring in 2019, which account for 3.9% of rental revenue we recognized during the six months ended June 30, 2018, and 12 leases expiring in 2020, which account for 11.2% of rental revenue recognized during the six months ended June 30, 2018.

Our available vacant space at June 30, 2018 represents 0.9% of our total square footage and the annual carrying costs on the vacant space, including real estate taxes and property operating expenses, are approximately $0.2 million. We continue to actively seek new tenants for these properties.

Our ability to make new investments is highly dependent upon our ability to procure financing. Our principal sources of financing generally include the issuance of equity securities, long-term mortgage loans secured by properties, borrowings under our $85.0 million senior unsecured revolving credit facility (“Revolver”), with KeyBank National Association (serving as a revolving lender, a letter of credit issuer and an administrative agent), which matures in October 2021, and our $75.0 million term loan facility (“Term Loan”), which matures in October 2022, which we refer to collectively herein as the Credit Facility. While lenders’ credit standards have tightened, we continue to look to national and regional banks, insurance companies and non-bank lenders, in addition to the collateralized mortgage backed securities market, (the “CMBS market”), to issue mortgages to finance our real estate activities.

In addition to obtaining funds through borrowing, we have been active in the equity markets during and subsequent to the six months ended June 30, 2018. We have issued shares of both common stock and Series D Preferred Stock through our at-the-market programs, or ATM Programs, pursuant to our open market sale agreements with Cantor Fitzgerald, discussed in more detail below.

Table of Contents

Recent Developments

2018 Sale Activity

During the six months ended June 30, 2018, we continued to execute our capital recycling program, whereby we sold non-core properties and redeployed proceeds to fund property acquisitions located in our target secondary growth markets, as well as repay outstanding debt. We will continue to execute our capital recycling plan and sell non-core properties as reasonable disposition opportunities are available. During the six months ended June 30, 2018, we sold two non-core properties located in Arlington, Texas and Tewksbury, Massachusetts, which are summarized in the table below (dollars in thousands):

Aggregate Square Footage Sold	Aggregate Sales Price	Aggregate Sales Costs	Aggregate Gain on Sale of Real Estate, net
166,200	$ 11,100	$ 327	$ 1,844

2018 Acquisition Activity

During the six months ended June 30, 2018, we acquired one property, located in Vance, Alabama, which is summarized in the table below (dollars in thousands):

Aggregate Square Footage	Weighted Average Lease Term	Aggregate Purchase Price	Acquisition Costs		Aggregate Annualized GAAP Rent
127,444	9.8 years	$ 14,341	$ 91	(1)	$ 1,087

(1) We accounted for this transaction under ASU 2017-01. As a result, we treated this acquisition as an asset acquisition rather than a business combination. As a result of this treatment, we capitalized $0.1 million of acquisition costs that would otherwise have been expensed under business combination treatment.

2018 Leasing Activity

During the six months ended June 30, 2018, we executed one new lease, which is summarized below (dollars in thousands):

Six Months Ended	Aggregate Square Footage	Weighted Average Lease Term	Aggregate Annualized GAAP Rent	Aggregate Leasing Commissions
June 30, 2018	34,441	3.6 years	$ 97	$ 14

2018 Financing Activity

During the six months ended June 30, 2018, we repaid one mortgage collateralized by one property and partially repaid one mortgage collateralized by two properties, releasing one of the collateralized properties, which are summarized below (dollars in thousands):

Variable Rate Debt Repaid	Interest Rate on Variable Rate Debt Repaid	Fixed Rate Debt Repaid	Interest Rate on Fixed Rate Debt Repaid
$6,738	LIBOR + 2.25%	$9,444	5.75 %

27

During six months ended June 30, 2018, we issued one mortgage, collateralized by one property, which is summarized below (dollars in thousands):

Debt Issued	Interest Rate on Debt
$9,380 (1)	4.58 % (2)

(1) We issued $9.4 million of swapped to fixed rate debt in connection with one property with a maturity date of March 1, 2023.
(2) We entered into an interest rate swap and will be paying an all in fixed rate of 4.58%.

On April 18, 2018, we extended the maturity dates on two variable rate mortgage notes totaling $13.0 million from July 2018 to July 2020.

On July 23, 2018, we extended the maturity date on one variable rate mortgage note totaling $4.0 million from September 2018 to September 2019.

2018 Equity Activities

Common Stock ATM Program

During the six months ended June 30, 2018, we sold 0.2 million shares of common stock, raising $3.5 million in net proceeds under our open market sales agreement with Cantor Fitzgerald (the “Common Stock ATM Program”). As of June 30, 2018, we had remaining capacity to sell up to $82.7 million of common stock under the Common Stock ATM Program.

Preferred ATM Programs

Series A and B Preferred Stock: Under another open market sales agreement (the “Series A and B Preferred ATM Program”), with Cantor Fitzgerald, we may, from time to time, offer to sell (i) shares of our 7.75% Series A Cumulative Redeemable Preferred Stock (“Series A Preferred”), and (ii) shares of our 7.50% Series B Cumulative Redeemable Preferred Stock (“Series B Preferred”), having an aggregate offering price of up to $40.0 million, through Cantor Fitzgerald, acting as sales agent and/or principal. We did not sell any shares of our Series A Preferred or Series B Preferred during six months ended June 30, 2018. As of June 30, 2018, we had remaining capacity to sell up to $37.2 million of preferred stock under the Series A and B Preferred ATM Program.

Series D Preferred Stock: Under a third open market sales agreement (the “Series D Preferred ATM Program”), with Cantor Fitzgerald, we may, from time to time, offer to sell shares of our 7.00% Series D Cumulative Redeemable Preferred (“Series D Preferred”), having an aggregate offering price of up to $50.0 million, through Cantor Fitzgerald, acting as sales agent and/or principal. During the six months ended June 30, 2018, we sold approximately 0.1 million shares of our Series D Preferred for net proceeds of $2.2 million. As of June 30, 2018, we had remaining capacity to sell up to $18.6 million of Series D Preferred under the Series D Preferred ATM Program.

Amendment to Articles of Incorporation

On April 11, 2018, we filed with the Maryland State Department of Assessments and Taxation an Articles Supplementary reclassifying 3,500,000 authorized but unissued shares of our convertible senior common stock (the

“Senior Common Stock”), as authorized but unissued shares of our common stock. As a result of the reclassification, there were 57,969 authorized but unissued shares of Senior Common Stock.

On April 11, 2018, we also filed with the Maryland State Department of Assessments and Taxation an Articles of Amendment to increase the number of shares of capital stock we have authority to issue to 100,000,000 and authorized common stock to 87,700,000 shares.

Table of Contents

Second Amended and Restated Agreement of Limited Partnership

On July 11, 2018, the Company, GCLP Business Trust I, and GCLP Business Trust II entered into the Second Amended and Restated Agreement of Limited Partnership of the Operating Partnership. The Second Amended and Restated Partnership Agreement consolidates the previous amendments to the First Amended and Restated Agreement of Limited Partnership of the Operating Partnership and reflects certain updates to applicable law.

