

Edgar Filing: SPIRIT REALTY CAPITAL, INC. - Form 10-K

SPIRIT REALTY CAPITAL, INC.

Form 10-K

February 21, 2019

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2018

Commission File Number 001-36004

SPIRIT REALTY CAPITAL, INC.

SPIRIT REALTY, L.P.

(Exact name of registrant as specified in its charter)

Spirit Realty Capital, Inc.	Maryland	20-1676382
Spirit Realty, L.P.	Delaware	20-1127940
	(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
	2727 North Harwood Street, Suite 300, Dallas, Texas 75201	(972) 476-1900
	(Address of principal executive offices; zip code)	(Registrant's telephone number, including area code)

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

	Title of each class:	Name of exchange on which registered:
Spirit Realty Capital, Inc.	Common Stock, \$0.05 par value per share	New York Stock Exchange
	6.000% Series A Cumulative Redeemable Preferred Stock, \$0.01 par value per share	New York Stock Exchange
Spirit Realty, L.P.	None	None

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

Spirit Realty Capital, Inc. None

Spirit Realty, L.P. None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Spirit Realty Capital, Inc. Yes ☒ No ☐ Spirit Realty, L.P. 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.

Spirit Realty Capital, Inc. Yes ☐ No ☒ Spirit Realty, L.P. 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 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.

Spirit Realty Capital, Inc. Yes ☒ No ☐ Spirit Realty, L.P. Yes ☐ No ☒

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for

Edgar Filing: SPIRIT REALTY CAPITAL, INC. - Form 10-K

such shorter period that the registrant was required to submit such files).

Spirit Realty Capital, Inc. Yes ☒ No ☐ Spirit Realty, L.P. Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒  
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Spirit Realty Capital, Inc.

Large accelerated filer ☒ Accelerated filer ☐ Non-accelerated filer ☐ Smaller reporting company ☐  
Emerging growth company ☐

Spirit Realty, L.P.

Large accelerated filer ☐ Accelerated filer ☒ Non-accelerated filer ☐ Smaller reporting company ☐  
Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Spirit Realty Capital, Inc. ☐ Spirit Realty, L.P. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Spirit Realty Capital, Inc. Yes ☐ No ☒ Spirit Realty, L.P. Yes ☐ No ☒

As of June 29, 2018 (the last business day of the registrant's most recently completed second fiscal quarter), the aggregate market value of Spirit Realty Capital, Inc.'s shares of common stock, \$0.05 par value, held by non-affiliates of the Registrant, was \$3.4 billion based on the last reported sale price of \$40.15 per share on the New York Stock Exchange on June 29, 2018.

There is no public trading market for the common units of limited partnership interest of Spirit Realty, L.P. As a result, the aggregate market value of the common units of limited partnership interest held by non-affiliates of Spirit Realty, L.P. cannot be determined.

The number of outstanding shares of Spirit Realty Capital, Inc.'s common stock, \$0.05 par value, as of February 19, 2019, was 85,918,339 shares.

#### Documents Incorporated by Reference

Certain specific portions of the definitive Proxy Statement for Spirit Realty Capital, Inc.'s 2019 Annual Meeting of Stockholders to be filed pursuant to Regulation 14A are incorporated by reference into Part III, Items 10, 11, 12, 13 and 14 of this Annual Report on Form 10-K. Only those portions of the Proxy Statement which are specifically incorporated by reference herein shall constitute a part of this Annual Report on Form 10-K.

## EXPLANATORY NOTE

This report combines the annual reports on Form 10-K for the year ended December 31, 2018 of Spirit Realty Capital, Inc., a Maryland corporation, and Spirit Realty, L.P., a Delaware limited partnership. Unless otherwise indicated or unless the context requires otherwise, all references in this report to “we,” “us,” “our,” or the “Company” refer to Spirit Realty Capital, Inc. together with its consolidated subsidiaries, including Spirit Realty, L.P. Unless otherwise indicated or unless the context requires otherwise, all references to the “Operating Partnership” refer to Spirit Realty, L.P. together with its consolidated subsidiaries.

