



**Who We Are:** We are a public real estate investment trust (or REIT) traded on NASDAQ. Our common stock trades under the symbol GOOD. Our three classes of preferred stock trade under the symbols GOODN, GOODO and GOODP. We pay monthly distributions to all our stockholders.

**What We Do:** As a REIT, we seek to invest in and own net-leased industrial, commercial and retail real estate properties. We own 96 properties, located in 23 states, totaling approximately 10.6 million square feet of rental space. These properties consist of office, warehouse, industrial, medical, retail and manufacturing facilities.

Our principal investment objectives are to generate cash from rents so that we can make monthly distributions to our stockholders. Our primary strategy to achieve our investment objectives is to own a diversified portfolio of leased industrial, commercial and retail real estate that we believe will produce stable cash payments to us and increase in value over time. We expect to sell some of our real estate assets from time to time when we determine that doing so would be advantageous.

**Our Adviser:** We are managed by Gladstone Management Corporation, our Adviser, whose principal office is located at 1521 Westbranch Drive, McLean, Virginia 22102, a suburb of Washington, DC. Our Adviser also has offices in New York, New York; Chicago, Illinois; and Los Angeles, California.



# CONSOLIDATED SELECTED FINANCIAL AND OTHER DATA

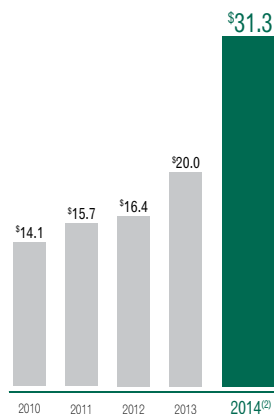
(Dollars in Thousands, Except Per Share Amounts)	For the year ended December 31,				
	2014	2013	2012	2011	2010
<b>OPERATING DATA:</b>					
Total operating revenue	\$ 73,756	\$ 61,343	\$ 51,270	\$ 43,976	\$ 41,928
Total operating expenses	(57,406)	(32,823)	(24,895)	(21,270)	(23,414)
Other expense	(22,252)	(26,993)	(22,614)	(16,992)	(13,586)
Net (loss) income	\$ (5,902)	\$ 1,527	\$ 3,761	\$ 5,714	\$ 4,928
Dividends attributable to preferred stock	(4,094)	(4,094)	(4,093)	(4,094)	(4,094)
Dividends attributable to senior common stock	(542)	(300)	(113)	(62)	(20)
Net (loss) income available to common stockholders	\$ (10,538)	\$ (2,867)	\$ (445)	\$ 1,558	\$ 814
<b>SHARE AND PER SHARE DATA:</b>					
(Loss) earnings per weighted average common share—basic & diluted	\$ (0.61)	\$ (0.22)	\$ (0.04)	\$ 0.15	\$ 0.09
Weighted average common shares outstanding—basic	17,253,503	13,164,244	10,953,325	10,236,859	8,576,303
Weighted average common shares outstanding—diluted	17,253,503	13,164,244	10,953,325	10,288,711	8,601,153
Cash dividends declared per common share	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50
<b>SUPPLEMENTAL DATA:</b>					
Net (loss) income available to common stockholders	\$ (10,538)	\$ (2,867)	\$ (445)	\$ 1,558	\$ 814
Add: Real estate depreciation and amortization	28,864	22,827	16,831	14,149	13,264
Add: Impairment charge	14,238	—	—	—	—
Less: Gain on sale of real estate	(1,240)	—	—	—	—
Funds from operations available to common stockholders <sup>(1)(2)</sup>	\$ 31,324	\$ 19,960	\$ 16,386	\$ 15,707	\$ 14,078
<b>BALANCE SHEET DATA:</b>					
Real estate, before accumulated depreciation	\$ 722,565	\$ 642,353	\$ 533,753	\$ 442,521	\$ 401,017
Total assets	787,794	690,525	564,779	453,147	410,609
Mortgage notes payable, term loan, term preferred stock and borrowings under the line of credit	541,099	485,502	422,685	304,050	286,595
Total stockholders' equity	217,672	183,146	122,365	135,314	111,375
Total common shares outstanding	19,589,606	15,662,414	11,083,584	10,945,379	8,724,613

1) The National Association of Real Estate Investment Trusts, or NAREIT, developed 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. For a reconciliation of FFO to net income, see the enclosed Annual Report on Form 10-K for the year ended December 31, 2014.

2) Funds from operations for the year ended December 31, 2014 includes a \$5.3 million non-cash gain on debt extinguishment.

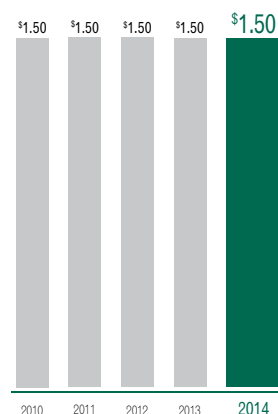
## Funds from Operations

Fiscal Years Ended December 31  
(dollars in millions)



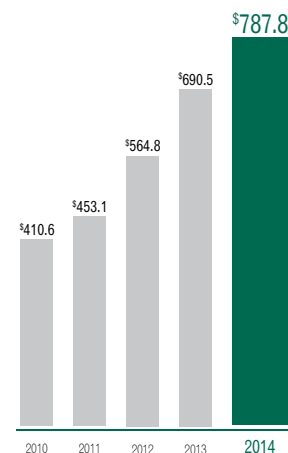
## Cash Distributions Per Common Share

Fiscal Years Ended December 31  
(in dollars)



## Total Assets

As of December 31  
(dollars in millions)



## TO OUR SHAREHOLDERS:



PICTURED FROM LEFT TO RIGHT:  
Terry L. Brubaker, David Gladstone, Bob Cutlip

**HIGHLIGHTS FOR 2014 INCLUDE:** increasing the number of properties we own, expanding an existing property, issuing a construction mortgage loan for a build-to-suit property, leasing one of our vacant properties, extending the terms of upcoming expiring leases, implementing a new stock issuance program, extending our line of credit, and obtaining mortgages for some of our properties. We are pleased that we have been very active and able to consistently grow our portfolio. We expect to continue to build on those successes in 2015.

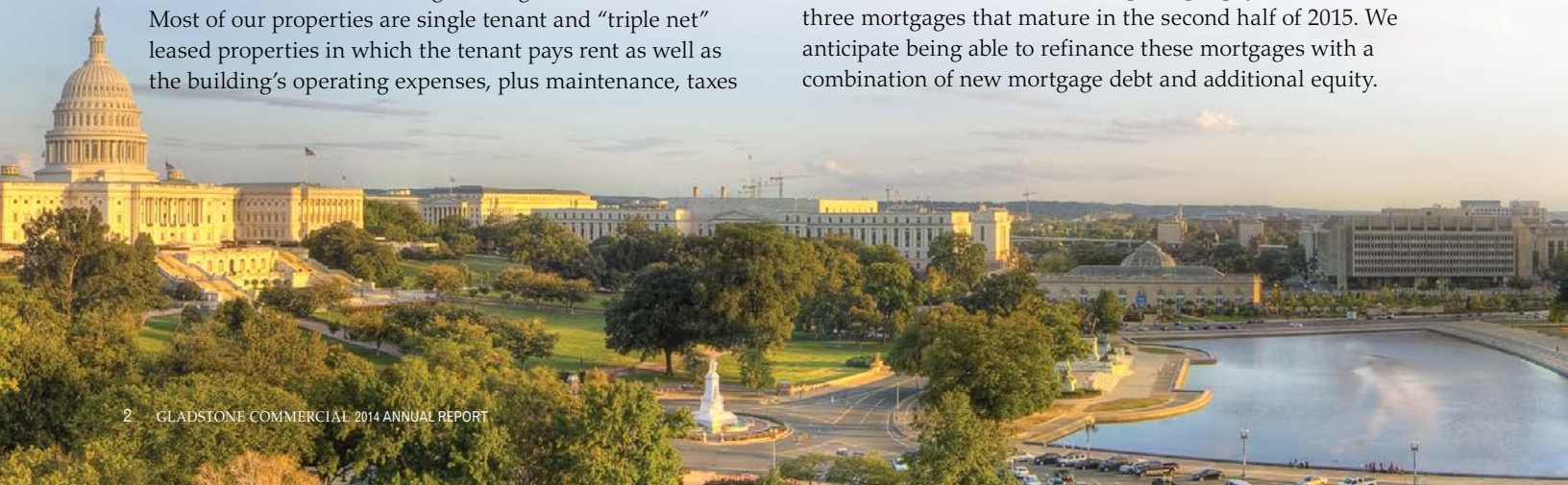
### OPERATING RESULTS

During the year, we invested approximately \$139 million in 11 new properties and the expansion of one of our existing buildings. We also invested \$5.6 million in a construction mortgage loan for a build-to-suit property. The weighted average yield for these new investments is 9.0%. We continue to focus on investing in strong, secondary markets and each of our regions had new investments during the year, including Phoenix, Denver, Dallas, Indianapolis, Sacramento and Columbus. We also borrowed or assumed about \$62 million in mortgages to finance a portion of the new properties we acquired, as we continue to take advantage of the low interest rates. The weighted average interest rate on the new mortgages is 4.5%. We currently own 96 properties, which are located in 23 states, leased to 91 different tenants in 19 different industries. This gives us great diversification. Most of our properties are single tenant and “triple net” leased properties in which the tenant pays rent as well as the building’s operating expenses, plus maintenance, taxes

and insurance; however, we are seeking to expand by purchasing a few strategic multitenant properties in which one tenant rents most of the building.

We continued to focus on maintaining our portfolio of quality tenants. During the year, we renewed five leases that were scheduled to expire in 2015 and leased one of our previously vacant buildings. At year end, all of our existing tenants were paying as agreed and our portfolio was 99% leased. We had one building without a tenant and one building that was partially vacant, but we continue to seek new tenants for each. We are also focused on extending the leases expiring in the next several years.

We have mortgage debt in the aggregate principal amount of \$42 million payable during 2015 and \$99 million payable during 2016. The 2015 principal amounts payable include \$34.6 million of balloon principal payments due on three mortgages that mature in the second half of 2015. We anticipate being able to refinance these mortgages with a combination of new mortgage debt and additional equity.



The 2016 principal amounts payable include \$92 million of principal payments due on nine mortgages that mature during the year. We anticipate being able to refinance these mortgages with a combination of new mortgages and some equity. We intend to decrease the amount of mortgages on these re-financings to continue our strategy of reducing our overall leverage.

## FINANCIAL RESULTS

Our 2014 Core Funds from Operations, or Core FFO, was approximately \$27.5 million, or \$1.55 per share, which was a 32.6% increase over total Core FFO from the prior year. Our 2014 results reflect the additional income from the 11 properties acquired during the year coupled with lower property operating expenses at certain of our vacant properties. This additional income was partially offset by an increase in interest expense from mortgages issued during the year plus an increase in general and administrative expenses related to the adjustment of a deferred rent balance for a tenant whereby the lease was modified during 2014.

At year end, our total assets increased to \$788 million, up 14% from 2013. The amounts outstanding under long-term mortgages plus the amount outstanding on our line of credit increased to \$503 million, up 12% from 2013. Our stockholders' equity increased by 19% to \$218 million. We believe our balance sheet remains strong as we continue our strategy to reduce our overall leverage. To this end we decreased the loan amount to the value of the real estate on new debt issued during 2014 to 60% from 68% in 2012.

## CAPITAL MARKETS

We were very active in the capital markets this year, issuing 3.9 million shares of common stock through one overnight offering and our at-the-market stock issuance programs (ATM). These two methods resulted in net proceeds of \$66 million. Our current ATM program is a very cost-efficient way for us to access the capital markets in order to fund our acquisitions.

## DIVIDENDS

Our monthly distribution during 2014 was \$0.125 per common share, or \$1.50 for the year. In January 2015, our board of directors maintained the monthly distribution of \$0.125 per common share for each of the months January, February and March 2015.

We are proud of the fact that we have never skipped, reduced or deferred a monthly distribution since our inception in 2003. As of February 27, 2015, we have paid 122 consecutive monthly cash distributions to our common stockholders, 110 consecutive monthly cash distributions to our Series A preferred stockholders, 101 consecutive monthly cash distributions to our Series B preferred stockholders and

37 consecutive monthly cash distributions to our Series C preferred stockholders.

As an owner of real estate, we are required to record depreciation on our properties. This depreciation and other items, such as impairment losses, shelter a portion of our distributions from income taxes. Therefore, in 2014, 100.0% of the distributions on our common stock were a tax-free return of capital. While the distribution is tax-free, this return of capital will reduce a stockholder's cost basis in the stock, which may result in a larger capital gains tax when the stock is sold. Our website, [www.GladstoneCommercial.com](http://www.GladstoneCommercial.com), has more information on this subject, but please consult your tax adviser for complete details.

## OUTLOOK

Our team is focused on improving our results in 2015 by leasing our vacant square footage and acquiring additional quality office and industrial properties on a consistent, measured basis. While there are no guarantees about the future, continuation of our monthly distributions to stockholders is paramount to our investment strategy. In addition we have a great team that believes strongly in the highest ethical standards and service to stockholders.

We are very hopeful about the future and believe 2015 will be another great year. We invite stockholders to attend our Annual Stockholders' Meeting on May 7, 2015, at the Hilton Hotel McLean Tyson's Corner, 7920 Jones Branch Drive, in McLean, Virginia. We also invite you to visit our website, [www.GladstoneCommercial.com](http://www.GladstoneCommercial.com), and sign up for email notices to keep up with our company's activities. You can also now follow us on Facebook at "The Gladstone Companies," and on Twitter at "GladstoneComps."

Best wishes and thank you for your continued support.



David Gladstone, *Chairman and CEO*



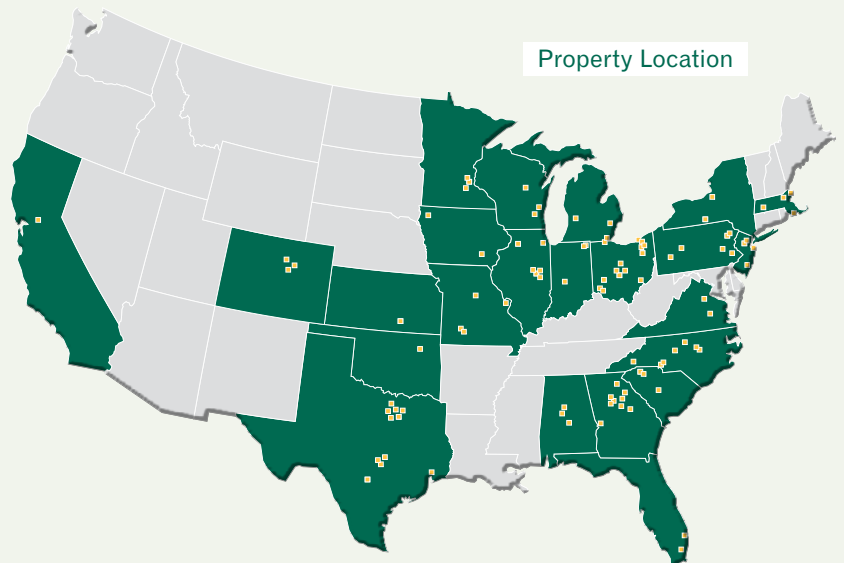
Terry L. Brubaker, *Vice Chairman and COO*



Bob Cutlip, *President*

## We currently own three types of real estate properties:

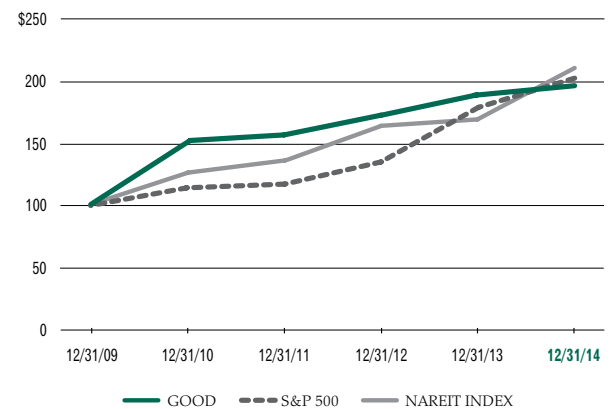
1. Real estate leased to tenants with small- and medium-sized unrated businesses, as well as larger rated businesses.
2. Real estate occupied by companies controlled by buyout funds. We are very familiar with the leveraged buyout business and are comfortable owning the real estate properties occupied by such tenants.
3. Real estate purchased from and leased back to businesses that are seeking to raise capital from the sale of their real estate so that they can invest the proceeds of the sale of their real estate into their business.



## PERFORMANCE MEASUREMENT COMPARISON

The following graph shows the total stockholder return on an investment of \$100 in cash on December 31, 2009 for (i) our common stock, (ii) the Standard and Poor's 500 Index (the "S&P 500") and (iii) the NAREIT Composite Index (the "NAREIT Index"). All values assume reinvestment of the full amount of all distributions.

### COMPARISON CUMULATIVE TOTAL RETURN ON INVESTMENT (in dollars)



	GOOD	S&P 500	NAREIT Index
12/31/09	\$100.00	\$100.00	\$100.00
12/31/10	\$153.86	\$115.06	\$127.58
12/31/11	\$156.17	\$117.49	\$136.86
12/31/12	\$173.99	\$136.30	\$164.44
12/31/13	\$188.76	\$180.44	\$169.71
12/31/14	\$196.23	\$205.14	\$215.78

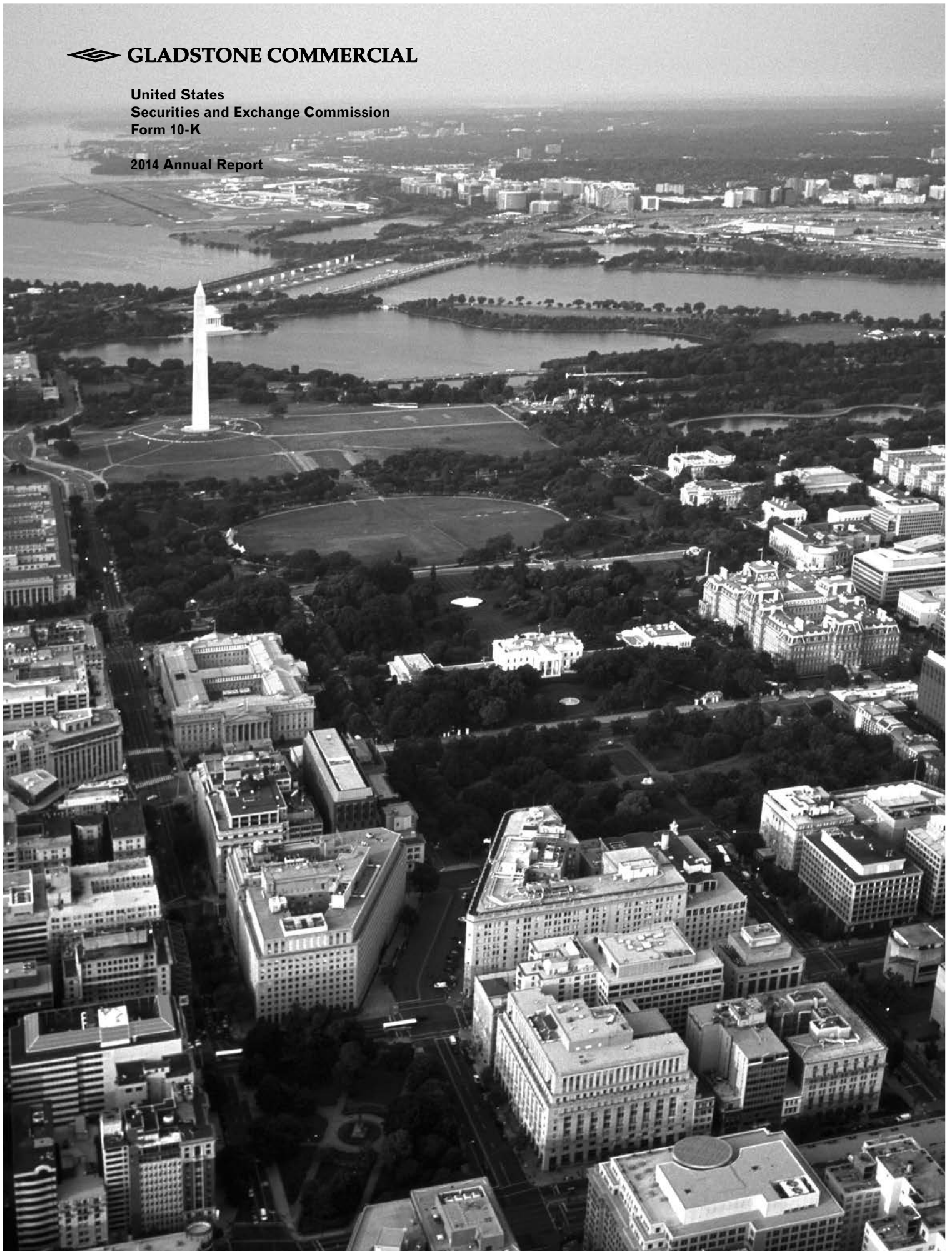
The total return performance shown in this graph is not necessarily indicative of and is not intended to suggest future total return performance.

This section is not "soliciting material," is not deemed "filed" with the Securities and Exchange Commission, and is not to be incorporated by reference in any of our filings under the Securities Act of 1933 or the Securities Exchange Act of 1934, whether made before or after the date hereof and irrespective of any general incorporation language contained in any such filing.

 **GLADSTONE COMMERCIAL**

**United States  
Securities and Exchange Commission  
Form 10-K**

**2014 Annual Report**



**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549**

**FORM 10-K**

**(Mark One)**

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
**For the fiscal year ended December 31, 2014**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**  
**Commission file number 001-33097**

**GLADSTONE COMMERCIAL CORPORATION**

(Exact name of registrant as specified in its charter)

**Maryland**

(State or other jurisdiction of  
incorporation or organization)

**1521 Westbranch Drive, Suite 100  
McLean, Virginia**

(Address of principal executive offices)

**02-0681276**

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

**22102**

(Zip Code)

**(703) 287-5800**

(Registrant's telephone number, including area code)

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

<u>(Title of each Class)</u>	<u>(Name of each exchange on which registered)</u>
Common Stock, \$0.001 par value per share	NASDAQ Global Select Market
7.75% Series A Cumulative Redeemable Preferred Stock, par value \$0.001 per share	NASDAQ Global Select Market
7.50% Series B Cumulative Redeemable Preferred Stock, par value \$0.001 per share	NASDAQ Global Select Market
7.125% Series C Cumulative Term Preferred Stock, par value \$0.001 per share	NASDAQ Global Select Market

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

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

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES  NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES  NO

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12 b-2 of the Act). YES  NO

The aggregate market value of the voting common stock held by non-affiliates of the Registrant on June 30, 2014, based on the closing price on that date of \$17.87 on the NASDAQ Global Select Market, was \$307,467,128. For the purposes of calculating this amount only, all directors and executive officers of the Registrant have been treated as affiliates. There were 20,359,081 shares of the Registrant's common stock, \$0.001 par value per share, outstanding as of February 18, 2015.

Documents Incorporated by Reference: Portions of the Registrant's Proxy Statement, to be filed no later than April 30, 2015, relating to the Registrant's 2015 Annual Meeting of Stockholders, are incorporated by reference into Part III of this Annual Report on Form 10-K.



**GLADSTONE COMMERCIAL CORPORATION**  
**FORM 10-K FOR THE YEAR ENDED**  
**DECEMBER 31, 2014**

**TABLE OF CONTENTS**

<b>PART I</b>	<b>PAGE</b>
Item 1. Business.	5
Item 1A. Risk Factors.	17
Item 1B. Unresolved Staff Comments.	32
Item 2. Properties.	33
Item 3. Legal Proceedings.	38
Item 4. Mine Safety Disclosures.	38
<b>PART II</b>	
Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.	39
Item 6. Selected Financial Data.	41
Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.	43
Item 7A. Quantitative and Qualitative Disclosures About Market Risk.	62
Item 8. Financial Statements and Supplementary Data.	63
Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure.	102
Item 9A. Controls and Procedures.	102
Item 9B. Other Information.	102
<b>PART III</b>	
Item 10. Directors, Executive Officers and Corporate Governance.	103
Item 11. Executive Compensation.	103
Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.	103
Item 13. Certain Relationships and Related Transactions, and Director Independence.	103
Item 14. Principal Accountant Fees and Services.	103
<b>PART IV</b>	
Item 15. Exhibits and Financial Statement Schedules.	104
SIGNATURES	108

## Forward-Looking Statements

Our disclosure and analysis in this Annual Report on Form 10-K, or Form 10-K, and the documents that are incorporated by reference herein, contain “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended, or Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or Exchange Act. We intend such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995 and include this statement for purposes of complying with these safe harbor provisions. Forward-looking statements relate to expectations, beliefs, projections, future plans and strategies, anticipated events or trends concerning matters that are not historical facts. These forward-looking statements include information about possible or assumed future events, including, among other things, discussion and analysis of our future financial condition, results of operations and funds from operations, or FFO, our strategic plans and objectives, cost management, occupancy and leasing rates and trends, liquidity and ability to refinance our indebtedness as it matures, anticipated capital expenditures (and access to capital) required to complete projects, amounts of anticipated cash distributions to our stockholders in the future and other matters. Words such as “anticipates,” “expects,” “intends,” “plans,” “believes,” “seeks,” “estimates,” “may” and variations of these words and similar expressions are intended to identify forward-looking statements, though not all forward-looking statements contain these words. These statements are not guarantees of future performance and are subject to risks, uncertainties and other factors, some of which are beyond our control, are difficult to predict and could cause actual results to differ materially from those expressed or forecasted in the forward-looking statements. Statements regarding the following subjects, among others, are forward-looking by their nature:

- re-leasing efforts;
- our business and financing strategy;
- our ability to implement our business plan;
- pending transactions;
- our projected operating results;
- our ability to obtain future financing arrangements;
- estimates relating to our future distributions;
- our understanding of our competition and our ability to compete effectively;
- market and industry trends;
- interest and insurance rates;
- estimates of our future operating expenses, including payments to our Adviser (as defined herein) under the terms of our Advisory Agreement (as defined herein);
- projected capital expenditures; and
- use of the proceeds of our Line of Credit (as defined herein), mortgage notes payable, future stock offerings and other future capital resources, if any.

Forward-looking statements involve inherent uncertainty and may ultimately prove to be incorrect or false. You are cautioned not to place undue reliance on forward-looking statements. Except as otherwise may be required by law, we undertake no obligation to update or revise forward-looking statements to reflect changed assumptions, the occurrence of unanticipated events or actual operating results. Our actual results

could differ materially from those anticipated in these forward-looking statements as a result of various factors, including, but not limited to:

- general volatility of the capital markets and the market price of our common and preferred stock;
- failure to qualify as a real estate investment trust, or REIT, and in the risk of changing laws that affect REITs;
- risks associated with negotiation and consummation of pending and future transactions;
- changes in our business strategy;
- the adequacy of our cash reserves and working capital;
- our failure to successfully integrate and operate acquired properties and operations;
- defaults upon or non-renewal of leases by tenants;
- decreased rental rates or increased vacancy rates;
- the degree and nature of our competition, including other real estate investment companies;
- availability, terms and deployment of capital, including the ability to maintain and borrow under our Line of Credit, arrange for long-term mortgages on our properties, secure additional long-term lines of credit and raise equity capital;
- our Adviser's ability to identify, hire and retain highly-qualified personnel;
- changes in our industry or the general economy;
- changes in real estate and zoning laws and increases in real property tax rates;
- changes in governmental regulations, tax rates and similar matters;
- environmental uncertainties and risks related to natural disasters; and
- the loss of any of our key officers, such as Mr. David Gladstone, our chairman and chief executive officer, Mr. Terry Lee Brubaker, our vice chairman and chief operating officer, or Mr. Robert Cutlip, our president.

This list of risks and uncertainties, however, is only a summary of some of the most important factors to us and is not intended to be exhaustive. You should carefully review the risks set forth herein under the caption "Item 1A. Risk Factors." New factors may also emerge from time to time that could have a material adverse affect on our business.

## **Item 1. Business.**

### **Overview**

Gladstone Commercial Corporation (which we refer to as “we,” “us,” or the “Company”) is a REIT that was incorporated under the General Corporation Laws of the State of Maryland on February 14, 2003, primarily for the purpose of investing in and owning net leased industrial, commercial and retail real property and selectively making long-term industrial and commercial mortgage loans. Our portfolio of real estate is leased to a wide cross section of tenants ranging from small businesses to large public companies, many of which are corporations that do not have publicly rated debt. As we have in the past, we intend to enter into, purchase agreements for real estate having triple net leases with terms of approximately 10 to 15 years and built-in rental increases. Under a triple net lease, the tenant is required to pay all operating, maintenance and insurance costs and real estate taxes with respect to the leased property. As of February 18, 2015, we owned a total of 96 properties.

We conduct substantially all of our activities, including the ownership of all of our properties, through Gladstone Commercial Limited Partnership, a Delaware limited partnership, which we refer to as our Operating Partnership. We control our Operating Partnership through our ownership of GCLP Business Trust II, a Massachusetts business trust, which is the general partner of our Operating Partnership, and of GCLP Business Trust I, a Massachusetts business trust, which currently holds all of the limited partnership units of our Operating Partnership. Our Operating Partnership may issue limited partnership units from time to time in exchange for industrial and commercial real property. Limited partners who hold limited partnership units in our Operating Partnership will generally be entitled to redeem these units for cash or, at our election, shares of our common stock on a one-for-one basis.

Our Operating Partnership is also the sole member of Gladstone Commercial Lending, LLC, which we refer to as Gladstone Commercial Lending. Gladstone Commercial Lending is a Delaware limited liability company that was formed to hold any real estate mortgage loans.

Our business is managed by our external adviser, Gladstone Management Corporation, or our Adviser. Gladstone Administration, LLC, or our Administrator, provides administrative services to us. Both our Adviser and our Administrator are affiliates of ours and each other.

### **Our Investment Objectives and Our Strategy**

Our principal investment objectives are to generate income from rental properties and, to a much lesser extent, mortgage loans, which we use to fund our continuing operations and to pay monthly cash distributions to our stockholders. Our primary strategy to achieve our investment objectives is to invest in and own a diversified portfolio of leased industrial, commercial and retail real estate that we believe will produce stable cash flow and increase in value. We may sell some of our real estate assets when our Adviser determines that doing so would be advantageous to us and our stockholders. We also expect to occasionally make mortgage loans secured by income-producing commercial, industrial or retail real estate, which loans may have some form of equity participation. We currently have one mortgage loan outstanding.

We use leverage to maximize potential returns to stockholders. We are not limited with respect to the amount of leverage that we may use for the acquisition of any specific property, although we have certain portfolio-level leverage covenants we must comply with under the terms of our unsecured line of credit, or the Line of Credit. We intend to use non-recourse mortgage financing that will allow us to limit our loss exposure on any property to the amount of equity invested in such property. The market for long-term mortgages continues to improve as they become more obtainable and the environment is competitive. The collateralized mortgage backed securities, or CMBS, market remains active but it is more conservative and restrictive than it was prior to the recent recession and uncertainty with regard to interest rates has made the CMBS market less predictable. Consequently, we continue to look to regional banks, insurance companies

and other non-bank lenders, in addition to the CMBS market, to issue mortgages to finance our real estate activities.

In addition to leverage, we were active in the equity markets during 2014 by issuing shares of common stock in one follow-on public offering, issuing shares under our at-the-market programs, or ATM Programs, pursuant to our former open market sale agreement with Jefferies, LLC, or Jefferies, and our current agreement with Cantor Fitzgerald & Co., or Cantor Fitzgerald, and also issuing shares of our convertible senior common stock.

## **Investment Policies**

### ***Types of Investments***

#### *Overview*

We intend that substantially all of our investments will be generated from the ownership of income-producing real property or, to a much lesser extent, mortgage loans secured by real property. We expect that a majority of our investments will be continue to be structured as net leases, but if a net lease would have an adverse impact on a potential tenant, or we assume a lease with a different existing structure in place, we may structure our investment as either a gross, or modified gross lease or as a mortgage loan. Investments are not restricted to geographical areas, but we expect that most of our investments in real estate will continue to be made within the continental United States. Some of our investments may also be made through joint ventures that would permit us to own interests in large properties without restricting the diversity of our portfolio. Our stockholders are not afforded the opportunity to evaluate the economic merits of our investments or the terms of any dispositions of properties and instead rely on the advice of our Adviser. See “*Risk Factors —Our success depends on the performance of our Adviser and if our Adviser makes inadvisable investment or management decisions, our operations could be materially adversely impacted.*”

We anticipate that we will make substantially all of our investments through our Operating Partnership and Gladstone Commercial Lending. Our Operating Partnership and Gladstone Commercial Lending may acquire interests in real property or mortgage loans in exchange for the issuance of limited partnership units, for cash or through a combination of both. Units issued by our Operating Partnership generally will be redeemable for cash or, at our election, shares of our common stock on a one-for-one basis. However, we may in the future also conduct some of our business and hold some of our interests in real properties or mortgage loans through one or more wholly-owned subsidiaries that are not owned, directly or indirectly, through our Operating Partnership or Gladstone Commercial Lending. We have not issued any limited partnership units to date.

#### *Property Acquisitions and Net Leasing*

To date, we have purchased a majority of our properties from owners that have leased their properties to non-affiliated tenants, and while we have engaged in some transactions with tenants who have consummated sale-leaseback transactions, these transactions do not comprise the dominant portion of our portfolio. We expect that some of our sale-leaseback transactions will be in conjunction with acquisitions, recapitalizations or other corporate transactions affecting our tenants. In these transactions, we may act as one of several sources of financing by purchasing one or more properties from the tenant and by leasing it on a net basis to the tenant or its successor in interest. For a discussion of the risks associated with leasing property to leveraged tenants, see “*Risk Factors—Highly leveraged tenants and borrowers may be unable to pay rent or make mortgage payments, which could adversely affect our cash available to make distributions to our stockholders.*”

In limited circumstances, we have granted tenants an option to purchase the leased property, and we anticipate granting these options to select tenants in the future. In these cases, we generally seek to fix the option purchase price at the greater of our purchase price for the property and the fair market value of the property at the time the option is exercised.

Our portfolio consists primarily of single-tenant commercial and industrial real property; however, we continue to acquire multi-tenant commercial and industrial properties, as well as retail and medical properties. Generally, we lease properties to tenants that our Adviser deems creditworthy under leases that will be full recourse obligations of our tenants or their affiliates. In most cases, our leases will be “triple net leases” that require the tenant to pay all the operating costs, costs of maintenance, insurance and real estate taxes on the property. We seek to obtain lease terms of approximately 10 to 15 years with built-in rental increases.

#### *Investments in Mortgage Loans*

Although we expect to make investments in mortgage loans sparingly, we may elect to structure our investment in a particular property as a mortgage loan secured by the property in situations where a standard net lease transaction would have an adverse tax impact on the seller or would otherwise be inappropriate for us. We anticipate that most of our lending transactions would be loans secured by industrial or commercial property or issued in connection with a build-to-suit transaction. Our Adviser will attempt to structure mortgage loans in a manner that would provide us with current income substantially similar to that which we could expect to receive had the investment been structured as a net lease transaction.

To the extent that we invest in mortgage loans, we will generally originate those loans. However, we may also purchase mortgage loans from banks, CMBS pools or other lenders provided that such transactions are otherwise consistent with our investment objectives. Our Adviser will service the mortgage loans in our portfolio by monitoring the collection of monthly principal and interest payments on our behalf. We currently have one mortgage loan outstanding.

#### *Underwriting Criteria, Due Diligence Process and Negotiating Lease Provisions*

We consider underwriting of the real estate and the tenant for the property (or the borrower in the case of a mortgage loan) to be the most important aspects of evaluating a prospective investment. Evaluating the creditworthiness of the tenant or borrower and its ability to generate sufficient cash flow to make payments to us pursuant to the lease or the mortgage loan is the one of the most important aspects of our underwriting procedures. In analyzing potential acquisitions of properties and leases, our Adviser reviews all aspects of the potential transaction, including tenant and real estate fundamentals, to determine whether potential acquisitions and leases can be structured to satisfy our acquisition criteria. The criteria listed below provide general guideposts that our Adviser may consider when underwriting leases and mortgage loans:

- *Credit Evaluation.* Our Adviser evaluates each potential tenant for its creditworthiness, considering factors such as the tenants rating by a national credit rating agency, if any, management experience, industry position and fundamentals, operating history and capital structure. Currently, 34% of our tenants are rated by a national credit rating agency. A prospective tenant that is deemed creditworthy does not necessarily mean that we will consider the tenant’s property to be “investment grade.” Our Adviser seeks tenants that range from small businesses, many of which do not have publicly rated debt, to large public companies. Our Adviser’s investment professionals have substantial experience in locating and financing these types of companies. By leasing properties to these tenants, we believe that we will generally be able to charge rent that is higher than the rent charged to tenants with unleveraged balance sheets and recognized credit, thereby enhancing current return from these properties as compared with properties leased to companies whose credit potential has already been recognized by the market. Furthermore, if a tenant’s credit improves, the value of our lease or investment will likely

increase (if all other factors affecting value remain unchanged). In evaluating a possible investment, we believe that the creditworthiness of a prospective tenant is normally a more significant factor than the unleased value of the property itself. While our Adviser selects tenants it believes to be creditworthy, tenants are not required to meet any minimum rating established by an independent credit rating agency. Our Adviser's standards for determining whether a particular tenant is creditworthy vary in accordance with a variety of factors relating to specific prospective tenants. The creditworthiness of a tenant is determined on a tenant-by-tenant and case-by-case basis. Therefore, general standards for creditworthiness cannot be applied.

- *Leases with Increasing Rent.* Our Adviser seeks to include a clause in each lease that provides for annual rent escalations over the term of the lease. These increases will generally be fixed; however certain of our leases are tied to increases in indices, such as the consumer price index.
- *Diversification.* Our Adviser attempts to diversify our portfolio to avoid dependence on any one particular tenant, facility type, geographic location or tenant industry. By diversifying our portfolio, our Adviser intends to reduce the adverse effect of a single under-performing investment or a downturn in any particular industry or geographic region. Please see Item 2 of this Form 10-K for a summary of our portfolio by industry and geographic location.
- *Property Valuation.* The business prospects and the financial strength of the tenant are important aspects of the evaluation of any sale and leaseback of property, or acquisition of property subject to a net lease, particularly a property that is specifically suited to the needs of the tenant. We generally require quarterly unaudited and annual audited financial statements of the tenant in order to continuously monitor the financial performance of the tenant. Our Adviser evaluates the financial capability of the tenant and its ability to perform per the terms of the lease, including obtaining certificates of insurance and verifying payment of real estate taxes on an annual basis. Our Adviser may also examine the available operating results of prospective investment properties to determine whether or not projected rental levels are likely to be met. As further described below, our Adviser also evaluates the physical characteristics of a prospective property investment and comparable properties as well as the geographic location of the property in the particular market to ensure that the characteristics are favorable for re-leasing the property at approximately the same or higher rental rate should that necessity arise. Our Adviser then computes the value of the property based on historical and projected operating results. In addition, each property that we propose to purchase is appraised by an independent appraiser. These appraisals may take into consideration, among other things, the terms and conditions of the particular lease transaction and the conditions of the credit markets at the time the purchase is negotiated. We generally limit the purchase price of each acquisition to less than 10% of our consolidated total assets.
- *Properties Important to Tenant Operations.* Our Adviser generally seeks to acquire investment properties that are essential or important to the ongoing operations of the prospective tenant. We believe that these investment properties provide better protection in the event a tenant files bankruptcy, as leases on properties essential or important to the operations of a bankrupt tenant are typically less likely to be rejected in bankruptcy or otherwise terminated.
- *Lease Provisions that Enhance and Protect Value.* When appropriate, our Adviser attempts to include provisions in our leases that require our consent to specified tenant activity or require the tenant to satisfy specific operating tests. These provisions may include, operational or financial covenants of the tenant, as well as indemnification of us by the tenant against environmental and other contingent liabilities. We believe that these provisions serve to protect our investments from changes in the operating and financial characteristics of a tenant that may impact its ability to satisfy its obligations to us or that could reduce the value of our properties. Our Adviser generally also seeks covenants requiring tenants to receive our consent prior to any change in control of the tenant.