Diversity of Our Portfolio

Gladstone Management Corporation, a Delaware corporation (our "Adviser") seeks to diversify our portfolio to avoid dependence on any one particular tenant, industry or geographic market. By diversifying our portfolio, our Adviser intends to reduce the adverse effect on our portfolio of a single under-performing investment or a downturn in any particular industry or geographic market. For the six months ended June 30, 2018, our largest tenant comprised only 4.7% of total rental income. The table below reflects the breakdown of our total rental income by tenant industry classification for the three and six months ended June 30, 2018 and 2017 (dollars in thousands):

	For the three months ended June 30,				For the six months ended June 30,			
	2018		2017		2018		2017	
Industry Classification	Rental Revenue	Percentage of Rental Revenue	Rental Revenue	Percentage of Rental Revenue	Rental Revenue	Percentage of Rental Revenue	Rental Revenue	Percentage of Rental Revenue
Telecommunications	$3,957	15.4 %	$3,866	17.2 %	$7,915	15.4 %	$7,721	17.4 %
Diversified/Conglomerate Services	3,459	13.5	2,014	9.0	6,916	13.5	4,014	9.0
Automobile	3,146	12.2	2,799	12.4	6,078	11.9	5,427	12.2
Healthcare	2,983	11.6	3,793	16.9	5,976	11.7	7,127	16.0
Banking	1,995	7.8	612	2.7	3,992	7.8	1,225	2.8
Information Technology	1,498	5.8	1,498	6.7	2,997	5.8	2,998	6.8
Personal, Food & Miscellaneous Services	1,459	5.7	892	4.0	2,920	5.7	1,785	4.0
Diversified/Conglomerate Manufacturing	1,216	4.7	1,205	5.4	2,434	4.7	2,411	5.4
Electronics	1,060	4.1	1,082	4.8	2,121	4.1	2,165	4.9
Buildings and Real Estate	1,017	4.0	606	2.7	2,033	4.0	1,167	2.6
Chemicals, Plastics & Rubber	726	2.8	723	3.2	1,453	2.8	1,493	3.4
Personal & Non-Durable Consumer Products	672	2.6	664	2.9	1,344	2.6	1,329	3.0
Machinery	560	2.2	560	2.5	1,120	2.2	1,120	2.5
Childcare	556	2.2	556	2.5	1,112	2.2	1,112	2.5
Containers, Packaging & Glass	454	1.8	430	1.9	909	1.8	949	2.1
Beverage, Food & Tobacco	352	1.4	525	2.3	797	1.6	1,051	2.4
Printing & Publishing	286	1.1	357	1.6	573	1.1	751	1.7
Education	164	0.6	164	0.7	328	0.6	328	0.7
Home & Office Furnishings	132	0.5	132	0.6	265	0.5	265	0.6
Total	$25,692	100.0 %	$22,478	100.0 %	$51,283	100.0 %	$44,438	100.0 %

Table of Contents

The tables below reflect the breakdown of total rental income by state for the three and six months ended June 30, 2018 and 2017 (dollars in thousands):

State	Rental Revenue for the three months ended June 30, 2018	Percentage of Rental Revenue	Number of Leases for the three months ended June 30, 2018	Rental Revenue for the three months ended June 30, 2017	Percentage of Rental Revenue	Number of Leases for the three months ended June 30, 2017
Texas	$ 3,702	14.4 %	12	$ 3,782	16.8 %	12
Pennsylvania	3,250	12.6	9	2,275	10.1	8
Florida	2,839	11.1	10	1,117	5.0	3
Ohio	2,393	9.3	15	2,754	12.3	13
Utah	1,664	6.5	3	946	4.2	2
North Carolina	1,516	5.9	8	1,502	6.7	8
Georgia	1,204	4.7	6	1,192	5.3	6
South Carolina	1,153	4.5	2	1,153	5.1	2
Michigan	1,082	4.2	4	1,082	4.8	4
Minnesota	922	3.6	6	928	4.1	6
All Other States	5,967	23.2	32	5,747	25.6	33
Total	$ 25,692	100.0 %	107	$ 22,478	100.0 %	97

State	Rental Revenue for the six months ended June 30, 2018	Percentage of Rental Revenue	Number of Leases for the six months ended June 30, 2018	Rental Revenue for the six months ended June 30, 2017	Percentage of Rental Revenue	Number of Leases for the six months ended June 30, 2017
Texas	$ 7,484	14.6 %	12	$ 7,550	17.0 %	12
Pennsylvania	6,504	12.7	9	4,508	10.1	8
Florida	5,676	11.1	10	2,235	5.0	3
Ohio	4,790	9.3	15	5,053	11.4	13
Utah	3,329	6.5	3	1,893	4.3	2
North Carolina	3,032	5.9	8	3,004	6.8	8
Georgia	2,408	4.7	6	2,384	5.4	6
South Carolina	2,306	4.5	2	2,306	5.2	2
Michigan	2,163	4.2	4	2,163	4.9	4
Minnesota	1,844	3.6	6	1,842	4.1	6
All Other States	11,747	22.9	32	11,500	25.8	33
	$ 51,283	100.0 %	107	$ 44,438	100.0 %	97

Our Adviser and Administrator

Our Adviser is led by a management team with extensive experience purchasing real estate and originating mortgage loans. Our Adviser and Gladstone Administration, LLC, a Delaware limited liability company (our "Administrator") are controlled by Mr. David Gladstone, who is also our chairman and chief executive officer. Mr. Gladstone also serves as the chairman and chief executive officer of both our Adviser and Administrator. Mr. Terry Lee Brubaker, our vice chairman and chief operating officer, is also the vice chairman and chief operating officer of our Adviser and Administrator. Mr. Robert Cutlip, our president, is also an executive managing director of our Adviser. Our Administrator employs our chief financial officer, treasurer, chief compliance officer, general counsel and secretary (who also serves as our Administrator's president, general counsel, and secretary) and their respective staffs.

Table of Contents

Our Adviser and Administrator also provide investment advisory and administrative services, respectively, to certain of our affiliates, including, but not limited to, Gladstone Capital Corporation and Gladstone Investment Corporation, both publicly-traded business development companies, as well as Gladstone Land Corporation, a publicly-traded REIT that primarily invests in farmland. With the exception of Mr. Michael Sodo, our chief financial officer, Mr. Jay Beckhorn, our treasurer, and Mr. Robert Cutlip, our president, all of our executive officers and all of our directors serve as either directors or executive officers, or both, of Gladstone Capital Corporation and Gladstone Investment Corporation. In addition, with the exception of Mr. Cutlip, and Mr. Sodo, all of our executive officers and all of our directors, serve as either directors or executive officers, or both, of Gladstone Land Corporation. Mr. Cutlip and Mr. Sodo do not put forth any material efforts in assisting affiliated companies. In the future, our Adviser may provide investment advisory services to other companies, both public and private.