Spirit General OP Holdings, LLC (“OP Holdings”) is the sole general partner of the Operating Partnership. The Company is a real estate investment trust (“REIT”) and the sole member of OP Holdings, as well as the special limited partner of the Operating Partnership. As sole member of the general partner of our Operating Partnership, our Company has the full, exclusive and complete responsibility for our Operating Partnership’s day-to-day management and control.

We believe combining the annual reports on Form 10-K of our Company and Operating Partnership into a single report results in the following benefits:

- enhancing investors’ understanding of our Company and Operating Partnership by enabling investors to view the business as a whole, reflective of how management views and operates the business;
- eliminating duplicative disclosure and providing a streamlined presentation as a substantial portion of the disclosures apply to both our Company and Operating Partnership; and
- creating time and cost efficiencies by preparing one combined report in lieu of two separate reports.

There are a few differences between our Company and Operating Partnership, which are reflected in the disclosures in this report. We believe it is important to understand these differences in the context of how we operate as an interrelated, consolidated company. Our Company is a REIT, the only material assets of which are the partnership interests in our Operating Partnership. As a result, our Company does not conduct business itself, other than acting as the sole member of the general partner of our Operating Partnership, issuing equity from time to time and guaranteeing certain debt of our Operating Partnership. Our Operating Partnership holds substantially all the assets of our Company. Our Company issued convertible notes and guarantees some of the debt of our Operating Partnership, see Note 4 to the consolidated financial statements herein for further discussion. Our Operating Partnership conducts the operations of the business and is structured as a partnership with no publicly traded equity. Except for net proceeds from issuance of convertible notes and equity issuances by our Company, which are generally contributed to our Operating Partnership in exchange for partnership units of our Operating Partnership, our Operating Partnership generates the capital required by our Company’s business through our Operating Partnership’s operations or our Operating Partnership’s incurrence of indebtedness.

The presentation of stockholders’ equity and partners’ capital are the main areas of difference between the consolidated financial statements of our Company and those of our Operating Partnership. The partnership units in our Operating Partnership are accounted for as partners’ capital in our Operating Partnership’s consolidated financial statements.

There are no non-controlling interests in the Company or the Operating Partnership.

To help investors understand the significant differences between our Company and our Operating Partnership, this report presents the consolidated financial statements separately for our Company and our Operating Partnership. All other sections of this report, including “Selected Financial Data,” “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and “Quantitative and Qualitative Disclosures About Market Risk,” are presented together for our Company and our Operating Partnership.

In order to establish that the Chief Executive Officer and the Chief Financial Officer of each entity have made the requisite certifications and that our Company and Operating Partnership are compliant with Rule 13a-15 or Rule 15d-15 of the Securities Exchange Act of 1934, or the Exchange Act, and 18 U.S.C. §1350, this report also includes separate “Item 9A. Controls and Procedures” sections and separate Exhibit 31 and 32 certifications for each of our Company and our Operating Partnership.