- *Credit Enhancement.* Our Adviser may also seek to enhance the likelihood of a tenant's lease obligations being satisfied through a cross-default with other tenant obligations, a letter of credit or a guaranty of lease obligations from each tenant's corporate parent. We believe that this type of credit enhancement, if obtained, provides us with additional financial security.

#### *Underwriting of the Real Estate and Due Diligence Process*

In addition to underwriting the tenant or borrower, our Adviser also underwrites the real estate to be acquired or secured by one of our mortgages. On our behalf, our Adviser performs a due diligence review with respect to each property, such as evaluating the physical condition of a property, zoning and site requirements to ensure the property is in compliance with all zoning regulations as well as an environmental site assessment, in an attempt to determine potential environmental liabilities associated with a property prior to its acquisition, although there can be no assurance that hazardous substances or wastes (as defined by present or future federal or state laws or regulations) will not be discovered on the property after we acquire it. We could incur significant costs related to government regulation and private litigation over environmental matters. See "*Risk Factors – We could be exposed to liability and remedial costs related to environmental matters.*"

Our Adviser also reviews the structural soundness of the improvements on the property and may engage a structural engineer to review multiple aspects of the structures to determine the longevity of each building on the property. This review normally also includes the components of each building, such as the roof, the structure and configuration, the electrical wiring, the heating and air-conditioning system, the plumbing, parking lot and various other aspects such as compliance with state and federal building codes.

Our Adviser also physically inspects the real estate and surrounding real estate as part of determining its value. All of our Adviser's due diligence is aimed at arriving at a valuation of the real estate under the assumption that it would not be rented to the existing tenant. As part of this process, our Adviser may consider one or more of the following items:

- The comparable value of similar real estate in the same general area of the prospective property. In this regard, comparable property is difficult to define because each piece of real estate has its own distinct characteristics. But to the extent possible, comparable property in the area that has sold or is for sale will be used to determine if the price to be paid for the property is reasonable. The question of comparable properties' sale prices is particularly relevant if a property might be sold by us at a later date.
- An assessment of the relative flexibility of the building configuration and its ability to be re-leased to other users in a single or multiple tenant arrangement.
- The comparable real estate rental rates for similar properties in the same area of the prospective property.
- Alternative property uses that may offer higher value.
- The cost of replacing the property at current construction prices if it were to be sold.
- The assessed value as determined by the local real estate taxing authority.

In addition, our Adviser supplements its valuation with an independent real estate appraisal in connection with each investment that we consider. When appropriate, our Adviser may engage experts to undertake some or all of the due diligence efforts described above.



### *Use of Leverage*

We use long-term mortgage borrowings as a financing mechanism in amounts that we believe will maximize the return to our stockholders. Currently, the majority of our long-term mortgage borrowings are structured as non-recourse to us, and we intend to structure any medium-term mortgages in the same manner, with limited exceptions that would trigger recourse to us only upon the occurrence of certain fraud, misconduct, environmental or bankruptcy events. The use of non-recourse financing allows us to limit our exposure to the amount of equity invested in the properties pledged as collateral for our borrowings. Non-recourse financing generally restricts a lender's claim on the assets of the borrower, and as a result, the lender generally may look only to the property securing the debt for its satisfaction. We believe that this financing strategy, to the extent available, protects our other assets. However, we can provide no assurance that non-recourse financing will be available on terms acceptable to us, or at all, and consequently, there may be circumstances where lenders have recourse to our other assets. To a much lesser extent, we use recourse financing. Of the \$459.3 million in long-term mortgages outstanding as of December 31, 2014, only \$2.0 million is recourse to the Company.

We believe that, by operating on a leveraged basis, we will have more funds available and, therefore, will make more investments than would otherwise be possible if we operated on a non-leveraged basis. We believe that this creates a more diversified portfolio and maximizes potential returns to our stockholders. We may refinance properties during the term of a loan when we believe it is advantageous.

### **Conflict of Interest Policy**

We have adopted policies to reduce potential conflicts of interest. In addition, our directors are subject to certain provisions of Maryland law that are designed to minimize conflicts. However, we cannot assure you that these policies or provisions of law will reduce or eliminate the influence of these conflicts.

Under our current conflict of interest policy, without the approval of a majority of our independent directors, we will not:

- acquire from or sell any assets or other property to any of our officers, directors or our Adviser's employees, or any entity in which any of our officers, directors or Adviser's employees has an interest of more than 5%;
- borrow from any of our directors, officers or our Adviser's employees, or any entity, in which any of our officers, directors or our Adviser's employees has an interest of more than 5%; or
- engage in any other transaction with any of our directors, officers or our Adviser's employees, or any entity in which any of our directors, officers or our Adviser's employees has an interest of more than 5% (except that our Adviser may lease office space in a building that we own, provided that the rental rate under the lease is determined by our independent directors to be at a fair market rate).

Our policy also prohibits us from purchasing any real property owned by or co-investing with our Adviser, any of its affiliates or any business in which our Adviser or any of its subsidiaries have invested, except that we may lease property to existing and prospective portfolio companies of current or future affiliates, such as Gladstone Capital Corporation, Gladstone Land Corporation or Gladstone Investment Corporation and other entities advised by our Adviser, so long as that entity does not control the portfolio company and the transaction is approved by both companies' board of directors. If we decide to change this policy on co-investments with our Adviser or its affiliates, we will seek our stockholders' approval.

### *Future Revisions in Policies and Strategies*

Our independent directors periodically review our investment policies to evaluate whether they are in the best interests of us and our stockholders. Our investment procedures, objectives and policies may vary as new investment techniques are developed or as regulatory requirements change, and except as otherwise provided in our charter or bylaws, may be altered by a majority of our directors (including a majority of our independent directors) without the approval of our stockholders, to the extent that our Board of Directors determines that such modification is in the best interest of our stockholders. Among other factors, developments in the market which affect the policies and strategies described in this report or which change our assessment of the market may cause our Board of Directors to revise our investment policies and strategies.

### **Code of Ethics**

The Company and its affiliates, including Gladstone Capital Corporation, Gladstone Investment Corporation, Gladstone Land Corporation, Gladstone Management Corporation, Gladstone Administration, LLC, and Gladstone Securities, LLC have adopted a code of ethics and business conduct applicable to all personnel of such companies that complies with the guidelines set forth in Item 406 of Regulation S-K of the Securities Act of 1933, as amended. This code establishes procedures for personal investments, restricts certain transactions by such personnel and requires the reporting of certain transactions and holdings by such personnel. A copy of this code is available for review, free of charge, at our website at [www.GladstoneCommercial.com](http://www.GladstoneCommercial.com). We intend to provide any required disclosure of any amendments to or waivers of the provisions of this code by posting information regarding any such amendment or waiver to our website within four days of its effectiveness.

### **Our Adviser and Administrator**

Our business is managed by our Adviser. The officers, directors and employees of our Adviser have significant experience in making investments in and lending to businesses of all sizes, and investing in real estate and making mortgage loans. We have entered into an investment advisory agreement with our Adviser, or the Advisory Agreement, under which our Adviser is responsible for managing our assets and liabilities, for operating our business on a day-to-day basis and for identifying, evaluating, negotiating and consummating investment transactions consistent with our investment policies as determined by our Board of Directors from time to time. Gladstone Administration, LLC, or our Administrator, employs our chief financial officer, treasurer, chief compliance officer, general counsel (who also serves as our Administrator's president) and secretary and their respective staffs and provides administrative services for us under the Administration Agreement.

David Gladstone, our chairman and chief executive officer, is also the chairman, chief executive officer and the controlling stockholder of our Adviser and our Administrator. Terry Lee Brubaker, our vice chairman and chief operating officer and a member of our Board of Directors, also serves in the same capacities for our Adviser and our Administrator. Robert Cutlip, our president, is also an executive managing director of our Adviser.

Our Adviser maintains our investment committee that approves each of our investments. This investment committee is currently comprised of Messrs. Gladstone, Cutlip and Brubaker. We believe that the review process of our investment committee gives us a unique competitive advantage over other REITs because of the substantial experience that its members possess and their unique perspective in evaluating the blend of corporate credit, real estate and lease terms that collectively provide an acceptable risk for our investments.

Our Adviser's board of directors has empowered our investment committee to authorize and approve our investments, subject to the terms of the Advisory Agreement. Before we acquire any property, the transaction is reviewed by our investment committee to ensure that, in its view, the proposed transaction satisfies our investment criteria and is within our investment policies. Approval by our investment committee is generally the final step in the property acquisition approval process, although the separate

approval of our Board of Directors is required in certain circumstances described below. For further detail on this process, please see “*Investment Policies - Underwriting Criteria, Due Diligence Process and Negotiating Lease Provisions.*”

Our Adviser and Administrator are headquartered in McLean, Virginia, a suburb of Washington, D.C., and our Adviser also has offices in several other states.

### ***Advisory and Administration Agreements***

Many of the services performed by our Adviser and Administrator in managing our day-to-day activities are summarized below. This summary is provided to illustrate the material functions which our Adviser and Administrator perform for us pursuant to the terms of the Advisory and Administration Agreements, respectively.

#### ***Advisory Agreement***

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 some or all of such fees on to our tenants and borrowers).

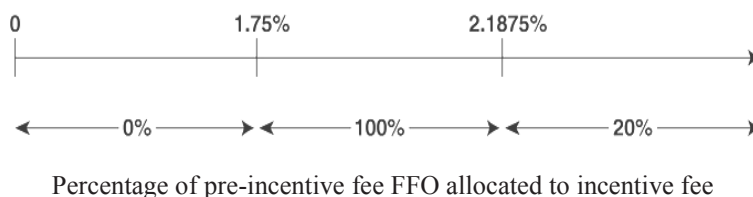
The Advisory Agreement provides for an annual base management fee equal to 2.0% of our total stockholders’ equity, less the recorded value of any preferred stock, and an incentive fee based on FFO. Our Adviser does not charge acquisition or disposition fees when we acquire or dispose of properties as is common in other externally managed REITs; however, our Adviser may earn fee income from our borrowers, tenants or other sources.

For purposes of calculating the incentive fee, FFO includes any realized capital gains and capital losses, less any distributions paid on preferred stock and convertible senior common stock, but FFO does not include any unrealized capital gains or losses. The incentive fee would reward our Adviser if our quarterly FFO, before giving effect to any incentive fee, or pre-incentive fee FFO, exceeds 1.75%, or the hurdle rate, of total stockholders’ equity, less the recorded value of any preferred stock. We pay our Adviser an incentive fee with respect to our pre-incentive fee FFO quarterly as follows:

- no incentive fee in any calendar quarter in which our pre-incentive fee FFO does not exceed the hurdle rate of 1.75% (7% annualized);
- 100% of the amount of the pre-incentive fee FFO that exceeds the hurdle rate, but is less than 2.1875% in any calendar quarter (8.75% annualized); and
- 20% of the amount of our pre-incentive fee FFO that exceeds 2.1875% in any calendar quarter (8.75% annualized).

### *Quarterly Incentive Fee Based on FFO*

Pre-incentive fee FFO  
(expressed as a percentage of total common stockholders' equity)



The incentive fee may be reduced because of our Line of Credit covenant which limits distributions to our stockholders to 100% of FFO with acquisition-related costs that are required to be expensed under Accounting Standards Codification, or ASC 805, Business Combinations, added back to FFO.

#### *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), and their respective staffs. Prior to July 1, 2014, our allocable portion was generally derived by multiplying that portion of the Administrator's expenses allocable to all funds managed by the Adviser by the percentage of our total assets at the beginning of each quarter in comparison to the total assets of all funds managed by the Adviser. As approved by our Board of Directors, effective July 1, 2014, 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. Management believes that the new methodology of allocating the Administrator's total expenses by approximate percentage of time services were performed among all companies serviced by our Administrator more closely approximates fees paid to actual services performed.

#### *Adviser Duties and Authority under the Advisory Agreement*

Under the terms of the Advisory Agreement, our Adviser is required to use its best efforts to present to us investment opportunities consistent with our investment policies and objectives as adopted by our Board of Directors. In performing its duties, our Adviser, either directly or indirectly by engaging an affiliate:

- finds, evaluates and enters into contracts to purchase real estate and make mortgage loans on our behalf in compliance with our investment procedures, objectives and policies, subject to approval of our Board of Directors, where required;
- provides advice to us and acts on our behalf with respect to the negotiation, acquisition, financing, refinancing, holding, leasing and disposition of real estate investments;
- takes the actions and obtains the services necessary to effect the negotiation, acquisition, financing, refinancing, holding, leasing and disposition of real estate investments; and
- provides day-to-day management of our business activities and other administrative services for us as requested by our Board of Directors.

Our Board of Directors has authorized our Adviser to make investments in any property on our behalf without the prior approval of our Board of Directors if the following conditions are satisfied:

- our Adviser has obtained an independent appraisal for the property indicating that the total cost of the property does not exceed its appraised value; and
- our Adviser has concluded that the property, in conjunction with our other investments and proposed investments, is reasonably expected to fulfill our investment objectives and policies as established by our Board of Directors then in effect.

The actual terms and conditions of transactions involving investments in properties and mortgage loans are determined at the sole discretion of our Adviser, subject at all times to compliance with the foregoing requirements. Some types of transactions, however, require the prior approval of our Board of Directors, including a majority of our independent directors, including the following:

- loans not secured or otherwise supported by real property;
- any acquisition or mortgage loan which at the time of investment would have a cost exceeding 20% of our total assets;
- transactions that involve conflicts of interest with our Adviser or other affiliates (other than reimbursement of expenses in accordance with the Advisory Agreement); and
- the lease of assets to our Adviser, its affiliates or any of our officers or directors.

Our Adviser and Administrator also engage in other business ventures and, as a result, their resources are not dedicated exclusively to our business. For example, our Adviser and Administrator also serve as the external adviser or administrator, respectively, to Gladstone Capital Corporation and Gladstone Investment Corporation, both publicly traded business development companies affiliated with us, and Gladstone Land Corporation, a publicly traded agricultural real estate company that is also our affiliate. However, under the Advisory Agreement, our Adviser is required to devote sufficient resources to the administration of our affairs to discharge its obligations under the agreement. The Advisory Agreement is not assignable or transferable by either us or our Adviser without the consent of the other party, except that our Adviser may assign the Advisory Agreement to an affiliate for whom our Adviser agrees to guarantee its obligations to us. Either we or our Adviser may assign or transfer the Advisory Agreement to a successor entity.

### **Gladstone Securities**

Gladstone Securities, LLC, or 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 controlled by Mr. David Gladstone, our chairman and chief executive officer. Mr. Gladstone also serves on the board of managers of Gladstone Securities.

### ***Dealer Manager Agreement***

In connection with the offering of our convertible senior common stock, or Senior Common Stock, we entered into a Dealer Manager Agreement, dated March 25, 2011, or the Dealer Manager Agreement, with Gladstone Securities, or the Dealer Manager, pursuant to which the Dealer Manager agreed to act as our exclusive dealer manager in connection with the offering. Pursuant to the terms of the Dealer Manager Agreement, the Dealer Manager is entitled to receive a sales commission in the amount of 7.0% of the gross proceeds of the shares of Senior Common Stock sold, plus a dealer manager fee in the amount of 3.0% of the gross proceeds of the shares of Senior Common Stock sold. Gladstone Securities, in its sole and absolute discretion, may re-allocate all of its selling commissions attributable to a participating broker-dealer and may also re-allocate a portion of its dealer manager fee earned in respect of the proceeds

generated by the participating broker-dealer to any participating broker-dealer as a non-accountable marketing allowance. In addition, we have agreed to indemnify the Dealer Manager against various liabilities, including certain liabilities arising under the federal securities laws. We made payments of approximately \$0.6 million and \$0.3 million during the years ended December 31, 2014 and 2013, respectively, to Gladstone Securities pursuant to this agreement, which are reflected as a component of Senior Common Stock costs in the statement of stockholders' equity. The Dealer Manager Agreement is scheduled to terminate on the earlier of (i) March 28, 2015 or (ii) the date on which 3,000,000 shares of Senior Common Stock are sold pursuant to the Dealer Manager Agreement. We have elected not to renew the program upon termination on March 28, 2015, and thus the Dealer Manager Agreement will simultaneously terminate on March 28, 2015.

### ***Mortgage Financing Arrangement Agreement***

We also 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. In connection with this engagement, Gladstone Securities may from time to time 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, will be 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 \$0.1 million for each of the years ended December 31, 2014 and 2013, respectively, on total mortgages secured of \$52.1 million and \$76.3 million, or 0.27% and 0.18%, respectively. The agreement is scheduled to terminate on August 31, 2015, unless renewed or earlier terminated.

### **Employees**

We do not currently have any employees and do not expect to have any employees in the foreseeable future. Currently, services necessary for our business are provided by individuals who are employees of our Adviser and our Administrator pursuant to the terms of the Advisory Agreement and the Administration Agreement, respectively. Each of our executive officers is an employee or officer, or both, of our Adviser or our Administrator. No employee of our Adviser or our Administrator will dedicate all of his or her time to us. However, we expect that a total of 15 to 20 full time employees of our Adviser and our Administrator will spend substantial time on our matters during calendar year 2015. To the extent that we acquire more investments, we anticipate that the number of employees of our Adviser and our Administrator who devote time to our matters will increase.

As of December 31, 2014, our Adviser and Administrator collectively had 61 full-time employees. A breakdown of these employees is summarized by functional area in the table below:

<u>Number of Individuals</u>	<u>Functional Area</u>
11	Executive Management
36	Investment Management, Portfolio Management and Due Diligence
14	Administration, Accounting, Compliance, Human Resources, Legal and Treasury

### **Competition**

We compete with a number of other real estate companies and traditional mortgage lenders, many of whom have greater marketing and financial resources than we do. Principal factors of competition in our primary business of investing in and owning leased industrial, commercial and retail real property are the quality of

properties, leasing terms, attractiveness and convenience of location. Additionally, our ability to compete depends upon, among other factors, trends of the national and local economies, investment alternatives, financial condition and operating results of current and prospective tenants and borrowers, availability and cost of capital, taxes and governmental regulations.

### **Available Information**

Copies of our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements and amendments, if any, to those reports filed or furnished with the Securities and Exchange Commission, or SEC, pursuant to Section 13(a) or 15(d) of the Securities Exchange Act are available free of charge through our website at [www.GladstoneCommercial.com](http://www.GladstoneCommercial.com). A request for any of these reports may also be submitted to us by sending a written request addressed to Investor Relations, Gladstone Commercial Corporation, 1521 Westbranch Drive, Suite 100, McLean, VA 22102, or by calling our toll-free investor relations line at 1-866-366-5745. The public may read and copy materials that we file with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. Information on the operation of the Public Reference Room may be obtained by calling the SEC at 1-800-SEC-0330. The SEC also maintains a website that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC at [www.sec.gov](http://www.sec.gov).

## **Item 1A. Risk Factors.**

*An investment in our securities involves a number of significant risks and other factors relating to our structure and investment objectives. As a result, we cannot assure you that we will achieve our investment objectives. You should consider carefully the following information before making an investment in our securities.*

### ***Risks related to our business and properties***

*Highly leveraged tenants and borrowers may be unable to pay rent or make mortgage payments, which could adversely affect our cash available to make distributions to our stockholders.*

Some of our tenants and borrowers may have recently been either restructured using leverage, or acquired in a leveraged transaction. Tenants and borrowers that are subject to significant debt obligations may be unable to make their rent or mortgage payments if there are adverse changes to their businesses or because of the impact of the recent recession. Tenants that have experienced leveraged restructurings or acquisitions will generally have substantially greater debt and substantially lower net worth than they had prior to the leveraged transaction. In addition, the payment of rent and debt service may reduce the working capital available to leveraged entities and prevent them from devoting the resources necessary to remain competitive in their industries.

In situations where management of the tenant or borrower will change after a transaction, it may be difficult for our Adviser to determine with reasonable certainty the likelihood of the tenant's or borrower's business success and of its ability to pay rent or make mortgage payments throughout the lease or loan term. These companies generally are more vulnerable to adverse economic and business conditions, and increases in interest rates.

*We are subject to the credit risk of our tenants, which in the event of bankruptcy, could adversely affect our results of operations.*

We are subject to the credit risk of our tenants . Any bankruptcy of a tenant or borrower could cause:

- the loss of lease or mortgage payments to us;
- an increase in the costs we incur to carry the property occupied by such tenant;
- a reduction in the value of our securities; or
- a decrease in distributions to our stockholders.

Under bankruptcy law, a tenant who is the subject of bankruptcy proceedings has the option of continuing or terminating any unexpired lease. If a bankrupt tenant terminates a lease with us, any claim we might have for breach of the lease (excluding a claim against collateral securing the lease) will be treated as a general unsecured claim. Our claim would likely be capped at the amount the tenant owed us for unpaid rent prior to the bankruptcy unrelated to the termination, plus the greater of one year's lease payments or 15% of the remaining lease payments payable under the lease (but no more than three years' lease payments). In addition, due to the long-term nature of our leases and terms providing for the repurchase of a property by the tenant, a bankruptcy court could re-characterize a net lease transaction as a secured lending transaction. If that were to occur, we would not be treated as the owner of the property, but might have additional rights as a secured creditor.

In addition, we may enter into in sale-leaseback transactions, whereby we would purchase a property and then lease the same property back to the person from whom we purchased it. In the event of the bankruptcy of a tenant, a transaction structured as a sale-leaseback may be re-characterized as either a financing or a joint venture, either of which outcomes could adversely affect our business. If the sale-leaseback were re-characterized as a financing, we might not be considered the owner of the property, and as a result would have the status of a creditor in relation to the tenant. In that event, we would no longer have the right to sell



or encumber our ownership interest in the property. Instead, we would have a claim against the tenant for the amounts owed under the lease, with the claim arguably secured by the property. The tenant/debtor might have the ability to propose a plan restructuring the term, interest rate and amortization schedule of its outstanding balance. If confirmed by the bankruptcy court, we could be bound by the new terms, and prevented from foreclosing our lien on the property. If the sale-leaseback were re-characterized as a joint venture, we could be treated as a co-venturer with our lessee with regard to the property. As a result, we could be held liable, under some circumstances, for debts incurred by the lessee relating to the property. Either of these outcomes could adversely affect our cash flow and our ability to pay distributions to stockholders.

*We may be unable to renew leases, lease vacant space or re-lease space as leases expire, which could adversely affect our business and our ability to make distributions to our stockholders.*

If we cannot renew leases, we may be unable to re-lease our properties to other tenants at rates equal to or above the current market rate. Even if we can renew leases, tenants may be able to negotiate lower rates as a result of market conditions. Market conditions may also hinder our ability to lease vacant space in newly developed or redeveloped properties. In addition, we may enter into or acquire leases for properties that are specially suited to the needs of a particular tenant. Such properties may require renovations, tenant improvements or other concessions in order to lease them to other tenants if the initial leases terminate. We may be required to expend substantial funds for tenant improvements and tenant refurbishments to re-lease the vacated space and cannot assure you that we will have sufficient sources of funding available to use in the future for such purposes and therefore may have difficulty in securing a replacement tenant. Any of these factors could adversely impact our financial condition, results of operations, cash flow or our ability to pay distributions to our stockholders.

*Net leases may not result in fair market lease rates over time, thereby failing to maximize income and distributions to our stockholders.*

A large portion of our rental income comes from triple net leases, which frequently provide the tenant greater discretion in using the leased property than ordinary property leases, such as the right to sublease the property, subject to our approval, to make alterations in the leased premises and to terminate the lease prior to its expiration under specified circumstances. Further, triple net leases are typically for longer lease terms and, thus, there is an increased risk that contractual rental increases in future years will fail to result in fair market rental rates during those years. As a result, our income and distributions to our stockholders could be lower than they would otherwise be if we did not engage in triple net leases.

*Multi-tenant properties expose us to additional risks.*

Our multi-tenant properties could expose us to the risk that a sufficient number of suitable tenants may not be found to enable the property to operate profitably. This loss of income could cause a material adverse impact to our results of operations and business. Multi-tenant properties are also subject to tenant turnover and fluctuation in occupancy rates, which could affect our operating results. Furthermore, multi-tenant properties expose us to the risk of increased operating expenses, which may occur when the actual cost of taxes, insurance and maintenance at the property exceeds the operating expenses paid by tenants and/or the amounts budgeted.

*We face certain risks associated with our build-to-suit activities.*

We may (1) provide a developer with either a combination of financing for construction of a build-to-suit property or a commitment to acquire a property upon completion of construction of a build-to-suit property and commencement of rent from the tenant or (2) acquire a property subject to a lease and engage a developer to complete construction of a build-to-suit property as required by the lease. We face uncertainties associated with a developer's timely performance and timely completion of a project, including the performance or timely completion of contractors and subcontractors. If a developer, contractor or subcontractor fails to perform, we may resort to legal action to compel performance, remove the developer or rescind the purchase or construction contract.

We may incur additional risks as we make periodic payments or other advances to developers before completion of construction. These and other factors can result in increased costs of a project or loss of our investment, and may be affected by conditions beyond both our and the developer's control.

*Illiquidity of real estate investments may make it difficult for us to sell properties in response to market conditions and could harm our financial condition and ability to make distributions to our stockholders.*

To the extent the properties are not subject to triple-net leases, some significant expenditures, such as real estate taxes and maintenance costs, are generally not reduced when circumstances cause a reduction in income from the investment. Should these events occur, our income and funds available for distribution could be adversely affected. In addition, as a REIT, we may be subject to a 100% tax on net income derived from the sale of property considered to be held primarily for sale to customers in the ordinary course of our business. We may seek to avoid this tax by complying with certain safe harbor rules that generally limit the number of properties we may sell in a given year, the aggregate expenditures made on such properties prior to their disposition, and how long we retain such properties before disposing of them. However, we can provide no assurance that we will always be able to comply with these safe harbors. If compliance is possible, the safe harbor rules may restrict our ability to sell assets in the future and achieve liquidity that may be necessary to fund distributions.

*Our real estate investments may include special use and single or multi-tenant properties that may be difficult to sell or re-lease upon tenant defaults or early lease terminations.*

We focus our investments on commercial, industrial and retail properties, a number of which include manufacturing facilities, special use storage or warehouse facilities and special use single or multi-tenant properties. These types of properties are relatively illiquid compared to other types of real estate and financial assets. This illiquidity will limit our ability to quickly change our portfolio in response to changes in economic or other conditions. With these properties, if the current lease is terminated or not renewed or, in the case of a mortgage loan, if we take such property in foreclosure, we may be required to renovate the property or to make rent concessions in order to lease the property to another tenant or sell the property. In addition, in the event we are forced to sell the property, we may have difficulty selling it to a party other than the tenant or borrower due to the special purpose for which the property may have been designed.

These and other limitations may affect our ability to sell or re-lease properties without adversely affecting returns to our stockholders.

*Many of our tenants are small and medium sized businesses, which exposes us to additional risks unique to these entities.*

Leasing real property or making mortgage loans to small and medium-sized businesses exposes us to a number of unique risks related to these entities, including the following:

- *Small and medium-sized businesses may have limited financial resources and may not be able to make their lease or mortgage payments on a timely basis, or at all.* A small or medium-sized tenant or borrower may be more likely to have difficulty making its lease or mortgage payments when it experiences adverse events, such as the failure to meet its business plan, a downturn in its industry or negative economic conditions because its financial resources may be more limited.
- *Small and medium-sized businesses typically have narrower product lines and smaller market shares than large businesses.* Because our target tenants and borrowers are typically smaller businesses that may have narrower product lines and smaller market share, they may be more vulnerable to competitors' actions and market conditions, as well as general economic downturns.

- *There is generally little or no publicly available information about our target tenants and borrowers.* Many of our tenants and borrowers are likely to be privately owned businesses, about which there is generally little or no publicly available operating and financial information. As a result, we will rely on our Adviser to perform due diligence investigations of these tenants and borrowers, their operations and their prospects. We may not learn all of the material information we need to know regarding these businesses through our investigations.
- *Small and medium-sized businesses generally have less predictable operating results.* We expect that many of our tenants and borrowers may experience significant fluctuations in their operating results, may from time to time be parties to litigation, may be engaged in rapidly changing businesses with products subject to a substantial risk of obsolescence, may require substantial additional capital to support their operations, to finance expansion or to maintain their competitive positions, may otherwise have a weak financial position or may be adversely affected by changes in the business cycle.
- *Small and medium-sized businesses are more likely to be dependent on one or two persons.* Typically, the success of a small or medium-sized business also depends on the management talents and efforts of one or two persons or a small group of persons. The death, disability or resignation of one or more of these persons could have a material adverse impact on our tenant or borrower and, in turn, on us.

*Our real estate investments have a limited number of tenants and are concentrated in a limited number of industries, which subjects us to an increased risk of significant loss if any one of these tenants is unable to pay or if particular industries experience downturns.*

As of December 31, 2014, we owned 96 properties and had 91 tenants in these properties, and our 5 largest tenants accounted for approximately 18.0% of our total rental income. A consequence of a limited number of tenants is that the aggregate returns we realize may be materially adversely affected by the unfavorable performance of a small number of tenants. We do not have fixed guidelines for industry concentration and our investments could potentially be concentrated in relatively few industries. As of December 31, 2014, 17.7% of our total rental income was earned from tenants in the telecommunications industry, 12.2% was earned from tenants in the healthcare industry, and 12.1% was earned from tenants in the automobile industry. As a result, a downturn in an industry in which we have invested a significant portion of our total assets could have a material adverse effect on us.

*Healthcare reform legislation may affect our results of operations and financial condition.*

In 2010, the President of the United States signed into law the Patient Protection and Affordable Care Act of 2010 and the Health Care and Education Reconciliation Act, which in part modified the Patient Protection and Affordable Care Act (collectively the “Acts”). Together, the Acts serve as the primary vehicle for comprehensive health care reform in the U.S. and are intended to reduce the number of individuals in the U.S. without health insurance and effect significant other changes to the ways in which health care is organized, delivered and reimbursed. The complexities and ramifications of the new legislation are significant, and have begun being implemented through a phased approach that will conclude in 2018. At this time, the effects of health care reform and its impact on our tenants’ business, results of operations and financial condition and the resulting impact on our operations cannot be determined. The Acts could adversely affect the financial and operational performance of our tenants in the healthcare industry specifically and increase the cost of providing healthcare coverage for all tenants generally and could adversely affect the financial and operational performance of our tenants and their results of operations. This may result in a decreased ability of our tenants to make lease payments, and thereby adversely affect our liquidity, financial condition, results of operations and ability to pay distributions to our stockholders.

*The inability of a tenant in a single tenant property to pay rent will reduce our revenues and increase our carrying costs of the building.*

Since most of our properties are occupied by a single tenant, the success of each investment will be materially dependent on the financial stability of these tenants. If a tenant defaults, our rental revenues would be reduced and our expenses associated with carrying the property would increase, as we would be responsible for payments such as taxes and insurance. Lease payment defaults by these tenants could adversely affect our cash flows and cause us to reduce the amount of distributions to stockholders. In the event of a default by a tenant, we may experience delays in enforcing our rights as landlord and may incur substantial costs in protecting our investment and re-leasing our property. If a lease is terminated, there is no assurance that we will be able to lease the property for the rent previously received or sell the property without incurring a loss.

*Liability for uninsured losses could adversely affect our financial condition.*

Losses from disaster-type occurrences (such as wars, floods or earthquakes) may be either uninsurable or not insurable on economically viable terms. Should such a loss occur, we could lose our capital investment or anticipated profits and cash flow from one or more properties.

*We could incur significant costs related to government regulation and private litigation over environmental matters.*

Under various environmental laws, including the Comprehensive Environmental Response, Compensation and Liability Act, or CERCLA, a current or previous owner or operator of real property may be liable for contamination resulting from the release or threatened release of hazardous or toxic substances or petroleum at that property, and an entity that arranges for the disposal or treatment of a hazardous or toxic substance or petroleum at another property may be held jointly and severally liable for the cost to investigate and clean up such property or other affected property. Such parties are known as potentially responsible parties, or PRPs. Environmental laws often impose liability without regard to whether the owner or operator knew of, or was responsible for, the presence of the contaminants, and the costs of any required investigation or cleanup of these substances can be substantial. PRPs are liable to the government as well as to other PRPs who may have claims for contribution. The liability is generally not limited under such laws and could exceed the property's value and the aggregate assets of the liable party. The presence of contamination or the failure to remediate contamination at our properties also may expose us to third-party liability for personal injury or property damage, or adversely affect our ability to sell, lease or develop the real property or to borrow using the real property as collateral.

Environmental laws also impose ongoing compliance requirements on owners and operators of real property. Environmental laws potentially affecting us address a wide variety of matters, including, but not limited to, asbestos-containing building materials, storage tanks, storm water and wastewater discharges, lead-based paint, wetlands and hazardous wastes. Failure to comply with these laws could result in fines and penalties and/or expose us to third-party liability. Some of our properties may have conditions that are subject to these requirements, and we could be liable for such fines or penalties and/or liable to third parties for those conditions.

*We could be exposed to liability and remedial costs related to environmental matters.*

Certain of our properties may contain, or may have contained, asbestos-containing building materials, or ACBMs. Environmental laws require that ACBMs be properly managed and maintained and may impose fines and penalties on building owners and operators for failure to comply with these requirements. Also, certain of our properties may contain, or may have contained, or are adjacent to or near other properties that have contained or currently contain storage tanks for the storage of petroleum products or other hazardous or toxic substances. These operations create a potential for the release of petroleum products or other hazardous or toxic substances. Certain of our properties may contain, or may have contained, elevated radon levels. Third parties may be permitted by law to seek recovery from owners or operators for property damage and/or personal injury associated with exposure to contaminants, including, but not limited to, petroleum products, hazardous or toxic substances and asbestos fibers. Also, certain of our properties may

contain regulated wetlands that can delay or impede development or require costs to be incurred to mitigate the impact of any disturbance. Absent appropriate permits, we can be held responsible for restoring wetlands and be required to pay fines and penalties.

Certain of our properties may contain, or may have contained, microbial matter such as mold and mildew. The presence of microbial matter could adversely affect our results of operations. In addition, if any of our property is not properly connected to a water or sewer system, or if the integrity of such systems are breached, or if water intrusion into our buildings otherwise occurs, microbial matter or other contamination can develop. When excessive moisture accumulates in buildings or on building materials, mold growth may occur, particularly if the moisture problem remains undiscovered or is not addressed over a period of time. Some molds may produce airborne toxins or irritants. If this were to occur, we could incur significant remedial costs and we may also be subject to material private damage claims and awards. Concern about indoor exposure to mold has been increasing, as exposure to mold may cause a variety of adverse health effects and symptoms, including allergic or other reactions. If we become subject to claims in this regard, it could materially and adversely affect us and our future insurability for such matters.

The assessments we perform on our acquisition of property may fail to reveal all environmental conditions, liabilities or compliance concerns. Material environmental conditions, liabilities or compliance concerns may have arisen after the assessments were conducted or may arise in the future, and future laws, ordinances or regulations may impose material additional environmental liability. We cannot assure you that costs of future environmental compliance will not affect our ability to make distributions or that such costs or other remedial measures will not be material to us.

*Our properties may be subject to impairment charges, which could adversely affect our results of operations.*

We are required to periodically evaluate our properties for impairment indicators. A property's value is considered impaired if management's estimate of the aggregate future cash flows (undiscounted and without interest charges) to be generated by the property, based upon its intended use, is less than the carrying value of the property. These estimates of cash flows are based upon factors such as expected future operating income, trends and prospects, as well as the effects of interest and capitalization rates, demand and occupancy, competition and other factors. These factors may result in uncertainty in valuation estimates and instability in the estimated value of our properties which, in turn, could result in a substantial decrease in the value of the properties and significant impairment charges.

We continually assess our properties to determine if any impairments are necessary or appropriate. No assurance can be given that we will be able to recover the current carrying amount of our properties in the future. Our failure to do so would require us to recognize additional impairment charges for the period in which we reached that conclusion, which could materially and adversely affect us and our results of operations.

*Mortgage loans may be affected by unfavorable real estate market conditions, including interest rate fluctuations, which could decrease the value of those loans and our results of operations.*

Investments in mortgage loans, exposes us to the risk of default by the borrowers on those mortgage loans as well as interest rate risks. To the extent we incur delays in liquidating such defaulted mortgage loans, we may not be able to obtain sufficient proceeds to repay all amounts due to us under the mortgage loans. Further, we will not know whether the values of the properties securing the mortgage loans will remain at the levels existing on the dates of origination of those mortgage loans. If the values of the underlying properties fall, our risk will increase because of the lower value of the security associated with such loans. We currently have one mortgage loan outstanding.

### ***Risks related to our financing***

*Capital markets and economic conditions can materially affect our financial condition and results of operations, the value of our equity securities, and our ability to sustain payment of our distribution at current levels.*

Many factors affect the value of our equity securities and our ability to make or maintain at current levels distributions to the holders of our shares of beneficial interest, including the state of the capital markets and the economy, which in recent years have negatively affected substantially all businesses, including ours. Demand for office, industrial, and retail space nationwide has slowly improved, it is approaching pre-recession levels. The availability of credit has been and may in the future again be adversely affected by illiquid credit markets. Regulatory pressures and the burden of troubled and uncollectible loans led some lenders and institutional investors to reduce, and in some cases, cease to provide funding to borrowers. If these market conditions recur, they may limit our ability and the ability of our tenants to timely refinance maturing liabilities and access the capital markets to meet liquidity needs, which may materially affect our financial condition and results of operations and the value of our equity securities and our ability to sustain payment of our distribution at current levels.

*Our Line of Credit contains various covenants which, if not complied with, could accelerate our repayment obligations, thereby materially and adversely affecting our liquidity, financial condition, results of operations and ability to pay distributions to stockholders.*

The agreement governing our Line of Credit requires us to comply with certain financial and operational covenants. These covenants require us to, among other things, maintain certain financial ratios, including fixed charge coverage, debt service coverage and a minimum net worth. We are also required to limit our distributions to stockholders to 100% of our FFO. As of December 31, 2014, we were in compliance with these covenants. However, our continued compliance with these covenants depends on many factors, and could be impacted by current or future economic conditions, and thus there are no assurances that we will continue to comply with these covenants. Failure to comply with these covenants would result in a default which, if we were unable to obtain a waiver from the lenders, could accelerate our repayment obligations under the Line of Credit and thereby have a material adverse impact on our liquidity, financial condition, results of operations and ability to pay distributions to stockholders.

*Our business strategy relies heavily on external financing, as a result we may be negatively affected by restrictions on additional borrowings, and the risks associated with leverage, including our debt service obligations.*

We use leverage so that we may make more investments than would otherwise be possible in order to maximize potential returns to stockholders. If the income generated by our properties and other assets fails to cover our debt service, we could be forced to reduce or eliminate distributions to our stockholders and may experience losses.