Advisory and Administration Agreements

We are externally managed pursuant to contractual arrangements with our Adviser and our Administrator, which collectively employ all of our personnel and pay their salaries, benefits and general expenses directly. Both our Adviser and Administrator are affiliates of ours, as their parent company is owned and controlled by Mr. David Gladstone, our chairman and chief executive officer. Two of our executive officers, Mr. Gladstone and Mr. Terry Brubaker (our vice chairman and chief operating officer) serve as directors and executive officers of our Adviser and our Administrator. Mr. Michael LiCalsi, our general counsel and secretary, serves as our Administrator's president, general counsel and secretary. We have entered into an advisory agreement with our Adviser, as amended from time to time (the "Advisory Agreement"), and an administration agreement with our Administrator (the "Administration Agreement"). The services and fees under the Advisory Agreement and Administration Agreement are described below.

Under the terms of the Advisory Agreement, we are responsible for all expenses incurred for our direct benefit. Examples of these expenses include legal, accounting, interest, directors' and officers' insurance, stock transfer services, stockholder-related fees, consulting and related fees. In addition, we are also responsible for all fees charged by third parties that are directly related to our business, which include real estate brokerage fees, mortgage placement fees, lease-up fees and transaction structuring fees (although we may be able to pass all or some of such fees on to our tenants and borrowers).

Base Management Fee

On January 10, 2017, we entered into a Fourth Amended and Restated Investment Advisory Agreement with the Adviser, effective as of October 1, 2016. Our original entrance into the Advisory Agreement and each subsequent amendment thereof (including the fourth amendment completed in January of 2017) was approved unanimously by our Board of Directors. Our Board of Directors also reviews and considers renewing the Advisory Agreement each July. During its July 2018 meeting, our Board of Directors reviewed and renewed the Advisory Agreement for an additional year, through August 31, 2019.

Under the Advisory Agreement, the calculation of the annual base management fee equals 1.5% of our adjusted total stockholders' equity, which is our total stockholders' equity plus total mezzanine equity (before giving effect to the base management fee and incentive fee), adjusted to exclude the effect of any unrealized gains or losses that do not affect realized net income (including impairment charges) and adjusted for any one-time events and certain non-cash items (the later to occur for a given quarter only upon the approval of our Compensation Committee). The fee is calculated and accrued quarterly as 0.375% per quarter of such adjusted total stockholders' equity figure. Our Adviser does not charge acquisition or disposition fees when we acquire or dispose of properties as is common in other externally managed REITs; however, our Adviser may earn fee income from our borrowers, tenants or other sources.

Incentive Fee

Pursuant to the Advisory Agreement, the calculation of the incentive fee rewards the Adviser in circumstances where our quarterly Core FFO (defined at the end of this paragraph), before giving effect to any incentive fee, or pre-incentive fee Core FFO, exceeds 2.0% quarterly, or 8.0% annualized, of adjusted total stockholders' equity (after giving effect to the base management fee but before giving effect to the incentive fee). We refer to this as the hurdle rate. The Adviser will receive 15.0% of the amount of our pre-incentive fee Core FFO that exceeds the hurdle rate. However, in no event shall the incentive fee for a particular quarter exceed by 15.0% (the cap) the average quarterly incentive fee paid by us for the previous four quarters (excluding quarters for which no incentive fee was paid). Core FFO (as defined in the Advisory Agreement) is GAAP net income (loss) available to common stockholders, excluding the incentive fee, depreciation and amortization, any realized and unrealized gains, losses or other non-cash items recorded in net income (loss) available to common stockholders for the period, and one-time events pursuant to changes in GAAP.

Table of Contents

Capital Gain Fee

Under the Advisory Agreement, we will pay to the Adviser a capital gains-based incentive fee that will be calculated and payable in arrears as of the end of each fiscal year (or upon termination of the Advisory Agreement). In determining the capital gain fee, we will calculate aggregate realized capital gains and aggregate realized capital losses for the applicable time period. For this purpose, aggregate realized capital gains and losses, if any, equals the realized gain or loss calculated by the difference between the sales price of the property, less any costs to sell the property and the current gross value of the property (which is calculated as the original acquisition price plus any subsequent non-reimbursed capital improvements). At the end of the fiscal year, if this number is positive, then the capital gain fee payable for such time period shall equal 15.0% of such amount. No capital gain fee was recognized during the three and six months ended June 30, 2018 or 2017.

Termination Fee

The Advisory Agreement includes a termination fee whereby, in the event of our termination of the agreement without cause (with 120 days' prior written notice and the vote of at least two-thirds of our independent directors), a termination fee would be payable to the Adviser equal to two times the sum of the average annual base management fee and incentive fee earned by the Adviser during the 24-month period prior to such termination. A termination fee is also payable if the Adviser terminates the agreement after the Company has defaulted and applicable cure periods have expired. The agreement may also be terminated for cause by us (with 30 days' prior written notice and the vote of at least two-thirds of our independent directors), with no termination fee payable. Cause is defined in the agreement to include if the Adviser breaches any material provisions of the agreement, the bankruptcy or insolvency of the Adviser, dissolution of the Adviser and fraud or misappropriation of funds.

Administration Agreement

Under the terms of the Administration Agreement, we pay separately for our allocable portion of our Administrator's overhead expenses in performing its obligations to us including, but not limited to, rent and our allocable portion of the salaries and benefits expenses of our Administrator's employees, including, but not limited to, our chief financial officer, treasurer, chief compliance officer, general counsel and secretary (who also serves as our Administrator's president, general counsel and secretary), and their respective staffs. Our allocable portion of the Administrator's expenses are generally derived by multiplying our Administrator's total expenses by the appropriate percentage of time the Administrator's employees perform services for us in relation to their time spent performing services for all companies serviced by our Administrator under contractual agreements.

Critical Accounting Policies and Estimates

The preparation of our financial statements in accordance with GAAP requires management to make judgments that are subjective in nature to make certain estimates and assumptions. Application of these accounting policies involves the exercise of judgment regarding the use of assumptions as to future uncertainties, and as a result, actual results could materially differ from these estimates. A summary of all of our significant accounting policies is provided in Note 1 to our consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2017, filed by us with the U.S. Securities and Exchange Commission (the "SEC") on February 14, 2018 (our "2017 Form 10-K"). There were no material changes to our critical accounting policies or estimates during the six months ended June 30, 2018.

Results of Operations

The weighted average yield on our total portfolio, which was 8.7% and 8.6% as of June 30, 2018 and 2017, respectively, is calculated by taking the annualized straight-line rents, reflected as rental income on our condensed consolidated statements of operations and other comprehensive income, of each acquisition since inception as a percentage of the acquisition cost plus subsequent capital improvements. The weighted average yield does not account for the interest expense incurred on the mortgages placed on our properties.