## GLOSSARY

1031 Exchange	Tax-deferred like-kind exchange of properties held for business or investment purposes, pursuant to Section 1031 of the Code
2015 Credit Agreement	Revolving credit facility agreement between the Operating Partnership and certain lenders dated March 31, 2015, as amended or otherwise modified from time to time
2015 Credit Facility	\$800.0 million unsecured credit facility pursuant to the 2015 Credit Agreement
2015 Term Loan	\$420.0 million senior unsecured term facility pursuant to the 2015 Term Loan Agreement
2015 Term Loan Agreement	Term loan agreement between the Operating Partnership and certain lenders dated November 3, 2015, as amended or otherwise modified from time to time
2017 Tax Legislation	Tax Cuts and Jobs Act
2019 Credit Facility	\$800.0 million unsecured revolving credit facility pursuant to the 2019 Revolving Credit and Term Loan Agreement
2019 Facilities Agreements	2019 Revolving Credit and Term Loan Agreement and A-2 Term Loan
2019 Notes	\$402.5 million convertible notes of the Corporation due in 2019
2019 Revolving Credit and Term Loan Agreement	Revolving credit and term loan agreement between the Operating Partnership and certain lenders dated January 14, 2019, as amended or otherwise modified from time to time
2021 Notes	\$345.0 million convertible notes of the Corporation due in 2021
401(k) Plan	Defined contribution retirement savings plan qualified under Section 401(k) of the Code
A-1 Term Loan	\$420.0 million unsecured term loan facility pursuant to the 2019 Revolving Credit and Term Loan Agreement
A-2 Term Loan	\$400.0 million unsecured term loan facility pursuant to a term loan agreement between the Operating Partnership and certain lenders dated January 14, 2019, as amended or otherwise modified from time to time
ABS	Asset Backed Securities
ACM	Asbestos-Containing Materials
ADA	Americans with Disabilities Act
Adjusted Debt	Adjusted Debt is a non-GAAP financial measure. See definition in Item 6. Selected Financial Data.
Adjusted EBITDA	Adjusted EBITDA are modified to include other adjustments that are not considered to be indicative of on-going operating performance. See definition in Item 6. Selected Financial Data.
AFFO	Adjusted Funds From Operations. See definition in Item 6. Selected Financial Data.
Amended Incentive Award Plan	Amended and Restated Spirit Realty Capital, Inc. and Spirit Realty, L.P. 2012 Incentive Award Plan
AOCL	Accumulated Other Comprehensive Loss
ASC	Accounting Standards Codification
Asset Management Agreement	Asset Management Agreement between Spirit Realty, L.P. and Spirit MTA REIT dated May 31, 2018
ASU	Accounting Standards Update
ATM Program	At the Market equity distribution program, pursuant to which the Corporation may offer and sell registered shares of common stock from time to time
CMBS	Commercial Mortgage Backed Securities
Code	Internal Revenue Code of 1986, as amended
Cole II	Cole Credit Property Trust II, Inc.
Company	The Corporation and its consolidated subsidiaries

Contractual Rent	Monthly contractual cash rent and earned income from direct financing leases, excluding percentage rents, from our properties owned fee-simple or ground leased, recognized during the final month of the reporting period, adjusted to exclude amounts received from properties sold during that period and adjusted to include a full month of contractual rent for properties acquired during that period. We use Contractual Rent when calculating certain metrics that are useful to evaluate portfolio credit, asset type, industry, and geographic diversity and to manage risk.
Convertible Notes	The 2019 Notes and 2021 Notes, together
Corporation	Spirit Realty Capital, Inc., a Maryland corporation
CPI	Consumer Price Index
EBITDA	Earnings Before Interest, Taxes, Depreciation and Amortization
EBITDAR	Earnings Before Interest, Taxes, Depreciation, Amortization and Rent
EBITDAre	EBITDAre is a non-GAAP financial measure and is computed in accordance with standards established by NAREIT. See definition in Item 6. Selected Financial Data.
EDF	Expected Default Frequency
Excess Cash	Rent received in excess of debt service obligations
Exchange Act	Securities Exchange Act of 1934, as amended
FASB	Financial Accounting Standards Board
FFO	Funds From Operations. See definition in Item 6. Selected Financial Data.
Fixed Charge Coverage Ratio	Ratio of Annualized Adjusted EBITDAre to Fixed Charges. See definition in Item 6. Selected Financial Data.
GAAP	Generally Accepted Accounting Principles in the United States
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standards
IPO	Initial Public Offering
IRS	Internal Revenue Service
LIBOR	London Interbank Offered Rate
Line of Credit	\$40.0 million secured revolving credit facility pursuant to the loan agreement between an indirect wholly-owned subsidiary of the Corporation and a certain lender dated March 27, 2013, as amended
Master Trust 2013	The asset-backed mortgage securitization trust established in December 2013
Master Trust 2014	The asset-backed securitization trust established in 2005, and amended and restated in 2014
Master Trust Exchange Costs	Legal, accounting and financial advisory services costs incurred in connection with the May 2014 exchange of the outstanding principal balance of three series of existing net-lease mortgage notes for three series of newly issued 2014 Notes
Master Trust Notes	Master Trust 2013 and Master Trust 2014, together
Master Trust Release	Proceeds from the sale of assets securing the Master Trust Notes held in restricted accounts until a qualifying substitution is made or until used for principal reduction
Merger	Acquisition on July 17, 2013 of Cole II by the Company, in which the Company merged with and into the Cole II legal entity
Merger Exchange Ratio	Merger exchange ratio of 1.9048
MGCL	Maryland General Corporation Law
Moody's	Moody's Investor Services
NAREIT	National Association of Real Estate Investment Trusts
NYSE	New York Stock Exchange