Our ability to achieve our investment objectives will be affected by our ability to borrow money in sufficient amounts and on favorable terms. We expect that we will borrow money that will be secured by our properties and that these financing arrangements will contain customary covenants such as those that limit our ability, without the prior consent of the lender, to further mortgage the applicable property or to discontinue insurance coverage. Accordingly, we may be unable to obtain the degree of leverage we believe to be optimal, which may cause us to have less cash for distribution to stockholders than we would have with an optimal amount of leverage. Our use of leverage could also make us more vulnerable to a downturn in our business or the economy, as it may become difficult to meet our debt service obligations if our cash flows are reduced due to tenant defaults. There is also a risk that a significant increase in the ratio of our indebtedness to the measures of asset value used by financial analysts may have an adverse effect on the market price of our securities.

*We face risks related to “balloon payments” and refinancing.*

Some of our debt financing arrangements may require us to make lump-sum or “balloon” payments at maturity. Our ability to make a balloon payment at maturity is uncertain and may depend upon our ability to obtain additional financing or to sell the financed property. At the time the balloon payment is due, we may not be able to refinance the balloon payment on terms as favorable as the original loan or sell the property at a price sufficient to make the balloon payment, which could adversely affect the amount of distributions to our stockholders. We have balloon payments of \$34.6 million payable during fiscal year 2015.

*We mortgage our properties, which subjects us to the risk of foreclosure in the event of non-payment.*

We intend to acquire additional properties by using our Line of Credit and by continuing to seek long-term financing, where we will borrow all or a portion of the purchase price of a potential acquisition and securing the loan with a mortgage on some or all of our existing real property. We look to regional banks, insurance companies and other non-bank lenders, and, to a lesser extent, the CMBS market to issue mortgages to finance our real estate activities. For the year ended December 31, 2014, we had obtained or assumed approximately \$62.2 million in long-term financing, which we have used to acquire additional properties. If we are unable to make our debt payments as required, a lender could foreclose on the property securing its loan. This could cause us to lose part or all of our investment in such property which in turn could cause the value of our securities or the amount of distributions to our stockholders to be reduced.

*We face a risk from the fact that certain of our properties are cross-collateralized.*

As of December 31, 2014, the mortgages on certain of our properties were cross-collateralized. To the extent that any of the properties in which we have an interest are cross-collateralized, any default by the property owner subsidiary under the mortgage note relating to the one property will result in a default under the financing arrangements relating to any other property that also provides security for that mortgage note or is cross-collateralized with such mortgage note.

*A change in the value of our assets could cause us to experience a cash shortfall or be in default of our loan covenants.*

We borrow on an unsecured basis under the Line of Credit. A significant reduction in the value of our pool of unencumbered assets could require us to pay down the balance of the Line of Credit. Although we believe that we have significant excess collateral and capacity, future asset values are uncertain. If we were unable to meet a request to add collateral to the Line of Credit, this inability could have a material adverse effect on our liquidity and our ability to meet our loan covenants.

*Interest rate fluctuations may adversely affect our results of operations.*

We may experience interest rate volatility in connection with mortgage loans on our properties or other variable-rate debt that we may obtain from time to time. Certain of our leases contain escalations based on market interest rates and the interest rate on our Line of Credit and one of our long-term mortgages is variable. Although we seek to mitigate this risk by structuring such provisions to contain a minimum interest rate or escalation rate, as applicable, these features do not eliminate this risk. We are also exposed to the effects of interest rate changes as a result of holding cash and cash equivalents in short-term, interest-bearing investments. We have entered into an interest rate cap to attempt to manage our exposure to interest rate fluctuations on our only outstanding variable rate mortgage. A significant change in interest rates could have an adverse impact on our results of operations.

### ***Risks related to the real estate industry***

*We are subject to certain risks associated with real estate ownership and lending which could reduce the value of our investments.*

Our investments include industrial, commercial and retail property. Our performance, and the value of our investments, is subject to risks inherent to the ownership and operation of these types of properties, including:

- changes in the general economic climate;
- changes in local conditions, such as an oversupply of space or reduction in demand for real estate;
- changes in interest rates and the availability of financing;
- competition from other available space; and
- changes in laws and governmental regulations, including those governing real estate usage, zoning and taxes.

The debt obligations of our tenants are dependent upon certain factors, which neither we nor our tenants or borrowers control, such as national, local and regional business and economic conditions, government economic policies, and the level of interest rates.

*Competition for the acquisition of real estate may impede our ability to make acquisitions or increase the cost of these acquisitions.*

We compete with many other entities to acquire properties, including financial institutions, institutional pension funds, other REITs, foreign real estate investors, other public and private real estate companies and private real estate investors. These competitors may prevent us from acquiring desirable properties, cause an increase in the price we must pay for real estate, have greater resources than we do, and may be willing to pay more for certain assets or may have a more compatible operating philosophy with our acquisition targets. In particular, larger REITs may enjoy significant competitive advantages that result from, among other things, a lower cost of capital and enhanced operating efficiencies. Our competitors may also adopt transaction structures similar to ours, which would decrease our competitive advantage in offering flexible transaction terms. In addition, the number of entities and the amount of funds competing for suitable investment properties may increase, resulting in increased demand and increased prices paid for these properties.

*Our ownership of properties through ground leases exposes us to risks which are different than those resulting from our ownership of fee title to other properties.*

We have acquired an interest in three of our properties by acquiring a leasehold interest in the land underlying the property, and we may acquire additional properties in the future that are subject to similar ground leases. In this situation, we have no economic interest in the land underlying the property and do not control this land, thus this type of ownership interest poses potential risks for our business because (i) if the ground lease terminates for any reason, we will lose our interest in the property, including any investment that we made in the property, (ii) if our tenant defaults under the previously existing lease, we will continue to be obligated to meet the terms and conditions of the ground lease without the annual amount of ground lease payments reimbursable to us by the tenant, and (iii) if the third party owning the land under the ground lease disrupts our use either permanently or for a significant period of time, then the value of our assets could be impaired and our results of operations could be adversely affected.



### ***Risks related to our Adviser***

*We are dependent upon our key personnel, who are employed by our Adviser, for our future success, particularly David Gladstone, Terry Lee Brubaker and Robert Cutlip.*

We are dependent on our senior management and other key management members to carry out our business and investment strategies. Our future success depends to a significant extent on the continued service and coordination of our senior management team, particularly David Gladstone, our chairman and chief executive officer, Terry Lee Brubaker, our vice chairman and chief operating officer, and Robert Cutlip, our president. The departure of any of our executive officers or key personnel could have a material adverse effect on our ability to implement our business strategy and to achieve our investment objectives.

*Our success depends on the performance of our Adviser and if our Adviser makes inadvisable investment or management decisions, our operations could be materially adversely impacted.*

Our ability to achieve our investment objectives and to pay distributions to our stockholders is dependent upon the performance of our Adviser in evaluating potential investments, selecting and negotiating property purchases and dispositions and mortgage loans, selecting tenants and borrowers, setting lease or mortgage loan terms and determining financing arrangements. Accomplishing these objectives on a cost-effective basis is largely a function of our Adviser's marketing capabilities, management of the investment process, ability to provide competent, attentive and efficient services and our access to financing sources on acceptable terms. Our stockholders have no opportunity to evaluate the terms of transactions or other economic or financial data concerning our investments and must rely entirely on the analytical and management abilities of our Adviser and the oversight of our Board of Directors. If our Adviser or our Board of Directors makes inadvisable investment or management decisions, our operations could be materially adversely impacted. As we grow, our Adviser may be required to hire, train, supervise and manage new employees. Our Adviser's failure to effectively manage our future growth could have a material adverse effect on our business, financial condition and results of operations.

*We may have conflicts of interest with our Adviser and other affiliates.*

Our Adviser manages our business and locates, evaluates, recommends and negotiates the acquisition of our real estate investments. At the same time, our Advisory Agreement permits our Adviser to conduct other commercial activities and provide management and advisory services to other entities, including, but not limited to, Gladstone Capital Corporation, or Gladstone Capital, Gladstone Investment Corporation, or Gladstone Investment, and Gladstone Land Corporation, or Gladstone Land. Moreover, with the exception of our chief financial officer, and president, all of our executive officers and directors are also executive officers and directors of Gladstone Capital and Gladstone Investment, which actively make loans to and invest in small and medium-sized companies. In addition, with the exception of our president, all of our executive officers and eight of our nine directors are also executive officers and directors of Gladstone Land. As a result, we may from time to time have conflicts of interest with our Adviser in its management of our business and with Gladstone Capital, Gladstone Investment and Gladstone Land, which may arise primarily from the involvement of our Adviser, Gladstone Capital, Gladstone Investment, Gladstone Land and their affiliates in other activities that may conflict with our business.

Examples of these potential conflicts include:

- our Adviser may realize substantial compensation on account of its activities on our behalf, and may, therefore, be motivated to approve acquisitions solely on the basis of increasing compensation to itself;
- we may experience competition with our affiliates for financing transactions;
- our Adviser may earn fee income from our borrowers or tenants; and
- our Adviser and other affiliates such as Gladstone Capital, Gladstone Investment and Gladstone Land could compete for the time and services of our officers and directors.

These and other conflicts of interest between us and our Adviser and other affiliates could have a material adverse effect on the operation of our business and the selection or management of our real estate investments.

*Our Adviser is not obligated to provide a waiver of the incentive fee, which could negatively impact our earnings and our ability to maintain our current level of, or increase, distributions to our stockholders.*

The Advisory Agreement contemplates a quarterly incentive fee based on our FFO. Our Adviser has the ability to issue a full or partial waiver of the incentive fee for current and future periods; however, our Adviser is not required to issue any waiver. Any waiver issued by our Adviser is a voluntary, unconditional and irrevocable waiver. For the years ended December 31, 2014, 2013 and 2012, an unconditional and irrevocable voluntary waiver was issued by our Adviser for approximately \$3.0 million, \$3.5 million and \$2.2 million, respectively. If our Adviser does not issue this waiver in future quarters, it could negatively impact our earnings and may compromise our ability to maintain our current level of, or increase, distributions to our stockholders, which could have a material adverse impact on the market price of our securities.

*We may be obligated to pay our Adviser incentive compensation even if we incur a loss.*

The Advisory Agreement entitles our Adviser to incentive compensation based on our FFO, which rewards the Adviser if our quarterly FFO (before giving effect to any incentive fee) exceeds 1.75% (7% annualized) of our total stockholders' equity (less the recorded value of any preferred stock). Our pre-incentive fee FFO for incentive compensation purposes excludes the effect of any unrealized gains, losses or other items that do not affect realized net income that we may incur in the fiscal quarter, even if such losses result in a net loss on our statement of operations for that quarter. Thus, we may be required to pay our Adviser incentive compensation for a fiscal quarter even if we incur a net loss for that quarter.

### **Risks Related to Qualification and Operation as a REIT**

*If we fail to qualify as a REIT, our operations and distributions to stockholders would be adversely impacted.*

We intend to continue to be organized and to operate to qualify as a REIT under the Internal Revenue Code of 1986, as amended, or the Code. A REIT generally is not taxed at the corporate level on income it currently distributes to its stockholders. Qualification as a REIT involves the application of highly technical and complex rules for which there are only limited judicial or administrative interpretations. The determination of various factual matters and circumstances not entirely within our control may affect our ability to continue to qualify as a REIT. In addition, new legislation, new regulations, administrative interpretations or court decisions could significantly change the tax laws, possibly with retroactive effect, with respect to qualification as a REIT or the federal income tax consequences of such qualification.

If we were to fail to qualify as a REIT in any taxable year:

- we would not be allowed to deduct our distributions to stockholders when computing our taxable income;
- we would be subject to federal income tax (including any applicable alternative minimum tax) on our taxable income at regular corporate rates;
- we would be disqualified from being taxed as a REIT for the four taxable years following the year during which qualification was lost, unless entitled to relief under certain statutory provisions;
- our cash available for distributions to stockholders would be reduced; and
- we may be required to borrow additional funds or sell some of our assets to pay corporate tax obligations that we may incur as a result of our disqualification.

*We may need to incur additional borrowings to meet the REIT minimum distribution requirement and to avoid excise tax.*

In order to maintain our qualification as a REIT, we are required to distribute to our stockholders at least 90% of our annual real estate investment trust taxable income (excluding any net capital gain and before application of the distributions paid deduction). To the extent that we satisfy this distribution requirement, but distribute less than 100% of our taxable income, we will be subject to federal corporate income tax on our undistributed taxable income. In addition, we are subject to a 4% nondeductible excise tax on the amount, if any, by which certain distributions paid by us with respect to any calendar year are less than the sum of (i) 85% of our ordinary income for that year, (ii) 95% of our net capital gain for that year and (iii) 100% of our undistributed taxable income from prior years. In order to meet the 90% distribution requirement and to avoid the 4% excise tax, we may need to incur additional borrowings. Although we intend to pay distributions to our stockholders in a manner that allows us to meet the 90% distribution requirement and avoid this 4% excise tax, we cannot assure you that we will always be able to do so.

*Complying with the REIT requirements may cause us to forgo otherwise attractive opportunities or liquidate otherwise attractive investments.*

To qualify as a REIT for federal income tax purposes, we must continually satisfy tests concerning, among other things, the nature of our assets, the sources of our gross income, the amounts we distribute to our stockholders and the ownership of our capital stock. In order to meet these tests, we may be required to forgo investments we might otherwise make. Thus, compliance with the REIT requirements may hinder our performance.

In particular, we must ensure that at the end of each calendar quarter, at least 75% of the value of our assets consists of cash, cash items, government securities and qualified real estate assets. The remainder of our investment in securities (other than government securities, securities of taxable REIT subsidiaries (each, a taxable REIT subsidiary, or TRS) and qualified real estate assets) generally cannot include more than 10% of the outstanding voting securities of any one issuer. In addition, in general, no more than 5% of the value of our assets (other than government securities, securities of TRSs and qualified real estate assets) can consist of the securities of any one issuer, and no more than 25% of the value of our total assets can be represented by the securities of one or more TRSs.

We also must ensure that (i) at least 75% of our gross income for each taxable year consists of certain types of income that we derive, directly or indirectly, from investments relating to real property or mortgages on real property or qualified temporary investment income and (ii) at least 95% of our gross income for each taxable year consists of income that is qualifying income for purposes of the 75% gross income test, other types of interest and distributions, gain from the sale or disposition of stock or securities, or any combination of these.

In addition, we may be required to make distributions to our stockholders at disadvantageous times or when we do not have funds readily available for distribution. If we fail to comply with these requirements at the end of any calendar quarter, we must qualify for certain statutory relief provisions to avoid losing our REIT qualification and suffering adverse tax consequences. As a result, we may be required to liquidate otherwise attractive investments, and may be unable to pursue investments that would otherwise be advantageous to us in order to satisfy the asset and gross income requirements for qualifying as a REIT. These actions could have the effect of reducing our income and the amounts available for distribution to our stockholders. Thus, compliance with the REIT requirements may hinder our ability to make, and, in certain cases, maintain ownership of certain attractive investments.

*To the extent that our distributions represent a return of capital for tax purposes, you could recognize an increased capital gain upon a subsequent sale of your stock.*

Distributions in excess of our current and accumulated earnings and profits and not treated by us as a dividend will not be taxable to a U.S. stockholder to the extent such distributions do not exceed the stockholder's adjusted tax basis in its shares of our stock but instead will constitute a return of capital and will reduce the stockholder's adjusted tax basis in its share of our stock. If our distributions result in a

reduction of a stockholder's adjusted basis in its shares of our stock, subsequent sales by such stockholder of its shares of our stock potentially will result in recognition of an increased capital gain or reduced capital loss due to the reduction in such stockholder's adjusted basis in its shares of our stock.

*We may be subject to adverse legislative or regulatory tax changes that could reduce the market price of our securities.*

At any time, the federal income tax laws governing REITs or the administrative interpretations of those laws may be amended. We cannot predict when or if any new federal income tax law, regulation, or administrative interpretation, or any amendment to any existing federal income tax law, regulation or administrative interpretation, will be adopted, promulgated or become effective and any such law, regulation, or interpretation may take effect retroactively. We and our stockholders could be adversely affected by any such change in, or any new, federal income tax law, regulation or administrative interpretation.

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

The REIT provisions of the Code substantially limit our ability to hedge our liabilities. Any income from a hedging transaction that we enter into to manage risk of interest rate changes, price changes or currency fluctuations with respect to borrowings made or to be made to acquire or carry real estate assets does not constitute "gross income" for purposes of the gross income requirements. To the extent that we enter into other types of hedging transactions, the income from those transactions is likely to be treated as non-qualifying income for purposes of both of the gross income tests. As a result of these rules, we may need to limit our use of advantageous hedging techniques or implement those hedges through TRSs. This could increase the cost of our hedging activities because any TRS would be subject to tax on gains or expose us to greater risks associated with changes in interest rates than we would otherwise want to bear. In addition, losses incurred by a TRS generally will not provide any tax benefit, except for being carried forward against future taxable income earned by the TRS.

*If our Operating Partnership fails to maintain its status as a disregarded entity or partnership for federal income tax purposes, its income may be subject to taxation.*

As we hold all of the ownership interests in our Operating Partnership, it is currently disregarded for income tax purposes. We intend that our Operating Partnership will qualify as a partnership for income tax purposes upon the admission of additional partners; however, if the IRS were to successfully challenge the status of our Operating Partnership as a partnership, it would be taxable as a corporation. In such event, this would reduce the amount of distributions that our Operating Partnership could make to us. This could also result in our losing REIT status and becoming subject to corporate level tax on our income. This would substantially reduce our cash available to pay distributions and the return on your investment. In addition, if any of the entities through which our Operating Partnership owns its properties, in whole or in part, loses its characterization as a disregarded entity or a partnership for federal income tax purposes, it would be subject to taxation as a corporation, thereby reducing distributions to our Operating Partnership. Such a re-characterization of an underlying property owner could also threaten our ability to maintain REIT status.

#### ***Other risks***

*We are subject to restrictions that may discourage a change of control. Certain provisions contained in our articles of incorporation and Maryland law may prohibit or restrict a change of control.*

- Our articles of incorporation prohibit ownership of more than 9.8% of the outstanding shares of our capital stock by one person. This restriction may discourage a change of control and may deter individuals or entities from making tender offers for our capital stock, which offers might otherwise be financially attractive to our stockholders or which might cause a change in our management.

- Our Board of Directors is divided into three classes, with the term of the directors in each class expiring every third year. At each annual meeting of stockholders, the successors to the class of directors whose term expires at such meeting will be elected to hold office for a term expiring at the annual meeting of stockholders held in the third year following the year of their election. After election, a director may only be removed by our stockholders for cause. Election of directors for staggered terms with limited rights to remove directors makes it more difficult for a hostile bidder to acquire control of us. The existence of this provision may negatively impact the price of our securities and may discourage third-party bids to acquire our securities. This provision may reduce any premiums paid to stockholders in a change in control transaction.
- Certain provisions of Maryland law applicable to us prohibit business combinations with:
  - any person who beneficially owns 10% or more of the voting power of our common stock, referred to as an “interested stockholder;”
  - an affiliate of ours who, at any time within the two-year period prior to the date in question, was an interested stockholder; or
  - an affiliate of an interested stockholder.

These prohibitions last for five years after the most recent date on which the interested stockholder became an interested stockholder. Thereafter, any business combination with the interested stockholder must be recommended by our Board of Directors and approved by the affirmative vote of at least 80% of the votes entitled to be cast by holders of our outstanding shares of common stock and two-thirds of the votes entitled to be cast by holders of our common stock other than shares held by the interested stockholder. These requirements could have the effect of inhibiting a change in control even if a change in control were in our stockholders’ interest. These provisions of Maryland law do not apply, however, to business combinations that are approved or exempted by our Board of Directors prior to the time that someone becomes an interested stockholder.

*Market conditions could adversely affect the market price and trading volume of our securities.*

The market price of our common and preferred stock may be highly volatile and subject to wide fluctuations, and the trading volume in our common and preferred stock may fluctuate and cause significant price variations to occur. We cannot assure investors that the market price of our common and preferred stock will not fluctuate or decline further in the future. Some market conditions that could negatively affect our share price or result in fluctuations in the price or trading volume of our securities include, but are not limited to:

- price and volume fluctuations in the stock market from time to time, which are often unrelated to the operating performance of particular companies;
- significant volatility in the market price and trading volume of shares of REITs, real estate companies or other companies in our sector, which is not necessarily related to the performance of those companies;
- price and volume fluctuations in the stock market as a result of terrorist attacks, or speculation regarding future terrorist attacks, in the United States or abroad;
- actual or anticipated variations in our quarterly operating results or distributions to stockholders;
- changes in our funds from operations or earnings estimates or the publication of research reports about us or the real estate industry generally;
- actions by institutional stockholders;
- speculation in the press or investment community;
- changes in regulatory policies or tax guidelines, particularly with respect to REITs; and
- investor confidence in the stock market.

*Shares of common stock eligible for future sale may have adverse effects on our share price.*

We cannot predict the effect, if any, of future sales of common stock, or the availability of shares for future sales, on the market price of our common stock. Sales of substantial amounts of common stock (including shares of common stock issuable upon the conversion of units of our operating partnership that we may issue from time to time or issuable upon conversion of our Senior Common Stock), or the perception that these sales could occur, may adversely affect prevailing market prices for our common stock.

*Compliance or failure to comply with laws requiring access to our properties by disabled persons could result in substantial cost.*

The Americans with Disabilities Act, or ADA, and other federal, state and local laws generally require public accommodations be made accessible to disabled persons. Noncompliance could result in the imposition of fines by the government or the award of damages to private litigants. These laws may require us to modify our existing properties. These laws may also restrict renovations by requiring improved access to such buildings by disabled persons or may require us to add other structural features which increase our construction costs. Legislation or regulations adopted in the future may impose further burdens or restrictions on us with respect to improved access by disabled persons. We may incur unanticipated expenses that may be material to our financial condition or results of operations to comply with ADA and other federal, state and local laws, or in connection with lawsuits brought by private litigants.

*Our Board of Directors may change our investment policy without stockholders' approval.*

Subject to our co-investment policy, our Board of Directors will determine our investment and financing policies, growth strategy and our debt, capitalization, distribution, acquisition, disposition and operating policies. Our Board of Directors may revise or amend these strategies and policies at any time without a vote by stockholders. Accordingly, stockholders' control over changes in our strategies and policies is limited to the election of directors, and changes made by our Board of Directors may not serve the interests of stockholders and could adversely affect our financial condition or results of operations, including our ability to distribute cash to stockholders or qualify as a REIT.

*Our failure to redeem our Series C Term Preferred Stock on its mandatory redemption date could trigger a change of control in our Board of Directors.*

If we fail to redeem or call for redemption the Series C Term Preferred Stock pursuant to the mandatory redemption required on January 31, 2017, the number of directors constituting our Board of Directors will be increased by the minimum number of directors, that when added to our Board of Directors, will constitute a majority, and the holders of our Series C Term Preferred Stock will be entitled, voting as a separate class (to the exclusion of the holders of all other classes or series of our stock), to elect such number of additional directors. Therefore, a change of control in our Board of Directors could occur, which could jeopardize the stability of our Company.

*Our rights and the rights of our stockholders to take action against our directors and officers are limited.*

Maryland law provides that a director or officer has no liability in that capacity if he or she performs his or her duties in good faith, in a manner he or she reasonably believes to be advisable and in our best interests and with the care that an ordinarily prudent person in a like position would use under similar circumstances. In addition, our charter (i) eliminates our directors' and officers' liability to us and our stockholders for money damages except for liability resulting from actual receipt of an improper benefit in money, property or services or active and deliberate dishonesty established by a final judgment and that is material to the cause of action and (ii) requires us to indemnify directors and officers for liability resulting from actions taken by them in those capacities to the maximum extent permitted by Maryland law. As a result, our stockholders and we may have more limited rights against our directors and officers than might otherwise exist under common law. In addition, we may be obligated to fund the defense costs incurred by our directors and officers.

*Our ability to pay dividends is limited by the requirements of Maryland law.*

Our ability to pay dividends on our stock is limited by the laws of Maryland. Under applicable Maryland law, a Maryland corporation generally may not make a distribution if, after giving effect to the distribution, the corporation would not be able to pay its debts as the debts become due in the usual course of business or the corporation's total assets would be less than the sum of its total liabilities plus, unless the corporation's charter permits otherwise, the amount that would be needed, if the corporation were dissolved at the time of the distribution, to satisfy the preferential rights upon dissolution of stockholders whose preferential rights are superior to those receiving the distribution. Accordingly, we generally may not make a distribution on our stock if, after giving effect to the distribution, we would not be able to pay our debts as they become due in the usual course of business or our total assets would be less than the sum of our total liabilities plus, unless the terms of such class or series provide otherwise, the amount that would be needed to satisfy the preferential rights upon dissolution of the holders of shares of any class or series of stock then outstanding, if any, with preferences upon dissolution senior to those of such class of stock with respect to which the distribution would be made.

**Item 1B. Unresolved Staff Comments.**

None.

## Item 2. Properties.

The following table provides certain summary information about our 96 wholly-owned, properties as of December 31, 2014 (dollars in thousands, except per square foot information).

Property	Year Built/ Improvements	Date of Purchase	Rentable Square Feet	Occupancy	Year of Lease Expiration	Total Rental Income for the year ended December 31, 2014 <sup>(4)</sup>	Total Rental Income per Occupied Square Foot	Encumbrances
208 South Rogers Lane (Raleigh NC)	1997	12/23/2003	58,926	100%	2015	\$ 624	\$ 10.59	\$ 4,796
3874 Highland Park NW (Canton, OH)	1994	1/30/2004	54,018	100%	2024	283	5.24	2,664
260 Springside Drive (Akron, OH)	<sup>(3)</sup> 1968/1999	4/29/2004	83,891	100%	2020	917	10.93	6,828
5815 Westpark Drive (Charlotte, NC)	1984/1995	6/30/2004	64,500	100%	2019	1,091	16.91	6,308
171 Great Oak Drive (Canton, NC)	1998/2014	7/6/2004	365,960	100%	2034	984	2.69	3,652
Rt. 219, Tax Parcel No. 33-251-0246, (Crenshaw, PA)	1991	8/5/2004	290,000	100%	2026	717	2.47	5,176
9698 Old US Hwy. 52 (Lexington, NC)	1986	8/5/2004	154,000	100%	2026	381	2.47	2,636
9100 Highway 290 East (Austin, TX)	2001	9/16/2004	51,933	100%	2022	705	13.58	6,500
13 Industrial Park Drive (Mt. Pocono, PA)	1995/1999	10/15/2004	223,275	100%	2021	633	2.84	4,889
6550 First Park Ten Boulevard (San Antonio, TX)	1999	2/10/2005	60,245	100%	2021	782	12.98	6,643
4630 Journal Street (Columbus, OH)	1995	2/10/2005	39,000	100%	2015	308	7.90	2,516
199 Sing Sing Road (Big Flats, NY)	2001	4/15/2005	120,000	100%	2023	494	4.12	5,365
2525 North Woodlawn Avenue (Wichita, KS)	2000	5/18/2005	69,287	100%	2017	780	11.26	7,466
725 & 737 Great Southwest Pkwy (Arlington, TX)	1966	5/26/2005	64,000	100%	2018	693	10.83	3,814
4032 Linden Avenue (Dayton, OH)	1956	6/30/2005	59,894	100%	2015	268	4.47	1,877
81 Corbett Way (Eatontown, NJ)	1991	7/7/2005	30,268	100%	2024	537	17.74	4,365
17 & 20 Veronica Avenue (Franklin Township, NJ)	1978	7/11/2005	183,000	100%	2020	988	5.40	6,471
150 Ridgeview Center Drive (Duncan, SC)	1984/2001/2007	7/14/2005	222,670	100%	2020	1,539	6.91	10,375
170 Ridgeview Center Drive (Duncan, SC)	1984/2001/2007	7/14/2005	55,350	100%	2020	383	6.92	2,579
5656 Campus Parkway (Hazelwood, MO)	1977	8/5/2005	51,155	100%	2023	213	4.16	2,291
914 Wohlert Street (Angola, IN)	1982	9/2/2005	52,080	100%	2023	127	2.44	626
800 Growth Parkway (Angola, IN)	1998	9/2/2005	50,000	100%	2023	127	2.54	601
802 East 11th Street (Rock Falls, IL)	1988	9/2/2005	52,000	100%	2023	127	2.44	626
2 Opportunity Way (Newburyport, MA)	1994	10/17/2005	86,308	100%	2015	891	10.32	6,276
255 Spring Street (Clintonville, WI)	1992/2013	10/31/2005	521,400	100%	2028	961	1.84	2,997
5700 Lee Road (Maple Heights, OH)	1974	12/21/2005	347,218	100%	2015	1,278	3.68	9,790



## Item 2. Properties (Continued)

Property	Year Built/ Improvements	Date of Purchase	Rentable Square Feet	Occupancy	Year of Lease Expiration	Total Rental Income for the year ended December 31, 2014 <sup>(4)</sup>	Total Rental Income per Occupied Square Foot	Encumbrances
7545 Midlothian Turnpike (Richmond, VA)	1972	12/30/2005	42,213	100%	2017	\$ 68	\$ 5.10 <sup>(2)</sup>	\$ 5,275
3930 Sunforest Court (Toledo, OH)	1979	12/30/2005	23,368	100%	2020	276	11.81	2,750
75 Canal Street (South Hadley, MA)	1978	2/15/2006	150,000	100%	2017	269	1.79	-
2101 Fox Drive (Champaign, IL)	1996	2/21/2006	20,400	100%	2024	263	12.89	1,545
2109 Fox Drive (Champaign, IL)	1996	2/21/2006	40,000	100%	2024	517	12.93	3,030
2215 Fox Drive (Champaign, IL)	1996	2/21/2006	25,000	100%	2024	323	12.92	1,894
2301 Fox Drive (Champaign, IL)	1996	2/21/2006	22,862	100%	2024	295	12.90	1,731
12000 Portland Avenue South (Burnsville, MN)	1984	5/10/2006	114,959	100%	2023	1,091	9.49	11,001
14701 Anthony Avenue (Menomonee Falls, WI)	1986/2000	6/30/2006	125,692	100%	2016	786	6.25	6,738
1025 Birdsong Drive (Baytown, TX)	1997	7/11/2006	12,000	0%	2013	-	-	2,000
2150, 2200 Pinson Valley Parkway (Birmingham, AL)	1961/1980	9/29/2006	63,514	100%	2016	271	4.27	-
2325 West Fairview Avenue (Montgomery, AL)	1962/1989	9/29/2006	29,472	100%	2016	126	4.28	-
5221 N Highway 763 (Columbia, MO)	1978	9/29/2006	16,275	100%	2016	69	4.24	-
4690 Parkway Drive (Mason, OH)	2002	1/5/2007	60,000	100%	2020	554	9.23	4,250
201 South Rogers Lane (Raleigh, NC)	1994	2/16/2007	115,500	100%	2015	717	6.21	5,164
1110 West Tenkiller (Tulsa, OK)	<sup>(3)</sup> 2004	3/1/2007	238,310	100%	2019	1,566	6.57	7,776
3725 East 10th Court (Hialeah, FL)	1956/1992	3/9/2007	132,337	100%	2027	1,109	8.38	-
554 Clark Road (Tewksbury, MA)	1985/1989	5/17/2007	102,200	100%	2017	799	7.82	-
5324 Natortp Boulevard (Mason, OH)	2007	7/1/2007	21,264	100%	2027	583	27.42	4,555
7282 William Barry Boulevard (Cicero, NY)	2005	9/6/2007	71,880	100%	2020	530	7.37	3,964
1515 Arboretum Drive SE (Grand Rapids, MI)	2001	9/28/2007	63,235	100%	2025	1,090	17.24	5,831
4 Territorial Court (Bolingbrook, IL)	<sup>(11)</sup> 2002	9/28/2007	55,480	38%	2022	636	11.46	-
2349 Lawrenceville Highway (Decatur, GA)	1989	12/13/2007	16,740	100%	2031	516	30.82	-
2341 Lawrenceville Highway (Decatur, GA)	1989	12/13/2007	4,372	100%	2031	135	30.88	-
2339 Lawrenceville Highway (Decatur, GA)	1989	12/13/2007	5,488	100%	2031	169	30.79	-

## Item 2. Properties (Continued)

Property	Year Built/ Improvements	Date of Purchase	Rentable Square Feet	Occupancy	Year of Lease Expiration	Total Rental Income for the year ended December 31, 2014 <sup>(4)</sup>	Total Rental Income per Occupied Square Foot	Encumbrances
311 Phillip Boulevard (Lawrenceville, GA)	2005	12/13/2007	12,412	100%	2031	\$ 447	\$ 36.01	\$ -
2096 McGee Road (Snelville, GA)	1986	12/13/2007	3,800	100%	2031	116	30.53	-
7174 Wheat Street (Covington, GA)	2000	12/13/2007	5,000	100%	2031	153	30.60	-
1055 Haw Creek Parkway (Cumming, GA)	2004	12/13/2007	13,919	100%	2026	486	34.92	3,145
1293 Wellbrook Circle (Conyers, GA)	1994	12/13/2007	6,400	100%	2031	195	30.47	-
425 Gateway Drive (Reading, PA)	2007	1/29/2008	42,900	100%	2028	717	16.71	3,983
6499 University Avenue NE (Fridley, MN)	1985/2006	2/26/2008	74,160	100%	2020	812	10.95	5,121
7528 Auburn Road (Concord Township, OH)	1957/2008	3/31/2008	273,300	100%	2024	1,665	6.09	-
10021 Rodney Street (Pineville, NC)	1985	4/30/2008	74,950	100%	2028	431	5.75	2,315
28305 State Route 7 (Marietta, OH)	1992/2007	8/29/2008	223,458	100%	2028	909	4.07	5,650
400 Highpoint Drive (Chalfont, PA)	1987	8/29/2008	67,200	100%	2016	758	11.28	5,510
1520 Albany Place SE (Orange City, IA)	1990	12/15/2010	487,121	100%	2026	1,229	2.52	9,015
2415 Century Place SE (Hickory, NC)	2008	4/4/2011	60,000	100%	2020	937	15.62	6,697
2645 North Airport Plaza Avenue, Lot 2 (Springfield, MO)	2006	6/20/2011	78,421	100%	2021	1,422	18.13	10,977
124 East Hines Road (Boston Heights, OH)	2011	10/20/2011	25,000	100%	2021	377	15.08	2,646
9 Syban Way (Parsippany, NJ)	1984	10/28/2011	60,111	100%	2026	1,157	19.25	6,799
495 State Road (Dartmouth, MA)	<sup>(3)(5)</sup> 2011	11/18/2011	16,340	100%	2086	625	38.25	4,049
1955 South National Avenue (Springfield, MO)	<sup>(3)(6)</sup> 2005	12/13/2011	14,560	100%	2080	315	21.63	1,823
810 Parish Street (Pittsburgh, PA)	1968	12/28/2011	26,080	100%	2026	400	15.34	2,757

## Item 2. Properties (Continued)

Property	Year Built/ Improvements	Date of Purchase	Rentable Square Feet	Occupancy	Year of Lease Expiration	Total Rental Income for the year ended December 31, 2014 <sup>(4)</sup>	Total Rental Income per Occupied Square Foot	Encumbrances
44426 Atwater Place (Ashburn, VA)	2002	1/25/2012	52,130	100%	2027	\$ 989	\$ 18.97	\$ 7,223
14955 6th Street (Ottumwa, IA)	1970	5/30/2012	352,860	100%	2023	693	1.96	4,426
7800 Walton Parkway (New Albany, OH)	2007	6/5/2012	89,000	100%	2023	1,357	15.25	9,066
7200 North Lake Drive (Columbus, GA)	2012	6/21/2012	32,000	100%	2023	656	20.50	4,507
3592 Corporate Drive (Columbus, OH)	1981	6/28/2012	31,293	100%	2022	331	10.58	2,845
1395 University Boulevard (Jupiter, FL)	2011	9/26/2012	60,000	100%	2023	1,372	22.87	10,252
1400 John Burgess Drive (Fort Worth, TX)	2005	11/8/2012	208,234	100%	2026	1,628	7.82	13,567
565 Spears Creek Church Road (Columbia, SC)	2010	11/21/2012	146,483	100%	2022	2,541	17.35	18,067
6725 Delilah Road (Egg Harbor Township, NJ)	1985	3/28/2013	29,257	100%	2023	496	16.95	3,551
17499 Brookwood Parkway (Vance, AL)	2013	5/9/2013	170,000	100%	2023	1,173	6.90	-
3785 Pheasant Ridge Drive NE (Blaine, MN)	2009	5/10/2013	92,275	100%	2020	1,475	15.98	8,045
717 E. Parmer Lane (Austin, TX)	1999	7/9/2013	320,000	100%	2020	4,805	15.02	34,567
805 Central Expressway South (Allen, TX)	<sup>(7)</sup> 1998	7/10/2013	115,200	100%	2021/2022	1,879 <sup>(9)</sup>	16.31	8,704
349 Inverness Drive South (Englewood, CO)	2008	12/11/2013	99,797	100%	2021	1,504	15.07	11,315
43700 Gen-Mar Drive (Novi, MI)	1988	12/27/2013	156,200	100%	2024	684	4.38	4,297
1207 West McDermott Drive (Allen, TX)	2004	3/27/2014	21,154	100%	2026	435	26.96 <sup>(2)</sup>	3,417
6805 Colleyville Boulevard (Colleyville, TX)	2000	3/27/2014	20,355	100%	2026	357	22.93 <sup>(2)</sup>	2,797
3078 Prospect Park Drive (Rancho Cordova, CA)	1986	4/22/2014	61,358	100%	2024	625 <sup>(9)</sup>	14.72 <sup>(2)</sup>	4,935
300 South Denton Tap Road (Coppell, TX)	2005	5/8/2014	21,171	100%	2026	390	28.40 <sup>(2)</sup>	3,767
7450 Huntington Park Drive (Columbus, OH)	<sup>(8)</sup> 1986	5/13/2014	114,786	100%	2016/2023	790 <sup>(9)</sup>	11.13 <sup>(2)</sup>	-
6 Kane Lane (Taylor, PA)	2000/2006	6/9/2014	955,935	100%	2024	1,908	3.56 <sup>(2)</sup>	22,600

## Item 2. Properties (Continued)

Property	Year Built/ Improvements	Date of Purchase	Rentable Square Feet	Occupancy	Year of Lease Expiration	Total Rental Income for the year ended December 31, 2014 <sup>(4)</sup>	Total Rental Income per Occupied Square Foot	Encumbrances
14800 East Moncrieff Place (Aurora, CO)	1983	7/1/2014	124,800	100%	2029	384	6.16 <sup>(2)</sup>	-
6626 E. 75th Street (Indianapolis, IN)	<sup>(10)</sup> 1981/2014	9/3/2014	86,495	96%	2015-2026	489 <sup>(9)</sup>	17.38 <sup>(2)</sup>	6,100
1485 East 61st Avenue (Denver, CO)	1985	10/31/2014	189,120	100%	2024	166	4.55 <sup>(2)</sup>	-
1833 Frenchtown Center Drive (Monroe, MI)	2004	12/23/2014	315,000	100%	2023	36	4.71 <sup>(2)</sup>	10,839
2200 Revard Road (Monroe, MI)	2004	12/23/2014	220,500	100%	2023	25	4.71 <sup>(2)</sup>	7,587
<b>Totals</b>			<u>10,633,474</u>			<u>\$ 69,928</u> <sup>(12)</sup>		<u>\$ 458,592</u>

<sup>(1)</sup> Two tenants occupy this building, each with separate leases ending in the same year.