Table of Contents

A comparison of our operating results for the three and six months ended June 30, 2018 and 2017 is below (dollars in thousands, except per share amounts):

	For the three months ended June 30,			
	2018	2017	$ Change	% Change
Operating revenues				
Rental revenue	$25,692	$22,478	$3,214	14.3 %
Tenant recovery revenue	901	389	512	131.6 %
Total operating revenues	26,593	22,867	3,726	16.3 %
Operating expenses				
Depreciation and amortization	11,773	9,926	1,847	18.6 %
Property operating expenses	2,816	1,505	1,311	87.1 %
Base management fee	1,260	1,207	53	4.4 %
Incentive fee	733	551	182	33.0 %
Administration fee	360	340	20	5.9 %
General and administrative	600	575	25	4.3 %
Impairment charge	—	253	(253)	(100.0)%
Total operating expenses	17,542	14,357	3,185	22.2 %
Other (expense) income				
Interest expense	(6,531)	(5,944)	(587)	9.9 %
Loss on sale of real estate, net	—	(1,914)	1,914	(100.0)%
Other income	5	9	(4)	(44.4)%
Total other expense, net	(6,526)	(7,849)	1,323	(16.9)%
Net income	2,525	661	1,864	282.0 %
Distributions attributable to Series A, B and D preferred stock	(2,609)	(2,437)	(172)	7.1 %
Distributions attributable to senior common stock	(233)	(249)	16	(6.4)%
Net loss attributable to common stockholders	$(317)	$(2,025)	$1,708	(84.3)%
Net loss attributable to common stockholders per weighted average share of common stock - basic and diluted	$(0.01)	$(0.08)	$0.07	(87.5)%
FFO available to common stockholders - basic (1)	$11,456	$10,068	$1,388	13.8 %
FFO available to common stockholders - diluted (1)	$11,689	$10,317	$1,372	13.3 %
FFO per weighted average share of common stock - basic (1)	$0.40	$0.40	$—	— %
FFO per weighted average share of common stock - diluted (1)	$0.40	$0.40	$—	— %

(1) Refer to the "Funds from Operations" section below within the Management's Discussion and Analysis section for the definition of FFO.

33

Table of Contents

	For the six months ended June 30,			
	2018	2017	$ Change	% Change
Operating revenues				
Rental revenue	$51,283	$44,438	$6,845	15.4 %
Tenant recovery revenue	1,663	744	919	123.5 %
Total operating revenues	52,946	45,182	7,764	17.2 %
Operating expenses				
Depreciation and amortization	23,358	19,845	3,513	17.7 %
Property operating expenses	5,609	2,884	2,725	94.5 %
Base management fee	2,556	2,387	169	7.1 %
Incentive fee	1,429	1,120	309	27.6 %
Administration fee	747	700	47	6.7 %
General and administrative	1,245	1,127	118	10.5 %
Impairment charge	—	3,999	(3,999)	(100.0)%
Total operating expenses	34,944	32,062	2,882	9.0 %
Other (expense) income				
Interest expense	(12,744)	(12,103)	(641)	5.3 %
Gain on sale of real estate, net	1,844	3,992	(2,148)	(53.8)%
Other income	28	11	17	154.5 %
Total other expense, net	(10,872)	(8,100)	(2,772)	34.2 %
Net income	7,130	5,020	2,110	42.0 %
Distributions attributable to Series A, B and D preferred stock	(5,191)	(4,810)	(381)	7.9 %
Distributions attributable to senior common stock	(465)	(497)	32	(6.4)%
Net income (loss) available (attributable) to common stockholders	$1,474	$(287)	$1,761	(613.6)%
Net income (loss) available (attributable) to common stockholders per weighted average share of common stock - basic & diluted	$0.05	$(0.01)	$0.06	(600.0)%
FFO available to common stockholders - basic (1)	$22,988	$19,565	$3,423	17.5 %
FFO available to common stockholders - diluted (1)	$23,453	$20,062	$3,391	16.9 %
FFO per weighted average share of common stock - basic (1)	$0.81	$0.78	$0.03	3.8 %
FFO per weighted average share of common stock - diluted (1)	$0.80	$0.77	$0.03	3.9 %

(1) Refer to the "Funds from Operations" section below within the Management's Discussion and Analysis section for the definition of FFO.

Same Store Analysis

For the purposes of the following discussion, same store properties are properties we owned as of January 1, 2017, which have not been subsequently vacated, or disposed of. Acquired and disposed of properties are properties which were either acquired, disposed of or classified as held for sale at any point subsequent to December 31, 2016. Properties with vacancy are properties that were fully vacant or had greater than 5.0% vacancy, based on square footage, at any point subsequent to January 1, 2017. Expanded properties are properties in which an expansion was completed at any point subsequent to December 31, 2016.

Table of Contents

Operating Revenues

	For the three months ended June 30, (Dollars in Thousands)			
Rental Revenues	2018	2017	$ Change	% Change
Same Store Properties	$20,051	$19,993	$58	0.3 %
Acquired & Disposed Properties	4,182	1,165	3,017	259.0 %
Properties with Vacancy	930	869	61	7.0 %
Expanded Properties	529	451	78	17.3 %
	$25,692	$22,478	$3,214	14.3 %

	For the six months ended June 30, (Dollars in Thousands)			
Rental Revenues	2018	2017	$ Change	% Change
Same Store Properties	$40,102	$39,960	$142	0.4 %
Acquired & Disposed Properties	8,254	1,994	6,260	313.9 %
Properties with Vacancy	1,869	1,740	129	7.4 %
Expanded Properties	1,058	744	314	42.2 %
	$51,283	$44,438	$6,845	15.4 %

Rental revenue from same store properties increased slightly for the three and six months ended June 30, 2018 from the comparable 2017 period, primarily due to an increase in rental charges related to lease extensions executed subsequent to the six months ended June 30, 2017, coupled with increases in rental charges on leases subject to consumer price indexes. Rental revenue increased for acquired and disposed of properties for the three and six months ended June 30, 2018, as compared to the three and six months ended June 30, 2017, because we acquired seven properties subsequent to June 30, 2017, offset by a loss of rental revenues from six properties we sold during and subsequent to the three and six months ended June 30, 2017 pursuant to our capital recycling program. Rental revenue increased for our properties with vacancy for the three and six months ended June 30, 2018 because we leased approximately 47,000 square feet of vacant space in properties with partial vacancies subsequent to the three and six months ended June 30, 2017. Rental revenue increased for our expanded properties because we completed an expansion project subsequent to the three and six months ended June 30, 2017 and, therefore, we were able to charge additional rent for such property during the three months ended June 30, 2018.

	For the three months ended June 30, (Dollars in Thousands)			
Tenant Recovery Revenue	2018	2017	$ Change	% Change
Same Store Properties	$474	$338	$136	40.2 %
Acquired & Disposed Properties	341	53	288	543.4 %
Properties with Vacancy	84	(5)	89	(1,780.0)%
Expanded Properties	2	3	(1)	(33.3)%
	$901	$389	$512	131.6 %

For the six months ended June 30,
(Dollars in Thousands)

Tenant Recovery Revenue	2018	2017	$ Change	% Change
Same Store Properties	$910	$652	$ 258	39.6 %
Acquired & Disposed Properties	619	54	565	1,046.3%
Properties with Vacancy	128	33	95	287.9 %
Expanded Properties	6	5	1	20.0 %
	$1,663	$744	$ 919	123.5 %

35

Table of Contents

The increase in same store tenant recovery revenues for the three and six months ended June 30, 2018, as compared to the three and six months ended June 30, 2017, is a result of increased recoveries from leases with base year expense stops at certain of our properties that were running above base year during the three and six months ended June 30, 2018. The increase in tenant recovery revenues on acquired and disposed of properties for the three and six months ended June 30, 2018, as compared to the three and six months ended June 30, 2017, is a result of increased recoveries from leases with base year expense stops at properties acquired subsequent to June 30, 2017 with base year leases.