Edgar Filing: SPIRIT REALTY CAPITAL, INC. - Form 10-K

Occupancy	The number of economically yielding owned properties divided by total owned properties
OP Holdings	Spirit General OP Holdings, LLC
Operating Partnership	Spirit Realty, L.P., a Delaware limited partnership

---

Porter's Five Forces	An analytical framework used to examine the attractiveness of an industry and potential for disruption in that industry based on: threats of new entrants, threats of substitutes, the bargaining power of customers, the bargaining power of suppliers and industry rivalry
Property Management and Servicing Agreement	Second amended and restated agreement governing the management services and special services provided to Master Trust 2014 by Spirit Realty, L.P., dated as of May 20, 2014, as amended, supplemented, amended and restated or otherwise modified
Real Estate Investment Value	The gross acquisition cost, including capitalized transaction costs, plus improvements and less impairments, if any
REIT	Real Estate Investment Trust
S&P	Standard & Poor's Rating Services
SEC	Securities and Exchange Commission
Securities Act	Securities Act of 1933, as amended
Senior Unsecured Notes	\$300 million aggregate principal amount of senior notes issued in August 2016
Series A Preferred Stock	6,900,000 shares of 6.000% Cumulative Redeemable Preferred Stock issued October 3, 2017, with a liquidation preference of \$25.00 per share.
Shopko	Specialty Retail Shops Holding Corp. and certain of its affiliates
SMTA	Spirit MTA REIT, a Maryland real estate investment trust
Spin-Off	Creation of an independent, publicly traded REIT, SMTA, through our contribution of properties leased to Shopko, assets that collateralize Master Trust 2014 and other additional assets to SMTA followed by the distribution by us to our stockholders of all of the common shares of beneficial interest in SMTA.
SubREIT	Spirit MTA SubREIT, a wholly-owned subsidiary of SMTA
Spirit Heat Map	An analysis of industries across Porter's Five Forces and potential causes of technological disruption to identify tenant industries which Spirit believes to have good fundamentals for future performance
Spirit Property Ranking Model	A proprietary model used annually to rank properties across twelve factors and weightings consisting of both real estate quality scores and credit underwriting criteria, in order to benchmark property quality, identify asset recycling opportunities and to enhance acquisition or disposition decisions
Total Debt	Principal debt outstanding before discounts, premiums or deferred financing costs
TRS	Taxable REIT Subsidiary, a corporation, other than a REIT, in which a REIT directly or indirectly holds stock and that has made a joint election with such REIT to be treated as a taxable REIT subsidiary and meets certain other requirements
TSR	Total Shareholder Return
U.S.	United States of America
Vacant	Owned properties which are not economically yielding

Unless otherwise indicated or unless the context requires otherwise, all references to the "registrant," the "Company," "Spirit Realty Capital," "we," "us" or "our" refer to the Corporation and its consolidated subsidiaries, including the Operating Partnership. Unless otherwise indicated or unless the context requires otherwise, all references to the "Operating Partnership" refer to Spirit Realty, L.P. and its consolidated subsidiaries.