<sup>(2)</sup> Rental income per occupied square foot is annualized, as if the building were held for all of 2014.

<sup>(3)</sup> Property subject to a ground lease.

<sup>(4)</sup> Total rental income included in this table is straight-line rental income calculated in accordance with Generally Accepted Accounting Principles in the United States.

<sup>(5)</sup> Tenant has the option to terminate the lease in years 2036-2086.

<sup>(6)</sup> Tenant has the option to terminate the lease in years 2030-2080.

<sup>(7)</sup> Two tenants occupy this building each with separate leases ending in different years. The tenant occupying 73% of the building has their lease expire in 2022. The tenant occupying the remaining space has their lease expire in 2021.

<sup>(8)</sup> Two tenants occupy this building each with separate leases ending in different years. The tenant occupying 92% of the building has their lease expire in 2023. The tenant occupying the remaining space has their lease expire in 2016.

<sup>(9)</sup> At lease one tenant occupying this properties is subject to a gross lease.

<sup>(10)</sup> Seven tenants occupy this building each with separate leases ending in different years. The tenant occupying 71% of the building lease expires in 2026. The remaining six tenants have lease terms expiring from 2015 through 2018.

<sup>(11)</sup> Our previous tenant's lease expired on December 31, 2014. Our current tenant is occupying approximately 38% of the building, and their lease expires in 2022.

<sup>(12)</sup> The rental income figure excludes rental revenues earned prior to our Sterling Heights, MI sale, and our Roseville, MN deed-in-lieu transaction. Total rental revenue for the year ended December 31, 2014 for these properties was \$1,283.

The following table summarizes the lease expirations by year for our properties for leases in place as of December 31, 2014 (dollars in thousands):

Year of Lease Expiration	Square Feet <sup>(1)</sup>	Number of Expiring Leases	Rental Revenue for the year ended December 31, 2014	% of Annualized Base Rent
2015	701,148	7	\$ 4,090	5.9%
2016	315,183	5	2,127	3.1
2017	372,885	6	1,931	2.8
2018	78,968	4	770	1.1
2019	302,810	2	2,657	3.8
2020	1,246,594	11	13,216	19.1
2021	518,276	6	5,119	7.4
2022+	<u>7,047,887</u>	<u>50</u>	<u>39,400</u>	<u>56.8</u>
<b>Total</b>	<u>10,583,751</u>	<u>91</u>	<u>\$ 69,310</u> <sup>(2)</sup>	<u>100%</u>

<sup>(1)</sup> Our fully vacant building in Baytown, TX contains 12,000 square feet. We have 34,535 square feet vacant in our Bolingbrook, IL property, and 3,188 square feet vacant in our Indianapolis, IN property.

<sup>(2)</sup> The rental income figure excludes rental revenues earned on our expired lease at Bolingbrook, IL, and rental income earned prior to our Sterling Heights, MI sale, and our Roseville, MN deed-in-lieu transaction. Total rental revenue for the year ended December 31, 2014 for these properties was \$1,901.

The following table summarizes the geographic locations of our properties as of December 31, 2014 (dollars in thousands):

State	Rental Revenue for the year ended December 31, 2014	% of Base Rent	Number of Leases for the year ended December 31, 2014
Texas	\$ 11,674	16.4%	10
Ohio	9,896	13.9	17
North Carolina	5,165	7.3	7
Pennsylvania	5,133	7.2	6
South Carolina	4,463	6.3	2
Minnesota	4,153	5.8	3
New Jersey	3,178	4.5	4
Georgia	2,874	4.0	3
Massachusetts	2,584	3.6	4
All Other States	22,091	31.0	35
<b>Total</b>	<b>\$ 71,211</b>	<b>100%</b>	<b>91</b>

The following table summarizes rental income by tenant industries for the years ended December 31, 2014, 2013 and 2012 (dollars in thousands):

Industry Classification	For the year ended December 31,					
	2014		2013		2012	
	Rental Income	Percentage of Rental Income	Rental Income	Percentage of Rental Income	Rental Income	Percentage of Rental Income
Telecommunications	\$ 12,570	17.7%	\$ 10,102	17.0%	\$ 7,351	14.4%
Healthcare	8,692	12.2	7,486	12.5	5,228	10.3
Automobile	8,587	12.1	5,589	9.4	1,944	3.8
Electronics	5,731	8.0	4,982	8.3	6,189	12.3
Personal, Food & Miscellaneous Services	5,493	7.7	5,231	8.8	2,479	4.9
Diversified/Conglomerate Manufacturing	4,049	5.7	3,665	6.1	3,664	7.2
Chemicals, Plastics & Rubber	3,256	4.6	3,236	5.4	3,153	6.2
Diversified/Conglomerate Services	3,153	4.4	1,244	2.1	1,244	2.4
Beverage, Food & Tobacco	2,994	4.2	3,007	5.0	2,844	5.6
Machinery	2,643	3.7	2,265	3.8	2,259	4.4
Personal & Non-Durable Consumer Products	2,607	3.7	2,583	4.3	2,507	4.9
Buildings and Real Estate	2,181	3.1	2,160	3.6	2,144	4.2
Containers, Packaging & Glass	2,086	2.9	2,171	3.6	2,344	4.6
Printing & Publishing	1,783	2.5	1,848	3.1	1,894	3.7
Childcare	1,765	2.5	583	1.0	583	1.1
Oil & Gas	1,278	1.8	1,275	2.1	1,271	2.5
Banking	1,157	1.6	1,156	1.9	1,149	2.3
Education	656	0.9	656	1.1	2,138	4.2
Home & Office Furnishings	530	0.7	530	0.9	530	1.0
	<b>\$ 71,211</b>	<b>100.0%</b>	<b>\$ 59,769</b>	<b>100.0%</b>	<b>\$ 50,915</b>	<b>100.0%</b>

### Item 3. 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 4. Mine Safety Disclosures.

Not applicable.

## PART II

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

Our common stock is traded on the NASDAQ Global Select Market, or NASDAQ, under the symbol “GOOD.” The following table reflects the range of the high and low sale prices of our common stock on NASDAQ and the distributions per common share for the years ended December 31, 2014 and 2013. Distributions to common stockholders are declared quarterly and paid monthly. Amounts presented represent the cumulative amount of the monthly common stock distributions declared and paid during such quarter.

	Price Range			Distributions Per
	High	Low		Common Share
<u>2013</u>				
3/31/2013	\$ 19.51	\$ 17.98	\$	0.375
6/30/2013	21.33	17.89		0.375
9/30/2013	19.16	17.25		0.375
12/31/2013	19.09	17.25		0.375
<u>2014</u>				
3/31/2014	\$ 18.67	\$ 17.08	\$	0.375
6/30/2014	17.99	16.84		0.375
9/30/2014	18.41	16.94		0.375
12/31/2014	18.25	16.41		0.375

Since inception in 2003, we have never reduced our per-share distributions nor have we missed payment of a scheduled distribution to our common stockholders. Our Board of Directors regularly evaluates our per share distribution payments as they monitor the capital markets and the impact that the economy has upon us. The decision whether to authorize and pay distributions on shares of our common stock in the future, as well as the timing, amount and composition of any such future distributions, will be at the sole and absolute discretion of our Board of Directors in light of conditions then existing, including our earnings, taxable income, FFO, financial condition, liquidity, capital requirements, debt maturities, the availability of capital, contractual prohibitions or other restrictions, applicable REIT and legal restrictions and general overall economic conditions and other factors. While the statements above concerning our distribution policy represent our current expectations, any actual distribution payable will be determined by our Board of Directors based upon the circumstances at the time of declaration and the actual number of common shares then outstanding, and any common distribution payable may vary from such expected amounts.

To qualify as a REIT, we are required to make ordinary dividend distributions to our common stockholders. The amount of these distributions must equal at least the sum of (A) 90% of our “REIT taxable income” (computed without regard to the dividends paid deduction and capital gain) and (B) 90% of the net income (after tax), if any, from foreclosure property.

For federal income tax purposes, our common distributions generally consist of ordinary income, capital gains, nontaxable return of capital or a combination of those items. Distributions that exceed our current and accumulated earnings and profits (calculated for tax purposes) constitute a return of capital rather than a dividend, which reduces a stockholder’s basis in its shares of stock and will not be taxable to the extent of the stockholder’s basis in its shares of our stock. To the extent a distribution exceeds the stockholder’s share of both our current and accumulated earnings and profits and the stockholder’s basis in its shares of our stock, that distribution will be treated as a gain from the sale or exchange of that stockholder’s shares of

our stock. Every year, we notify stockholders of the taxability of distributions paid to stockholders during the preceding year.

A covenant in the agreement governing our Line of Credit requires us to, among other things, limit our distributions to stockholders to 100% of our FFO, and continued compliance with this covenant may require us to limit our distributions to stockholders in the future. For a discussion of our Line of Credit, including the financial and operating covenants required for us to access this source of financing, see “*Risk Factors – Our Line of Credit contains various covenants which, if not complied with, could accelerate our repayment obligations, thereby materially and adversely affecting our liquidity, financial condition, results of operations and ability to pay distributions to stockholders*” and “*Management’s Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Capital Resources – Line of Credit*” herein.

As of February 4, 2015, there were 15,093 beneficial owners of our common stock.

The Company pays distributions on shares of Senior Common Stock in an amount equal to \$1.05 per share per annum, declared daily and paid at the rate of \$0.0875 per share per month. The Senior Common Stock is not traded on any exchange or automated quotation system.

As of February 4, 2015, there were 284 beneficial owners of our Senior Common Stock.

## Item 6. Selected Financial Data.

The following selected financial data as of and for each of the fiscal years ended December 31, 2014, 2013, 2012, 2011 and 2010 is derived from our audited consolidated financial statements. The data should be read in conjunction with our consolidated financial statements and notes thereto, included elsewhere in this report, and “*Management’s Discussion and Analysis of Financial Condition and Results of Operations*” included in Item 7 of this report.

	For the year ended December 31				
	(Dollars in Thousands, Except Per Share Amounts)				
	2014	2013	2012	2011	2010
<b>Operating Data:</b>					
Total operating revenue	\$ 73,756	\$ 61,343	\$ 51,270	\$ 43,976	\$ 41,928
Total operating expenses	(57,406)	(32,823)	(24,895)	(21,270)	(23,414)
Other expense	(22,252)	(26,993)	(22,614)	(16,992)	(13,586)
Net (loss) income	\$ (5,902)	\$ 1,527	\$ 3,761	\$ 5,714	\$ 4,928
Dividends attributable to preferred stock	(4,094)	(4,094)	(4,093)	(4,094)	(4,094)
Dividends attributable to senior common stock	(542)	(300)	(113)	(62)	(20)
Net (loss) income available to common stockholders	\$ (10,538)	\$ (2,867)	\$ (445)	\$ 1,558	\$ 814
<b>Share and Per Share Data:</b>					
(Loss) earnings per weighted average common share - basic & diluted	\$ (0.61)	\$ (0.22)	\$ (0.04)	\$ 0.15	\$ 0.09
Weighted average common shares outstanding-basic	17,253,503	13,164,244	10,953,325	10,236,859	8,576,303
Weighted average common shares outstanding-diluted	17,253,503	13,164,244	10,953,325	10,288,711	8,601,153
Cash dividends declared per common share	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50
<b>Supplemental Data:</b>					
Net (loss) income available to common stockholders	\$ (10,538)	\$ (2,867)	\$ (445)	\$ 1,558	\$ 814
Add: Real estate depreciation and amortization	28,864	22,827	16,831	14,149	13,264
Add: Impairment charge	14,238	-	-	-	-
Less: Gain on sale of real estate	(1,240)	-	-	-	-
Funds from operations available to common stockholders <sup>(1)</sup>	\$ 31,324	\$ 19,960	\$ 16,386	\$ 15,707	\$ 14,078
<b>Balance Sheet Data:</b>					
Real estate, before accumulated depreciation	\$ 722,565	\$ 642,353	\$ 533,753	\$ 442,521	\$ 401,017
Total assets	787,794	690,525	564,779	453,147	410,609
Mortgage notes payable, term loan, term preferred stock and borrowings under the line of credit	541,099	485,502	422,685	304,050	286,595
Total stockholders’ equity	217,672	183,146	122,365	135,314	111,375
Total common shares outstanding	19,589,606	15,662,414	11,083,584	10,945,379	8,724,613

(1) The National Association of Real Estate Investment Trusts, or NAREIT, developed 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 and 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 preferred share and Senior Common Stock share distributions. We believe that net (loss) income available to common stockholders is the most directly comparable GAAP measure to FFO available to common stockholders.

Basic funds from operations per share, or Basic FFO per share, and diluted funds from operations per share, or 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, or 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.

The following table provides a reconciliation of our FFO for the years ended December 31, 2014, 2013, 2012, 2011 and 2010 to the most directly comparable GAAP measure, net (loss) income, and a computation of basic and diluted FFO per weighted average common share:

	For the year ended December 31,				
	(Dollars in Thousands, Except for Per Share Amounts)				
	2014	2013	2012	2011	2010
Net (loss) income	\$ (5,902)	\$ 1,527	\$ 3,761	\$ 5,714	\$ 4,928
Less: Distributions attributable to preferred and senior common stock	(4,636)	(4,394)	(4,206)	(4,156)	(4,114)
Net (loss) income attributable to common stockholders	\$ (10,538)	\$ (2,867)	\$ (445)	\$ 1,558	\$ 814
Adjustments:					
Add: Real estate depreciation and amortization	28,864	22,827	16,831	14,149	13,264
Add: Impairment charge	14,238	-	-	-	-
Less: Gain on sale of real estate	(1,240)	-	-	-	-
FFO available to common stockholders	\$ 31,324	\$ 19,960	\$ 16,386	\$ 15,707	\$ 14,078
Weighted average common shares outstanding - basic	17,253,503	13,164,244	10,953,325	10,236,859	8,576,303
Weighted average common shares outstanding - diluted	17,682,012	13,402,370	11,075,216	10,288,711	8,601,153
Basic FFO per weighted average share of common stock	\$ 1.82	\$ 1.52	\$ 1.50	\$ 1.53	\$ 1.64
Diluted FFO per weighted average share of common stock	\$ 1.77	\$ 1.49	\$ 1.48	\$ 1.53	\$ 1.64
Distributions declared per share of common stock	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50

## **Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**

*The following analysis of our financial condition and results of operations should be read in conjunction with our financial statements and the notes thereto contained elsewhere in this Form 10-K.*

### **General**

We are an externally-advised real estate investment trust, or REIT, that was incorporated under the General Corporation Law of the State of Maryland on February 14, 2003, primarily for the purpose of investing in and owning net leased industrial, commercial and retail real property and selectively making long-term industrial and commercial mortgage loans. Our portfolio of real estate is leased to a wide cross section of tenants ranging from small businesses to large public companies, many of which are corporations that do not have publicly-rated debt. We have historically entered into, and intend in the future to enter into, purchase agreements for real estate having triple net leases with terms of approximately 10 to 15 years and built in rental rate increases. Under a triple net lease, the tenant is required to pay all operating, maintenance and insurance costs and real estate taxes with respect to the leased property. 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 currently own 96 properties totaling 10.6 million square feet, which have a total gross and net carrying value, including intangible assets, of \$861.3 million and \$729.2 million, respectively. We also currently have one mortgage loan receivable outstanding for \$5.6 million.

### **Business Environment**

The strength of the global economy and the U.S. economy in particular, continues to be uncertain and volatile, and we remain cautious about a long-term economic recovery. Vacancy rates have decreased for both office and industrial properties in many markets as increased user demand with restrained new construction activity has led to improved conditions. However, vacancy rates in certain markets are still higher than pre-recessionary levels, as job growth has yet to return to all areas of the country even though the national unemployment rate has dropped over the past 12 months. Interest rates have decreased since the beginning of the year, and remain at historic lows. This continued low interest rate environment is leading to increasing competition for new acquisitions. In addition, the uncertainty surrounding the ability of the federal government to address its fiscal condition in both the near and long term has increased domestic and global economic instability. These developments and the government's credit concerns in general, could cause interest rates and borrowing costs to rise, which may negatively impact our ability to access both the debt and equity markets on favorable terms. In addition, a further decrease to the U.S. credit rating could create broader financial turmoil and uncertainty, which may weigh heavily on our stock price. Continued adverse economic conditions could have a material adverse effect on one or more of our tenants, or our business, financial condition and results of operations.

We continue to focus on re-leasing vacant space, renewing upcoming lease maturities and acquiring additional properties. We now only have one fully vacant building located in Baytown, Texas and one partially vacant building located in Bolingbrook, Illinois. Our Baytown, Texas tenant vacated upon their lease termination in April 2013, and our Bolingbrook, Illinois tenant vacated upon their lease termination in December 2014. We have identified a partial space user for our Bolingbrook, Illinois property, which took occupancy in December 2014. We originally had 12 leases expiring in 2015, and we have successfully extended the leases for 7 of these tenants, one in negotiation with the tenant, and one in which we are negotiating to sell the property to a subtenant. We have been notified that 3 tenants will leave. We are aggressively pursuing new tenants for these properties. The 3 leases, where we know the tenants are vacating, comprise less than 3% of our projected 2015 rental income, and 50% of this income does not expire until December 2015. While we originally had 12 leases rolling in 2015, we only have 4 leases expiring in 2016, 4 in 2017 and 1 in 2018, which are each less than 2% of annualized rents for each respective year.

Our available vacant space at December 31, 2014 comprises less than 1.0% of our total square footage and the annual carrying costs are approximately \$0.3 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 external financing. Our principal sources of external financing generally include the issuance of equity securities, long-term mortgage loans secured by properties and borrowings under our line of credit, or the Line of Credit. The market for long-term mortgages continues to improve and long-term mortgages are readily obtainable. The collateralized mortgage backed securities, or CMBS, market remains active but it is more conservative and restrictive than it was prior to the recession and uncertainty with regard to interest rates has made the CMBS market less predictable. We continue to look to regional banks, insurance companies and other non-bank lenders, in addition to 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 2014. We have issued shares of common stock in both an overnight offering in June and through our at-the-market programs, or ATM Programs, pursuant to our former open market sale agreement with Jefferies, LLC, or Jefferies, and our current agreement with Cantor Fitzgerald & Co., or Cantor Fitzgerald, each discussed in more detail below. In addition, we have issued shares of our convertible senior common stock, or the Senior Common Stock, also discussed in more detail below.

## **Recent Developments**

### *2014 Investment Activity*

*Allen and Colleyville, Texas:* On March 27, 2014, we acquired two office buildings, totaling 41,509 square feet, located in Allen and Colleyville, Texas for a total of \$10.0 million, excluding related acquisition expenses of \$0.07 million. We funded these acquisitions with existing cash on hand as well as assuming \$6.3 million of existing mortgage debt on the properties. The same tenant has leased both properties for 12 years and has 4 options to renew the lease for additional periods of 5 years each. The leases provide for prescribed rent escalations over the life of the lease, with annualized straight line rents of \$1.0 million.

*Rancho Cordova, California:* On April 22, 2014, we acquired a 61,358 square foot office building located in Rancho Cordova, California for \$8.2 million, excluding related acquisition expenses of \$0.07 million. We funded this acquisition with existing cash on hand and the issuance of \$4.9 million of mortgage debt on the property. The tenant has leased the property for 10 years and has 1 option to renew the lease for an additional 5 years. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line gross rents of \$0.9 million.

*Coppell, Texas:* On May 8, 2014, we acquired an office building, totaling 21,171 square feet, located in Coppell, Texas for a total of \$5.8 million, excluding related acquisition expenses of \$0.03 million. We funded these acquisitions with existing cash on hand as well as assuming \$3.8 million of existing mortgage debt on this property. The tenant has leased this property for 12 years and has 4 options to renew the lease for additional periods of 5 years each. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of \$0.6 million.

*Columbus, Ohio:* On May 13, 2014, we acquired a 114,786 square foot office building located in Columbus, Ohio for \$11.8 million, excluding related acquisition expenses of \$0.07 million. We funded this acquisition with existing cash on hand. There are 2 tenants in this property, the largest of which occupies 92% of the space and has 9.5 years remaining on the lease. The other tenant has 2.5 years remaining on the lease. The two leases provide for prescribed rent escalations over the life of the respective leases, with annualized straight line rents of \$1.3 million.

*Taylor, Pennsylvania:* On June 9, 2014, we acquired a 955,935 square foot bulk distribution warehouse located in a submarket of Scranton, Pennsylvania for \$39.0 million, excluding related acquisition expenses of \$0.7 million. We funded this acquisition with existing cash on hand as well as the issuance of \$22.6 million of mortgage debt on the property. The tenant has leased the property for 10 years and has 3 options to renew the lease for an additional 5 years each and a fourth successive term of 4 years and 11 months. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of \$3.4 million.

*Aurora, Colorado:* On July 1, 2014, we acquired a 124,800 square foot building located in Aurora, Colorado, an eastern submarket of Denver near the Denver International Airport, for \$8.3 million,

excluding related acquisition expenses of \$0.09 million. We funded this acquisition with existing cash on hand. The tenant has leased the property for 15 years and has 2 options to renew the lease for an additional 5 years each. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of \$0.8 million.

*Phoenix, Arizona:* On July 25, 2014, we closed a \$5.6 million second mortgage development loan for the construction of an 81,371 square foot, build-to-suit transitional care facility located on a major hospital campus in Phoenix, Arizona. Construction is scheduled to be completed by July 2015 and we will earn 9.0% interest, paid currently in cash, on the loan during construction and through maturity. Prior to completion of the facility, we will be granted a right of first offer to purchase the property at fair value. If we do not purchase the property we will receive an exit fee when the property is sold and the loan is repaid in an amount sufficient for us to earn an internal rate of return of 22% on the second mortgage development loan. The loan is scheduled to mature in July 2016, but has a one-year extension option.

*Indianapolis, Indiana:* On September 3, 2014, we acquired an 86,495 square foot office building located in Indianapolis, Indiana for \$10.5 million, excluding related acquisition expenses of \$0.06 million. We funded this acquisition with existing cash on hand as well as the issuance of \$6.1 million of mortgage debt on the property. There are 7 tenants in this property, the largest of which occupies 71% of the space and has 11.5 years remaining on the lease. This tenant has 2 options to renew the lease for an additional 5 years each. The remaining tenants are occupying between 1,427 and 7,639 square feet in their respective suites, with lease terms expiring from December 2015 through October 2018. Six out of seven leases provide for prescribed rent escalations over the life of the respective leases, with annualized straight line gross rents for all leases of \$1.5 million.

*Denver, Colorado:* On October 31, 2014, we acquired a 189,120 square foot building located in Denver, Colorado, for \$10.0 million, excluding related acquisition expenses of \$0.1 million. We funded this acquisition with existing cash on hand. The tenant has leased the property for 10 years and has 2 options to renew the lease for an additional 10 years each. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of \$0.9 million.

*Monroe, Michigan:* On December 23, 2014, we acquired two industrial buildings, totaling 535,500 square feet, located in Monroe, Michigan for a total of \$30.8 million, excluding related acquisition expenses of \$0.07 million. We funded these acquisitions with existing cash on hand as well as the issuance of \$18.5 million of mortgage debt on the properties. The same tenant has leased both properties for 8.5 years and has 2 options to renew the leases for additional periods of 5 years each. The leases provide for prescribed rent escalations over the life of the leases, with annualized straight line rents of \$2.5 million.

#### *2014 Sale Activity*

*Sterling Heights, Michigan:* On June 6, 2014, we completed the sale of our Sterling Heights, Michigan property for \$11.4 million and recognized a gain on sale of \$1.2 million. We considered this industrial asset to be non-core to our long term strategy, and we re-deployed the proceeds from this sale into new acquisitions described above.

#### *2014 Disposal Activity*

*Roseville, Minnesota:* On November 12, 2014, we completed a deed-in-lieu transaction on our Roseville, Minnesota property, where we returned the property to the lender in exchange for cancellation of obligations under our debt agreement with the lender. We recorded an impairment charge on this property for \$14.2 million reducing the fair value to \$10.0 million. When the lender accepted the deed-in-lieu of the outstanding mortgage, and released us from our obligation, we recorded a gain on debt extinguishment of \$5.3 million.

## 2014 Financing Activity

The following is a summary of our recent financings:

*Wells Fargo:* On March 27, 2014, through two wholly-owned subsidiaries, we assumed \$6.3 million pursuant to a long-term note payable from Wells Fargo, which is collateralized by a security interest in two of our properties. The note accrues interest at a fixed rate of 5.583% per year and the note has a maturity date of February 2016. We assumed the note in connection with the acquisition of the two properties located in Allen and Colleyville, Texas.

*KeyBank Line of Credit:* On March 28, 2014, we amended our Line of Credit to extend the maturity date one additional year to August 2017. We also modified certain terms under the Line of Credit, including the calculation of the total asset value and unencumbered asset value. The applicable London Interbank Offered Rate, or LIBOR, margins were also reduced by 25 basis points at each pricing level. As a result of these modifications, the availability under our Line of Credit increased by \$1.3 million. In addition, on November 20, 2014, we expanded our Line of Credit from \$60.0 million to \$75.0 million and also increased the maximum commitment by \$25.0 million to \$100.0 million.

*KeyBank:* On April 22, 2014, through a wholly-owned subsidiary, we borrowed \$4.9 million pursuant to a long-term note payable from KeyBank National Association, which is collateralized by a security interest in one of our properties. The note accrues interest at a fixed rate of 4.9% per year and we may not repay this note prior to the last three months of the term, or we would be subject to a prepayment penalty. The note has a maturity date of May 1, 2024. We used the proceeds from the note to acquire the property in Rancho Cordova, California on the same date.

*Wells Fargo:* On May 8, 2014, through a wholly-owned subsidiary, we assumed \$3.8 million pursuant to a long-term note payable from Wells Fargo, which is collateralized by a security interest in one of our properties. The note accrues interest at a fixed rate of 6.3% per year and has a maturity date of June 2016. We assumed the note in connection with the acquisition of the property located in Coppell, Texas on the same date.

*Prudential:* On June 9, 2014, through a wholly-owned subsidiary, we borrowed \$22.6 million pursuant to a long-term note payable from Prudential Mortgage Capital Company, which is collateralized by a security interest in one of our properties. The note accrues interest at a fixed rate of 4.23% per year and has a maturity date of July 1, 2019. We used the proceeds from the note to acquire the property in Taylor, Pennsylvania on the same date.

*Everbank:* On September 3, 2014, through a wholly-owned subsidiary, we borrowed \$6.1 million pursuant to a long-term note payable from Everbank, which is collateralized by a security interest in one of our properties. The note accrues interest at a fixed rate of 4.4% per year and has a maturity date of October 1, 2024. We used the proceeds from the note to acquire the property in Indianapolis, Indiana on the same date.

*Prudential:* On December 23, 2014, through a wholly-owned subsidiary, we borrowed \$18.5 million pursuant to a long-term note payable from Prudential Mortgage Capital Company, which is collateralized by a security interest in two of our properties. The note accrues interest at a fixed rate of 4.04% per year and has a maturity date of January 1, 2025. We used the proceeds from the note to acquire two properties in Monroe, Michigan on the same date.

## 2014 Leasing Activities

*Newburyport, Massachusetts:* On April 4, 2014, our tenant occupying our Newburyport, Massachusetts property notified us of their intention not to exercise their renewal option as the tenant is relocating to Rhode Island. The tenant will continue paying rent and operating expenses through the lease termination date of April 30, 2015. A marketing representative has been hired and re-leasing activity is currently underway.

*Austin, Texas:* On May 6, 2014, we extended the lease with the tenant occupying our property located in Austin, Texas. The lease covering this property was extended for an additional eight years, through June 2022. The lease was originally set to expire in June 2015. The lease provides for

prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$0.7 million. In connection with the extension of the lease and modification of certain terms of the lease, we paid \$0.2 million in leasing commissions, and will pay \$1.3 million in tenant improvements prior to second quarter 2015.

*Burnsville, Minnesota:* On June 11, 2014, we extended the lease with the tenant occupying our property located in Burnsville, Minnesota. The new lease covers approximately two-thirds of the space and was extended for an additional eight years, through January 2023. The lease was originally set to expire in June 2015. The tenant in this property will continue to pay rent on the entire building through June 2015, and we are working to identify tenants to lease the remaining one-third of the building. The new lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of \$1.0 million. Rental income per square foot increased 14% from the previous lease. The lease grants the tenant two options to extend the lease for an additional three years each. In connection with the extension of the lease and the modification of certain terms under the lease, we paid \$0.5 million in leasing commissions, and will pay \$3.3 million in tenant improvements prior to the end of first quarter 2015.

*Akron, Ohio:* On July 7, 2014, we extended the lease with one of the tenants occupying our property located in Akron, Ohio. The new lease covers approximately two-thirds of the space and was extended for an additional five years, through March 2020. The lease was originally set to expire in March 2015. This tenant will continue to pay its existing rent through March 2015. The new lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of \$0.6 million. The lease grants the tenant two options to extend the lease for an additional five years each. In connection with the extension of the lease and the modification of certain terms under the lease, we paid \$0.2 million in leasing commissions, and will pay \$0.9 million in tenant improvements prior to the end of second quarter 2015. On December 24, 2014, we extended the lease with the other tenant occupying our property located in Akron, Ohio. The new lease covers the remaining space and was extended for an additional five years through March 2020. The lease was originally set to expire in March 2015. This tenant will also continue to pay its existing rent through March 2015. The new lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of \$0.1 million. The lease grants the tenant two options to extend the lease for an additional five years each. In connection with the extension of the lease and the modification of certain terms under the lease, we will pay \$0.1 million in tenant improvements during fiscal year 2015.

*Concord Township, Ohio:* On September 25, 2014, we modified the lease with the tenant occupying our property located in Concord Township, Ohio. The lease covering this property was adjusted to defer a portion of rental payments covering the period August 2014 through December 2014. The tenant will repay the deferred rent balance monthly during calendar year 2015. On November 14, 2014, we further modified the lease with this tenant. The lease covering this property was adjusted to change the lease termination date from August 2034, to December 2024. Accordingly, annual straight line rent decreased from \$1.7 million under the prior amendment, to \$1.4 million. The lease grants the tenant three options to extend the lease for an additional five years each. Upon execution of this lease amendment, we determined that a portion of our existing deferred rent balance of \$2.5 million was uncollectible, due to the reduction in lease payments and lease term, and we adjusted the balance by approximately \$0.8 million.

*Richmond, Virginia:* On October 16, 2014, we executed a lease with a tenant to occupy our previously vacant property located in Richmond, Virginia. The lease became effective as of September 8, 2014 and has a three-year term. The tenant has an early termination option at any time after July 31, 2016, contingent upon the tenant losing a contract with the customer supporting their operations in our building. The tenant is subject to a termination payment of approximately \$0.03 million if they exercise this option. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$0.2 million. The tenant has one option to renew the lease for an additional period of three years. In connection with the extension of

the lease and modification of certain terms of the lease, we paid \$0.1 million in leasing commissions. No tenant improvements were paid by us in connection with the new lease.

*Canton, North Carolina:* On October 22, 2014, we extended the lease with the tenant occupying our property located in Canton, North Carolina for 10 years through September 2034. The lease was originally set to expire in July 2024. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$1.4 million, as compared to straight line rents of \$0.6 million under the previous lease. We financed a \$5.5 million expansion project on this property, which added an additional 150,000 square feet to the building, which was completed in November 2014.

*South Hadley, Massachusetts:* On October 27, 2014, we extended the lease with the tenant occupying our property located in South Hadley, Massachusetts. The lease covering this property was extended for an additional two years through January 2017. The lease was originally set to expire in January 2015. The lease provides a scheduled rent increase over the previous lease, with annualized straight line rents of approximately \$0.3 million. The tenant has two options to renew the lease for additional periods of one year each. In connection with the extension of the lease and modification of certain terms of the lease, we paid \$0.01 million in leasing commissions.

*Tewksbury, Massachusetts:* On October 30, 2014, we modified the lease with the tenant occupying our property located in Tewksbury, Massachusetts. The lease covering this property was amended to reduce rental charges through the remaining lease term, which is set to expire May 31, 2017. In the event we identify a tenant or a purchaser for the property, we can terminate the lease with the current tenant. Straight line rent on this lease decreased from \$0.9 million per year to \$0.4 million per year after the amendment.

*Maple Heights, Ohio:* On December 1, 2014, we executed a lease with a tenant to occupy a 7,125 square foot vacant outbuilding located on our property in Maple Heights, Ohio. The lease was effective as of December 1, 2014 and has a three-year term. The lease provides for consistent rental payments of \$0.03 million annually. In connection with the extension of the lease and modification of certain terms of the lease, we paid \$0.01 million in leasing commissions.

*Bolingbrook, Illinois:* On December 1, 2014, we executed a lease with a tenant to occupy a portion of our property located in Bolingbrook, Illinois. The lease is for seven years and the tenant occupies 38% of the building. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$0.2 million. The tenant has one option to renew the lease for an additional period of five years. In connection with the extension of the lease and modification of certain terms of the lease, we paid \$0.2 million in leasing commissions, and committed to \$0.5 million in tenant improvements.

*Raleigh, North Carolina:* On February 9, 2015, we modified the leases with the tenant occupying two of our properties, both located in Raleigh, North Carolina. The leases covering these properties were extended for an additional five years each, through July 2020. Both leases were originally set to expire in July 2015. The tenant was previously fully occupying both buildings, totaling 174,426 square feet, but had reduced their space requirement in one of their buildings by 94,200 square feet. Both leases contain prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$0.9 million, as compared to annualized straight line rents of \$1.3 million under the previous terms of the lease. The tenant has two options to renew both leases for an additional period of five years. In connection with the extension of the lease and modification of certain terms of the lease, we anticipate paying \$0.2 million in leasing commissions, and committed to \$0.1 million in tenant improvements.

### *2014 Equity Activities*

The equity issuances summarized below were issued under our universal shelf registration statement (File No. 333-190931) that was effective and on file with the Securities and Exchange Commission at the time of each respective issuance.

*Common Equity:* We completed a public offering totaling 1,610,000 shares of common stock, which closed on June 6, 2014, at a public offering price of \$17.00 per share. Gross proceeds of this offering totaled \$27.4 million and net proceeds, after deducting offering expenses and underwriter discounts, were \$26.0 million. The proceeds from this offering were used to acquire real estate.

*ATM Programs:* During 2014, we sold 2.3 million shares, raising an aggregate of \$39.6 million in net proceeds under our ATM Programs with both Jefferies LLC, or Jefferies, and Cantor Fitzgerald. Proceeds from these offerings were used to acquire real estate, repay indebtedness and for other general corporate purposes. On August 26, 2014, we provided notice of termination of our prior open market sale agreement, or the Prior ATM, with Jefferies under which we offered to sell shares of our common stock with an aggregate sales price of up to \$25.0 million on the open market through Jefferies, as agent, or to Jefferies, as principal. We raised \$7.6 million in net proceeds under the Prior ATM during 2014. On September 2, 2014, we entered into a new At the Market sales agreement, or the New ATM, with Cantor Fitzgerald. Under the New ATM we may, from time to time, offer to sell shares of our common stock with an aggregate sales price of up to \$100.0 million on the open market through Cantor Fitzgerald, as agent, or to Cantor Fitzgerald, as principal, based upon our instructions (including any price, time or size limits or other customary parameters or conditions that we may impose). We raised \$32.0 million in net proceeds under the New ATM during 2014. Sales of shares of our common stock through our New ATM are executed by means of ordinary brokers' transactions on the NASDAQ Global Select Market, or the NASDAQ, or otherwise at market prices, in privately negotiated transactions, crosses or block transactions, as may be agreed between us and Cantor Fitzgerald, including a combination of any of these transactions.

*Senior Common Equity:* During 2014, we sold 430,963 shares of our Senior Common Stock at \$15.00 per share in an ongoing best-efforts public offering and issued 14,093 shares of our Senior Common Stock under the Dividend Reinvestment Plan, or DRIP, program. The net proceeds, after deducting the underwriting discount and commission were \$5.6 million, net of \$0.2 million of investor redemptions. This offering will terminate on March 28, 2015. Proceeds from this offering were used to acquire real estate and for general corporate purposes.

### **Our Adviser and Administrator**

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

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 Ms. Danielle Jones, our chief financial officer, 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 our president and our chief financial officer, all of our executive officers and all of our directors, with the exception of Mr. David



Dullum, serve as either directors or executive officers, or both, of Gladstone Land Corporation. 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. Our Adviser and Administrator employ all of our personnel and pay their payroll, benefits and general expenses directly. We have an investment advisory agreement with our Adviser, or the Advisory Agreement, and an administration agreement with our Administrator, or the Administration Agreement.

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 on short-term debt and mortgages, tax preparation, 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 some or all of such fees on to our tenants and borrowers).

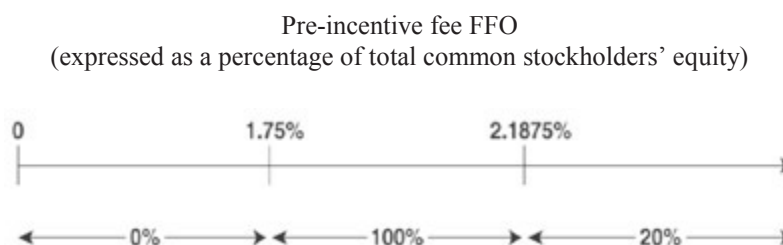
#### *Advisory Agreement*

The Advisory Agreement provides for an annual base management fee equal to 2.0% of our total stockholders' equity, less the recorded value of any preferred stock, or total common stockholders' equity, and for an incentive fee based on FFO. Our Adviser does not charge acquisition or disposition fees when we acquire or dispose of properties as is common with other externally-advised REITs; however, our Adviser may earn fee income from our borrowers or tenants or other sources. For the year ended December 31, 2014, tenants paid \$310,000 in fees to our Adviser, \$150,000 of which was voluntarily credited to our base management fee, discussed further below. For the years ended December 31, 2013 and 2012, tenants paid \$10,000 in fees to our Adviser, respectively.

For purposes of calculating the incentive fee, FFO includes any realized capital gains and capital losses, less any distributions paid on preferred stock and Senior Common Stock, but FFO does not include any unrealized capital gains or losses. The incentive fee would reward our Adviser if our quarterly FFO, before giving effect to any incentive fee, or pre-incentive fee FFO, exceeds 1.75%, or the hurdle rate, of total common stockholders' equity. We pay our Adviser an incentive fee with respect to our pre-incentive fee FFO quarterly as follows:

- no incentive fee in any calendar quarter in which our pre-incentive fee FFO does not exceed the hurdle rate of 1.75% (7% annualized);
- 100% of the amount of the pre-incentive fee FFO that exceeds the hurdle rate, but is less than 2.1875% in any calendar quarter (8.75% annualized); and
- 20% of the amount of our pre-incentive fee FFO that exceeds 2.1875% in any calendar quarter (8.75% annualized).

#### *Quarterly Incentive Fee Based on FFO*



## Percentage of pre-incentive fee FFO allocated to the incentive fee

The incentive fee may be reduced because of a covenant which exists in our Line of Credit agreement which limits distributions to our stockholders to 100% of FFO with acquisition-related costs that are required to be expensed under ASC 805, Business Combinations, added back to FFO. In order to comply with this covenant, our Board of Directors accepted our Adviser's offer to unconditionally, irrevocably and voluntarily waive on a quarterly basis a portion of the incentive fee for the years ended December 31, 2014, 2013 and 2012, which allowed us to maintain the current level of distributions to our stockholders. These waived fees may not be recouped by our Adviser in the future. Our Adviser has indicated that it intends to continue to waive all or a portion of the incentive fee in order to support the current level of distributions to our stockholders; however, our Adviser is not required to issue any such waiver, either in whole or in part.