Operating Expenses

Depreciation and amortization increased for the three and six months ended June 30, 2018, as compared to the three and six months ended June 30, 2017, due to depreciation on capital projects completed subsequent to June 30, 2017, coupled with depreciation on the seven properties acquired subsequent to June 30, 2017, partially offset by decreased depreciation on the six properties sold during and subsequent to the three and six months ended June 30, 2017.

	For the three months ended June 30, (Dollars in Thousands)			
Property Operating Expenses	2018	2017	$ Change	% Change
Same Store Properties	$1,115	$1,142	$(27)	(2.4)%
Acquired & Disposed Properties	1,440	183	1,257	686.9 %
Properties with Vacancy	252	172	80	46.5 %
Expanded Properties	9	8	1	12.5 %
	$2,816	$1,505	$1,311	87.1 %

	For the six months ended June 30, (Dollars in Thousands)			
Property Operating Expenses	2018	2017	$ Change	% Change
Same Store Properties	$2,136	$2,118	$18	0.8 %
Acquired & Disposed Properties	2,964	293	2,671	911.6 %
Properties with Vacancy	495	461	34	7.4 %
Expanded Properties	14	12	2	16.7 %
	$5,609	$2,884	$2,725	94.5 %

Property operating expenses consist of franchise taxes, property management fees, insurance, ground lease payments, property maintenance and repair expenses paid on behalf of certain of our properties. The decrease in property operating expenses for same store properties for the three months ended June 30, 2018, as compared to the three months ended June 30, 2017, is a result of an overall decrease in property operating expenses incurred at our properties with tenants on base year expense stop leases, offset by an increase in landlord obligated property expenses on our triple net leased properties. The increase in property operating expenses for same store properties for the six months ended June 30, 2018, as compared to the six months ended June 30, 2017, is a result of an overall increase in property insurance expense and franchise tax expense, offset by an overall decrease in property operating expenses incurred at our properties with tenants on base year expense stop leases. The increase in property operating expenses for acquired and disposed of properties for the three and six months ended June 30, 2018, as compared to the three and six months ended June 30, 2017, is primarily a result of increased property operating expenses from properties acquired subsequent to June 30, 2017, as a majority of these properties are subject to base year leases, partially offset by a reduction of operating expenses from properties sold subsequent to June 30, 2017. The increase in property operating expenses for properties with vacancy during the three and six months ended June 30, 2018, as compared to the three and six months ended June 30, 2017, is primarily due to increased property operating expenses associated with one property with increased vacant space due to a lease expiration.

The base management fee paid to the Adviser increased for the three and six months ended June 30, 2018, as compared to the three and six months ended June 30, 2017, due to the increase in total adjusted stockholders' equity in the past 12 months. The calculation of the base management fee is described in detail above in "Advisory and Administration Agreements."

The incentive fee paid to the Adviser increased for the three and six months ended June 30, 2018, as compared to the three and six months ended June 30, 2017, due to pre-incentive fee Core FFO increasing faster than the hurdle rate, resulting in a higher incentive fee. The increase in FFO is a result of an increase in total operating revenues, partially offset by an increase in total operating expenses and interest expense. The calculation of the incentive fee is described in detail above in "Advisory and Administration Agreements."

Table of Contents

The administration fee paid to the Administrator increased for the three and six months ended June 30, 2018, as compared to the three and six months ended June 30, 2017, due to using a greater share of our Administrator's resources during the three and six months ended June 30, 2018. The calculation of the administration fee is described in detail above in "Advisory and Administration Agreements."

General and administrative expenses increased for the three and six months ended June 30, 2018, as compared to the three and six months ended June 30, 2017, primarily as a result of an increase in travel expenses.

We did not recognize an impairment charge for the three and six months ended June 30, 2018. The impairment charge for the six months ended June 30, 2017 resulted from an impairment recorded on our Concord Township, Ohio and Newburyport, Massachusetts properties, as we determined the carrying value of these properties was unrecoverable through our quarterly impairment testing. Both the Concord Township, Ohio property and the Newburyport, Massachusetts property were sold during the year ended December 31, 2017.

Other Income and Expenses

Interest expense increased for the three and six months ended June 30, 2018, as compared to the three and six months ended June 30, 2017. This increase was primarily a result of us issuing or assuming $53.9 million in mortgage debt subsequent to the six months ended June 30, 2017, coupled with an increase in LIBOR, which is the interest rate benchmark for all of our outstanding variable rate debt, partially offset by our repayment of $65.4 million in maturing mortgage debt during and subsequent to the six months ended June 30, 2017.

Gain on sale of real estate, net, for the six months ended June 30, 2018 is attributable to two non-core industrial assets sold during the period. Gain on sale of real estate, net, for the six months ended June 30, 2017 is attributable to three non-core industrial assets sold during the period.

Net (Loss) Income (Attributable) Available to Common Stockholders

Net loss attributable to common stockholders decreased for the three months ended June 30, 2018, as compared to the three months ended June 30, 2017, primarily due to the increase in total operating revenues related to asset acquisition activity and leasing vacant space, partially offset by an increase in property operating expenses, depreciation and amortization expenses, base management and incentive fees, interest expenses, and the loss on sale of real estate, net, during the three months ended June 30, 2017. Net income available to common stockholders for the six months ended June 30, 2018, as compared to net loss attributable to common stockholders for the six months ended June 30, 2017, is primarily due to the increase in total operating revenues related to asset acquisition activity and leasing vacant space in addition to the impairment loss during the six months ended June 30, 2017, partially offset by an increase in property operating expenses and depreciation and amortization expenses, coupled with a decrease in gain on sale of real estate, net.

Liquidity and Capital Resources

Overview

Our sources of liquidity include cash flows from operations, cash and cash equivalents, borrowings under our Revolver and issuing additional equity securities. Our available liquidity as of June 30, 2018, was $50.7 million, consisting of approximately $4.6 million in cash and cash equivalents and an available borrowing capacity of $46.1 million under our Revolver. Our available borrowing capacity under the Revolver increased to $51.6 million as of July 30, 2018.

Future Capital Needs

We actively seek conservative investments that are likely to produce income to pay distributions to our stockholders. We intend to use the proceeds received from future equity raised and debt capital borrowed to continue to invest in industrial and office real property, make mortgage loans, or pay down outstanding borrowings under our Revolver. Accordingly, to ensure that we are able to effectively execute our business strategy, we routinely review our liquidity requirements and continually evaluate all potential sources of liquidity. Our short-term liquidity needs include proceeds necessary to fund our distributions to stockholders, pay the debt service costs on our existing long-term mortgages, refinancing maturing debt and fund our current operating costs. Our long-term liquidity needs include proceeds necessary to grow and maintain our portfolio of investments.