INDEX

PART I

Item 1.	Business	<u>6</u>
Item 1A.	Risk Factors	<u>12</u>
Item 1B.	Unresolved Staff Comments	<u>38</u>
Item 2.	Properties	<u>39</u>
Item 3.	Legal Proceedings	<u>42</u>
Item 4.	Mine Safety Disclosure	<u>42</u>

PART II

Item 5.	Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	<u>43</u>
Item 6.	Selected Financial Data	<u>45</u>
Item 7.	Management's Discussion and Analysis of Financial Condition and Results of Operations	<u>50</u>
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk	<u>69</u>
Item 8.	Financial Statements and Supplementary Data	<u>70</u>

PART III

Item 9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	<u>123</u>
Item 9A.	Controls and Procedures	<u>123</u>
Item 9B.	Other Information	<u>123</u>
Item 10.	Directors, Executive Officers and Corporate Governance	<u>124</u>
Item 11.	Executive Compensation	<u>124</u>
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	<u>124</u>
Item 13.	Certain Relationships and Related Transactions, and Director Independence	<u>124</u>
Item 14.	Principal Accountant Fees and Services	<u>124</u>

PART IV

Item 15.	Exhibits, Financial Statement Schedules	<u>125</u>
SIGNATURES		<u>185</u>



## PART I

The following discussion relates to our consolidated financial statements and should be read in conjunction with the consolidated financial statements and notes thereto appearing elsewhere in this Annual Report on Form 10-K. Statements contained in Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations" that are not historical facts may be forward-looking statements. Such statements are subject to certain risks and uncertainties, which could cause actual results to differ materially from those projected. Some of the information presented is forward-looking in nature, including information concerning projected future occupancy rates, rental rate increases, property development timing and investment amounts. Although the information is based on our current expectations, actual results could vary from expectations stated in this report. Numerous factors will affect our actual results, some of which are beyond our control. These include the breadth and duration of the current economic environment and its impact on our tenants, the strength of commercial and industrial real estate markets, market conditions affecting tenants, competitive market conditions, interest rate levels, volatility in our stock price and capital market conditions. You are cautioned not to place undue reliance on this information, which speaks only as of the date of this report. We assume no obligation to update publicly any forward-looking information, whether as a result of new information, future events, or otherwise, except to the extent we are required to do so in connection with our ongoing requirements under federal securities laws to disclose material information. For a discussion of important risks related to our business, and related to investing in our securities, including risks that could cause actual results and events to differ materially from results and events referred to in the forward-looking information, see Item 1A. "Risk Factors - Special Note Regarding Forward-Looking Statements." In light of these risks, uncertainties and assumptions, the forward-looking events discussed in this Annual Report on Form 10-K might not occur.

### Available Information

The Corporation's principal executive offices are located at 2727 North Harwood Street, Suite 300, Dallas, Texas 75201. Our telephone number at that location is 972-476-1900. We maintain a website at [www.spiritrealty.com](http://www.spiritrealty.com). On the Investor Relations page of our website, we post the following filings as soon as reasonably practicable after they are electronically filed with or furnished to the SEC: our Annual Report on Form 10-K, our Quarterly Reports on Form 10-Q, our Current Reports on Form 8-K, and the Section 16 filings of our directors and officers, as well as any amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act. All such filings on our Investor Relations page of our website are available to be viewed free of charge. Also available on our website, free of charge, are our corporate governance guidelines, the charters of the nominating and corporate governance, audit and compensation committees of our Board of Directors and our code of business conduct and ethics (which applies to all directors and employees, including our principal executive officer, principal financial officer and principal accounting officer).

Information contained on or hyperlinked from our website is not incorporated by reference into and should not be considered part of this Annual Report on Form 10-K or our other filings with the SEC. A copy of this Annual Report on Form 10-K is available without charge upon written request to: Investor Relations, Spirit Realty Capital, Inc., 2727 North Harwood Street, Suite 300, Dallas, Texas 75201. All reports we file with the SEC are available free of charge on the SEC's website at [www.sec.gov](http://www.sec.gov). Shares of our common stock are traded on the NYSE under the symbol "SRC."

## Item 1. Business

### THE COMPANY

We are a self-administered and self-managed REIT with in-house capabilities, including asset management, acquisition, credit, research, finance, IT and accounting functions. We primarily invest in single-tenant, operationally essential real estate throughout the U.S., which is generally acquired through sale-leaseback transactions and subsequently leased on a long-term, triple-net basis to high-quality tenants with business operations within predominantly retail, but also office and industrial property types.