### *Administration Agreement*

Pursuant to the Administration Agreement, we pay for our allocable portion of our Administrator's overhead expenses incurred while performing its obligations to us, including, but not limited to, rent and the salaries and benefits expenses of our personnel, including our chief financial officer, treasurer, chief compliance officer, general counsel and secretary (who also serves as our Administrator's president), and their respective staffs. Prior to July 1, 2014, our allocable portion was generally derived by multiplying that portion of the Administrator's expenses allocable to all funds managed by the Adviser by the percentage of our total assets at the beginning of each quarter in comparison to the total assets of all funds managed by the Adviser. As approved by our Board of Directors, effective July 1, 2014, our allocable portion of the Administrator's expenses will generally be 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. Management believes that the new methodology of allocating the Administrator's total expenses by approximate percentage of time services were performed among all companies serviced by our Administrator more closely approximates fees paid to actual services performed.

### **Critical Accounting Policies**

The preparation of our financial statements in accordance with Generally Accepted Accounting Principles in the U.S., or GAAP, requires management to make judgments that are subjective in nature in order 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 included elsewhere in this Form 10-K. Below is a summary of accounting policies involving estimates and assumptions that require complex, subjective or significant judgments in their application and that materially affect our results of operations. There were no material changes to our critical accounting policies during the year ended December 31, 2014.

### *Allocation of Purchase Price*

When we acquire real estate, we allocate the purchase price to (i) the acquired tangible assets and liabilities, consisting of land, building, tenant improvements and long-term debt and (ii) the identified intangible assets and liabilities, consisting of the value of above-market and below-market leases, in-place leases, unamortized lease origination costs, tenant relationships and capital lease obligations, based in each case on their fair values in accordance with ASC 805, Business Combinations. All expenses related to the acquisition are expensed as incurred.

Our Adviser estimates value using methods similar to those used by independent appraisers (e.g., discounted cash flow analysis). Factors considered by management in its analysis include an estimate of carrying costs during hypothetical expected lease-up periods, considering current market conditions and costs to execute similar leases. Our Adviser also considers information obtained about each property as a result of our pre-acquisition due diligence, marketing and leasing activities in estimating the fair value of the tangible and intangible assets and liabilities acquired. In estimating carrying costs, management also

includes real estate taxes, insurance and other operating expenses and estimates of lost rentals at market rates during the hypothetical expected lease-up periods, which primarily range from 9 to 18 months, depending on specific local market conditions. Our Adviser also estimates costs to execute similar leases, including leasing commissions, legal and other related expenses to the extent that such costs are not already incurred in connection with a new lease origination as part of the transaction. Our Adviser also considers the nature and extent of our existing business relationships with the tenant, growth prospects for developing new business with the tenant, the tenant's credit quality and management's expectations of lease renewals (including those existing under the terms of the lease agreement), among other factors. A change in any of the assumptions above, which are very subjective, could have a material impact on our results of operations.

The allocation of the purchase price directly affects the following in our consolidated financial statements:

- The amount of purchase price allocated to the various tangible and intangible assets on our balance sheet;
- The amounts allocated to the value of above-market and below-market lease values are amortized to rental income over the remaining non-cancelable terms of the respective leases. The amounts allocated to all other tangible and intangible assets are amortized to depreciation or amortization expense. Thus, depending on the amounts allocated between land and other depreciable assets, changes in the purchase price allocation among our assets could have a material impact on our FFO, a metric which is used by many REIT investors to evaluate our operating performance; and
- The period of time over which tangible and intangible assets are depreciated varies greatly, and thus, changes in the amounts allocated to these assets will have a direct impact on our results of operations. Intangible assets are generally amortized over the respective life of the leases, which normally range from 10 to 15 years. Also, we depreciate our buildings over 39 years, but do not depreciate our land. These differences in timing could have a material impact on our results of operations.

#### *Asset Impairment Evaluation*

We periodically review the carrying value of each property to determine if circumstances that indicate impairment in the carrying value of the investment exist or that depreciation periods should be modified. In determining if impairment exists, our Adviser considers such factors as our tenants' payment histories, the financial condition of our tenants, including calculating the current leverage ratios of tenants, the likelihood of lease renewal, business conditions in the industries in which our tenants operate and whether the carrying value of our real estate has decreased. If any of the factors above indicate the possibility of impairment, we prepare a projection of the undiscounted future cash flows, without interest charges, of the specific property and determine if the carrying amount of such property is recoverable. In preparing the projection of undiscounted future cash flows, we estimate the holding periods of the properties and cap rates using information that we obtain from market comparability studies and other comparable sources. If impairment were indicated, the carrying value of the property would be written down to its estimated fair value based on our best estimate of the property's discounted future cash flows using assumptions from market participants. Any material changes to the estimates and assumptions used in this analysis could have a significant impact on our results of operations, as the changes would impact our determination of whether impairment is deemed to have occurred and the amount of impairment loss that we would recognize.

Using the methodology discussed above, we evaluated our entire portfolio as of December 31, 2014, for any impairment indicators and performed an impairment analysis on those select properties that had an indication of impairment. We concluded that our Roseville, Minnesota property was impaired as of March 31, 2014. We determined that the expected undiscounted cash flows, based upon a revised estimated holding period of this property, were below the current carrying value. The estimated holding period was revised after a potential tenant that we were anticipating to lease a large portion of the vacant space, during the three months ended March 31, 2014, did not execute a lease on the property. Consequently, we revised

the holding period to coincide with maturity of the mortgage loan on the property in June 2014. Accordingly, we reduced the carrying value of this property to its estimated fair value, less cost to sell, and we recognized an impairment loss of \$14.2 million during the year ended December 31, 2014. This property was returned to the lender in a deed-in-lieu transaction on November 12, 2014.

We had previously reported that our property located in South Hadley, Massachusetts was at risk of becoming impaired in the future. The existing tenant extended the lease on the property for two years, and it will now expire in January 2017. Because of this lease extension, we are no longer at risk of having to impair this property in fiscal year 2015.

We will continue to monitor our portfolio for any other indicators of impairment. There have been no other impairments recognized on our real estate assets since inception.

## Results of Operations

The weighted-average yield on our total portfolio, which was 8.7% as of December 31, 2014, is calculated by taking the annualized straight-line rents, reflected as rental income on our consolidated statements of operations, of each acquisition as a percentage of the acquisition cost. The weighted-average yield does not account for the interest expense incurred on the mortgages placed on our properties.

*A comparison of our operating results for the years ended December 31, 2014 and 2013 is below (dollars in thousands, except per share amounts):*

	For the year ended December 31,			
	2014	2013	\$ Change	% Change
Operating revenues				
Rental revenue	\$ 71,211	\$ 59,769	\$ 11,442	19%
Tenant recovery revenue	2,079	1,574	505	32
Interest income from mortgage note receivable	466	-	466	NM
Total operating revenues	<u>73,756</u>	<u>61,343</u>	<u>12,413</u>	<u>20</u>
Operating expenses				
Depreciation and amortization	28,864	22,827	6,037	26
Property operating expenses	4,711	3,348	1,363	41
Acquisition related expenses	1,438	768	670	87
Base management fee	2,798	2,014	784	39
Incentive fee	4,305	4,201	104	2
Administration fee	1,526	1,467	59	4
General and administrative	2,689	1,655	1,034	62
Impairment charge	14,238	-	14,238	NM
Total operating expenses before credit to incentive fee	<u>60,569</u>	<u>36,280</u>	<u>24,289</u>	<u>67</u>
Credit to base management fee	(150)	-	(150)	NM
Credit to incentive fee	(3,013)	(3,457)	444	(13)
Total operating expenses	<u>57,406</u>	<u>32,823</u>	<u>24,583</u>	<u>75</u>
Other income (expense)				
Interest expense	(26,197)	(24,351)	(1,846)	8
Distributions attributable to Series C mandatorily redeemable preferred stock	(2,743)	(2,743)	-	-
Gain on sale of real estate	1,240	-	1,240	NM
Gain on debt extinguishment	5,274	-	5,274	NM
Other income	174	101	73	72
Total other expense	<u>(22,252)</u>	<u>(26,993)</u>	<u>4,741</u>	<u>(18)</u>
Net (loss) income	<u>(5,902)</u>	<u>1,527</u>	<u>(7,429)</u>	<u>(487)</u>
Distributions attributable to Series A and B preferred stock	(4,094)	(4,094)	-	-
Distributions attributable to senior common stock	(542)	(300)	(242)	81
Net loss attributable to common stockholders	<u>\$ (10,538)</u>	<u>\$ (2,867)</u>	<u>\$ (7,671)</u>	<u>268</u>
Net loss attributable to common stockholders per weighted average share of common stock - diluted	<u>\$ (0.61)</u>	<u>\$ (0.22)</u>	<u>\$ (0.39)</u>	<u>179</u>
FFO available to common stockholders	<u>\$ 31,324</u>	<u>\$ 19,960</u>	<u>\$ 11,364</u>	<u>57</u>
FFO per weighted average share of common stock - diluted	<u>\$ 1.77</u>	<u>\$ 1.49</u>	<u>\$ 0.28</u>	<u>19</u>

NM = Not meaningful

### Operating Revenues

Rental income increased for the year ended December 31, 2014, as compared to the year ended December 31, 2013, because of the 11 properties acquired during 2014, partially offset by a loss of approximately \$1.1 million of rental income due to vacancies and property sales in our portfolio during 2014.

Tenant recovery revenue increased for the year ended December 31, 2014, as compared to the year ended December 31, 2013. This increase was primarily due to operating expense recoveries from nine tenants in properties acquired in 2014 that are subject to a base year or gross lease.

Interest income from mortgage note receivable increased for the year ended December 31, 2014, as compared to the year ended December 31, 2013, because of interest earned on the mortgage loan issued in July 2014 that was not outstanding during 2013.

### *Operating Expenses*

Depreciation and amortization expenses increased for the year ended December 31, 2014, as compared to the year ended December 31, 2013, because of the 11 properties acquired during 2014 and a full year of depreciation for properties acquired in 2013.

Property operating expenses consist of franchise taxes, management fees, insurance, ground lease payments and overhead expenses paid on behalf of certain of our properties. Property operating expenses increased for the year ended December 31, 2014, as compared to the year ended December 31, 2013, primarily because of an increase in overhead (maintenance, repair and utilities) expenses at our vacant properties, coupled with expenses at certain properties acquired during 2014 that are subject to a base year or gross lease.

Acquisition related expenses primarily consist of legal fees and fees incurred for third-party reports prepared in connection with potential acquisitions and our due diligence analyses related thereto. Acquisition related expense increased for the year ended December 31, 2014, as compared to the year ended December 31, 2013, as a result of acquiring 11 properties during 2014, as compared to 7 properties during 2013.

The base management fee increased for the year ended December 31, 2014, as compared to the year ended December 31, 2013, due to an increase in total common stockholders' equity, the main component of the calculation, partially offset by a credit to the base management fee received during the year ended December 31, 2014 related to an advisory fee received by our Advisor from one of our tenants. The calculation of the base management fee is described in detail above under "*Advisory and Administration Agreements.*"

The incentive fee increased slightly for the year ended December 31, 2014, as compared to the year ended December 31, 2013, because of an increase in pre-incentive fee FFO. The increase in pre-incentive fee FFO was due to an increase in rental revenues from the properties acquired during 2014, which was partially offset by an increase in property operating and interest expenses during the year ended December 31, 2014, as compared to the year ended December 31, 2013; however this was partially offset by no incentive fee being recorded during the fourth quarter of 2014 because of the realization of the loss related to the Roseville, Minnesota property. The incentive fee credit decreased for the year ended December 31, 2014, as compared to the year ended December 31, 2013, because of an increase in total operating revenues from the properties acquired in the past year partially offset by the amount of common distributions paid on the shares issued during the past year coupled with higher expenses at our vacant properties. The calculation of the incentive fee is described in detail above within "*Advisory and Administration Agreements.*"

The administration fee increased slightly for the year ended December 31, 2014, as compared to the year ended December 31, 2013. The increase was primarily from an increase in the amount of the fee allocated to us by our Administrator during the first half of 2014; however, in July 2014, the allocation of the fee was revised such that the fee is generally now based upon the percentage of time employees of the Administrator spend on our matters in relation to time spent on other funds contractually managed by our Administrator versus the prior methodology whereby we were generally allocated the fee based upon our total assets in relation to other funds managed by our Administrator. We anticipate our future administration fees to be lower under the new methodology. The calculation of the administration fee is described in detail above within "*Advisory and Administration Agreements.*"

General and administrative expenses increased for the year ended December 31, 2014, as compared to the year ended December 31, 2013, as a result of an increase in professional fees from the increase in our portfolio coupled with the write off of \$0.8 million of the deferred rent asset associated with our property located in Concord Township, Ohio.

The impairment charge is a result of the impairment of our Roseville, Minnesota property. We did not recognize an impairment charge during the year ended December 31, 2013.

### Other Income and Expenses

Interest expense increased for the year ended December 31, 2014, as compared to the year ended December 31, 2013. This increase was primarily a result of interest on the \$62.2 million of mortgage debt assumed and issued during 2014, partially offset by reduced interest expense on our long-term financings from amortizing and balloon principal payments made during 2014.

The gain on sale of real estate is a result of our property we sold located in Sterling Heights, Michigan in June 2014.

The gain on debt extinguishment is a result of the deed-in-lieu transaction related to our Roseville, Minnesota property that was completed in November 2014. The outstanding debt on the property that was deemed satisfied in exchange for the property was in excess of the carrying value of the property. We did not recognize a gain on debt extinguishment during the year ended December 31, 2013.

Other income increased during the year ended December 31, 2014, as compared to the year ended December 31, 2013, because of an increase in management fees collected from certain of our tenants.

### Net Loss Available to Common Stockholders

Net loss available to common stockholders increased for the year ended December 31, 2014, as compared to the year ended December 31, 2013, primarily because of the realized loss from the Roseville, Minnesota property coupled with increased interest expense, property operating expenses, depreciation expense, partially offset by an increase in rental income earned from the 11 properties acquired during 2014 and the gain on sale of real estate.

A comparison of our operating results for the years ended December 31, 2013 and 2012 is below (dollars in thousands, except per share amounts):

	For the year ended December 31,			
	2013	2012	\$ Change	% Change
<b>Operating revenues</b>				
Rental income	\$ 59,769	\$ 50,915	\$ 8,854	17%
Tenant recovery revenue	1,574	355	1,219	343%
Total operating revenues	61,343	51,270	10,073	20%
<b>Operating expenses</b>				
Depreciation and amortization	22,827	16,831	5,996	36%
Property operating expenses	3,348	1,588	1,760	111%
Acquisition related expense	768	949	(181)	-19%
Base management fee	2,014	1,467	547	37%
Incentive fee	4,201	3,569	632	18%
Administration fee	1,467	1,118	349	31%
General and administrative	1,655	1,594	61	4%
Total operating expenses before credit to incentive fee	36,280	27,116	9,164	34%
Credit to incentive fee	(3,457)	(2,221)	(1,236)	56%
Total operating expenses	32,823	24,895	7,928	32%
<b>Other income (expense)</b>				
Interest expense	(24,351)	(20,226)	(4,125)	20%
Distributions attributable to Series C mandatorily redeemable preferred stock	(2,743)	(2,515)	(228)	9%
Other income	101	127	(26)	-20%
Total other expense	(26,993)	(22,614)	(4,379)	19%
<b>Net income</b>	1,527	3,761	(2,234)	-59%
Distributions attributable to Series A and B preferred stock	(4,094)	(4,093)	(1)	0%
Distributions attributable to senior common stock	(300)	(113)	(187)	165%
<b>Net loss available to common stockholders</b>	<u>\$ (2,867)</u>	<u>\$ (445)</u>	<u>\$ (2,422)</u>	<u>544%</u>
<b>Net loss available to common stockholders per weighted average share of common stock - diluted</b>	<u>\$ (0.22)</u>	<u>\$ (0.04)</u>	<u>\$ (0.18)</u>	<u>450%</u>
<b>FFO available to common stockholders</b>	<u>\$ 19,960</u>	<u>\$ 16,386</u>	<u>\$ 3,574</u>	<u>22%</u>
<b>FFO per weighted average share of common stock - diluted</b>	<u>\$ 1.49</u>	<u>\$ 1.48</u>	<u>\$ 0.01</u>	<u>1%</u>

### *Operating Revenues*

Rental income increased for the year ended December 31, 2013, as compared to the year ended December 31, 2012, because of the seven properties acquired during 2013, partially offset by a loss of rental income due to vacancies in our portfolio during 2013.

Tenant recovery revenue increased for the year ended December 31, 2013, as compared to the year ended December 31, 2012. This increase was primarily due to reimbursements from our tenant in our partially vacant building located in Roseville, Minnesota.

### *Operating Expenses*

Depreciation and amortization expenses increased for the year ended December 31, 2013, as compared to the year ended December 31, 2012, because of the seven properties acquired during 2013 and a full year of depreciation for properties acquired in 2012.

Property operating expenses consist of franchise taxes, management fees, insurance, ground lease payments and overhead expenses paid on behalf of certain of our properties. Property operating expenses increased for the year ended December 31, 2013, as compared to the year ended December 31, 2012, primarily because of an increase in overhead (maintenance, repair and utilities) expenses at our partially vacant Roseville, Minnesota building.

Acquisition related expenses primarily consist of legal fees and fees incurred for third-party reports prepared in connection with potential acquisitions and our due diligence analyses related thereto. Acquisition related expense decreased for the year ended December 31, 2013, as compared to the year ended December 31, 2012, as a result of acquiring only seven properties during 2013, as compared to eight properties during 2012.

The base management fee increased for the year ended December 31, 2013, as compared to the year ended December 31, 2012, due to an increase in total common stockholders' equity, the main component of the calculation. The calculation of the base management fee is described in detail above under "*Advisory and Administration Agreements.*"

The incentive fee increased for the year ended December 31, 2013, as compared to the year ended December 31, 2012, because of an increase in pre-incentive fee FFO. The increase in pre-incentive fee FFO was due to an increase in rental revenues from the properties acquired during 2013, which was partially offset by an increase in property operating and interest expenses during the year ended December 31, 2013, as compared to the year ended December 31, 2012.

The incentive fee credit increased for the year ended December 31, 2013, as compared to the year ended December 31, 2012, because of an increase in the amount of common distributions paid from the shares issued during 2013. The calculation of the incentive fee is described in detail above within "*Advisory and Administration Agreements.*"

The administration fee increased for the year ended December 31, 2013, as compared to the year ended December 31, 2012, as a result of an increase in the amount of the total expenses our Administrator incurred during 2013, coupled with a larger percentage of the fee being allocated to us as a result of the increase in our total assets during 2013. The calculation of the administration fee is described in detail above within "*Advisory and Administration Agreements.*"

General and administrative expenses increased for the year ended December 31, 2013, as compared to the year ended December 31, 2012, as a result of an increase in professional fees related to tax and audit services from the increase in our portfolio.



### *Other Income and Expenses*

Interest expense increased for the year ended December 31, 2013, as compared to the year ended December 31, 2012. This increase was primarily a result of interest on the \$80.0 million of mortgage debt assumed and issued during 2013, partially offset by reduced interest expense on our long-term financings from amortizing and balloon principal payments made during 2013.

Distributions for our mandatorily redeemable preferred stock increased for the year ended December 31, 2013, as compared to the year ended December 31, 2012, because the public offering of shares of our 7.125% Series C Cumulative Term Preferred stock, or Term Preferred Stock, was completed in February 2012, and thus was not outstanding for the full year ended December 31, 2012.

Other income decreased during the year ended December 31, 2013, as compared to the year ended December 31, 2012, because of lower interest income on employee loans earned during 2013, as compared to 2012 due to principal repayments made by employees of our Adviser during 2013.

### *Net Loss Available to Common Stockholders*

Net loss available to common stockholders increased for the year ended December 31, 2013, as compared to the year ended December 31, 2012, primarily because of increased interest expense, property operating expenses, depreciation expense and increased distributions to our preferred stockholders from the issuance of our Term Preferred Stock, partially offset by an increase in rental income earned from the seven properties acquired during 2013.

## **Liquidity and Capital Resources**

### *Overview*

Our sources of liquidity include cash flows from operations, cash and cash equivalents, borrowings under our Line of Credit, obtaining mortgages on our unencumbered properties and issuing additional equity securities. Our available liquidity at December 31, 2014, was \$17.9 million, including \$8.6 million in cash and cash equivalents and an available borrowing capacity of \$9.3 million under our Line of Credit. Our available borrowing capacity under the Line of Credit has increased to \$28.3 million since the end of the year.

### *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, commercial and retail real property, make mortgage loans, or pay down outstanding borrowings under our Line of Credit. 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 and on borrowings under our Line of Credit, and fund our current operating costs. Our long-term liquidity needs include proceeds necessary to grow and maintain our portfolio of investments.

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 borrowings under our Line of Credit and fund our current operating costs in the near term. 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. Historically, our Adviser has provided such partial credits to our management fees on a quarterly basis. 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 2014, we raised net proceeds of \$26.0 million in common equity in an underwritten follow-on public offering, at a share price of \$17.00. We also raised net proceeds of \$7.6 million of common equity under our Prior ATM with Jefferies, at an average share price of \$17.47, and net proceeds of \$32.0 million of common equity under our New ATM with Cantor Fitzgerald at an average share price of \$17.35. Furthermore, we raised \$5.6 million in net proceeds of senior common equity, net of \$0.2 million of investor redemptions. We used these proceeds to acquire additional real estate and for general corporate purposes.

As of February 18, 2015, we have the ability to raise up to \$185.7 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. 333-190931), or the Universal Shelf, in one or more future public offerings. Of the \$185.7 million of available capacity under our Universal Shelf, \$54.0 million of common stock is reserved for additional sales under our New ATM and \$40.9 million is reserved for sales of our Senior Common Stock. Our Senior Common Stock offering will terminate on March 28, 2015. We believe that our ATM program is a sufficient source of liquidity for 2015, and our Senior Common Stock offerings will not materially impact our 2015 acquisitions.

### *Debt Capital*

As of December 31, 2014, we had mortgage notes payable in the aggregate principal amount of \$459.3 million, collateralized by a total of 77 properties with terms at issuance ranging from 4 years to 25 years. The weighted-average interest rate on the mortgage notes payable as of December 31, 2014 was 5.3%.

The CMBS market has recovered from the recent recession; see the discussion in “*Business Environment*” above. Specifically, we continue to see banks and other non-bank lenders willing to issue 10-year mortgages. Consequently, we are focused on obtaining mortgages through regional banks, non-bank lenders and the CMBS market.

We have mortgage debt in the aggregate principal amount of \$42.4 million payable during 2015 and \$99.0 million payable during 2016. The 2015 principal amounts payable include both amortizing principal payments and 3 balloon principal payments due in the second half of the year. We anticipate being able to refinance the mortgages that come due during 2015 and 2016 with a combination of new mortgage debt and additional equity.

### *Operating Activities*

Net cash provided by operating activities during the year ended December 31, 2014, was \$28.2 million, as compared to net cash provided by operating activities of \$19.9 million for the year ended December 31, 2013. This increase was primarily a result of an increase in rental income received from the properties acquired during 2014, partially offset by the loss of rental income from vacancies in our portfolio and property operating expenses we are responsible for at certain of our vacant properties. The majority of cash from operating activities is generated from the rental payments 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 Line of Credit, distributions to our stockholders, management fees to our Adviser, and other entity-level expenses.

### *Investing Activities*

Net cash used in investing activities during the year ended December 31, 2014, was \$130.4 million, which primarily consisted of the acquisition of 11 properties, the expansion at another property and tenant improvements performed at certain of our properties, partially offset by the proceeds from the sale of a property during the year ended December 31, 2014, as compared to net cash used in investing activities during the year ended December 31, 2013, of \$137.1 million, which primarily consisted of the acquisition of seven properties, and the expansion at another property coupled with tenant improvements performed at certain of our properties.

### *Financing Activities*

Net cash provided by financing activities during the year ended December 31, 2014, was \$102.3 million, which primarily consisted of proceeds from the sale of common stock, borrowings under our Line of Credit and proceeds from the issuance of mortgage notes payable, partially offset by the increase in distributions paid to our stockholders and principal repayments on mortgage notes payable. Net cash provided by financing activities for the year ended December 31, 2013, was \$120.2 million, which primarily consisted of proceeds from the sale of common stock and proceeds from the issuance of mortgage notes payable, partially offset by the increase in distributions paid to our stockholders and principal repayments on mortgage notes payable.

### *Line of Credit*

In August 2013, we procured our \$60.0 million Line of Credit, expanded to \$75.0 million in November 2014, with KeyBank National Association (serving as a revolving lender, a letter of credit issuer and an administrative agent) and added Citizens Bank of Pennsylvania as an additional lender. Comerica Bank was subsequently added as another lender in December 2013. In March 2014, we amended our Line of Credit to extend the maturity date by one year to August 2017. We also modified certain terms under the Line of Credit, including the calculation of the total asset value and unencumbered asset value. The applicable LIBOR margins were also reduced 25 basis points at each pricing level. As a result of these modifications, the availability under our Line of Credit increased by \$1.3 million.

The Line of Credit initially matures in August 2017; however, we have a one-year extension option subject to the payment of an extension fee equal to 25 basis points on the initial maturity date and certain other customary conditions.

The Line of Credit has a letter of credit sublimit of up to \$20.0 million. In addition, we may expand the Line of Credit up to a total of \$100.0 million upon satisfaction of certain conditions and payment of the associated up front and arrangement fees at the time of such increase. The interest rate per annum applicable to the Line of Credit is equal to the London Interbank Offered Rate, or LIBOR, plus an applicable margin of up to 3.25%, depending upon our leverage. The leverage ratio used in determining the applicable margin for interest on the Line of Credit is recalculated quarterly. We are subject to an annual maintenance fee of \$0.03 million per year and an unused commitment fee of 25 basis points per year, which accrues quarterly. Our ability to access this source of financing is subject to our continued ability to meet customary lending requirements, such as compliance with financial and operating covenants and our meeting certain lending limits. One such covenant requires us to limit distributions to our stockholders to 100% of our FFO, with acquisition-related costs required to be expensed under ASC 805 added back to FFO. In addition, the maximum amount we may draw under the Line of Credit is based on a percentage of the value of a pool of unencumbered properties, which must meet agreed upon eligibility standards.

If and when long-term mortgages are arranged for properties in the unencumbered pool, the banks will reduce the availability under the Line of Credit by the amount advanced against that property's value. Conversely, as we purchase new properties meeting the eligibility standards, we may add these new properties to the unencumbered pool to obtain additional availability under the Line of Credit. The availability under the Line of Credit is also reduced by letters of credit used in the ordinary course of business. We may use the advances under the Line of Credit for both general corporate purposes and the acquisition of new investments.

As of December 31, 2014, there was \$43.3 million outstanding under our Line of Credit at an interest rate of approximately 3.17% and \$4.5 million outstanding under letters of credit at a weighted average interest rate of 3.0%. As of February 18, 2015, the maximum additional amount we could draw was \$28.3 million. We were in compliance with all covenants under the Line of Credit as of December 31, 2014.

## Contractual Obligations

The following table reflects our material contractual obligations as of December 31, 2014 (in thousands):

Contractual Obligations	Payments Due by Period				
	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Debt Obligations <sup>(1)</sup>	\$ 540,392	\$ 42,436	\$ 248,495	\$ 55,196	\$ 194,265
Interest on Debt Obligations <sup>(2)</sup>	120,258	26,617	38,560	22,982	32,099
Operating Lease Obligations <sup>(3)</sup>	6,685	429	861	866	4,529
Purchase Obligations <sup>(4)</sup>	5,331	5,331	-	-	-
Total	<u>\$ 672,666</u>	<u>\$ 74,813</u>	<u>\$ 287,916</u>	<u>\$ 79,044</u>	<u>\$ 230,893</u>

(1) Debt obligations represent borrowings under our Line of Credit, which represents \$43.3 million of the debt obligation due in 2017, mortgage notes payable that were outstanding as of December 31, 2014, and amounts due to the holders of our Term Preferred Stock.

(2) Interest on debt obligations includes estimated interest on our borrowings under our Line of Credit, mortgage notes payable and interest due to the holders of our Term Preferred Stock. The balance and interest rate on our Line of Credit is variable; thus, the amount of interest calculated for purposes of this table was based upon rates and balances as of December 31, 2014.

(3) Operating lease obligations represent the ground lease payments due on our Tulsa, Oklahoma, Dartmouth, Massachusetts, and Springfield, Missouri properties.

(4) Purchase obligations consist of \$1.2 million to fund tenant improvements at two of our Ohio properties, \$2.8 million in tenant improvements at our Burnsville, MN property, \$0.8 million of tenant improvements at our Austin, TX property, and \$0.5 million of tenant improvements at our Bolingbrook, IL property. These items were recognized on our balance sheet for the year ended December 31, 2014.

## Off-Balance Sheet Arrangements

We did not have any off-balance sheet arrangements as of December 31, 2014.

#### Item 7A. 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 Line of Credit 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 a derivative contract with Wells Fargo to cap interest rates for the variable rate note payable on our Champaign, Illinois property. We paid a fee of \$0.03 million to cap LIBOR rates at 3.0%, to limit our exposure to interest rates on this note payable.

To illustrate the potential impact of changes in interest rates on our net income for the year ended December 31, 2014, we have performed the following analysis, which assumes that our balance sheet remains 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 in the one month LIBOR as of December 31, 2014. As of December 31, 2014, our effective average LIBOR was 0.17%; thus, a 1%, 2% or 3% decrease could not occur.

Interest Rate Change	(Dollars in Thousands)	
	Increase to Interest Expense	Net Decrease to Net Income
1% Increase to LIBOR	\$ 522	\$ (522)
2% Increase to LIBOR	1,044	(1,044)
3% Increase to LIBOR	1,525	(1,525)

As of December 31, 2014, the fair value of our mortgage debt outstanding was \$476.9 million. Interest rate fluctuations may affect the fair value of our debt instruments. If interest rates on our debt instruments, using rates at December 31, 2014, had been one percentage point higher or lower, the fair value of those debt instruments on that date would have decreased or increased by \$26.3 million and \$11.0 million, respectively.

In the future, we may be exposed to additional effects of interest rate changes, primarily as a result of our Line of Credit 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.

**Item 8. Financial Statements and Supplementary Data.**

**Index to Consolidated Financial Statements**

Report of Management on Internal Controls over Financial Reporting	64
Report of Independent Registered Public Accounting Firm	65
Consolidated Balance Sheets as of December 31, 2014 and 2013	66
Consolidated Statements of Operations for the years ended December 31, 2014, 2013 and 2012	67
Consolidated Statements of Stockholders' Equity for the years ended December 31, 2014, 2013 and 2012	68
Consolidated Statements of Cash Flows for the years ended December 31, 2014, 2013 and 2012	69
Notes to Consolidated Financial Statements	70
Schedule III – Real Estate and Accumulated Depreciation	95
Schedule IV – Mortgage Loans on Real Estate	101

## **Report of Management on Internal Controls over Financial Reporting**

To the Stockholders and Board of Directors of Gladstone Commercial Corporation:

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rule 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934. Our internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and include those policies and procedures that pertain to the maintenance of records that in reasonable detail accurately and fairly reflect our transactions and the dispositions of our assets, provide reasonable assurance that our transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with appropriate authorizations; and provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on our financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

Under the supervision and with the participation of our management, we assessed the effectiveness of our internal control over financial reporting based on the framework in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations (COSO). Based on our assessment, management concluded that our internal control over financial reporting was effective as of December 31, 2014.

The effectiveness of our internal control over financial reporting as of December 31, 2014 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report which is included herein.

February 18, 2015

## Report of Independent Registered Public Accounting Firm

To the Stockholders and Board of Directors of Gladstone Commercial Corporation:

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, stockholders' equity, and cash flows present fairly, in all material respects, the financial position of Gladstone Commercial Corporation and its subsidiaries at December 31, 2014 and December 31, 2013, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2014 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedules listed in the accompanying index present fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2014, based on criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements and financial statement schedules, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Report of Management on Internal Controls over Financial Reporting. Our responsibility is to express opinions on these financial statements, on the financial statement schedules, and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ PricewaterhouseCoopers LLP  
McLean, Virginia  
February 18, 2015



**Gladstone Commercial Corporation**  
**Consolidated Balance Sheets**  
(Dollars in Thousands, Except Share and Per Share Data)

	December 31, 2014	December 31, 2013
<b>ASSETS</b>		
Real estate, at cost	\$ 722,565	\$ 642,353
Less: accumulated depreciation	92,133	81,241
Total real estate, net	630,432	561,112
Lease intangibles, net	98,814	79,632
Mortgage note receivable	5,600	-
Cash and cash equivalents	8,599	8,546
Restricted cash	3,547	5,051
Funds held in escrow	11,096	8,653
Deferred rent receivable, net	21,728	18,905
Deferred financing costs, net	6,213	6,840
Other assets	1,765	1,786
	787,794	690,525
<b>TOTAL ASSETS</b>	<b>\$ 787,794</b>	<b>\$ 690,525</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>LIABILITIES</b>		
Mortgage notes payable	\$ 459,299	\$ 422,602
Borrowings under line of credit	43,300	24,400
Series C mandatorily redeemable preferred stock, par value \$0.001 per share; \$25 per share liquidation preference; 1,700,000 shares authorized; and 1,540,000 shares issued and outstanding at December 31, 2014 and December 31, 2013, respectively	38,500	38,500
Deferred rent liability, net	8,594	6,015
Asset retirement obligation	3,616	3,884
Accounts payable and accrued expenses	8,285	2,359
Due to Adviser and Administrator <sup>(1)</sup>	916	1,360
Other liabilities	7,612	8,259
	570,122	507,379
Total Liabilities	<b>\$ 570,122</b>	<b>\$ 507,379</b>
Commitments and contingencies <sup>(2)</sup>		
<b>STOCKHOLDERS' EQUITY</b>		
Series A and B redeemable preferred stock, par value \$0.001 per share; \$25 per share liquidation preference; 2,300,000 shares authorized and 2,150,000 shares issued and outstanding at December 31, 2014 and December 31, 2013, respectively	\$ 2	\$ 2
Senior common stock, par value \$0.001 per share; 7,500,000 shares authorized and 809,411 and 374,484 shares issued and outstanding at December 31, 2014 and December 31, 2013, respectively	1	-
Common stock, par value \$0.001 per share, 38,500,000 shares authorized and 19,589,606 and 15,662,414 shares issued and outstanding at December 31, 2014 and December 31, 2013, respectively	20	16
Additional paid in capital	369,748	298,751
Notes receivable - employee	(375)	(375)
Distributions in excess of accumulated earnings	(151,724)	(115,248)
	217,672	183,146
Total Stockholders' Equity	<b>217,672</b>	<b>183,146</b>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$ 787,794</b>	<b>\$ 690,525</b>

<sup>(1)</sup> Refer to Note 2 "Related-Party Transactions"

<sup>(2)</sup> Refer to Note 9 "Commitments and Contingencies"

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

**Gladstone Commercial Corporation**  
**Consolidated Statements of Operations**  
(Dollars in Thousands, Except Per Share Data)

	For the year ended December 31,		
	2014	2013	2012
Operating revenues			
Rental revenue	\$ 71,211	\$ 59,769	\$ 50,915
Tenant recovery revenue	2,079	1,574	355
Interest income from mortgage note receivable	466	-	-
Total operating revenues	<u>73,756</u>	<u>61,343</u>	<u>51,270</u>
Operating expenses			
Depreciation and amortization	28,864	22,827	16,831
Property operating expenses	4,711	3,348	1,588
Acquisition related expenses	1,438	768	949
Base management fee <sup>(1)</sup>	2,798	2,014	1,467
Incentive fee <sup>(1)</sup>	4,305	4,201	3,569
Administration fee <sup>(1)</sup>	1,526	1,467	1,118
General and administrative	2,689	1,655	1,594
Impairment charge	14,238	-	-
Total operating expenses before credit to incentive fee	<u>60,569</u>	<u>36,280</u>	<u>27,116</u>
Credit to base management fee <sup>(1)</sup>	(150)	-	-
Credit to incentive fee <sup>(1)</sup>	(3,013)	(3,457)	(2,221)
Total operating expenses	<u>57,406</u>	<u>32,823</u>	<u>24,895</u>
Other income (expense)			
Interest expense	(26,197)	(24,351)	(20,226)
Distributions attributable to Series C mandatorily redeemable preferred stock	(2,743)	(2,743)	(2,515)
Gain on sale of real estate	1,240	-	-
Gain on debt extinguishment	5,274	-	-
Other income	174	101	127
Total other expense	<u>(22,252)</u>	<u>(26,993)</u>	<u>(22,614)</u>
Net (loss) income	<u>(5,902)</u>	<u>1,527</u>	<u>3,761</u>
Distributions attributable to Series A and B preferred stock	(4,094)	(4,094)	(4,093)
Distributions attributable to senior common stock	(542)	(300)	(113)
Net loss attributable to common stockholders	<u>\$ (10,538)</u>	<u>\$ (2,867)</u>	<u>\$ (445)</u>
Loss per weighted average share of common stock - basic & diluted			
Loss attributable to common shareholders	<u>\$ (0.61)</u>	<u>\$ (0.22)</u>	<u>\$ (0.04)</u>
Weighted average shares of common stock outstanding			
Basic and Diluted	<u>17,253,503</u>	<u>13,164,244</u>	<u>10,953,325</u>
Earnings per weighted average share of senior common stock	<u>\$ 1.05</u>	<u>\$ 1.04</u>	<u>\$ 1.06</u>
Weighted average shares of senior common stock outstanding - basic	<u>516,937</u>	<u>287,178</u>	<u>106,271</u>

<sup>(1)</sup> Refer to Note 2 "Related-Party Transactions"

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

**Gladstone Commercial Corporation**  
**Consolidated Statements of Stockholders' Equity**  
**(Dollars in Thousands)**

	Shares Issued			Preferred Stock	Senior Common Stock	Common Stock	Additional Paid in Capital	Notes Receivable from Employees	Distributions in Excess of Accumulated Earnings	Total Stockholders' Equity
	Preferred Stock	Senior Common Stock	Common Stock							
Balance at December 31, 2011	<u>2,150,000</u>	<u>60,290</u>	<u>10,945,379</u>	\$ 2	\$ -	\$ 11	\$ 211,553	\$ (422)	\$ (75,830)	\$ 135,314
Issuance of senior common stock and common stock, net	-	119,221	138,205	-	-	-	3,917	-	-	3,917
Repayment of principal on employee notes receivable	-	-	-	-	-	-	-	12	-	12
Distributions declared to common, senior common and preferred stockholders	-	-	-	-	-	-	-	-	(20,639)	(20,639)
Net income	-	-	-	-	-	-	-	-	3,761	3,761
Balance at December 31, 2012	<u>2,150,000</u>	<u>179,511</u>	<u>11,083,584</u>	\$ 2	\$ -	\$ 11	\$ 215,470	\$ (410)	\$ (92,708)	\$ 122,365
Issuance of senior common stock and common stock, net	-	194,973	4,578,830	-	-	5	83,281	-	-	83,286
Repayment of principal on employee notes receivable	-	-	-	-	-	-	-	35	-	35
Distributions declared to common, senior common and preferred stockholders	-	-	-	-	-	-	-	-	(24,067)	(24,067)
Net income	-	-	-	-	-	-	-	-	1,527	1,527
Balance at December 31, 2013	<u>2,150,000</u>	<u>374,484</u>	<u>15,662,414</u>	\$ 2	\$ -	\$ 16	\$ 298,751	\$ (375)	\$ (115,248)	\$ 183,146
Issuance of senior common stock and common stock, net	-	434,927	3,927,192	-	1	4	70,997	-	-	71,002
Distributions declared to common, senior common and preferred stockholders	-	-	-	-	-	-	-	-	(30,574)	(30,574)
Net loss	-	-	-	-	-	-	-	-	(5,902)	(5,902)
Balance at December 31, 2014	<u>2,150,000</u>	<u>809,411</u>	<u>19,589,606</u>	\$ 2	\$ 1	\$ 20	\$ 369,748	\$ (375)	\$ (151,724)	\$ 217,672