Table of Contents

We believe that our available liquidity is sufficient to fund our distributions to stockholders, pay the debt service costs on our existing long-term mortgages and fund our current operating costs in the near term. We also believe we will be able to refinance our mortgage debt as it matures. Additionally, to satisfy our short-term obligations, we may request credits to our management fees that are issued from our Adviser, although our Adviser is under no obligation to provide any such credits, either in whole or in part. We further believe that our cash flow from operations coupled with the financing capital available to us in the future are sufficient to fund our long-term liquidity needs.

Equity Capital

During the six months ended June 30, 2018, we raised net proceeds of (i) $3.5 million of common equity under our Common Stock ATM Program at a net weighted average per share price of $19.03, and (ii) $2.2 million under our Series D Preferred ATM Program at a net weighted average per share price of $24.74. We used these proceeds to pay down outstanding debt and for other general corporate purposes. We did not sell any shares of our Series A Preferred or Series B Preferred pursuant to our Series A and B Preferred ATM Program during the six months ended June 30, 2018.

As of July 30, 2018, we had the ability to raise up to $288.9 million of additional equity capital through the sale and issuance of securities that are registered under our universal shelf registration statement on Form S-3 (File No. 333-208953), (the "Universal Shelf"), in one or more future public offerings. Of the $288.9 million of available capacity under our Universal Shelf, approximately $81.0 million of common stock is reserved for additional sales under our Common Stock ATM Program, approximately $37.2 million of preferred stock is reserved for additional sales under our Series A and B Preferred ATM Program, and approximately $18.6 million is reserved for additional sales under our Series D Preferred ATM Program as of July 30, 2018. We expect to continue to use our ATM programs as a source of liquidity for the remainder of 2018.

Debt Capital

As of June 30, 2018, we had 45 mortgage notes payable in the aggregate principal amount of $439.9 million, collateralized by a total of 66 properties with a remaining weighted average maturity of 6.3 years. The weighted-average interest rate on the mortgage notes payable as of June 30, 2018 was 4.63%.

We continue to see banks and other non-bank lenders willing to issue mortgages. Consequently, we are focused on obtaining mortgages through regional banks, non-bank lenders and the CMBS market.

As of June 30, 2018, we had mortgage debt in the aggregate principal amount of $20.7 million payable during the remainder of 2018 and $48.0 million payable during 2019. The 2018 principal amounts payable include both amortizing principal payments and three balloon principal payments due in the remainder of 2018. We anticipate being able to refinance our mortgages that come due during the remainder of 2018 and 2019 with a combination of new debt and the issuance of additional equity securities. In addition, we have raised substantial equity under our ATM programs and plan to continue to use these programs.

Operating Activities

Net cash provided by operating activities during the six months ended June 30, 2018, was $26.0 million, as compared to net cash provided by operating activities of $21.4 million for the six months ended June 30, 2017. This increase was primarily a result of an increase in rental receipts from acquisitions completed subsequent to June 30, 2017 and contractual rent increases on the in-place portfolio. This increase was partially offset by an increase in property operating expenses. The majority of cash from operating activities is generated from the rental payments and operating expense recoveries that we receive from our tenants. We utilize this cash to fund our property-level operating expenses and use the excess cash primarily for debt and interest payments on our mortgage notes payable, interest payments on our Revolver and Term Loan, distributions to our stockholders, management fees to our Adviser, Administration fees to our Administrator and other entity-level operating expenses.

Investing Activities

Net cash used in investing activities during the six months ended June 30, 2018, was $5.6 million, which primarily consisted of one property acquisition, coupled with capital improvements performed at certain of our properties, partially offset by proceeds from the sale of two properties. Net cash provided by investing activities during the six months ended June 30, 2017, was $14.6 million, which primarily consisted of proceeds from the sale of three properties, coupled with recovering funds held in escrow from our lender for the mortgages we repaid, partially offset by capital improvements performed at certain of our properties.

Table of Contents

Financing Activities

Net cash used in financing activities during the six months ended June 30, 2018, was $22.2 million, which primarily consisted of the repayment of $22.0 million of mortgage principal, coupled with distributions paid to common, senior common and preferred shareholders, partially offset by an increase in borrowings from our Revolver, the issuance of $5.8 million of equity and mezzanine equity and the issuance of $9.4 million of new mortgage debt. Net cash used in financing activities for the six months ended June 30, 2017, was $35.9 million, which primarily consisted of the repayment of $40.6 million of mortgage principal, coupled with distributions paid to common, senior common and preferred shareholders, partially offset by proceeds from issuance of equity.

Credit Facility

On August 7, 2013, we procured our Revolver with KeyBank (serving as a revolving lender, a letter of credit issuer and an administrative agent). In October 2015, we expanded our Revolver to $85.0 million, and entered into a Term Loan, whereby we added a $25.0 million, five-year Term Loan subject to the same leverage tiers as the Revolver, with the interest rate at each leverage tier being 5 basis points lower than that of the Revolver. We have the option to repay the Term Loan in full, or in part, at any time without penalty or premium prior to the maturity date. On October 27, 2017, we amended our Credit Facility, increasing the Term Loan from $25.0 million, to $75.0 million, with the Revolver commitment remaining at $85.0 million. The Term Loan has a new five-year term, with a maturity date of October 27, 2022, and the Revolver has a new four-year term, with a maturity date of October 27, 2021. The interest rate for the Credit Facility was reduced by 25 basis points at each of the leverage tiers. We entered into interest rate cap agreements on the amended Term Loan, which cap LIBOR at 2.75%. We used the net proceeds of the amended Credit Facility to repay all previously existing borrowings under the Revolver. We incurred fees of approximately $0.9 million in connection with the Credit Facility amendment. The bank syndicate is now comprised of KeyBank, Fifth Third Bank, US Bank National Association and The Huntington National Bank.

As of June 30, 2018, there was $108.4 million outstanding under our Credit Facility at a weighted average interest rate of approximately 3.81% and $1.0 million outstanding under letters of credit at a weighted average interest rate of 1.75%. As of July 30, 2018, the maximum additional amount we could draw under the Revolver and Term Loan was $51.6 million. We were in compliance with all covenants under the Credit Facility as of June 30, 2018.

Contractual Obligations

The following table reflects our material contractual obligations as of June 30, 2018 (in thousands):

	Payments Due by Period				
Contractual Obligations	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Debt Obligations (1)	$548,277	$ 35,255	$80,276	$247,431	$ 185,315
Interest on Debt Obligations (2)	111,268	23,005	41,729	28,791	17,743
Operating Lease Obligations (3)	6,111	465	933	638	4,075
Purchase Obligations (4)	891	465	426	—	—
	$666,547	$ 59,190	$123,364	$276,860	$ 207,133

(1) Debt obligations represent borrowings under our Revolver, which represents $33.4 million of the debt obligation due in 2021, our Term Loan, which represents $75.0 million of the debt obligation due in 2022, and mortgage notes payable that were outstanding as of June 30, 2018. This figure does not include $0.3 million of premiums and discounts, net and $5.5 million of deferred financing costs, net, which are reflected in mortgage notes payable, net, borrowings under Revolver, net and borrowings under Term Loan, net on the condensed consolidated balance sheets.

