

GLADSTONE COMMERCIAL CORP

Form 10-Q

July 25, 2016

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2016

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 02-0681276
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

1521 WESTBRANCH DRIVE, SUITE 100 22102
MCLEAN, VIRGINIA
(Address of principal executive offices) (Zip Code)

(703) 287-5800
(Registrant's telephone number, including area code)

Not Applicable
(Former name, former address and formal fiscal year, if changed since last report)

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 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 (Do not check if a smaller reporting company) Smaller reporting company

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

The number of shares of the registrant's Common Stock, \$0.001 par value, outstanding as of July 25, 2016 was 22,583,722.

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June 30, 2016
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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

Gladstone Commercial Corporation

Condensed Consolidated Balance Sheets

(Dollars in Thousands, Except Share and Per Share Data)

(Unaudited)

	June 30, 2016	December 31, 2015
ASSETS		
Real estate, at cost	\$790,232	\$780,377
Less: accumulated depreciation	122,827	112,243
Total real estate, net	667,405	668,134
Lease intangibles, net	101,683	104,914
Real estate and related assets held for sale, net	3,820	1,077
Mortgage note receivable	—	5,900
Cash and cash equivalents	3,993	5,152
Restricted cash	3,902	4,205
Funds held in escrow	5,922	7,534
Deferred rent receivable, net	28,909	27,443
Other assets	2,651	2,825
TOTAL ASSETS	\$818,285	\$827,184
LIABILITIES, MEZZANINE EQUITY AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Mortgage notes payable, net	\$441,604	\$455,863
Borrowings under line of credit, net	60,229	44,591
Borrowings under term loan facility, net	24,887	24,878
Series C mandatorily redeemable preferred stock, net, par value \$0.001 per share; \$25 per share liquidation preference; 1,700,000 shares authorized; and 540,000 and 1,540,000 shares issued and outstanding at June 30, 2016 and December 31, 2015, respectively	13,424	38,100
Deferred rent liability, net	8,964	9,657
Asset retirement obligation	3,645	3,674
Accounts payable and accrued expenses	3,681	6,388
Liabilities related to assets held for sale	357	868
Due to Adviser and Administrator (1)	1,884	1,858
Other liabilities	7,523	7,436
TOTAL LIABILITIES	\$566,198	\$593,313
Commitments and contingencies (2)		
MEZZANINE EQUITY		
Series D redeemable preferred stock, net, par value \$0.001 per share; \$25 per share liquidation preference; 6,000,000 shares authorized; and 1,063,705 shares issued and outstanding at June 30, 2016 (3)	\$25,532	\$—
TOTAL MEZZANINE EQUITY	\$25,532	\$—
STOCKHOLDERS' EQUITY		
Series A and B redeemable preferred stock, par value \$0.001 per share; \$25 per share liquidation preference; 5,350,000 and 2,300,000 shares authorized and 2,264,000 and 2,150,000 shares issued and outstanding at June 30, 2016 and December 31, 2015, respectively	\$2	\$2
Senior common stock, par value \$0.001 per share; 4,450,000 and 7,500,000 shares authorized and 959,552 and 972,214 shares issued and outstanding at June 30, 2016 and December 31, 2015, respectively	1	1

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Common stock, par value \$0.001 per share, 32,500,000 and 38,500,000 shares authorized and 22,983,604 and 22,485,607 shares issued and outstanding at June 30, 2016 and December 31, 2015, respectively	23	22
Additional paid in capital	429,608	418,897
Distributions in excess of accumulated earnings	(203,079)	(185,051)
TOTAL STOCKHOLDERS' EQUITY	226,555	233,871
TOTAL LIABILITIES, MEZZANINE EQUITY AND STOCKHOLDERS' EQUITY	\$818,285	\$827,184

(1) Refer to Note 2 "Related-Party Transactions"

(2) Refer to Note 9 "Commitments and Contingencies"

(3) Refer to Note 10 "Stockholders' Equity and Mezzanine Equity"

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

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

	For the three months ended June 30,		For the six months ended June 30,	
	2016	2015	2016	2015
Operating revenues				
Rental revenue	\$20,890	\$20,012	\$41,547	\$39,300
Tenant recovery revenue	357	394	842	718
Interest income from mortgage note receivable	—	282	385	549
Total operating revenues	21,247	20,688	42,774	40,567
Operating expenses				
Depreciation and amortization	9,205	8,947	18,338	17,154
Property operating expenses	1,434	1,178	3,045	2,139
Acquisition related expenses	117	255	126	451
Base management fee (1)	856	866	1,717	1,717
Incentive fee (1)	655	1,760	1,273	3,433
Administration fee (1)	370	366	775	728
General and administrative	609	539	1,184	1,229
Impairment charge	187	—	230	—
Total operating expenses before credit to incentive fee	13,433	13,911	26,688	26,851
Credit to incentive fee (1)	—	(1,316)	—	(2,500)
Total operating expenses	13,433	12,595	26,688	24,351
Other (expense) income				
Interest expense	(6,579)	(6,999)	(13,310)	(13,770)
Distributions attributable to Series C mandatorily redeemable preferred stock	(686)	(686)	(1,372)	(1,372)
Other income	334	23	334	51
Total other expense	(6,931)	(7,662)	(14,348)	(15,091)
Net income	883	431	1,738	1,125
Distributions attributable to Series A, B and D preferred stock	(1,263)	(1,023)	(2,290)	(2,047)
Distributions attributable to senior common stock	(251)	(261)	(504)	(485)
Net loss attributable to common stockholders	\$(631)	\$(853)	\$(1,056)	\$(1,407)
Loss per weighted average share of common stock - basic & diluted				
Loss attributable to common shareholders	\$(0.03)	\$(0.04)	\$(0.05)	\$(0.07)
Weighted average shares of common stock outstanding				
Basic	22,684,392	20,833,787	22,614,832	20,524,101
Diluted	22,684,392	20,833,787	22,614,832	20,524,101
Earnings per weighted average share of senior common stock	\$0.26	\$0.26	\$0.52	\$0.52
Weighted average shares of senior common stock outstanding - basic	959,552	995,852	961,794	928,323

(1) Refer to Note 2 “Related-Party Transactions”

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

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

	For the six months ended June 30,	
	2016	2015
Cash flows from operating activities:		
Net income	\$1,738	\$1,125
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	18,338	17,154
Impairment charge	230	—
Amortization of deferred financing costs	1,090	878
Amortization of deferred rent asset and liability, net	(215)	(270)
Amortization of discount and premium on assumed debt	(116)	(154)
Asset retirement obligation expense	73	76
Decrease (increase) in other assets	196	(538)
Increase in deferred rent receivable	(1,959)	(1,843)
(Decrease) increase in accounts payable, accrued expenses, and amount due Adviser and Administrator	(655)	1,021
Decrease in other liabilities	(402)	(683)
Leasing commissions paid	(486)	(291)
Net cash provided by operating activities	17,832	16,475
Cash flows from investing activities:		
Acquisition of real estate and related intangible assets	(17,000)	(58,248)
Improvements of existing real estate	(2,654)	(3,072)
Proceeds from sale of real estate	200	—
Issuance of mortgage note receivable	—	(300)
Collection of mortgage note receivable	5,900	—
Receipts from lenders for funds held in escrow	2,719	642
Payments to lenders for funds held in escrow		