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

**Gladstone Commercial Corporation**  
**Consolidated Statements of Cash Flows**  
**(Dollars in Thousands)**

	For the year ended December 31,		
	2014	2013	2012
Cash flows from operating activities:			
Net (loss) income	\$ (5,902)	\$ 1,527	\$ 3,761
Adjustments to reconcile net (loss) income to net cash provided by operating activities:			
Depreciation and amortization	28,864	22,827	16,831
Impairment charge	14,238	-	-
Gain on debt extinguishment	(5,274)	-	-
Gain on sale of real estate	(1,240)	-	-
Amortization of deferred financing costs	1,656	1,780	1,502
Amortization of deferred rent asset and liability, net	(389)	(333)	(772)
Amortization of discount and premium on assumed debt	(267)	(171)	9
Asset retirement obligation expense	104	129	168
Increase in other assets	(265)	(399)	(211)
Increase in deferred rent liability	-	-	2,510
Increase in deferred rent receivable	(3,230)	(3,700)	(2,144)
Increase (decrease) in accounts payable, accrued expenses, and amount due Adviser and Administrator	204	(2,171)	2,746
Increase in other liabilities	857	1,437	743
Leasing commissions paid	(1,159)	(1,041)	(1,738)
Net cash provided by operating activities	<u>28,197</u>	<u>19,885</u>	<u>23,405</u>
Cash flows from investing activities:			
Acquisition of real estate and related intangible assets	(124,315)	(131,188)	(82,239)
Improvements of existing real estate	(6,347)	(5,176)	(5,557)
Proceeds from sale of real estate	11,162	-	-
Issuance of mortgage note receivable	(5,600)	-	-
Receipts from lenders for funds held in escrow	2,911	5,545	1,959
Payments to lenders for funds held in escrow	(8,659)	(6,606)	(5,463)
Receipts from tenants for reserves	3,101	6,085	2,870
Payments to tenants from reserves	(4,298)	(3,949)	(2,543)
Decrease (increase) in restricted cash	1,504	(2,117)	(461)
Deposits on future acquisitions	(3,050)	(2,375)	(550)
Deposits applied against real estate investments	3,150	2,725	-
Net cash used in investing activities	<u>(130,441)</u>	<u>(137,056)</u>	<u>(91,984)</u>
Cash flows from financing activities:			
Proceeds from issuance of equity	73,931	88,121	4,191
Offering costs	(3,140)	(4,963)	(300)
Proceeds from issuance of mandatorily redeemable preferred stock	-	-	38,500
Borrowings under mortgage notes payable	52,085	79,995	99,455
Payments for deferred financing costs	(1,029)	(2,051)	(4,598)
Principal repayments on mortgage notes payable	(8,144)	(16,407)	(52,285)
Principal repayments on employee notes receivable	-	35	12
Borrowings from line of credit	98,450	75,400	41,800
Repayments on line of credit	(79,550)	(76,000)	(35,500)
Increase (decrease) in security deposits	57	(19)	134
Distributions paid for common, senior common and preferred stock	(30,363)	(23,940)	(20,613)
Net cash provided by financing activities	<u>102,297</u>	<u>120,171</u>	<u>70,796</u>
Net increase in cash and cash equivalents	53	3,000	2,217
Cash and cash equivalents, beginning of period	8,546	5,546	3,329
Cash and cash equivalents, end of period	<u>\$ 8,599</u>	<u>\$ 8,546</u>	<u>\$ 5,546</u>
<b>NON-CASH INVESTING AND FINANCING INFORMATION</b>			
Cash paid during year for interest	<u>\$ 27,557</u>	<u>\$ 26,679</u>	<u>\$ 21,239</u>
Increase in asset retirement obligation assumed in acquisition	<u>\$ 405</u>	<u>\$ -</u>	<u>\$ 298</u>
Fixed rate principal debt assumed in connection with acquisition	<u>\$ 10,146</u>	<u>\$ -</u>	<u>\$ 24,926</u>
Senior common dividend issued in the dividend reinvestment program	<u>\$ 211</u>	<u>\$ 126</u>	<u>\$ 26</u>
Capital improvements included in accounts payable and accrued expenses	<u>\$ 5,510</u>	<u>\$ 350</u>	<u>\$ -</u>
Fixed asset additions paid for by tenant	<u>\$ 2,031</u>	<u>\$ -</u>	<u>\$ -</u>
Property conveyed in deed in lieu for full satisfaction of mortgage note payable	<u>\$ 17,373</u>	<u>\$ -</u>	<u>\$ -</u>
Security deposit applied to rental income	<u>\$ 147</u>	<u>\$ -</u>	<u>\$ -</u>

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

**Gladstone Commercial Corporation**  
**Notes to Consolidated Financial Statements**

**1. Organization, Basis of Presentation and Significant Accounting Policies**

Gladstone Commercial Corporation is a real estate investment trust, or REIT, that was incorporated under the General Corporation Laws of the State of Maryland on February 14, 2003 primarily for the purpose of investing in and owning net leased industrial, commercial and retail real property and selectively making long-term industrial and commercial mortgage loans. Subject to certain restrictions and limitations, our business is managed by Gladstone Management Corporation, a Delaware corporation, or the Adviser, and administrative services are provided by Gladstone Administration, LLC, a Delaware limited liability company, or 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.

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. All references to the number of properties and square footage are unaudited.

*Subsidiaries*

We conduct substantially all of our operations through a subsidiary, Gladstone Commercial Limited Partnership, a Delaware limited partnership, or the Operating Partnership. As we currently own all of the general and limited partnership interests of the Operating Partnership through two of our subsidiaries, GCLP Business Trust I and II, the financial position and results of operations of the Operating Partnership are consolidated within our financial statements.

Gladstone Commercial Lending, LLC, a Delaware limited liability company, or Gladstone Commercial Lending, a subsidiary of ours, was created to conduct all operations related to our real estate mortgage loans. As the Operating Partnership currently owns all of the membership interests of Gladstone Commercial Lending, the financial position and results of operations of Gladstone Commercial Lending are consolidated with ours.

Gladstone Commercial Advisers, Inc., a Delaware corporation, or Commercial Advisers, and a wholly-owned subsidiary of ours, is a taxable REIT subsidiary, or TRS, which was created to collect any non-qualifying income related to our real estate portfolio. There has been no such income earned to date. Since we own 100% of the voting securities of Commercial Advisers, the financial position and results of operations of Commercial Advisers are consolidated within our financial statements.

GCLP Business Trust I and GCLP Business Trust II, each a subsidiary and business trust of ours, were formed under the laws of the Commonwealth of Massachusetts on December 28, 2005. We transferred our 99% limited partnership interest in the Operating Partnership to GCLP Business Trust I in exchange for 100 shares of the trust. Gladstone Commercial Partners, LLC transferred its 1% general partnership interest in the Operating Partnership to GCLP Business Trust II in exchange for 100 trust shares.

*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.

### *Real Estate and Lease Intangibles*

We record investments in real estate at cost and capitalize improvements and replacements when they extend the useful life or improve the efficiency of the asset. We expense costs of repairs and maintenance as such costs are incurred. We compute depreciation using the straight-line method over the estimated useful life, or 39 years, for buildings and improvements, 5 to 20 years for equipment and fixtures, and the shorter of the useful life or the remaining lease term for tenant improvements and leasehold interests.

Certain of our acquisitions involve sale-leaseback transactions with newly-originated leases, which we account for as asset acquisitions under Accounting Standards Codification, or ASC, 805, "Business Combinations." In the case of an asset acquisition, we will capitalize the transaction costs incurred in connection with the acquisition. Other of our acquisitions involve the acquisition of properties that are already being operated as rental properties, which we will generally consider to be a business combination under ASC 805. Business combination guidance is generally applicable to us when properties are acquired with leases in place at the time of acquisition. When an acquisition is considered a business combination, ASC 805 requires that the purchase price of real estate be allocated to the acquired tangible assets and liabilities, consisting of land, building, tenant improvements, long-term debt assumed and identified intangible assets and liabilities, typically the value of above-market and below-market leases, the value of in-place leases, the value of unamortized lease origination costs and the value of tenant relationships, based in each case on their fair values. ASC 805 also requires that all expenses related to an acquisition accounted for as a business combination to be expensed as incurred, rather than capitalized into the cost of the acquisition.

Management's estimates of fair value are made using methods similar to those used by independent appraisers (e.g. discounted cash flow analysis). Factors considered by management in its analysis include an estimate of carrying costs during hypothetical expected lease-up periods considering current market conditions and costs to execute similar leases. We also consider information obtained about each property as a result of our pre-acquisition due diligence, marketing and leasing activities in estimating the fair value of the tangible and intangible assets acquired and liabilities assumed. In estimating carrying costs, management also includes lost reimbursement of real estate taxes, insurance and other operating expenses as well as estimates of lost rentals at market rates during the hypothetical expected lease-up periods, which primarily range from 9 to 18 months, depending on specific local market conditions. Management also estimates costs to execute similar leases, including leasing commissions, legal and other related expenses to the extent that such costs are not already incurred in connection with a new lease origination as part of the transaction.

We allocate purchase price to the fair value of the tangible assets of an acquired property by valuing the property as if it were vacant. The "as-if-vacant" value is allocated to land, building and tenant improvements based on management's determination of the relative fair values of these assets on the date of acquisition. Real estate depreciation expense on these tangible assets was \$18.8 million, \$15.5 million, and \$11.9 million for the years ended December 31, 2014, 2013, and 2012, respectively

Above-market and below-market in-place lease fair values for owned properties are recorded based on the present value (using an interest rate which reflects the risks associated with the leases acquired) of the difference between (i) the contractual amounts to be paid pursuant to the in-place leases and (ii) management's estimate of fair market lease rates for the corresponding in-place leases, measured over a period equal to the remaining non-cancelable term of the lease. When determining the non-cancelable term of the lease, we evaluate which fixed-rate renewal options, if any, should be included. The capitalized above-market lease values, included in the accompanying condensed consolidated balance sheets as part of deferred rent receivable, are amortized as a reduction of rental income over the remaining non-cancelable terms of the respective leases. Total amortization related to above-market lease values was \$0.3 million, for each of the years ended December 31, 2014, 2013, and 2012, respectively. The capitalized below-market lease values, included in the accompanying condensed consolidated balance sheets as part of deferred rent liability, are amortized as an increase to rental income over the remaining non-cancelable terms of the respective leases, including any below market renewal periods. Total amortization related to below-market

lease values was \$0.7 million, \$0.6 million, and \$1.1 million for the years ended December 31, 2014, 2013, and 2012, respectively.

The total amount of the remaining intangible assets acquired, which consists of in-place lease values, unamortized lease origination costs, and customer relationship intangible values, are allocated based on management's evaluation of the specific characteristics of each tenant's lease and our overall relationship with that respective tenant. Characteristics to be considered by management in determining these values include the nature and extent of our existing business relationships with the tenant, growth prospects for developing new business with the tenant, the tenant's credit quality and our expectations of lease renewals (including those existing under the terms of the lease agreement), among other factors.

The value of in-place leases and lease origination costs are amortized to amortization expense over the remaining term of the respective leases, which generally range from 10 to 15 years. The value of customer relationship intangibles, which is the benefit to us resulting from the likelihood of an existing tenant renewing its lease, are amortized to amortization expense over the remaining term and any anticipated renewal periods in the respective leases, but in no event does the amortization period for intangible assets exceed the remaining depreciable life of the building. Total amortization expense related to these intangible assets and liabilities was \$10.0 million, \$7.3 million, and \$4.9 million for the years ended December 31, 2014, 2013, and 2012, respectively.

Should a tenant terminate its lease, the unamortized portion of the above-market and below-market lease values would be charged to rental income and the unamortized portion of in-place lease values, lease origination costs and customer relationship intangibles will be immediately charged to amortization expense.

#### *Impairment Charges*

We account for the impairment of real estate, including intangible assets, in accordance with ASC 360-10-35, "Property, Plant, and Equipment," which requires us to periodically review the carrying value of each property to determine if circumstances indicate impairment of the carrying value of the investment exists or that depreciation periods should be modified. If circumstances indicate the possibility of impairment, we prepare a projection of the undiscounted future cash flows, without interest charges, of the specific property and determine if the carrying value of the investment in such property is recoverable. In performing the analysis, we consider such factors as each tenant's payment history and financial condition, the likelihood of lease renewal, business conditions in the industry in which the tenants operate, whether there are indications that the fair value of the real estate has decreased and our intended holding period of the property. If the carrying amount is more than the aggregate undiscounted future cash flows, we would recognize an impairment loss to the extent the carrying amount exceeds the estimated fair value of the property. We evaluate our entire portfolio of properties each quarter for any impairment indicators and perform an impairment analysis on those select properties that have an indication of impairment.

#### *Cash and Cash Equivalents*

We consider cash equivalents to be short-term, highly-liquid investments that are both readily convertible to cash and have a maturity of three months or less at the time of purchase, except that any such investments purchased with funds held in escrow or similar accounts are classified as restricted cash. Items classified as cash equivalents include money-market deposit accounts. At times, the balance of our cash and cash equivalents may exceed federally insurable limits.

#### *Restricted Cash*

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. For purposes of the consolidated statements of cash flows, changes in restricted cash caused

by changes in reserves held for tenants are shown as investing activities. Changes in restricted cash caused by changes in security deposits are reflected as financing activities.

#### *Funds Held in Escrow*

Funds held in escrow consist of funds held by certain of our lenders for properties held as collateral by these lenders. These funds will be released to us upon completion of agreed upon tasks, as specified in the mortgage agreements, mainly consisting of maintenance and repairs on the buildings, and when evidence of insurance and tax payments has been submitted to the lenders.

#### *Deferred Financing Costs*

Deferred financing costs consist of costs incurred to obtain financing, including legal fees, origination fees and administrative fees. The costs are deferred and amortized using the straight-line method, which approximates the effective interest method, over the term of the secured financing. We made payments of \$1.0 million, \$2.1 million, and \$4.6 million for deferred financing costs during the years ended December 31, 2014, 2013, and 2012, respectively. Total amortization expense related to deferred financing costs is included in interest expense and was \$1.7 million, \$1.8 million, and \$1.5 million for the years ended December 31, 2014, 2013, and 2012, respectively.

#### *Gains on Property Sales and Debt Extinguishment*

Gains on property sales and gains on debt extinguishment consist of the excess consideration or forgiveness of debt received for a property over the property carrying value at the time of sale or forgiveness. We recognize gains on property sales and gains on debt extinguishment in accordance with ASC 360-20, "Real Estate Sales", or the date the debt is extinguished.

#### *Revenue Recognition*

Rental revenue includes rents that each tenant pays in accordance with the terms of its respective lease reported evenly over the non-cancelable term of the lease. Most of our leases contain rental increases at specified intervals. We recognize such revenues on a straight-line basis. Deferred rent receivable in the accompanying consolidated balance sheet includes the cumulative difference between rental revenue, as recorded on a straight-line basis, and rents received from the tenants in accordance with the lease terms, along with the capitalized above-market or in-place lease values of certain acquired properties. Accordingly, we determine, in our judgment, to what extent the deferred rent receivable applicable to each specific tenant is collectable. We review deferred rent receivable, as it relates to straight line rents, on a quarterly basis and take into consideration the tenant's payment history, the financial condition of the tenant, business conditions in the industry in which the tenant operates and economic conditions in the geographic area in which the property is located. In the event that the collectability of deferred rent with respect to any given tenant is in doubt, we record an allowance for uncollectable accounts or record a direct write-off of the specific rent receivable. We have incurred \$0.8 million in deferred rent expense during the year ended December 31, 2014. No such reserves or direct write offs were recorded during the years ended December 31, 2013, and 2012, respectively.

Tenant recovery revenue includes payments from tenants as reimbursements for franchise taxes, management fees, insurance, maintenance and repairs, utilities, and ground lease payments. We recognize tenant recovery revenue in the same periods that we incur the related expenses.

#### *Mortgage Note Receivable*

Management considers its loans and other lending investments to be held-for-investment. We reflect our loans classified as long-term investments at amortized cost, less allowance for loan losses, acquisition premiums or discounts, and deferred loan fees. On occasion, we may acquire loans at small premiums or discounts based on the credit characteristics of such loans. These premiums or discounts would be



recognized as yield adjustments over the lives of the related loans. Loan origination fees, as well as direct loan origination costs, are also deferred and recognized over the lives of the related loans as yield adjustments. If loans with premiums, discounts, or loan origination fees are prepaid, we would immediately recognize the unamortized portion as a decrease or increase in the prepayment gain or loss. Interest income is recognized using the effective interest method applied on a loan-by-loan basis. Prepayment penalties or yield maintenance payments from borrowers are recognized as additional income when received.

#### *Income Taxes*

We have operated and intend to continue to operate in a manner that will allow us to qualify as a REIT under the Internal Revenue Code of 1986, as amended, and, accordingly, will not be subject to federal income taxes on amounts distributed to stockholders (except income from foreclosure property), provided that we distribute at least 90% of our REIT taxable income to our stockholders and meet certain other conditions. To the extent that we satisfy the distribution requirement but distribute less than 100% of our taxable income, we will be subject to federal corporate income tax on our undistributed income.

Commercial Advisers is a wholly-owned TRS that is subject to federal and state income taxes. Though Commercial Advisers has had no activity to date, we would account for any future income taxes in accordance with the provisions of ASC 740, "Income Taxes." Under ASC 740-10-25, we would account for income taxes using the asset and liability method under which deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases.

We may recognize a tax benefit from an uncertain tax position when it is more-likely-than-not (defined as a likelihood of more than 50%) that the position will be sustained upon examination, including resolutions of any related appeals or litigation processes, based on the technical merits. If a tax position does not meet the more-likely-than-not recognition threshold, despite our belief that the filing position is supportable, the benefit of that tax position is not recognized in the statements of operations. We recognize interest and penalties, as applicable, related to unrecognized tax benefits as a component of income tax expense. We recognize unrecognized tax benefits in the period that the uncertainty is eliminated by either affirmative agreement of the uncertain tax position by the applicable taxing authority, or by expiration of the applicable statute of limitation. For the years ended December 31, 2014, 2013 and 2012, we did not record any provisions for uncertain tax positions.

#### *Asset Retirement Obligations*

ASC 410, "Asset Retirement and Environmental Obligation," requires an entity to recognize a liability for a conditional asset retirement obligation when incurred if the liability can be reasonably estimated. ASC 410-20-20 clarifies that the term "Conditional Asset Retirement Obligation" refers to a legal obligation (pursuant to existing laws or by contract) to perform an asset retirement activity in which the timing and/or method of settlement are conditional on a future event that may or may not be within the control of the entity. ASC 410-20-25-6 clarifies when an entity would have sufficient information to reasonably estimate the fair value of an asset retirement obligation. We have accrued a liability at the present value of the estimated payments expected to be made and corresponding increase to the cost of the related properties for disposal related to all properties constructed prior to 1985 that have, or may have, asbestos present in the building. The liabilities are accreted to their estimated obligation over the life of the leases for the respective properties. We accrued \$0.4 million, \$0.0 million and \$0.3 million in liabilities in connection with acquisitions for the years ended December 31, 2014, 2013 and 2012, respectively. We recorded expense of \$0.1 million, \$0.1 million, and \$0.2 million during the years ended December 31, 2014, 2013 and 2012, respectively, to general and administrative expense. Costs of future expenditures for obligations are discounted to their present value. The aggregate undiscounted obligation on all properties is \$9.4 million and the discount rates used in the calculations range from 2.5% to 7.6%. We do not expect to make any payments in conjunction with these obligations in each of the next five years.

### *Stock Issuance Costs*

We account for stock issuance costs in accordance with SEC Staff Accounting Bulletin (“SAB”) Topic 5.A, which states that incremental costs directly attributable to a proposed or actual offering of securities may properly be deferred and charged against the gross proceeds of the offering. Accordingly, we record costs incurred related to our ongoing equity offerings to other assets on our consolidated balance sheet and ratably apply these amounts to the cost of equity as stock is issued. If an equity offering is subsequently terminated and there are amounts remaining in other assets that have not been allocated to the cost of the offering, the remaining amounts are recorded as a general and administrative expense on our consolidated statements of operations.

### *Comprehensive Income (Loss)*

For the years ended December 31, 2014, 2013, and 2012, comprehensive income (loss) equaled net income (loss); therefore, a separate statement of comprehensive income (loss) is not included in the accompanying consolidated financial statements.

### *Segment Reporting*

We manage our operations on an aggregated, single segment basis for purposes of assessing performance and making operating decisions, and, accordingly, have only one reporting and operating segment.

### *Recently Issued Accounting Pronouncements*

In August 2014, the Financial Accounting Standards Board, or FASB, issued Accounting Standards Update 2014-15 (“ASU 2014-15”), “Presentation of Financial Statements – Going Concern (Subtopic 205 – 40): Disclosure of Uncertainties About an Entity’s Ability to Continue as a Going Concern.” ASU 2014-15 requires management to evaluate whether there are conditions or events that raise substantial doubt about the entity’s ability to continue as a going concern, and to provide certain disclosures when it is probable that the entity will be unable to meet its obligations as they become due within one year after the date that the financial statements are issued. Since this guidance is primarily around certain disclosures to the financial statements, we anticipate no impact on our financial position, results of operations or cash flows from adopting this standard. We are currently assessing the additional disclosure requirements, if any, of ASU 2014-15. ASU 2014-15 is effective for the annual period ending after December 15, 2016 and for annual periods and interim periods thereafter, with early adoption permitted.

In May 2014, the FASB issued ASU 2014-09, “Revenue from Contracts with Customers,” which supersedes or replaces nearly all GAAP revenue recognition guidance. The new guidance establishes a new control-based revenue recognition model, changes the basis for deciding when revenue is recognized over time or at a point in time and will expand disclosures about revenue. We are currently assessing the impact of ASU 2014-09. ASU 2014-09 is effective for annual reporting periods that begin after December 15, 2016 and interim periods within those years. Early adoption is not permitted.

In April 2014, the FASB issued ASU No. 2014-08, “Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity.” Under this revised guidance, only disposals representing a strategic shift in operations, such as a disposal of a major geographic area, a major line of business or a major equity method investment, will be presented as discontinued operations. This standard is effective for our fiscal year beginning January 1, 2015; however, the FASB has permitted early adoption beginning with the first quarter of 2014. We adopted this standard during the quarter ended March 31, 2014, and accordingly we did not present our assets classified as held for sale during the quarter ended March 31, 2014 as discontinued operations.

## 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 controlled by Mr. David Gladstone, our chairman and chief executive officer. We have an advisory agreement with our Adviser, or the Advisory Agreement, and an administration agreement with our Administrator, or the Administration Agreement. The management and administrative services and fees under the Advisory and Administration Agreements are described below. At December 31, 2014 and 2013, \$0.9 million and \$1.4 million, respectively, was collectively due to our Adviser and Administrator.

#### *Advisory Agreement*

The Advisory Agreement provides for an annual base management fee equal to 2% of our total stockholders' equity, less the recorded value of any preferred stock and adjusted to exclude the effect of any unrealized gains, losses or other items that do not affect realized net income (including impairment charges), or common stockholders' equity, and an incentive fee based on funds from operations, or FFO. For the years ended December 31, 2014, 2013, and 2012, we recorded a base management fee of \$2.8 million, \$2.0 million, and \$1.5 million, respectively. The Adviser's Board of Directors voted to give us a credit to the base management fee for the year ended December 31, 2014 of \$0.2 million.

For purposes of calculating the incentive fee, FFO includes any realized capital gains and capital losses, less any distributions paid on preferred stock and Senior Common Stock, but FFO does not include any unrealized capital gains or losses (including impairment charges). The incentive fee rewards the Adviser if our quarterly FFO, before giving effect to any incentive fee, or pre-incentive fee FFO, exceeds 1.75%, or 7% annualized, or the hurdle rate, of total common stockholders' equity. The Adviser receives 100% of the amount of the pre-incentive fee FFO that exceeds the hurdle rate, but is less than 2.1875% of our common stockholders' equity. The Adviser also receives an incentive fee of 20% of the amount of our pre-incentive fee FFO that exceeds 2.1875% of common stockholders' equity.

For the years ended December 31, 2014, 2013, and 2012, we recorded an incentive fee of \$4.3 million, \$4.2 million, and \$3.6 million, respectively, offset by credits related to unconditional, voluntary and irrevocable waivers issued by the Adviser of \$3.0 million, \$3.5 million, and \$2.2 million, respectively, resulting in a net incentive fee for the years ended December 31, 2014, 2013, and 2012, of \$1.3 million, \$0.7 million, and \$1.4 million, respectively. Our Board of Directors accepted the Adviser's offer to waive, on a quarterly basis, a portion of the incentive fee for the years ended December 31, 2014, 2013, and 2012, in order to support the current level of distributions to our stockholders. This waiver may not be recouped by the Adviser in the future.

#### *Administration Agreement*

Pursuant to the Administration Agreement, we pay for our allocable portion of the Administrator's expenses in performing services to us, including, but not limited to, rent and the salaries and benefits of its personnel, including our chief financial officer, treasurer, chief compliance officer, general counsel and secretary (who also serves as our Administrator's president), and their respective staffs. Prior to July 1, 2014, our allocable portion was generally derived by multiplying that portion of the Administrator's expenses allocable to all funds managed by the Adviser by the percentage of our total assets at the beginning of each quarter in comparison to the total assets of all funds managed by the Adviser. As approved by our Board of Directors, effective July 1, 2014, our allocable portion of the Administrator's expenses will generally be 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 years ended December 31, 2014, 2013, and 2012, we recorded an administration fee of \$1.5 million, \$1.5 million, and \$1.1 million, respectively.

## Gladstone Securities

Gladstone Securities, LLC, or 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 controlled by Mr. David Gladstone, our chairman and chief executive officer. Mr. Gladstone also serves on the board of managers of Gladstone Securities.

### *Dealer Manager Agreement*

In connection with the offering of our Senior Common Stock (see Note 10, “Stockholders’ Equity,” for further details) we entered into a Dealer Manager Agreement, dated March 25, 2011, or the Dealer Manager Agreement, with Gladstone Securities pursuant to which Gladstone Securities agreed to act as our exclusive dealer manager in connection with the offering. Pursuant to the terms of the Dealer Manager Agreement, Gladstone Securities is entitled to receive a sales commission in the amount of 7.0% of the gross proceeds of the shares of Senior Common Stock sold, plus a dealer manager fee in the amount of 3.0% of the gross proceeds of the shares of Senior Common Stock sold. Gladstone Securities, in its sole and absolute discretion, may re-allocate all of its selling commissions attributable to a participating broker-dealer and may also re-allocate a portion of its dealer manager fee earned in respect of the proceeds generated by the participating broker-dealer to any participating broker-dealer as a non-accountable marketing allowance. In addition, we have agreed to indemnify Gladstone Securities against various liabilities, including certain liabilities arising under the federal securities laws. We made approximately \$0.6 million, \$0.3 million, and \$0.2 million of payments during the years ended December 31, 2014, 2013, and 2012 respectively, to Gladstone Securities pursuant to this agreement, which are reflected as a component of Senior Common Stock costs in the consolidated statement of stockholders’ equity. The Dealer Manager Agreement currently is scheduled to terminate on the earlier of (i) March 28, 2015 or (ii) the date on which 3,000,000 shares of Senior Common Stock are sold pursuant to the Dealer Manager Agreement. We have elected not to renew the program upon termination on March 28, 2015 and thus the Dealer Manager Agreement will also simultaneously terminate on March 28, 2015.

### *Mortgage Financing Arrangement Agreement*

We also 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. In connection with this engagement, Gladstone Securities may from time to time 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 \$0.1 million during both the years ended December 31, 2014, and 2013, respectively, which are reflected as deferred financing costs in the consolidated balance sheets, on total mortgages secured of \$52.1 million and \$76.3 million, or 0.27% and 0.18%, respectively. The agreement is scheduled to terminate on August 31, 2015, unless renewed or earlier terminated pursuant to the provisions contained therein.

### 3. Loss per Share of Common Stock

The following tables set forth the computation of basic and diluted loss per share of common stock for the years ended December 31, 2014, 2013, and 2012. We computed basic loss per share for the years ended December 31, 2014, 2013 and 2012 using the weighted average number of shares outstanding during the periods. Diluted loss per share for the years ended December 31, 2014, 2013 and 2012, reflects additional shares of common stock related to our convertible 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 year ended December 31,		
	2014	2013	2012
<b>Calculation of basic loss per share of common stock:</b>			
Net loss attributable to common stockholders	\$ (10,538)	\$ (2,867)	\$ (445)
Denominator for basic weighted average shares of common stock	<u>17,253,503</u>	<u>13,164,244</u>	<u>10,953,325</u>
Basic loss per share of common stock	<u>\$ (0.61)</u>	<u>\$ (0.22)</u>	<u>\$ (0.04)</u>
<b>Calculation of diluted loss per share of common stock:</b>			
Net loss attributable to common stockholders	\$ (10,538)	\$ (2,867)	\$ (445)
Add: Income impact of assumed conversion of senior common stock <sup>(1)</sup>	-	-	-
Net loss attributable to common stockholders plus assumed conversions	\$ (10,538)	\$ (2,867)	\$ (445)
Denominator for basic weighted average shares of common stock	17,253,503	13,164,244	10,953,325
Effect of convertible senior common stock <sup>(1)</sup>	-	-	-
Denominator for diluted weighted average shares of common stock	<u>17,253,503</u>	<u>13,164,244</u>	<u>10,953,325</u>
Diluted loss per share of common stock	<u>\$ (0.61)</u>	<u>\$ (0.22)</u>	<u>\$ (0.04)</u>

(1) We excluded convertible senior common shares of 428,509, 238,126, and 121,891 from the calculation of diluted earnings per share for the years ended December 31, 2014, 2013 and 2012, respectively, because it was anti-dilutive.

### 4. Real Estate and Intangible Assets

#### Real Estate

The following table sets forth the components of our investments in real estate as of December 31, 2014 and 2013 (dollars in thousands):

	December 31, 2014	December 31, 2013
Real estate:		
Land	\$ 88,394	\$ 79,153
Building and improvements	593,155	527,230
Tenant improvements	41,016	35,970
Accumulated depreciation	<u>(92,133)</u>	<u>(81,241)</u>
Real estate, net	<u>\$ 630,432</u>	<u>\$ 561,112</u>

## 2014 Real Estate Activity

During the year ended December 31, 2014, we completed 10 acquisitions of 11 properties and completed an expansion of one property, which are summarized below (dollars in thousands):

Location	Acquisition Date	Square Footage (unaudited)	Lease Term	Renewal Options	Total Purchase Price/Expansion Funded	Acquisition Expenses	Annualized Straight Line Rent	Debt Issued & Assumed
Allen, TX	3/27/2014	21,154	12 Years	4 (5 years each)	\$ 5,525	\$ 33	\$ 570	\$ 3,481
Colleyville, TX	3/27/2014	20,355	12 Years	4 (5 years each)	4,523	33	467	2,849
Rancho Cordova, CA <sup>(4)</sup>	4/22/2014	61,358	10 Years	1 (5 year)	8,225	73	902	4,935
Coppell, TX	5/8/2014	21,171	12 Years	4 (5 years each)	5,838	26	601	3,816
Columbus, OH	5/13/2014	114,786	9.5 Years <sup>(1)</sup>	N/A <sup>(1)</sup>	11,800	70	1,278 <sup>(3)</sup>	N/A
Taylor, PA	6/9/2014	955,935	10 Years	4 (5 years each)	39,000	730	3,400	22,600
Aurora, CO	7/1/2014	124,800	15 Years	2 (5 years each)	8,300	93	768	N/A
Indianapolis, IN <sup>(4)</sup>	9/3/2014	86,495	11.5 Years <sup>(2)</sup>	2 (5 years each) <sup>(2)</sup>	10,500	63	1,504 <sup>(3)</sup>	6,100
Denver, CO	10/31/2014	189,120	10 Years	2 (10 years each)	10,000	103	860	N/A
Canton, NC <sup>(5)</sup>	11/1/2014	365,960	20 Years	2 (10 years each)	5,550	N/A	1,343	N/A
Monroe, MI <sup>(6)</sup>	12/23/2014	535,500	8.5 Years	2 (5 years each)	30,750	68	2,523	18,450
<b>Total</b>		<b>2,496,634</b>			<b>\$ 140,011</b>	<b>\$ 1,292</b>	<b>\$ 14,216</b>	<b>\$ 62,231</b>

<sup>(1)</sup> Lease term and renewal options are reflective of the largest tenant. The smaller tenant's lease terminates in November 2016 and contains no renewal options.

<sup>(2)</sup> Lease term and renewal options are reflective of the largest tenant. The other tenants in the building have varying lease expirations from December 2015 to October 2018. No other tenants have renewal options.

<sup>(3)</sup> Rent figure is reflective of aggregate rent among all tenants occupying the building.

<sup>(4)</sup> Tenants occupying these properties are subject to a gross lease. The largest tenant in this property occupies 61,306 square feet.

<sup>(5)</sup> The Canton, NC property was originally acquired in July 2004 for \$5.2 million. After the expansion was completed in November 2014, our total investment in the property is \$10.8 million.

<sup>(6)</sup> This property acquisition consists of two buildings with two separate leases which have identical lease terms. The figures above are aggregated to reflect both buildings.

In accordance with ASC 805, we determined the fair value of the acquired assets and assumed liabilities related to the 11 properties acquired during the year ended December 31, 2014 as follows (dollars in thousands):

	Land	Building	Tenant Improvements	In-place Leases	Leasing Costs	Customer Relationships	Above Market Leases	Below Market Leases	Premium on Assumed Debt	Total Purchase Price
Allen, TX	\$ 874	\$ 3,509	\$ 125	\$ 598	\$ 273	\$ 218	\$ -	\$ -	\$ (72)	\$ 5,525
Colleyville, TX	1,277	2,307	117	486	220	181	-	(6)	(59)	4,523
Rancho Cordova, CA	752	5,898	278	473	546	278	-	-	-	8,225
Coppell, TX	1,448	3,221	128	636	293	230	-	-	(118)	5,838
Columbus, OH	990	6,080	1,937	823	719	990	261	-	-	11,800
Taylor, PA	3,102	24,449	956	6,171	1,452	2,870	-	-	-	39,000
Aurora, CO	2,882	3,825	92	413	806	282	-	-	-	8,300
Indianapolis, IN	502	5,334	1,088	1,990	741	732	126	(13)	-	10,500
Denver, CO	1,621	6,503	568	1,152	721	652	-	(1,217)	-	10,000
Monroe, MI <sup>(1)</sup>	1,118	23,890	942	1,497	1,350	1,953	-	-	-	30,750
	<b>\$ 14,566</b>	<b>\$ 85,016</b>	<b>\$ 6,231</b>	<b>\$ 14,239</b>	<b>\$ 7,121</b>	<b>\$ 8,386</b>	<b>\$ 387</b>	<b>\$ (1,236)</b>	<b>\$ (249)</b>	<b>\$ 134,461</b>

<sup>(1)</sup> This property acquisition consists of two buildings with two separate leases which have identical lease terms. The figures above are aggregated to reflect both buildings.

Below is a summary of the total revenue and earnings recognized on the 11 properties acquired during the year ended December 31, 2014 (dollars in thousands):

Location	Acquisition Date	For the year ended December 31,	
		2014	
		Rental Revenue	Earnings <sup>(1)</sup>
Allen, TX	3/27/2014	\$ 435	\$ 249
Colleyville, TX	3/27/2014	357	206
Rancho Cordova, CA	4/22/2014	625	239
Coppell, TX	5/8/2014	390	226
Columbus, OH	(2) 5/13/2014	790	272
Taylor, PA	6/9/2014	1,908	890
Aurora, CO	7/1/2014	384	253
Indianapolis, IN	(2) 9/3/2014	489	44
Denver, CO	10/31/2014	166	82
Monroe, MI	(3) 12/23/2014	61	31
		<u>\$ 5,605</u>	<u>\$ 2,492</u>

<sup>(1)</sup> Earnings is calculated as net income exclusive of both interest expense and acquisition related costs that are required to be expensed under ASC 805.

<sup>(2)</sup> Rental revenue and earnings is reflective of aggregate rent and operating expenses among all tenants occupying the building.

<sup>(3)</sup> We acquired two properties and two leases with this acquisition. Rental revenue and earnings is reflective of aggregate rent and operating expenses among both properties.

### Pro Forma

The following table reflects pro-forma consolidated statements of operations as if the properties acquired during the years ended December 31, 2014 and 2013, respectively were acquired as of January 1, 2013. The table also assumes that properties acquired during the years ended December 31, 2013 and 2012, respectively, were acquired as of January 1, 2012. The pro-forma earnings for the years ended December 31, 2014, 2013 and 2012 were adjusted to assume that acquisition-related costs were incurred as of the beginning of the earliest period presented (dollars in thousands, except per share amounts):

	For the year ended December 31, (unaudited)		
	2014	2013	2012
<b>Operating Data:</b>			
Total operating revenue	\$ 80,759	\$ 80,081	\$ 68,940
Total operating expenses	(60,728)	(46,223)	(37,457)
Other expenses	(24,290)	(32,929)	(28,754)
Net income (loss)	(4,259) <sup>(1)</sup>	929	2,729
Dividends attributable to preferred and senior common stock	(4,636)	(4,394)	(4,206)
Net loss attributable to common stockholders	<u>\$ (8,895)</u>	<u>\$ (3,465)</u>	<u>\$ (1,477)</u>
<b>Share and Per Share Data:</b>			
Basic and diluted loss per share of common stock	\$ (0.52)	\$ (0.26)	\$ (0.13)
Weighted average shares outstanding-basic and diluted	17,253,503	13,164,244	10,953,325

<sup>(1)</sup> We recognized a \$14.2 million impairment loss and a \$5.3 million gain on debt extinguishment as a result of our Roseville, MN deed in lieu transaction during the year ended December 31, 2014.

*Significant Real Estate Activity on Existing Assets*

On April 4, 2014, our tenant occupying our Newburyport, Massachusetts property notified us of their intention not to exercise their renewal option, as the tenant is relocating to Rhode Island. The tenant will continue paying rent and operating expenses through the lease termination date of April 30, 2015.

On May 6, 2014, we extended the lease with the tenant occupying our property located in Austin, Texas. The lease covering this property was extended for an additional eight years, through June 2022. The lease was originally set to expire in June 2015. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$0.7 million. In connection with the extension of the lease and modification of certain terms of the lease, we paid \$0.2 million in leasing commissions, and will pay a total of approximately \$1.3 million in tenant improvements prior to the end of second quarter 2015.