(2) Interest on debt obligations includes estimated interest on borrowings under our Revolver and Term Loan and mortgage notes payable. The balance and interest rate on our Revolver and Term Loan is variable; thus, the interest payment obligation calculated for purposes of this table was based upon rates and balances as of June 30, 2018.
(3) Operating lease obligations represent the ground lease payments due on our four of our properties.
(4) Purchase obligations consist of tenant and capital improvements at four of our properties.

Off-Balance Sheet Arrangements

We did not have any material off-balance sheet arrangements as of June 30, 2018.

39

Table of Contents

Funds from Operations

The National Association of Real Estate Investment Trusts (“NAREIT”) developed Funds from Operations (“FFO”) as a relevant non-GAAP supplemental measure of operating performance of an equity REIT to recognize that income-producing real estate historically has not depreciated on the same basis determined under GAAP. FFO, as defined by NAREIT, is net income (computed in accordance with GAAP), excluding gains or losses from sales of property and impairment losses on property, plus depreciation and amortization of real estate assets, and after adjustments for unconsolidated partnerships and joint ventures.

FFO does not represent cash flows from operating activities in accordance with GAAP, which, unlike FFO, generally reflects all cash effects of transactions and other events in the determination of net income. FFO should not be considered an alternative to net income as an indication of our performance or to cash flows from operations as a measure of liquidity or ability to make distributions. Comparison of FFO, using the NAREIT definition, to similarly titled measures for other REITs may not necessarily be meaningful due to possible differences in the application of the NAREIT definition used by such REITs.

FFO available to common stockholders is FFO adjusted to subtract distributions made to holders of preferred stock and senior common stock. We believe that net income available to common stockholders is the most directly comparable GAAP measure to FFO available to common stockholders.

Basic funds from operations per share (“Basic FFO per share”), and diluted funds from operations per share (“Diluted FFO per share”), is FFO available to common stockholders divided by the number of weighted average shares of common stock outstanding and FFO available to common stockholders divided by the number of weighted average shares of common stock outstanding on a diluted basis, respectively, during a period. We believe that FFO available to common stockholders, Basic FFO per share and Diluted FFO per share are useful to investors because they provide investors with a further context for evaluating our FFO results in the same manner that investors use net income and earnings per share (“EPS”), in evaluating net income available to common stockholders. In addition, because most REITs provide FFO available to common stockholders, Basic FFO and Diluted FFO per share information to the investment community, we believe these are useful supplemental measures when comparing us to other REITs. We believe that net income is the most directly comparable GAAP measure to FFO, Basic EPS is the most directly comparable GAAP measure to Basic FFO per share, and that Diluted EPS is the most directly comparable GAAP measure to Diluted FFO per share.

Table of Contents

The following table provides a reconciliation of our FFO available to common stockholders for the three and six months ended June 30, 2018 and 2017, respectively, to the most directly comparable GAAP measure, net income available to common stockholders, and a computation of basic and diluted FFO per weighted average share of common stock:

	For the three months ended June 30, (Dollars in Thousands, Except for Per Share Amounts)		For the six months ended June 30, (Dollars in Thousands, Except for Per Share Amounts)	
	2018	2017	2018	2017
Calculation of basic FFO per share of common stock				
Net income	$2,525	$ 661	$7,130	$ 5,020
Less: Distributions attributable to preferred and senior common stock	(2,842)	(2,686)	(5,656)	(5,307)
Net (loss) income (attributable) available to common stockholders	$(317)	$ (2,025)	$1,474	$ (287)
Adjustments:				
Add: Real estate depreciation and amortization	$11,773	$ 9,926	$23,358	$ 19,845
Add: Impairment charge	—	253	—	3,999
Add: Loss on sale of real estate, net	—	1,914	—	—
Less: Gain on sale of real estate, net	—	—	(1,844)	(3,992)
FFO available to common stockholders - basic	$11,456	$ 10,068	$22,988	$ 19,565
Weighted average common shares outstanding - basic	28,437,852	25,276,824	28,429,470	25,121,239
Basic FFO per weighted average share of common stock	$0.40	$ 0.40	$0.81	$ 0.78
Calculation of diluted FFO per share of common stock				
Net income	$2,525	$ 661	$7,130	$ 5,020
Less: Distributions attributable to preferred and senior common stock	(2,842)	(2,686)	(5,656)	(5,307)
Net (loss) income (attributable) available to common stockholders	$(317)	$ (2,025)	$1,474	$ (287)
Adjustments:				
Add: Real estate depreciation and amortization	$11,773	$ 9,926	$23,358	$ 19,845
Add: Impairment charge	—	253	—	3,999
Add: Income impact of assumed conversion of senior common stock	233	249	465	497
Add: Loss on sale of real estate, net	—	1,914	—	—
Less: Gain on sale of real estate, net	—	—	(1,844)	(3,992)
FFO available to common stockholders plus assumed conversions	$11,689	$ 10,317	$23,453	$ 20,062
Weighted average common shares outstanding - basic	28,437,852	25,276,824	28,429,470	25,121,239
Effect of convertible senior common stock	744,327	783,236	744,327	783,236
Weighted average common shares outstanding - diluted	29,182,179	26,060,060	29,173,797	25,904,475
Diluted FFO per weighted average share of common stock	$0.40	$ 0.40	$0.80	$ 0.77
Distributions declared per share of common stock	$0.375	$ 0.375	$0.750	$ 0.750

Table of Contents

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Market risk includes risks that arise from changes in interest rates, foreign currency exchange rates, commodity prices, equity prices and other market changes that affect market sensitive instruments. The primary risk that we believe we are and will be exposed to is interest rate risk. Certain of our leases contain escalations based on market indices, and the interest rate on our Credit Facility is variable. Although we seek to mitigate this risk by structuring such provisions of our loans and leases to contain a minimum interest rate or escalation rate, as applicable, these features do not eliminate this risk. To that end, we have entered into derivative contracts to cap interest rates for our variable rate notes payable, and we have entered into interest rate swaps whereby we pay a fixed interest rate to our respective counterparty, and receive one month LIBOR in return. For details regarding our rate cap agreements and our interest rate swap agreements see Note 6 – Mortgage Notes Payable and Credit Facility of the accompanying condensed consolidated financial statements.

To illustrate the potential impact of changes in interest rates on our net income for the six months ended June 30, 2018, we have performed the following analysis, which assumes that our condensed consolidated balance sheets remain constant and that no further actions beyond a minimum interest rate or escalation rate are taken to alter our existing interest rate sensitivity.