On June 11, 2014, we extended the lease with the tenant occupying our property located in Burnsville, Minnesota. The new lease covers approximately two-thirds of the space and was extended for an additional eight years, through January 2023. The lease was originally set to expire in June 2015. The tenant in this property will continue to pay rent on the entire building through June 2015, and we are working to identify tenants to lease the remaining one-third of the building. The new lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of \$1.0 million. Rental income per square foot increased 14% from the previous lease. The lease grants the tenant two options to extend the lease for an additional three years each. In connection with the extension of the lease and the modification of certain terms under the lease, we paid \$0.5 million in leasing commissions, and will pay \$3.3 million in tenant improvements prior to the end of first quarter 2015.

On July 7, 2014, we extended the lease with one of the tenants occupying our property located in Akron, Ohio. The new lease covers approximately two-thirds of the space and was extended for an additional five years, through March 2020. The lease was originally set to expire in March 2015. This tenant will continue to pay its existing rent through March 2015. The new lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of \$0.6 million. The lease grants the tenant two options to extend the lease for an additional five years each. In connection with the extension of the lease and the modification of certain terms under the lease, we paid \$0.2 million in leasing commissions, and will pay \$0.9 million in tenant improvements prior to the end of second quarter 2015. On December 24, 2014, we extended the lease with the other tenant occupying our property located in Akron, Ohio. The new lease covers the remaining space and was extended for an additional five years through March 2020. The lease was originally set to expire in March 2015. This tenant will also continue to pay its existing rent through March 2015. The new lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of \$0.1 million. The lease grants the tenant two options to extend the lease for an additional five years each. In connection with the extension of the lease and the modification of certain terms under the lease, we will pay \$0.1 million in tenant improvements during fiscal year 2015.

On September 25, 2014, we modified the lease with the tenant occupying our property located in Concord Township, Ohio. The lease covering this property was adjusted to defer a portion of rental payments covering the period August 2014 through December 2014. The tenant will repay the deferred rent balance monthly during calendar year 2015. On November 14, 2014, we further modified the lease with this tenant. The lease covering this property was adjusted to change the lease termination date from August 2034, to December 2024. Accordingly, annual straight line rent decreased from \$1.7 million under the prior amendment, to \$1.4 million. The lease grants the tenant three options to extend the lease for an additional five years each. Upon execution of this lease amendment, we determined that a portion of our existing deferred rent balance of \$2.5 million was uncollectible, due to the reduction in lease payments and lease term, and we adjusted the balance by approximately \$0.8 million, which is recorded in general and administrative expense.

On October 16, 2014, we executed a lease with a tenant to occupy our previously vacant property located in Richmond, Virginia. The lease was effective as of September 8, 2014 and has a three-year term. The tenant



has an early termination option at any time after July 31, 2016, contingent upon the tenant losing a contract with the vendor supporting their operations in our building. The tenant is subject to a termination payment of approximately \$0.03 million if they exercise this option. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$0.2 million. The tenant has one option to renew the lease for an additional period of three years. In connection with the extension of the lease and modification of certain terms of the lease, we paid \$0.1 million in leasing commissions. No tenant improvements were paid in connection with the new lease.

On October 22, 2014, we extended the lease with the tenant occupying our property located in Canton, North Carolina. We financed a \$5.5 million expansion project on this property, which added an additional 150,000 square feet to the building, which was completed in November 2014. The lease covering this property was extended for an additional 10 years, through September 2034. The lease was originally set to expire in July 2024. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$1.4 million, as compared to straight line rents of \$0.6 million under the previous lease.

On October 27, 2014, we extended the lease with the tenant occupying our property located in South Hadley, Massachusetts. The lease covering this property was extended for an additional two years through January 2017. The lease was originally set to expire in January 2015. The lease provides a scheduled rent increase over the previous lease, with annualized straight line rents of approximately \$0.3 million. The tenant has two options to renew the lease for additional periods of one year each.

On October 30, 2014, we modified the lease with the tenant occupying our property located in Tewksbury, Massachusetts. The lease covering this property was amended to reduce rental charges through the remaining lease term, which is set to expire May 31, 2017. In the event we identify a tenant or a purchaser for the property, we can terminate the lease with the current tenant. Straight line rent on this lease has decreased from \$0.9 million per year to \$0.4 million per year after the amendment.

On December 1, 2014, we executed a lease with a tenant to occupy a 7,125 square foot vacant outbuilding located on our property in Maple Heights, Ohio. The lease was effective as of December 1, 2014 and has a three-year term. The lease provides for consistent rental payments of \$0.03 million annually. In connection with the extension of the lease and modification of certain terms of the lease, we paid \$0.01 million in leasing commissions.

On December 1, 2014, we executed a lease with a tenant to occupy a portion of our property located in Bolingbrook, Illinois. The lease is for seven years and the tenant occupies 38% of the building. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$0.2 million. The tenant has one option to renew the lease for an additional period of five years. In connection with the extension of the lease and modification of certain terms of the lease, we paid \$0.2 million in leasing commissions, and will pay to \$0.5 million in tenant improvements during fiscal year 2015.

### 2013 Real Estate Activity

During the year ended December 31, 2013, we acquired seven properties, and completed an expansion of one property, which are summarized below (dollars in thousands):

Location	Acquisition/ Expansion Date	Square Footage (unaudited)	Lease Term	Renewal Options	Total Purchase/ Expansion Price	Acquisition Expenses	Annualized Straight Line Rent	Debt Issued
Egg Harbor Township, NJ	3/28/2013	29,257	10 years	1 (5 years)	\$ 5,650	\$ 152	\$ 490	\$ 3,700
Clintonville, WI <sup>(1)</sup>	4/11/2013	102,400	15 years	N/A	3,250	N/A	961	-
Vance, AL	5/9/2013	170,000	10 years	2 (5 years)	13,388	186	1,173	-
Blaine, MN	5/10/2013	92,275	7 years	2 (5 years)	14,450	79	1,475	8,200
Austin, TX	7/9/2013	320,000	7 years	3 (3 years)	57,000	155	4,641	35,300
Allen, TX	7/10/2013	115,200	9 years	2 (5 years)	15,150	81	1,478	8,900
Englewood, CO	12/11/2013	99,797	8 years	2 (5 years)	18,250	66	1,497	11,315
Novi, MI	12/27/2013	156,200	10 years	1 (5 years)	7,300	42	684	4,380
Total		1,085,129			\$ 134,438	\$ 761	\$ 12,399	\$ 71,795

<sup>(1)</sup> The Clintonville, WI property was originally acquired in November 2005 for \$5.3 million. After the expansion was completed in April 2013, the total investment in the property is \$8.6 million.

In accordance with ASC 805, we determined the fair value of acquired assets related to the seven properties acquired during the year ended December 31, 2013 as follows (dollars in thousands):

	Land	Building	Tenant Improvements	In-place Leases	Leasing Costs	Customer Relationships	Above Market Leases	Below Market Leases	Total Purchase Price
Egg Harbor Township, NJ	\$ 1,627	\$ 2,735	\$ 282	\$ 558	\$ 189	\$ 259	\$ -	\$ -	\$ 5,650
Vance, AL	457	9,721	808	1,097	678	627	-	-	13,388
Blaine, MN	1,060	9,347	1,172	1,361	694	816	-	-	14,450
Austin, TX	2,330	37,207	6,814	6,118	1,906	3,793	-	(1,168)	57,000
Allen, TX	2,699	5,758	2,187	1,525	1,146	1,499	336	-	15,150
Englewood, CO	1,503	9,889	1,850	2,036	1,178	1,850	-	(56)	18,250
Novi, MI	352	5,354	272	663	434	225	-	-	7,300
	\$ 10,028	\$ 80,011	\$ 13,385	\$ 13,358	\$ 6,225	\$ 9,069	\$ 336	\$ (1,224)	\$ 131,188

Below is a summary of the total revenue and earnings recognized on the seven properties acquired during the year ended December 31, 2013 (dollars in thousands):

Location	Acquisition Date	For the year ended December 31,	
		Rental Revenue	Earnings <sup>(1)</sup>
Egg Harbor Township, NJ	3/28/2013	\$ 373	\$ 209
Vance, AL	5/9/2013	757	363
Blaine, MN	5/10/2013	947	424
Austin, TX	7/9/2013	2,299	655
Allen, TX	7/10/2013	685	300
Englewood, CO	12/11/2013	85	25
Novi, MI	12/27/2013	9	5
		\$ 5,155	\$ 1,981

<sup>(1)</sup> Earnings is calculated as net income exclusive of both interest expense and acquisition related costs that are required to be expensed under ASC 805.

### Future Lease Payments

Future operating lease payments from tenants under non-cancelable leases, excluding tenant reimbursement of expenses, for each of the five succeeding fiscal years and thereafter is as follows (dollars in thousands):

Year	Tenant Lease Payments
2015	\$ 70,794
2016	68,669
2017	68,290
2018	67,983
2019	68,405
Thereafter	312,030

In accordance with the lease terms, substantially all operating expenses are required to be paid by the tenant; however, we would be required to pay property taxes on the respective properties in the event the tenants fail to pay them. The total annual property taxes for all properties owned by us as of December 31, 2014, were \$12.6 million.

### Intangible Assets

The following table summarizes the carrying value of intangible assets and the accumulated amortization for each intangible asset class (in thousands):

	December 31, 2014		December 31, 2013	
	Lease Intangibles	Accumulated Amortization	Lease Intangibles	Accumulated Amortization
In-place leases	\$ 59,233	\$ (17,379)	\$ 47,442	\$ (15,158)
Leasing costs	38,305	(11,411)	31,339	(9,323)
Customer relationships	41,243	(11,177)	35,739	(10,407)
	<u>\$ 138,781</u>	<u>\$ (39,967)</u>	<u>\$ 114,520</u>	<u>\$ (34,888)</u>
	Deferred Rent Receivable/Liability	Accumulated Amortization	Lease Intangibles	Accumulated Amortization
Above market leases	\$ 8,314	\$ (6,384)	\$ 7,928	\$ (6,085)
Below market leases	\$ 15,939	\$ (7,345)	\$ 12,672	\$ (6,657)
	<u>\$ 24,253</u>	<u>\$ (13,729)</u>	<u>\$ 20,600</u>	<u>\$ (12,742)</u>
Total	<u>\$ 163,034</u>	<u>\$ (53,696)</u>	<u>\$ 135,120</u>	<u>\$ (47,630)</u>

The weighted average amortization periods in years for the intangible assets acquired and liabilities assumed during the years ended December 31, 2014 and 2013, respectively, were as follows:

Intangible Assets & Liabilities	2014	2013
In-place leases	10.1	8.9
Leasing costs	10.1	8.9
Customer relationships	15.1	13.7
Above market leases	9.3	8.8
Below market leases	10.0	7.5
All intangible assets & liabilities	<u>11.5</u>	<u>10.0</u>

The estimated aggregate amortization expense to be recorded for in-place leases, leasing costs and customer relationships for each of the five succeeding fiscal years and thereafter is as follows (dollars in thousands):

Year	Estimated Amortization Expense
2015	\$ 12,801
2016	11,972
2017	11,733
2018	11,633
2019	11,610
Thereafter	39,065
Total	\$ 98,814

The estimated aggregate rental income to be recorded for the amortization of both above and below market leases for each of the five succeeding fiscal years and thereafter is as follows (dollars in thousands):

Year	Estimated Rental Income
2015	\$ 557
2016	438
2017	432
2018	432
2019	432
Thereafter	4,374
Total	\$ 6,665

## 5. Real Estate Dispositions and Impairment Charges

### *Real Estate Dispositions*

On June 6, 2014, we sold our property located in Sterling Heights, Michigan to the tenant currently occupying the building for \$11.4 million and incurred approximately \$0.2 million in selling costs. We recognized a gain of \$1.2 million on the sale.

The table below summarizes the components of income from real estate and related assets disposed of for the Sterling Heights, Michigan property during the years ended December 31, 2014, 2013 and 2012, respectively (dollars in thousands):

	For the year ended December 31,		
	2014	2013	2012
Operating revenue	\$ 507	\$ 1,167	\$ 1,167
Operating expense	46	228	221
Income from real estate and related assets sold	\$ 461	\$ 939	\$ 946

### *Impairment Charges*

We performed the evaluation and analysis of our portfolio and concluded that our Roseville, Minnesota property was impaired as of March 31, 2014. We determined that the expected undiscounted cash flows based upon a revised estimated holding period of this property was below the current carrying value. The estimated holding period was revised after a potential tenant that we were anticipating to lease a large portion of the vacant space, during the three months ended March 31, 2014, did not execute a lease on the property. Consequently, we revised the holding period to coincide with the maturity of the mortgage loan in June 2014. Accordingly, we reduced the carrying value of this property to its estimated fair value, less cost to sell, and we recognized an impairment loss of \$14.2 million during the year ended December 31, 2014. This property was returned to the lender in a deed in lieu transaction on November 12, 2014 (see Note 7).

We performed an analysis of both the real estate disposition and impaired property for the year ended December 31, 2014 and determined that these properties should not be classified as discontinued operations as neither constituted a strategic shift in our operations in accordance with ASU 2014-08.

We had previously reported that our property located in South Hadley, Massachusetts was at risk of becoming impaired in the future. We recently extended the lease on this property for two years, and it will now expire in January 2017. As a result of this lease extension, we no longer view this property as at risk for impairment.

We continue to monitor our portfolio for any other indicators of impairment.

### **6. Mortgage Note Receivable**

On July 25, 2014, we closed a \$5.6 million second mortgage development loan for the construction of an 81,371 square foot, build-to-suit transitional care facility located on a major hospital campus in Phoenix, Arizona. Construction is scheduled to be completed in July 2015 and we will earn 9.0% interest, paid currently in cash, on the loan during construction and through maturity. Prior to completion of the facility, we will be granted a right of first offer to purchase the property at fair value. If we do not purchase the property we will receive an exit fee upon maturity of the loan in an amount sufficient for us to earn an internal rate of return of 22% on the second mortgage development loan, inclusive of interest earned. The loan is scheduled to mature in July 2016, but has a one-year extension option. We have recognized \$0.5 million in both cash interest income and accrued exit fee revenue during the year ended December 31, 2014.

### **7. Mortgage Notes Payable and Line of Credit**

Our mortgage notes payable and line of credit as of December 31, 2014 and December 31, 2013 are summarized below (dollars in thousands):

Date of Issuance/ Assumption	Principal Maturity Date	Stated Interest Rate at December 31, 2014 <sup>(1)</sup>	Principal Balance Outstanding	
			December 31, 2014	December 31, 2013
02/21/06	06/30/14	5.20%	-	17,455
08/25/05	09/01/15	5.33%	19,262	19,664
09/12/05	09/01/15	5.21%	11,369	11,593
09/06/07	12/11/15	5.81%	3,964	4,052
12/21/05	01/08/16	5.71%	17,482	17,816
03/27/14	02/01/16	5.58%	6,214	-
03/29/06	04/01/16	5.92%	16,201	16,434
04/27/06	05/05/16	6.58%	12,316	12,696
08/29/08	06/01/16	6.80%	5,510	5,687
05/08/14	06/01/16	6.25%	3,767	-
06/20/11	06/30/16	6.08%	10,977	11,164
11/22/06	12/01/16	5.76%	13,093	13,324
11/26/13	12/01/16	LIBOR +2.15% <sup>(2)</sup>	8,200	8,200
12/22/06	01/01/17	5.79%	20,026	20,376
02/08/07	03/01/17	6.00%	13,775	13,775
06/05/07	06/08/17	6.11%	13,825	13,999
10/15/07	11/08/17	6.63%	14,609	14,848
09/26/12	07/01/18	5.75%	10,252	10,478
11/18/11	11/01/18	4.50%	4,049	4,155
06/09/14	07/01/19	4.23%	22,600	-
12/06/11	12/06/19	6.00%	7,776	8,031
10/28/11	11/01/21	6.00%	6,799	6,938
04/05/12	05/01/22	6.10%	18,116	18,467
06/21/12	07/06/22	5.05%	4,507	4,608
08/03/12	07/31/22	5.00%	2,845	2,911
07/24/12	08/01/22	5.60%	9,066	9,361
10/01/12	10/01/22	4.86%	32,397	33,133
11/21/12	12/06/22	4.04%	18,067	18,525
03/28/13	04/06/23	4.16%	3,551	3,638
07/03/13	08/01/23	5.00%	8,045	8,163
07/10/13	08/01/23	4.20%	8,704	8,852
07/09/13	08/06/23	4.81%	34,567	35,093
12/27/13	01/01/24	5.28%	4,297	4,380
04/22/14	05/01/24	4.90%	4,935	-
09/03/14	10/01/24	4.40%	6,100	-
12/23/14	01/01/25	4.04%	18,426	-
12/15/10	12/10/26	6.63%	9,015	9,496
05/16/12	12/31/26	4.30%	2,757	2,829
11/08/12	02/01/27	5.69%	13,567	13,864
05/30/12	05/10/27	6.50%	4,426	4,653
06/27/12	07/01/29	5.10%	1,823	1,905
12/18/13	01/06/39	4.74%	11,315	11,315

Contractual Mortgage Notes Payable:	\$ 458,592	\$ 421,878
Premiums and (Discounts), net:	707	724
Total Mortgage Notes Payable:	<u>\$ 459,299</u>	<u>\$ 422,602</u>
Variable-Rate Line of Credit:		
08/07/13 08/07/17 LIBOR +3.00%	\$ 43,300	\$ 24,400
Total Mortgage Notes Payable and Line of Credit	<u>\$ 502,599</u>	<u>\$ 447,002</u>

(1) The weighted average interest rate on all debt outstanding at December 31, 2014, was approximately 5.11%.

(2) At December 31, 2014, one month LIBOR was approximately 0.17%.

### *Mortgage Notes Payable*

As of December 31, 2014, we had 41 mortgage notes payable, collateralized by a total of 77 properties and the net book value of these collateralized properties was \$642.5 million. Gladstone Commercial Corporation has 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 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. The weighted-average interest rate on the mortgage notes payable as of December 31, 2014 was 5.3%.

During the year ended December 31, 2014, we assumed two long-term mortgages, collateralized by three properties, and issued four long-term mortgages, collateralized by five properties, which are summarized below (dollars in thousands):

<u>Date of Issuance</u>	<u>Issuing Bank</u>	<u>Debt Issued</u>	<u>Interest Rate</u>	<u>Maturity Date</u>
3/27/2014	Wells Fargo N.A.	\$ 6,330	5.58%	2/1/2016
4/22/2014	Keybank N.A.	4,935	4.90%	5/1/2024
5/8/2014	Wells Fargo N.A.	3,816	6.25%	6/1/2016
6/9/2014	Prudential Mortgage Capital Company	22,600	4.23%	7/1/2019
9/3/2014	Everbank	6,100	4.40%	10/1/2024
12/23/2014	Prudential Mortgage Capital Company	18,450	4.04%	1/1/2025
		<u>\$ 62,231</u>		

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

<u>Year</u>	<u>Scheduled Principal Payments</u>
2015	\$ 42,436 <sup>(1)</sup>
2016	99,042
2017	67,653
2018	20,260
2019	34,936
Thereafter	<u>194,265</u>
	<u>\$ 458,592</u>

<sup>(1)</sup> We are planning to refinance the 3 balloon principal payments that mature in the second half of 2015 with a combination of new mortgage debt or equity.

On November 12, 2014, we completed a deed-in-lieu transaction on our Roseville, Minnesota property, where we returned the property to the lender in exchange for cancellation of obligations under our debt agreement with the lender. At the time of the deed-in-lieu transaction, the carrying value of the property was approximately \$9.8 million, the principal balance of the debt outstanding, net of reserves held by the lender, was approximately \$14.1 million and the resulting gain on debt extinguishment was approximately

\$5.3 million. The lender accepted the deed in lieu of the outstanding mortgage, and released us from our obligation.

### *Interest Rate Cap*

We have entered into an interest rate cap agreement with Wells Fargo that caps the interest rate on the note payable for our Champaign, Illinois property. The agreement provides that the interest rate on the note payable for our Champaign, Illinois property is capped at a certain interest rate when one-month LIBOR is in excess of 3.0%. The fair value of the interest rate cap agreement is recorded in other assets on our accompanying consolidated balance sheets. We record changes in the fair value of the interest rate cap agreement quarterly based on the current market valuations at quarter end as other income (loss) on our accompanying consolidated statements of operations. Generally, we will estimate the fair value of our interest rate cap using estimates of value provided by the counterparty and our own assumptions in the absence of observable market data, including estimated remaining life, counterparty credit risk, current market yield and interest rate spreads of similar securities as of the measurement date. At December 31, 2014 and 2013, our interest rate cap agreement was valued using Level 3 inputs. The following table summarizes the key terms of each interest rate cap agreement (dollars in thousands):

<u>Interest Rate Cap</u>	<u>Notional Amount</u>	<u>LIBOR Cap</u>	<u>Maturity Date</u>	<u>As of December 31, 2014</u>		<u>As of December 31, 2013</u>	
				<u>Cost</u>	<u>Fair Value</u>	<u>Cost</u>	<u>Fair Value</u>
November 26, 2013	\$ 8,200	3.00%	December 1, 2016	\$ 31	\$ 4	\$ 31	\$ 22

### *Fair Value*

The fair value of all mortgage notes payable outstanding as of December 31, 2014, was \$476.9 million, as compared to the carrying value stated above of \$459.3 million. The fair value is calculated based on a discounted cash flow analysis, using interest rates based on 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."

### *Line of Credit*

In August 2013, we procured a \$60.0 million Line of Credit, expanded to \$75.0 million in November 2014, with KeyBank National Association (serving as a revolving lender, a letter of credit issuer and an administrative agent) and added Citizens Bank of Pennsylvania as an additional lender. Comerica Bank was subsequently added as another lender in December 2013. In March 2014, we amended our Line of Credit to extend the maturity date by one year to August 2017. We also modified certain terms under the Line of Credit, including the calculation of the total asset value and unencumbered asset value. The applicable LIBOR margins were also reduced 25 basis points at each pricing level. As a result of these modifications, the availability under our Line of Credit increased by \$1.3 million.

The Line of Credit initially matures in August 2017; however, we have a one-year extension option subject to the payment of an extension fee equal to 25 basis points on the initial maturity date and certain other customary conditions.

The Line of Credit has a letter of credit sublimit of up to \$20.0 million. In addition, we may expand the Line of Credit up to a total of \$100.0 million upon satisfaction of certain conditions and payment of the associated up front and arrangement fees at the time of such increase. The interest rate per annum applicable to the Line of Credit is equal to the London Interbank Offered Rate, or LIBOR, plus an applicable margin of up to 3.25%, depending upon our leverage. The leverage ratio used in determining the applicable margin for interest on the Line of Credit is recalculated quarterly. We are subject to an annual maintenance fee of \$0.03 million per year and an unused commitment fee of 25 basis points per year, which accrues quarterly. Our ability to access this source of financing is subject to our continued ability to meet customary lending requirements, such as compliance with financial and operating covenants and our meeting certain lending limits. One such covenant requires us to limit distributions to our stockholders to 100% of our FFO, with acquisition-related costs required to be expensed under ASC 805 added back to



FFO. In addition, the maximum amount we may draw under the Line of Credit is based on a percentage of the value of a pool of unencumbered properties, which must meet agreed upon eligibility standards.

If and when long-term mortgages are arranged for properties in the unencumbered pool, the banks will reduce the availability under the Line of Credit by the amount advanced against that property's value. Conversely, as we purchase new properties meeting the eligibility standards, we may add these new properties to the unencumbered pool to obtain additional availability under the Line of Credit. The availability under the Line of Credit is also reduced by letters of credit used in the ordinary course of business. We may use the advances under the Line of Credit for both general corporate purposes and the acquisition of new investments.

As of December 31, 2014, there was \$43.3 million outstanding under our Line of Credit at an interest rate of approximately 3.17% and \$4.5 million outstanding under letters of credit at a weighted average interest rate of 3.0%. As of February 18, 2015, the maximum additional amount we could draw was \$28.3 million. We were in compliance with all covenants under the Line of Credit as of December 31, 2014.

## **8. Mandatorily Redeemable Preferred Stock**

In February 2012, we completed a public offering of 1,540,000 shares of 7.125% Series C Cumulative Term Preferred Stock, par value \$0.001 per share, or the Term Preferred Stock, at a public offering price of \$25.00 per share. Gross proceeds of the offering totaled \$38.5 million and net proceeds, after deducting offering expenses borne by us, were \$36.7 million and were used to repay a portion of outstanding borrowings under our Line of Credit, for acquisitions of real estate and for working capital. The Term Preferred Stock is traded under the ticker symbol GOODN on the NASDAQ Global Select Market, or the NASDAQ. The Term Preferred Stock is not convertible into our common stock or any other security of ours. Generally, we may not redeem shares of the Term Preferred Stock prior to January 31, 2016, except in limited circumstances to preserve our status as a REIT. On or after January 31, 2016, we may redeem the shares at a redemption price of \$25.00 per share, plus any accumulated and unpaid dividends to and including the date of redemption. The shares of the Term Preferred Stock have a mandatory redemption date of January 31, 2017. We incurred \$1.8 million in total offering costs related to these transactions, which have been recorded as deferred financing costs on the consolidated balance sheet and will be amortized over the redemption period ending January 31, 2017.

The Term Preferred Stock is recorded as liability in accordance with ASC 480, "Distinguishing Liabilities from Equity," which states that mandatorily redeemable financial instruments should be classified as liabilities and therefore the related dividend payments are treated as a component of interest expense in the consolidated statements of operations.

The fair value of our Term Preferred Stock as of December 31, 2014, was \$39.7 million, as compared to the carrying value stated above of \$38.5 million. The fair value is calculated based on the closing share price as of December 31, 2014 of \$25.80. The fair value was calculated using Level 1 inputs of the hierarchy established by ASC 820, "Fair Value Measurements and Disclosures."

## 9. Commitments and Contingencies

### Ground Leases

We are obligated as lessee under three ground leases. Future minimum rental payments due under the terms of these leases as of December 31, 2014, are as follows (dollars in thousands):

Location	Lease End Date	For the year ended December 31,						Thereafter
		2015	2016	2017	2018	2019	2020	
Tulsa, OK	Apr-21	\$ 169	\$ 169	\$ 169	\$ 169	\$ 169	\$ 169	\$ 85
Dartmouth, MA	May-36	174	174	174	174	174	174	3,127
Springfield, MA	Feb-30	86	86	89	90	90	90	884
		<u>\$ 429</u>	<u>\$ 429</u>	<u>\$ 432</u>	<u>\$ 433</u>	<u>\$ 433</u>	<u>\$ 433</u>	<u>\$ 4,096</u>

Expenses recorded in connection to rental expense incurred for the properties listed above during the years ended December 31, 2014, 2013, and 2012 were \$0.4 million for each of the three years. Rental expenses are reflected in property operating expenses on the consolidated statements of operations.

## 10. Stockholders' Equity

### Distributions

Our Board of Directors declared the following distributions per share for the years ended December 31, 2014, 2013, and 2012:

	For the year ended December 31,		
	2014	2013	2012
Common Stock	\$ 1.50	\$ 1.50	\$ 1.50
Senior Common Stock	1.05	1.05	1.05
Series A Preferred Stock	1.9374996	1.9374996	1.9374996
Series B Preferred Stock	1.8750	1.8750	1.8750
Series C Preferred Stock	1.7813	1.7813	1.6328 <sup>(1)</sup>

<sup>(1)</sup>The Series C Preferred Stock was issued on January 31, 2012.

For federal income tax purposes, distributions paid to stockholders may be characterized as ordinary income, capital gains, return of capital or a combination of the foregoing. We had no capital gains during the last three years. The characterization of distributions during each of the last three years is reflected in the table below:

	<u>Ordinary Income</u>	<u>Return of Capital</u>
Common Stock		
For the year ended December 31, 2012	0.00000%	100.00000%
For the year ended December 31, 2013	18.32962%	81.67038%
For the year ended December 31, 2014	0.00000%	100.00000%
Senior Common Stock		
For the year ended December 31, 2012	0.00000%	100.00000%
For the year ended December 31, 2013	100.00000%	0.00000%
For the year ended December 31, 2014	0.00000%	100.00000%
Series A Preferred Stock		
For the year ended December 31, 2012	91.70830%	8.29170%
For the year ended December 31, 2013	100.00000%	0.00000%
For the year ended December 31, 2014	24.10732%	75.89268%
Series B Preferred Stock		
For the year ended December 31, 2012	91.70830%	8.29170%
For the year ended December 31, 2013	100.00000%	0.00000%
For the year ended December 31, 2014	24.10732%	75.89268%
Series C Preferred Stock		
For the year ended December 31, 2012	91.70830%	8.29170%
For the year ended December 31, 2013	100.00000%	0.00000%
For the year ended December 31, 2014	24.10732%	75.89268%

#### *Recent Activity*

On June 6, 2014, we completed a public offering of 1,610,000 shares of our common stock at a public offering price of \$17.00 per share. Gross proceeds of the offering totaled \$27.4 million and net proceeds, after deducting offering expenses borne by us, were \$26.0 million, which we used to acquire real estate.

#### *Ongoing Activity*

On September 2, 2014, we entered into an open market sale arrangement, or the New ATM, with Cantor Fitzgerald & Co., or Cantor Fitzgerald, pursuant to which we may, from time to time, offer to sell shares of our common stock with an aggregate sales price of up to \$100.0 million on the open market through Cantor Fitzgerald, acting as sales agent and/or principal. Under the New ATM, Cantor Fitzgerald is entitled to compensation equal to up to 2.0% of the gross proceeds of the common shares it sells. During 2014, we sold a total of 1.9 million shares with aggregate net proceeds of \$32.0 million, and have a remaining capacity to sell up to \$67.5 million of common stock under the New ATM with Cantor Fitzgerald.

On August 26, 2014, we provided notice of our termination of our prior open market sale arrangement, or the Prior ATM, with Jefferies LLC, or Jefferies, under which we offered to sell shares of our common stock with an aggregate sales price of up to \$25.0 million on the open market through Jefferies, as agent, or to Jefferies, as principal. From November 2009 through August 2014, we issued and sold \$21.8 million in gross proceeds under the Prior ATM. During 2014, we raised approximately \$7.6 million in net proceeds under the Prior ATM.

In March 2011, we commenced an offering of an aggregate of 3,500,000 shares of our Senior Common Stock, par value \$0.001 per share, at a price to the public of \$15.00 per share, of which 3,000,000 shares

are intended to be offered pursuant to the primary offering and 500,000 shares are intended to be offered pursuant to our senior common distribution reinvestment plan, or the DRIP. We, however, reserve the right to reallocate the number of shares being offered between the primary offering and the DRIP. As of December 31, 2014, we had sold 738,942 shares of Senior Common Stock in this ongoing offering, for gross proceeds of \$11.1 million, and issued an additional 24,315 shares of Senior Common Stock under the DRIP program. We have elected not to renew this offering program and it will terminate on March 28, 2015.

#### Note to Employee

The following table is a summary of the outstanding note issued to an employee of the Adviser for the exercise of stock options (dollars in thousands):

<u>Date Issued</u>	<u>Outstanding Balance of Employee Loan at December 31, 2014</u>	<u>Outstanding Balance of Employee Loan at December 31, 2013</u>	<u>Maturity Date of Note</u>	<u>Interest Rate on Note</u>
Nov 2006	\$ 375	\$ 375	Nov 2015	8.15%

The employee stock option program terminated in 2006. In accordance with ASC 505-10-45-2, "Equity," receivables from employees for the issuance of capital stock to employees prior to the receipt of cash payment should be reflected in the balance sheet as a reduction to stockholders' equity. Therefore, this note was recorded as a full recourse loan to the employee and is included in the equity section of the accompanying consolidated balance sheets. As of December 31, 2014, this loan maintained its full recourse status.

#### 11. Quarterly Financial Information (unaudited)

The following table reflects the quarterly results of operations for the years ended December 31, 2014 and 2013 (dollars in thousands).

	Quarter ended			
	December 31, 2014	September 30, 2014	June 30, 2014	March 31, 2014
Operating revenues	\$ 19,216	\$ 19,014	\$ 18,390	\$ 17,136
Operating expenses	10,970	11,457	11,243	23,736
Other expense	(2,082)	(7,328)	(5,928)	(6,914)
Net income (loss)	6,164	229	1,219	(13,514)
Dividends attributable to preferred and senior common stock	(1,220)	(1,160)	(1,133)	(1,123)
Net income (loss) available to common stockholders	4,944 <sup>(1)</sup>	(931)	86	(14,637) <sup>(2)</sup>
Net income (loss) available to common stockholders - basic & diluted	\$ 0.36	\$ (0.05)	\$ 0.01	\$ (0.93)

	Quarter ended			
	December 31, 2013	September 30, 2013	June 30, 2013	March 31, 2013
Operating revenues	\$ 16,860	\$ 16,190	\$ 14,258	\$ 14,035
Operating expenses	9,542	8,639	7,369	7,273
Other expense	(6,984)	(7,242)	(6,438)	(6,329)
Net income	334	309	451	433
Dividends attributable to preferred and senior common stock	(1,120)	(1,106)	(1,092)	(1,076)
Net loss available to common stockholders	(786)	(797)	(641)	(643)
Net loss available to common stockholders - basic & diluted	\$ (0.05)	\$ (0.06)	\$ (0.05)	\$ (0.06)

(1) Includes a \$5.3 million gain on debt extinguishment recorded during the three months ended December 31, 2014.

(2) Includes a \$14.0 million impairment loss recorded during the three months ended March 31, 2014.

## 12. Subsequent Events

On January 13, 2015, our Board of Directors declared the following monthly distributions:

<u>Record Date</u>	<u>Payment Date</u>	<u>Common Stock Distributions per Share</u>	<u>Series A Preferred Distributions per Share</u>	<u>Series B Preferred Distributions per Share</u>	<u>Series C Preferred Distributions per Share</u>
January 23, 2015	February 3, 2015	\$ 0.125	\$ 0.1614583	\$ 0.15625	\$ 0.1484375
February 18, 2015	February 27, 2015	0.125	0.1614583	0.15625	0.1484375
March 20, 2015	March 31, 2015	<u>0.125</u>	<u>0.1614583</u>	<u>0.15625</u>	<u>0.1484375</u>
Total		<u>\$ 0.375</u>	<u>\$ 0.4843749</u>	<u>\$ 0.46875</u>	<u>\$ 0.4453125</u>

### Senior Common Stock Distributions

<u>Payable to the Holders of Record During the Month of:</u>	<u>Payment Date</u>	<u>Distribution per Share</u>
January	February 6, 2015	\$ 0.0875
February	March 6, 2015	0.0875
March	April 7, 2015	<u>0.0875</u>
Total		<u>\$ 0.2625</u>

On February 9, 2015, we modified the leases with the tenant occupying two of our properties located in Raleigh, North Carolina. The leases covering these properties were extended for an additional five years through July 2020. Both leases were originally set to expire in July 2015. The tenant was previously fully occupying both buildings, totaling 174,426 square feet, but had reduced their space requirement in one of their buildings by 94,200 square feet. Both leases contain prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$0.9 million, as compared to annualized straight line rents of \$1.3 million under the previous terms of the lease. In connection with the extension of the lease and modification of certain terms of the lease, we anticipate paying \$0.2 million in leasing commissions, and committed to \$0.1 million in tenant improvements.

**GLADSTONE COMMERCIAL CORPORATION**  
**SCHEDULE III—REAL ESTATE AND ACCUMULATED DEPRECIATION**  
**DECEMBER 31, 2014 (Dollars in Thousands)**

Location of Property	Initial Cost				Total Cost				Accumulated Depreciation (2)	Net Real Estate	Year Construction/Improvements	Date Acquired
	Encumbrances	Land	Buildings & Improvements	Improvement Costs Capitalized Subsequent to Acquisition	Land	Buildings & Improvements	Total (1)					
Raleigh, North Carolina Office Building	\$ 4,796	\$ 960	\$ 4,481	\$ -	\$ 960	\$ 4,481	\$ 5,441	\$ 1,773	\$ 3,668	1997	12/23/2003	
Canton, Ohio Office Building	2,664	186	3,083	500	186	3,583	3,769	972	2,797	1994	1/30/2004	
Akron, Ohio Office Building	6,828	1,973	6,771	1,279	1,973	8,050	10,023	1,916	8,107	1968/1999	4/29/2004	
Charlotte, North Carolina Office Building	6,308	740	8,423	61	740	8,484	9,224	2,319	6,905	1984/1995	6/30/2004	
Canton, North Carolina Industrial Building	3,652	150	5,050	7,285	150	12,335	12,485	1,401	11,084	1998/2014	7/6/2004	
Crenshaw, Pennsylvania Industrial Building	5,176	100	6,574	269	100	6,843	6,943	1,800	5,143	1991	8/5/2004	
Lexington, North Carolina Industrial Building	2,636	820	2,107	69	820	2,176	2,996	584	2,412	1986	8/5/2004	
Austin, Texas Office Building	6,500	1,000	6,296	1,396	1,000	7,692	8,692	1,726	6,966	2001	9/16/2004	
Mt. Pocono, Pennsylvania Industrial Building	4,889	350	5,819	18	350	5,837	6,187	1,551	4,636	1995/1999	10/15/2004	
San Antonio, Texas Office Building	6,643	843	7,514	621	843	8,135	8,978	2,389	6,589	1999	2/10/2005	
Columbus, Ohio Industrial Building	2,516	410	2,385	-	410	2,385	2,795	610	2,185	1995	2/10/2005	
Big Flats, New York Industrial Building	5,365	275	6,459	34	275	6,493	6,768	1,623	5,145	2001	4/15/2005	
Wichita, Kansas Office Building	7,466	1,525	9,703	77	1,525	9,780	11,305	2,510	8,795	2000	5/18/2005	
Arlington, Texas Industrial Building	3,814	636	3,695	416	636	4,111	4,747	1,012	3,735	1966	5/26/2005	
Dayton, Ohio Office Building	1,877	525	1,877	120	525	1,997	2,522	820	1,702	1956	6/30/2005	
Eatontown, New Jersey Office Building	4,365	1,351	3,520	534	1,351	4,054	5,405	1,012	4,393	1991	7/7/2005	
Franklin Township, New Jersey Industrial Building	6,471	1,632	6,200	-	1,632	6,200	7,832	1,514	6,318	1978	7/11/2005	
Duncan, South Carolina Industrial Building	10,375	783	10,790	1,615	783	12,405	13,188	2,979	10,209	1984/2001/2007	7/14/2005	
Duncan, South Carolina Industrial Building	2,579	195	2,682	419	195	3,101	3,296	740	2,556	1984/2001/2007	7/14/2005	
Hazelwood, Missouri Industrial Building	2,291	763	2,309	683	763	2,992	3,755	642	3,113	1977	8/5/2005	

**GLADSTONE COMMERCIAL CORPORATION**  
**SCHEDULE III—REAL ESTATE AND ACCUMULATED DEPRECIATION (Continued)**

**DECEMBER 31, 2014 (Dollars in Thousands)**

Location of Property	Initial Cost				Total Cost				Accumulated Depreciation (2)	Net Real Estate	Year Construction/Improvements	Date Acquired
	Encumbrances	Land	Buildings & Improvements	Improvement Costs Capitalized Subsequent to Acquisition	Land	Buildings & Improvements	Total (1)					
Angola, Indiana Industrial Building	\$ 626	\$ 66	\$ 1,075	\$ 49	\$ 66	\$ 1,124	\$ 1,190	\$ 271	\$ 919	1982	9/2/2005	
Angola, Indiana Industrial Building	601	132	1,130	51	132	1,181	1,313	421	892	1998	9/2/2005	
Rock Falls, Illinois Industrial Building	626	35	1,113	50	35	1,163	1,198	144	1,054	1988	9/2/2005	
Newburyport, Massachusetts Industrial Building	6,276	629	6,504	1,847	629	8,351	8,980	1,873	7,107	1994	10/17/2005	
Clintonville, Wisconsin Industrial Building	2,997	55	4,717	3,250	55	7,967	8,022	1,316	6,706	1992/2013	10/31/2005	
Maple Heights, Ohio Industrial Building	9,790	1,609	10,065	1,221	1,609	11,286	12,895	3,237	9,658	1974	12/21/2005	
Richmond, Virginia Office Building	5,275	736	5,336	36	736	5,372	6,108	1,286	4,822	1972	12/30/2005	
Toledo, Ohio Medical Office Building	2,750	263	2,812	390	263	3,202	3,465	736	2,729	1979	12/30/2005	
South Hadley, Massachusetts Industrial Building	-	471	2,765	71	471	2,836	3,307	637	2,670	1978	2/15/2006	
Champaign, Illinois Office Building	1,545	687	2,036	2	687	2,038	2,725	495	2,230	1996	2/21/2006	
Champaign, Illinois Office Building	3,030	1,347	3,992	4	1,347	3,996	5,343	971	4,372	1996	2/21/2006	
Champaign, Illinois Office Building	1,894	842	2,495	2	842	2,497	3,339	607	2,732	1996	2/21/2006	
Champaign, Illinois Office Building	1,731	770	2,281	2	770	2,283	3,053	555	2,498	1996	2/21/2006	
Burnsville, Minnesota Office Building	11,001	3,511	8,746	3,525	3,511	12,271	15,782	2,515	13,267	1984	5/10/2006	
Menomonee Falls, Wisconsin Industrial Building	6,738	625	6,911	57	625	6,968	7,593	1,553	6,040	1986/2000	6/30/2006	
Baytown, Texas Medical Office Building	2,000	221	2,443	-	221	2,443	2,664	593	2,071	1997	7/11/2006	
Birmingham, Alabama <sup>(3)</sup> Industrial Building	-	612	2,326	-	612	2,326	2,938	504	2,434	1961/1980	9/29/2006	
Montgomery, Alabama <sup>(3)</sup> Industrial Building	-	222	844	-	222	844	1,066	183	883	1962/1989	9/29/2006	

**GLADSTONE COMMERCIAL CORPORATION**  
**SCHEDULE III—REAL ESTATE AND ACCUMULATED DEPRECIATION (Continued)**  
**DECEMBER 31, 2014 (Dollars in Thousands)**

Location of Property	Encumbrances	Initial Cost			Improvement Costs Capitalized Subsequent to Acquisition	Total Cost			Accumulated Depreciation (2)	Net Real Estate	Year Construction/ Improvements	Date Acquired
		Land	Buildings & Improvements			Land	Buildings & Improvements	Total (1)				
Columbia, Missouri <sup>(3)</sup> Industrial Building	\$ -	\$ 146	\$ 555	\$ -	\$ 146	\$ 555	\$ 701	120	\$ 581	1978	9/29/2006	
Mason, Ohio Office Building	4,250	797	6,258	540	797	6,798	7,595	1,563	6,032	2002	1/5/2007	
Raleigh, North Carolina Industrial Building	5,164	1,606	5,513	-	1,606	5,513	7,119	1,142	5,977	1994	2/16/2007	
Tulsa, Oklahoma Industrial Building	7,776	-	14,057	-	-	14,057	14,057	3,312	10,745	2004	3/1/2007	
Hialeah, Florida <sup>(3)</sup> Industrial Building	-	3,562	6,672	685	3,562	7,357	10,919	1,435	9,484	1956/1992	3/9/2007	
Tewksbury, Massachusetts <sup>(3)</sup> Industrial Building	-	1,395	8,893	-	1,395	8,893	10,288	1,882	8,406	1985/1989	5/17/2007	
Mason, Ohio Retail Building	4,555	1,201	4,961	-	1,201	4,961	6,162	969	5,193	2007	7/1/2007	
Cicero, New York Industrial Building	3,964	299	5,019	-	299	5,019	5,318	942	4,376	2005	9/6/2007	
Grand Rapids, Michigan Office Building	5,831	1,629	10,500	37	1,629	10,537	12,166	2,055	10,111	2001	9/28/2007	
Bolingbrook, Illinois Industrial Building	-	1,272	5,003	475	1,272	5,478	6,750	993	5,757	2002	9/28/2007	
Decatur, Georgia <sup>(3)</sup> Medical Office Building	-	784	3,245	-	784	3,245	4,029	653	3,376	1989	12/13/2007	
Decatur, Georgia <sup>(3)</sup> Medical Office Building	-	205	848	-	205	848	1,053	171	882	1989	12/13/2007	
Decatur, Georgia <sup>(3)</sup> Medical Office Building	-	257	1,064	-	257	1,064	1,321	214	1,107	1989	12/13/2007	
Lawrenceville, Georgia <sup>(3)</sup> Medical Office Building	-	679	2,809	-	679	2,809	3,488	565	2,923	2005	12/13/2007	
Snellville, Georgia <sup>(3)</sup> Medical Office Building	-	176	729	-	176	729	905	147	758	1986	12/13/2007	
Covington, Georgia <sup>(3)</sup> Medical Office Building	-	232	959	-	232	959	1,191	193	998	2000	12/13/2007	
Cumming, Georgia Medical Office Building	3,145	738	3,055	2,511	738	5,566	6,304	615	5,689	2004	12/13/2007	
Conyers, Georgia <sup>(3)</sup> Medical Office Building	-	297	1,228	-	297	1,228	1,525	247	1,278	1994	12/13/2007	
Reading, Pennsylvania Industrial Building	3,983	491	6,202	-	491	6,202	6,693	1,104	5,589	2007	1/29/2008	
Fridley, Minnesota Office Building	5,121	1,354	8,074	397	1,381	8,444	9,825	1,816	8,009	1985/2006	2/26/2008	



**GLADSTONE COMMERCIAL CORPORATION**  
**SCHEDULE III—REAL ESTATE AND ACCUMULATED DEPRECIATION (Continued)**

**DECEMBER 31, 2014 (Dollars in Thousands)**

Location of Property	Initial Cost			Improvement Costs Capitalized Subsequent to Acquisition	Total Cost			Accumulated Depreciation (2)	Net Real Estate	Year Construction/ Improvements	Date Acquired
	Encumbrances	Land	Buildings & Improvements		Land	Buildings & Improvements	Total (1)				
Concord Township, Ohio <sup>(3)</sup> Office Building	\$ -	\$ 1,796	\$ 11,154	\$ (11)	\$ 1,785	\$ 11,154	\$ 12,939	\$ 2,048	\$ 10,891	1957/2008	3/31/2008
Pineville, North Carolina Industrial Building	2,315	669	3,028	6	669	3,034	3,703	535	3,168	1985	4/30/2008
Marietta, Ohio Industrial Building	5,650	829	6,607	209	829	6,816	7,645	1,106	6,539	1992/2007	8/29/2008
Chalfont, Pennsylvania Industrial Building	5,510	1,249	6,420	171	1,249	6,591	7,840	1,270	6,570	1987	8/29/2008
Orange City, Iowa Industrial Building	9,015	258	5,861	-	258	5,861	6,119	743	5,376	1990	12/15/2010
Hickory, North Carolina Office Building	6,697	1,163	6,605	-	1,163	6,605	7,768	1,124	6,644	2008	4/4/2011
Springfield, Missouri Office Building	10,977	1,700	12,038	-	1,700	12,038	13,738	1,278	12,460	2006	6/20/2011
Boston Heights, Ohio Office Building	2,646	449	3,010	-	449	3,010	3,459	427	3,032	2011	10/20/2011
Parsippany, New Jersey Office Building	6,799	1,696	7,077	81	1,696	7,158	8,854	855	7,999	1984	10/28/2011
Dartmouth, Massachusetts Retail Location	4,049	-	4,236	-	-	4,236	4,236	368	3,868	2011	11/18/2011
Springfield, Missouri Retail Location	1,823	-	2,275	-	-	2,275	2,275	250	2,025	2005	12/13/2011
Pittsburgh, Pennsylvania Office Building	2,757	281	3,205	-	281	3,205	3,486	311	3,175	1968	12/28/2011
Ashburn, Virginia Office Building	7,223	706	7,858	-	706	7,858	8,564	767	7,797	2002	1/25/2012
Ottumwa, Iowa Industrial Building	4,426	212	5,072	287	212	5,359	5,571	499	5,072	1970	5/30/2012
New Albany, Ohio Office Building	9,066	1,658	8,746	-	1,658	8,746	10,404	831	9,573	2007	6/5/2012
Columbus, Georgia Office Building	4,507	1,378	4,520	-	1,378	4,520	5,898	471	5,427	2012	6/21/2012
Columbus, Ohio Office Building	2,845	542	2,453	11	542	2,464	3,006	287	2,719	1981	6/28/2012
Jupiter, Florida Office Building	10,252	1,160	11,994	-	1,160	11,994	13,154	827	12,327	2011	9/26/2012
Fort Worth, Texas Industrial Building	13,567	963	15,647	-	963	15,647	16,610	1,022	15,588	2005	11/8/2012
Columbia, South Carolina Office Building	18,067	1,905	20,648	-	1,905	20,648	22,553	1,864	20,689	2010	11/21/2012

**GLADSTONE COMMERCIAL CORPORATION**  
**SCHEDULE III—REAL ESTATE AND ACCUMULATED DEPRECIATION (Continued)**  
**DECEMBER 31, 2014 (Dollars in Thousands)**

Location of Property	Initial Cost				Total Cost				Accumulated Depreciation (2)	Net Real Estate	Year Construction/Improvements	Date Acquired
	Encumbrances	Land	Buildings & Improvements	Improvement Costs Capitalized Subsequent to Acquisition	Land	Buildings & Improvements	Total (1)					
Egg Harbor, New Jersey												
Office Building	\$ 3,551	\$ 1,627	\$ 3,017	\$ 236	\$ 1,627	3,253	\$ 4,880	\$ 201	\$ 4,679	1985	3/28/2013	
Vance, Alabama <sup>(3)</sup>												
Industrial Building	-	457	10,529	-	457	10,529	10,986	604	10,382	2013	5/9/2013	
Blaine, Minnesota												
Office Building	8,045	1,060	10,519	-	1,060	10,519	11,579	748	10,831	2009	5/10/2013	
Austin, Texas												
Office Building	34,567	2,330	44,021	122	2,330	44,143	46,473	3,071	43,402	1999	7/9/2013	
Allen, Texas												
Office Building	8,704	2,699	7,945	-	2,699	7,945	10,644	602	10,042	1998	7/10/2013	
Englewood, Colorado												
Office Building	11,315	1,503	11,739	-	1,503	11,739	13,242	546	12,696	2008	12/11/2013	
Novi, Michigan												
Industrial Building	4,297	352	5,626	-	352	5,626	5,978	197	5,781	1988	12/27/2013	
Allen, Texas												
Retail Building	3,417	874	3,634	-	874	3,634	4,508	95	4,413	2004	3/27/2014	
Colleyville, Texas												
Retail Building	2,797	1,277	2,424	-	1,277	2,424	3,701	72	3,629	2000	3/27/2014	
Rancho Cordova, California												
Office Building	4,935	752	6,176	-	752	6,176	6,928	150	6,778	1986	4/22/2014	
Coppell, Texas												
Retail Building	3,767	1,448	3,349	-	1,448	3,349	4,797	74	4,723	2005	5/8/2014	
Columbus, Ohio <sup>(3)</sup>												
Office Building	-	990	8,017	-	990	8,017	9,007	266	8,741	1986	5/13/2014	
Taylor, Pennsylvania												
Industrial Building	22,600	3,102	25,405	-	3,102	25,405	28,507	451	28,056	2000/2006	6/9/2014	
Aurora, Colorado <sup>(3)</sup>												
Industrial Building	-	2,882	4,013	-	2,882	4,013	6,895	82	6,813	1983	7/1/2014	
Indianapolis, Indiana												
Office Building	6,100	502	6,490	-	502	6,490	6,992	99	6,893	1981/2014	9/3/2014	
Denver, Colorado <sup>(3)</sup>												
Industrial Building	-	1,621	7,314	-	1,621	7,314	8,935	46	8,889	1985	10/31/2014	
Monroe, Michigan												
Industrial Building	10,839	658	14,607	-	658	14,607	15,265	11	15,254	2004	12/23/2014	
Monroe, Michigan												
Industrial Building	7,587	460	10,225	-	460	10,225	10,685	7	10,678	2004	12/23/2014	
	<u>\$ 458,592</u>	<u>\$ 88,378</u>	<u>\$ 602,477</u>	<u>\$ 31,710</u>	<u>\$ 88,394</u>	<u>\$ 634,171</u>	<u>\$ 722,565</u>	<u>\$ 92,133</u>	<u>\$ 630,432</u>			

<sup>(1)</sup> The aggregate cost for land and building improvements for federal income tax purposes is the same as the total gross cost of land and building improvements.

<sup>(2)</sup> Depreciable life of all buildings is 39 years. Depreciable life of all improvements is the shorter of the useful life of the assets or the life of the respective leases on each building, which range from 5-20 years.

<sup>(3)</sup> These properties are in our unencumbered pool of assets on our Line of Credit.

The following table reconciles the change in the balance of real estate during the years ended December 31, 2014, 2013 and 2012, respectively (in thousands):

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Balance at beginning of period	\$ 642,353	\$ 533,753	\$ 442,521
<b>Additions:</b>			
Acquisitions during period	105,813	103,424	85,462
Improvements	13,889	5,176	5,770
<b>Deductions:</b>			
Dispositions during period	(39,490)	-	-
Balance at end of period	<u>\$ 722,565</u>	<u>\$ 642,353</u>	<u>\$ 533,753</u>

The following table reconciles the change in the balance of accumulated depreciation during the years ended December 31, 2014, 2013 and 2012, respectively (in thousands):

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Balance at beginning of period	\$ 81,241	\$ 65,730	\$ 53,784
Additions during period	18,814	15,511	11,946
Dispositions during period	<u>(7,922)</u>	<u>-</u>	<u>-</u>
Balance at end of period	<u>\$ 92,133</u>	<u>\$ 81,241</u>	<u>\$ 65,730</u>

**GLADSTONE COMMERCIAL CORPORATION**  
**SCHEDULE IV – MORTGAGE LOANS ON REAL ESTATE**  
**DECEMBER 31, 2014**  
**(Dollars in Thousands)**

Location and Type of Real Estate	Type of Loan	Interest Rate	Final Maturity Date	Periodic Payment Term	Prior Lien	Face Amount of Mortgage	Carrying Amount of Mortgage	Principal Amount of Loans Subject to Delinquent Principal or Interest
Phoenix, Arizona; Build-to-Suit Healthcare Facility	Second Mortgage	9% Current Interest, 22% internal rate of return on exit	7/31/2016	9.0% interest, paid currently in cash on the loan during construction and through maturity. Exit fee upon maturity of the loan in an amount sufficient to earn a 22% internal rate of return.	-	\$ 5,600	\$ 5,600	\$ -
						<u>\$ 5,600</u>	<u>\$ 5,600</u>	

The following table reconciles the change in the balance of mortgage loans on real estate during the years ended December 31, 2014, 2013 and 2012, respectively:

	2014	2013	2012
Balance at beginning of period	\$ -	\$ -	\$ -
New mortgage loans	5,600	-	-
Collections of principal	-	-	-
Balance at end of period	<u>\$ 5,600</u>	<u>\$ -</u>	<u>\$ -</u>

**Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure.**

None.

**Item 9A. Controls and Procedures.**

**a) Evaluation of Disclosure Controls and Procedures**

As of December 31, 2014, 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, management, including the chief executive officer and chief financial officer, concluded that our disclosure controls and procedures were effective as of December 31, 2014 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) Management's Annual Report on Internal Control Over Financial Reporting**

Refer to Management's Report on Internal Controls over Financial Reporting located in Item 8 of this Form 10-K.

**c) Attestation Report of the Registered Public Accounting Firm**

Refer to the Report of Independent Registered Public Accounting Firm located in Item 8 of this Form 10-K.

**d) Changes in Internal Control over Financial Reporting**

There were no changes in our internal control over financial reporting that occurred during the quarter ended December 31, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**Item 9B. Other Information.**

None.

### **Part III**

We will file a definitive Proxy Statement for our 2015 Annual Meeting of Stockholders (the “2015 Proxy Statement”) with the Securities and Exchange Commission, pursuant to Regulation 14A, not later than 120 days after December 31, 2014. Accordingly, certain information required by Part III has been omitted under General Instruction G(3) to Form 10-K. Only those sections of the 2015 Proxy Statement that specifically address the items set forth herein are incorporated by reference.

#### **Item 10. Directors, Executive Officers and Corporate Governance.**

The information required by Item 10 is hereby incorporated by reference from our 2015 Proxy Statement under the captions “Election of Directors to Class of 2018,” “Information Regarding the Board of Directors and Corporate Governance,” “Compensation Committee Report,” and “Section 16(a) Beneficial Ownership Reporting Compliance,” and sub-caption “Code of Business Conduct and Ethics.”

#### **Item 11. Executive Compensation.**

The information required by Item 11 is hereby incorporated by reference from our 2015 Proxy Statement under the captions “Executive Compensation,” “Director Compensation,” and “Compensation Committee Report,” and sub-caption “Compensation Committee Interlocks and Insider Participation.”

#### **Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.**

The information required by Item 12 is hereby incorporated by reference from our 2015 Proxy Statement under the caption “Security Ownership of Certain Beneficial Owners and Management.”

#### **Item 13. Certain Relationships and Related Transactions, and Director Independence.**

The information required by Item 13 is hereby incorporated by reference from our 2015 Proxy Statement under the captions “Transactions with Related Persons” and “Information Regarding the Board of Directors and Corporate Governance.”

#### **Item 14. Principal Accountant Fees and Services.**

The information required by Item 14 is hereby incorporated by reference from our 2015 Proxy Statement under the sub-captions “Independent Registered Public Accounting Firm Fees” and “Pre-Approval Policy and Procedures” under the caption “Ratification of Selection of Independent Registered Public Accounting Firm.”

**Item 15. Exhibits and Financial Statement Schedules**

**a. DOCUMENTS FILED AS PART OF THIS REPORT**

1. The following financial statements are filed herewith:

Report of Management on Internal Controls over Financial Reporting  
Report of Independent Registered Public Accounting Firm  
Consolidated Balance Sheets as of December 31, 2014 and 2013  
Consolidated Statements of Operations for the years ended December 31, 2014, 2013 and 2012  
Consolidated Statements of Stockholders' Equity for the years ended December 31, 2014, 2013 and 2012  
Consolidated Statements of Cash Flows for the years ended December 31, 2014, 2013 and 2012  
Notes to Financial Statements

2. Financial statement schedules

Schedule III – Real Estate and Accumulated Depreciation is filed herewith.

All other schedules are omitted because they are not applicable, or because the required information is included in the financial statements or notes thereto.

3. Exhibits

The following exhibits are filed as part of this report or hereby incorporated by reference to exhibits previously filed with the Securities and Exchange Commission:

## Exhibit Index

Exhibit Number	Exhibit Description
3.1	Articles of Restatement, incorporated by reference to Exhibit 3.1 to the Registrant's Quarterly Report on Form 10-Q (File No. 001-33097), filed April 30, 2012.
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.
3.3	First Amendment to Bylaws of the Registrant, incorporated by reference to Exhibit 99.1 of the Registrant's Current Report on Form 8-K (File No. 001-33097), filed July 10, 2007.
4.1	Form of Certificate for Common Stock of the Registrant, incorporated by reference to Exhibit 4.1 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 7.125% Series C Cumulative Term Preferred Stock of the Registrant, incorporated by reference to Exhibit 4.4 to the Registrant's Current Report on Form 8-A12B (File No. 001-33097), filed January 31, 2012.
10.1	First Amended and Restated Agreement of Limited Partnership of Gladstone Commercial Limited Partnership, incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K (File No. 000-50363), filed February 1, 2006.
10.2	Gladstone Commercial Limited Partnership Schedule 4.2(a)(2) to First Amended and Restated Agreement of Limited Partnership Designation of 7.50% Series B Cumulative Redeemable Preferred Units, incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed October 25, 2006.
10.3	Amended and Restated Investment Advisory Agreement between the Registrant and Gladstone Management Corporation, dated January 1, 2007, incorporated by reference to Exhibit 99.1 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed January 3, 2007.
10.4	Administration Agreement between the Registrant and Gladstone Administration, LLC, dated January 1, 2007, incorporated by reference to Exhibit 99.2 of the Registrant's Current Report on Form 8-K (File No. 001-33097), filed January 3, 2007.
10.5	Amendment to First Amended and Restated Agreement of Limited Partnership of Gladstone Commercial Limited Partnership, incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed April 29, 2010.
10.6	Gladstone Commercial Limited Partnership Schedule 4.2(a)(3) to First Amended and Restated Agreement of Limited Partnership Designation of Senior Common Units, incorporated by reference to Exhibit 10.2 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed April 29, 2010.
10.7	Second Amendment to First Amended and Restated Agreement of Limited Partnership of Gladstone Commercial Limited Partnership, incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed February 3, 2012.
10.8	Gladstone Commercial Limited Partnership Schedule 4.2(a)(4) to First Amended and Restated Agreement of Limited Partnership Designation of 7.125% Series C Cumulative Term Preferred



- Units, incorporated by reference to Exhibit 10.2 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed February 3, 2012.
- 10.9 Agreement of Purchase and Sale and Joint Escrow Instructions, by and between Gladstone Commercial Limited Partnership and Karlin Parmer Office, LLC, dated May 20, 2013, incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed June 14, 2013.
- 10.10 Loan Agreement between NH10 CUMMING GA LLC, D08 MARIETTA OH LLC, MPI06 MASON OH LLC, SRFF08 READING PA, L.P., RPT08 PINEVILLE NC, L.P., IPA12 ASHBURN VA SPE LLC, and FTCHI07 GRAND RAPIDS MI LLC and KeyBank National Association, incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed October 3, 2012.
- 10.11 Promissory Note in favor of KeyBank National Association, dated as of October 1, 2012 (File No. 001-33097), incorporated by reference to Exhibit 10.2 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed October 3, 2012.
- 10.12 Guaranty Agreement, dated as of October 1, 2012 between the Registrant and KeyBank National Association, incorporated by reference to Exhibit 10.3 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed October 3, 2012.
- 10.13 Credit Agreement, dated as of August 7, 2013, by and among Gladstone Commercial Limited Partnership, the Registrant, each of the financial institutions initially a signatory thereto together with their successors and assignees and KeyBank National Association, incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed August 9, 2013.
- 10.14 Unconditional Guaranty of Payment and Performance, dated as of August 7, 2013, by the Registrant, AL13 Brookwood LLC, CMS06-3 LLC, EI07 Tewksbury MA LLC, NJT06 Sterling Heights MI LLC, RB08 Concord OH LLC, DBPI07 Bolingbrook IL LLC, RCOG07 Georgia LLC, APLM07 Hialeah FL LLC for the benefit of KeyBank National Association, incorporated by reference to Exhibit 10.2 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed August 9, 2013.
- 10.15 First Amendment to Credit Agreement, dated as of March 28, 2014, by and among Gladstone Commercial Limited Partnership, the Registrant and certain of its wholly owned subsidiaries, each of the financial institutions initially a signatory thereto together with their successors and assignees and KeyBank National Association, incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed March 31, 2014.
- 10.16 Controlled Equity Offering Sales Agreement, dated September 2, 2014, by and among the Registrant, Gladstone Commercial Limited Partnership, and Cantor Fitzgerald & Co., incorporated by reference to Exhibit 1.1 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed September 2, 2014.
- 10.17 Second Amendment to Credit Agreement and Unconditional Guaranty of Payment and Performance, dated as of November 20, 2014, by and among Gladstone Commercial Limited Partnership, the Registrant and certain of its wholly owned subsidiaries, each of the financial institutions initially a signatory thereto together with their successors and assignees, and KeyBank National Association, incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K (File No. 001-33097), filed November 21, 2014.
- 11 Computation of Per Share Earnings from Operations (included in the notes to the audited financial statements contained in this Report).

12	Statements re: computation of ratios (filed herewith).
21	List of Subsidiaries of the Registrant (filed herewith).
23	Consent of PricewaterhouseCoopers LLP (filed herewith).
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
32.1	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).
32.2	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).
101.INS***	XBRL Instance Document
101.SCH***	XBRL Taxonomy Extension Schema Document
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

\*\*\* Attached as Exhibit 101 to this Annual Report on Form 10-K are the following materials, formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Balance Sheets as of December 31, 2014 and 2013, (ii) the Consolidated Statements of Operations for the years ended December 31, 2014, 2013 and 2012, (iii) the Consolidated Statements of Stockholders' Equity for the years ended December 31, 2014, 2013 and 2012, (iv) the Consolidated Statements of Cash Flows for the years ended December 31, 2014, 2013 and 2012 and (v) the Notes to Consolidated Financial Statements.

## SIGNATURES

Pursuant to the requirements of Sections 13 or 15(d) 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: February 18, 2015

By: /s/ Danielle Jones

Danielle Jones  
Chief Financial Officer

Date: February 18, 2015

By: /s/ David Gladstone

David Gladstone  
Chief Executive Officer and  
Chairman of the Board of Directors

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Date: February 18, 2015

By: /s/ David Gladstone

David Gladstone  
Chief Executive Officer and Chairman of the  
Board of Directors (principal executive officer)

Date: February 18, 2015

By: /s/ Terry Lee Brubaker

Terry Lee Brubaker  
Vice Chairman, Chief Operating Officer and  
Director

Date: February 18, 2015

By: /s/ Danielle Jones

Danielle Jones  
Chief Financial Officer  
(principal financial and accounting officer)

Date: February 18, 2015

By: /s/ David A.R. Dullum

David A.R. Dullum  
Director

Date: February 18, 2015

By: /s/ Anthony W. Parker

Anthony W. Parker  
Director

Date: February 18, 2015

By: /s/ Michela A. English

Michela A. English  
Director

Date: February 18, 2015

By: /s/ Paul Adelgren

Paul Adelgren  
Director

Date: February 18, 2015

By: /s/ John Outland

John Outland

Director

Date: February 18, 2015

By: /s/ Walter H. Wilkinson

Walter H. Wilkinson

Director

Date: February 18, 2015

By: /s/ Caren D. Merrick

Caren D. Merrick

Director

## Statements re: computation of ratios

(Dollars in Thousands, Except Ratios)

	For the year ended December 31,				
	2014	2013	2012	2011	2010
Net (loss) income from continuing operations <sup>(1)</sup>	\$ (5,902)	\$ 1,527	\$ 3,761	\$ 5,714	\$ 4,928
Add: fixed charges and preferred and senior common distributions	33,592	31,506	26,962	21,247	21,191
Less: preferred and senior common distributions	<u>(4,636)</u>	<u>(4,394)</u>	<u>(4,206)</u>	<u>(4,156)</u>	<u>(4,114)</u>
Earnings	\$ 23,054	\$ 28,639	\$ 26,517	\$ 22,805	\$ 22,005
Fixed charges and preferred and senior common distributions:					
Interest expense <sup>(2)</sup>	27,284	25,314	21,239	16,158	16,031
Amortization of deferred financing fees	1,656	1,780	1,502	918	1,031
Estimated interest component of rent	16	18	15	15	15
Preferred and senior common distributions	<u>4,636</u>	<u>4,394</u>	<u>4,206</u>	<u>4,156</u>	<u>4,114</u>
Total fixed charges and preferred and senior common distributions	\$ 33,592	\$ 31,506	\$ 26,962	\$ 21,247	\$ 21,191
Ratio of earnings to combined fixed charges and preferred distributions	N/A <sup>(3)</sup>	N/A <sup>(4)</sup>	N/A <sup>(5)</sup>	1.1	1.0

<sup>(1)</sup> We recognized a \$14.2 million impairment loss and a \$5.3 million gain on debt extinguishment as a result of our Roseville, MN deed in lieu transaction during the year ended December 31, 2014.

<sup>(2)</sup> Interest expense includes dividends paid on our mandatorily redeemable term preferred stock.

<sup>(3)</sup> For the year ended December 31, 2014, earnings, as defined, were insufficient to cover fixed charges and preferred and common distributions by \$10,538.

<sup>(4)</sup> For the year ended December 31, 2013, earnings, as defined, were insufficient to cover fixed charges and preferred and common distributions by \$2,867.

<sup>(5)</sup> For the year ended December 31, 2012, earnings, as defined, were insufficient to cover fixed charges and preferred and common distributions by \$445.

N/A: Not Applicable

The calculation of the ratio of earnings to combined fixed charges and preferred distributions is above. "Earnings" consist of net income from continuing operations before fixed charges. "Fixed charges" consist of interest expense, amortization of deferred financing fees and the portion of operating lease expense that represents interest. The portion of operating lease expense that represents interest is calculated by dividing the amount of rent expense, allocated to us by our Adviser as part of the administration fee payable under the Advisory Agreement, by three.

SUBSIDIARIES OF GLADSTONE COMMERCIAL CORPORATION

**Delaware**

2525 N Woodlawn Vstrm Wichita KS, LLC  
 260 Springside Drive, Akron OH LLC  
 ABC12 Ottumwa IA LLC  
 ACI06 Champaign IL LLC  
 AC07 Lawrenceville GA LLC  
 AFL05 Duncan SC LLC  
 AFL05 Duncan SC Member LLC  
 AFR11 Parsippany NJ LLC  
 AL13 Brookwood LLC  
 APM107 Hialeah FL LLC  
 AZ14 Phoenix LLC  
 CA14 Rancho Cordova GP LLC  
 CA14 Rancho Cordova LP  
 CBP11 Green Tree PA GP LLC  
 CBP11 Green Tree PA, L.P.  
 C08 Fridley MN LLC  
 CDLCI07 Mason OH LLC  
 CI05 Clintonville WI LLC  
 CMI04 Canton NC LLC  
 CMS06-3 LLC  
 CO13 Englewood LLC  
 CO14 Aurora LLC  
 CO14 Denver LLC  
 COCO04 Austin TX, L.P.  
 COCO04 Austin TX GP LLC  
 Corning Big Flats LLC  
 CVG12 New Albany OH LLC  
 D08 Marietta OH LLC  
 DBP107 Bolingbrook IL LLC  
 EE 208 South Rogers Lane, Raleigh NC LLC  
 EE07 Raleigh NC, L.P.  
 EE07 Raleigh NC GP LLC  
 EI07 Tewksbury MA LLC  
 ELF08 Florida LLC  
 First Park Ten COCO San Antonio, L.P.  
 First Park Ten COCO San Antonio GP LLC  
 FL13 Orlando LLC  
 FMCT08 Chalfont PA GP LLC  
 FMCT08 Chalfont PA LP  
 FS11 Hickory NC GP LLC  
 FS11 Hickory NC, LP  
 FTCH107 Grand Rapids MI LLC  
 GBI07 Syracuse NY LLC  
 GCC1302 Egg Harbor NJ LLC  
 GCC Acquisition Holdings, LLC  
 GCC Dorval LLC  
 GCC Granby LLC  
 GCO12 Jupiter FL LLC  
 Gladstone Commercial Advisers, Inc.  
 Gladstone Commercial Corporation  
 Gladstone Commercial Limited Partnership  
 Gladstone Commercial Partners LLC

Gladstone Commercial Lending LLC  
GSM, LLC  
HMBF05 Newburyport MA LLC  
IN14 Indianapolis LLC  
IPA12 Ashburn VA LLC  
IPA12 Ashburn VA SPE LLC  
LittleArch04 Charlotte NC Member LLC  
Little Arch Charlotte NC LLC  
MI13 Novi LLC  
MI14 Monroefrenchtown LLC  
MI14 Revard LLC  
MN13 Blaine, LLC  
MPI06 Mason OH LLC  
MSI05-3 LLC  
NARA12 Fort Worth TX, L.P.  
NARA12 Fort Worth TX GP LLC  
NCH12 Columbus OH LLC  
NH10 Cumming GA LLC  
NJT06 Sterling Heights MI LLC  
NV14 Las Vegas LLC  
NW05 Richmond VA LLC  
OB Crenshaw GCC, L.P.  
OB Crenshaw SPE GP LLC  
OB Midway NC Gladstone Commercial LLC  
OH14 Columbus LLC  
OS08 Winchester VA LLC  
PA14 Taylor LLC  
PNA11 Boston Heights OH LLC  
Pocono PA GCC GP LLC  
Pocono PA GCC, L.P.  
PZ05 Maple Heights OH LLC  
RB08 Concord OH LLC  
RC06 Menomonee Falls WI LLC  
RCOG07 Georgia LLC  
RPT08 Pineville NC GP LLC  
RPT08 Pineville NC LP  
SCC10 Orange City IA LLC  
SJM06 Baytown TX GP LLC  
SJM06 Baytown TX L.P.  
SLEE Grand Prairie, L.P.  
SRFF08 Reading PA GP LLC  
SRFF08 Reading PA LP  
STI05 Franklin NJ LLC  
SVMMC05 Toledo OH LLC  
TCI06 Burnsville MN LLC  
TMC11 Springfield MO LLC  
TUP12 Columbus GA LLC  
TX13 Allen LLC  
TX13 Austin LLC  
TX14 Allen II LLC  
TX14 Colleyville LLC  
TX14 Coppell LLC  
VW12 Columbia SC LLC  
WC11 Springfield MO LLC  
WEC11 Dartmouth MA LLC  
WMI05 Columbus OH LLC  
WMI05 Hazelwood MO LLC  
WPI07 Tulsa OK LLC  
YCC06 South Hadley MA LLC  
YorkTC05 Eatontown NJ LLC

**Ohio**

Hemingway at Boston Heights, LLC

**Massachusetts**

GCLP Business Trust I

GCLP Business Trust II

**Nova Scotia**

3094174 Nova Scotia Company

3094175 Nova Scotia Company



CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We hereby consent to the incorporation by reference in the Registration Statement on Form S-3 (No. 333-190931) of Gladstone Commercial Corporation of our report dated February 18, 2015 relating to the financial statements, financial statement schedules and the effectiveness of internal control over financial reporting, which appears in this Form 10-K.

/s/ PricewaterhouseCoopers LLP  
McLean, VA  
February 18, 2015

**CERTIFICATION**  
**Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, David Gladstone, certify that:

1. I have reviewed this annual report on Form 10-K of Gladstone Commercial Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 18, 2015

/s/ David Gladstone

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David Gladstone  
Chief Executive Officer and  
Chairman of the Board of Directors

**CERTIFICATION**  
**Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Danielle Jones, certify that:

1. I have reviewed this annual report on Form 10-K of Gladstone Commercial Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 18, 2015

/s/ Danielle Jones

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Danielle Jones  
Chief Financial Officer

**Exhibit 32.1**

**CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER PURSUANT TO SECTION 906 OF THE  
SARBANES-OXLEY ACT OF 2002**

The undersigned, the Chief Executive Officer of Gladstone Commercial Corporation (the “Company”), hereby certifies on the date hereof, pursuant to 18 U.S.C. §1350(a), as adopted pursuant to Section 906 of The Sarbanes-Oxley Act of 2002, that the Annual Report on Form 10-K for the year ended December 31, 2014 (“Form 10-K”), filed concurrently herewith by the Company, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that the information contained in the Form 10-K fairly presents, in all material respects, the financial condition and results of operations of the Company.

A signed original of this written statement as required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

Dated: February 18, 2015

/s/ David Gladstone  
David Gladstone  
Chief Executive Officer

**CERTIFICATION OF THE CHIEF FINANCIAL OFFICER PURSUANT TO SECTION 906 OF THE  
SARBANES-OXLEY ACT OF 2002**

The undersigned, the Chief Financial Officer of Gladstone Commercial Corporation (the “Company”), hereby certifies on the date hereof, pursuant to 18 U.S.C. §1350(a), as adopted pursuant to Section 906 of The Sarbanes-Oxley Act of 2002, that the Annual Report on Form 10-K for the year ended December 31, 2014 (“Form 10-K”), filed concurrently herewith by the Company, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that the information contained in the Form 10-K fairly presents, in all material respects, the financial condition and results of operations of the Company.

A signed original of this written statement as required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

Dated: February 18, 2015

/s/ Danielle Jones

\_\_\_\_\_  
Danielle Jones  
Chief Financial Officer

## Corporate Information

### Board of Directors and Executive Officers

**David Gladstone**

*Chairman of the Board and Chief Executive Officer*

**Terry Lee Brubaker**

*Vice Chairman of the Board and Chief Operating Officer*

**Bob Cutlip**

*President*

**Danielle Jones**

*Chief Financial Officer and Assistant Treasurer*

**Jay Beckhorn**

*Treasurer*

**Paul Adelgren**

*Director and Pastor of Missionary Alliance Church*

**David A.R. Dullum**

*Director and President of Gladstone Investment Corporation*

**Michela A. English**

*Director, President and Chief Executive Officer of Fight for Children*

**Caren Merrick**

*Director, Founder & CEO of Pocket Mentor*

**John H. Outland**

*Director and Private Investor*

**Anthony W. Parker**

*Director, Founder and Chairman of Parker Tide Corp.*

**Walter H. Wilkinson, Jr.**

*Director, Chairman and CEO of Kitty Hawk Capital, Inc.*

### Other Officers

**Arthur S. "Buzz" Cooper**

*Senior Managing Director*

**Jack Dellafiora**

*Chief Compliance Officer*

**Michael LiCalsi**

*General Counsel and Secretary*

**Matt Tucker**

*Managing Director*

**Andrew White**

*Managing Director*

### Stock Exchange Listing

Our common stock trades on the NASDAQ Global Market under the symbol GOOD. Our preferred stocks trade on the NASDAQ Global Select Market under the symbols GOODN, GOODO and GOODP.

### Transfer Agent

Computershare, Inc.  
P.O. Box 43006  
Providence, RI 02940

### Stockholder Inquiries

Website:  
[www.computershare.com/investor](http://www.computershare.com/investor)  
Toll Free Dedicated Number:  
1-866-214-7543  
Foreign Stockholders:  
1-201-680-6578  
TDD Hearing Impaired:  
1-800-231-5469  
TDD Foreign Stockholders:  
1-201-680-6610

### Financial Information

Stockholders may receive a copy of our Annual Report on Form 10-K and Quarterly Reports on Form 10-Q by contacting us or going to our website at [www.gladstonecommercial.com](http://www.gladstonecommercial.com), the SEC's website at [www.SEC.gov](http://www.SEC.gov) or by visiting the SEC at 100 F Street NE, Washington, DC 20549.

### Independent Registered Public Accounting Firm

PricewaterhouseCoopers LLP

### Legal Counsel

Bass, Berry & Sims PLC  
Dickstein Shapiro LLP

### Company Website

[www.gladstonecommercial.com](http://www.gladstonecommercial.com)

*This 2014 Annual Report contains forward-looking statements. Such forward-looking statements can generally be identified by our use of forward-looking terminology such as "may," "will," "expect," "intend," "anticipate," "estimate," "believe," "continue," or other similar words. Readers of this 2014 Annual Report should be aware that there are various factors that could cause actual results to differ materially from any forward-looking statements made in this report. Factors that could cause or contribute to such differences include, but are not limited to, changes in general economic and business conditions, industry trends, changes in government rules and regulations (including changes in tax laws) and environmental rules and regulations. Accordingly, readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this 2014 Annual Report.*



### Jacoby

*Office mascot and official greeter at the McLean, VA headquarters.*

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