The following table summarizes the annual impact of a 1%, 2% and 3% increase, and a 1% and 2% decrease in the one month LIBOR as of June 30, 2018. As of June 30, 2018, our effective average LIBOR was 2.09%. Given that a 3% decrease in LIBOR would result in a negative rate, the impact of this fluctuation is not presented below (dollars in thousands).

Interest Rate Change	(Decrease) increase to Interest Expense	Net increase (decrease) to Net Income
2% Decrease to LIBOR	$ (3,414)	$ 3,414
1% Decrease to LIBOR	(1,724)	1,724
1% Increase to LIBOR	1,237	(1,237)
2% Increase to LIBOR	1,605	(1,605)
3% Increase to LIBOR	1,951	(1,951)

As of June 30, 2018, the fair value of our mortgage debt outstanding was $435.1 million. Interest rate fluctuations may affect the fair value of our debt instruments. If interest rates on our debt instruments, using rates at June 30, 2018, had been one percentage point higher or lower, the fair value of those debt instruments on that date would have decreased or increased by $17.2 million and $18.4 million, respectively.

The amount outstanding under the Credit Facility approximates fair value as of June 30, 2018.

In the future, we may be exposed to additional effects of interest rate changes, primarily as a result of our Revolver, Term Loan or long-term mortgage debt, which we use to maintain liquidity and fund expansion of our real estate investment portfolio and operations. Our interest rate risk management objectives are to limit the impact of interest rate changes on earnings and cash flows and to lower overall borrowing costs. To achieve these objectives, we will borrow primarily at fixed rates or variable rates with the lowest margins available and, in some cases, with the ability to convert variable rates to fixed rates. We may also enter into derivative financial instruments such as interest rate swaps and caps in order to mitigate the interest rate risk on a related financial instrument. We will not enter into derivative or interest rate transactions for speculative purposes.

In addition to changes in interest rates, the value of our real estate is subject to fluctuations based on changes in local and regional economic conditions and changes in the creditworthiness of lessees and borrowers, all of which may affect our ability to refinance debt, if necessary.

Table of Contents

Item 4. Controls and Procedures.

a) Evaluation of Disclosure Controls and Procedures

As of June 30, 2018, our management, including our chief executive officer and chief financial officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures. Based on that evaluation, the chief executive officer and chief financial officer, concluded that our disclosure controls and procedures were effective as of June 30, 2018 in providing a reasonable level of assurance that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in applicable SEC rules and forms, including providing a reasonable level of assurance that information required to be disclosed by us in such reports is accumulated and communicated to our management, including our chief executive officer and our chief financial officer, as appropriate to allow timely decisions regarding required disclosure. However, in evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated can provide only reasonable assurance of necessarily achieving the desired control objectives, and management was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

b) Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the quarter ended June 30, 2018 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

PART II – OTHER INFORMATION

Item 1. Legal Proceedings.

We are not currently subject to any material legal proceedings, nor, to our knowledge, is any material legal proceeding threatened against us.

Item 1A. Risk Factors.

Our business is subject to certain risks and events that, if they occur, could adversely affect our financial condition and results of operations and the trading price of our securities. For a discussion of these risks, please refer to the section captioned "Item 1A. Risk Factors" in our 2017 Form 10-K. There are no material changes to risks associated with our business or investment in our securities from those previously set forth in the reports described above.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Sales of Unregistered Securities

None.

Issuer Purchases of Equity Securities

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

Exhibit Index

Exhibit Number	Exhibit Description
3.1	Articles of Restatement of the Registrant, incorporated by reference to Exhibit 3.2 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed January 12, 2017.
3.2	Bylaws of the Registrant, incorporated by reference to Exhibit 3.2 to the Registrant's Registration Statement on Form S-11 (File No. 333-106024), filed June 11, 2003.

44

3.3	First Amendment to Bylaws of the Registrant, incorporated by reference to Exhibit 99.1 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed July 10, 2007.
3.4	Second Amendment to Bylaws of the Registrant, incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed December 1, 2016.
3.5	Articles Supplementary, filed with the Maryland State Department of Assessments and Taxation on April 11, 2018, incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed April 12, 2018.
3.6	Articles of Amendment, filed with the Maryland State Department of Assessments and Taxation on April 11, 2018, incorporated by reference to Exhibit 3.2 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed April 12, 2018.
4.1	Form of Certificate for Common Stock of the Registrant, incorporated by reference to Exhibit 4.1 to Pre-Effective Amendment No. 2 to the Registrant's Registration Statement on Form S-11 (File No. 333-106024), filed August 8, 2003.
4.2	Form of Certificate for 7.75% Series A Cumulative Redeemable Preferred Stock of the Registrant, incorporated by reference to Exhibit 4.1 to the Registrant's Form 8-A12G (File No. 000-50363), filed January 19, 2006.
4.3	Form of Certificate for 7.50% Series B Cumulative Redeemable Preferred Stock of the Registrant, incorporated by reference to Exhibit 4.2 to the Registrant's Form 8-A12B (File No. 001-33097), filed October 19, 2006.
4.4	Form of Certificate for 7.00% Series D Cumulative Redeemable Preferred Stock of the Registrant, incorporated by reference to Exhibit 4.1 to the Registrant's Form 8-K (File No. 001-33097), filed May 25, 2016.
10.1	Second Amended and Restated Agreement of Limited Partnership of Gladstone Commercial Limited, incorporated by reference to Exhibit 10.1 to the Registrant's Form 8-K (File No. 001-33097), filed July 11, 2018.
11	Computation of Per Share Earnings from Operations.
12	Statements re: computation of ratios.
31.1*	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1**	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2**	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
99.1**	Estimated Value Methodology for Senior Common Stock at June 30, 2018 (filed herewith).
101.INS***	XBRL Instance Document

101.SCH*** XBRL Taxonomy Extension Schema Document

45

101.CAL***	XBRL Taxonomy Extension Calculation Linkbase Document
101.LAB***	XBRL Taxonomy Extension Label Linkbase Document
101.PRE***	XBRL Taxonomy Extension Presentation Linkbase Document
101.DEF***	XBRL Definition Linkbase

* Filed herewith

** Furnished herewith

*** Attached as Exhibit 101 to this Quarterly Report on Form 10-Q are the following materials, formatted in XBRL (eXtensible Business Reporting Language): (i) the Condensed Consolidated Balance Sheets as of June 30, 2018 and December 31, 2017, (ii) the Condensed Consolidated Statements of Operations and Comprehensive Income for the three and six months ended June 30, 2018 and 2017, (iii) the Condensed Consolidated Statements of Cash Flows for the six months ended June 30, 2018 and 2017 and (iv) the Notes to Condensed Consolidated Financial Statements.

Table of Contents

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

		Gladstone Commercial Corporation
Date: July 30, 2018	By:	/s/ Mike Sodo Mike Sodo Chief Financial Officer
Date: July 30, 2018	By:	/s/ David Gladstone David Gladstone Chief Executive Officer and Chairman of the Board of Directors