We began operations through a predecessor legal entity in 2003, which became a public company in December 2004 and was subsequently taken private in August 2007 by a consortium of private investors. On September 25, 2012, we completed our initial public offering and on July 17, 2013, we completed the acquisition of Cole II through the Merger. The surviving entity, which was renamed Spirit Realty Capital, Inc., began trading on the NYSE under the symbol "SRC." Cole II was the "legal acquirer" in the Merger for certain legal and regulatory matters and the Corporation was deemed the "accounting acquirer" in the Merger for accounting and financial reporting purposes,

including the financial information set forth herein. On May 31, 2018, the Company completed the Spin-Off of SMTA which included all of the assets that collateralize Master Trust 2014, all of the Company's properties leased to Shopko, and certain other assets.

In conjunction with the Spin-Off, the Company entered into the Asset Management Agreement with SMTA, pursuant to which the Company acts as external asset manager for SMTA and is entitled to an annual management fee of \$20.0 million per annum.

As of December 31, 2018, our undepreciated gross investment in real estate and loans totaled approximately \$5.12 billion, representing investments in 1,514 properties, including properties securing our mortgage loans. Of this amount, 99.1% consisted of our gross investment in real estate, representing ownership of 1,462 properties, and the remaining 0.9% consisted primarily of commercial mortgage loans receivable secured by 52 real properties. See Item 2. "Properties - Our Real Estate Investment Portfolio" for further information on our properties and tenants.

Our operations are carried out through the Operating Partnership. OP Holdings, one of our wholly-owned subsidiaries, is the sole general partner and owns approximately 1% of the Operating Partnership. We and one of our wholly-owned subsidiaries are the only limited partners and together own the remaining 99% of the Operating Partnership.

Although the Operating Partnership is wholly-owned by us, in the future, we may issue partnership interests in the Operating Partnership to third parties in exchange for assets owned by such third parties. In general, any partnership interests of the Operating Partnership issued to third parties would be exchangeable for cash or, at our election, shares of our common stock at specified ratios set when partnership interests in the Operating Partnership are issued.

As of December 31, 2018, we had 89 employees, as compared to 87 employees as of December 31, 2017. None of these employees are represented by a labor union.

#### BUSINESS AND GROWTH STRATEGIES

Our objective is to maximize stockholder value by seeking superior risk-adjusted returns with an emphasis on stable rental revenue, primarily by investing in and managing a portfolio of single-tenant, operationally essential real estate throughout the U.S. We generate revenue primarily by leasing our properties to our tenants. See Item 2. "Properties" for property information and Item 6. "Selected Financial Data" for additional financial and asset information.

Single-tenant, operationally essential real estate consists of properties that are generally free-standing, commercial real estate facilities where our tenants conduct activities essential to the generation of their sales and profits. Under a triple-net lease, the tenant is typically responsible for all improvements and is contractually obligated to pay all property operating expenses, such as real estate taxes, insurance premiums and repair and maintenance costs. In support of our primary business of owning and leasing real estate, we have also strategically originated or acquired long-term, commercial mortgage and other loans. We view our operations as one reporting segment consisting of net leasing operations. We intend to pursue our objective through the following business and growth strategies:

##### Enhanced Portfolio Management Using Proprietary Tools

When monitoring existing investments or evaluating new investments, we typically consider three broad categories of risk: (1) tenant financial distress risk, (2) lease renewal risk and (3) suboptimal lease structures. We seek to manage these risks by utilizing our Spirit Heat Map and Spirit Property Ranking Model, as well as our overall internal credit underwriting and risk management processes. Since our inception, our Occupancy, a measure of portfolio quality, has never fallen below 96.1%, despite the economic downturn of 2008 through 2010.

Focus on Diversified Assets in Target Industries. Our investment strategy will be to continue to increase our exposure to industries that we determine are attractive based on our proprietary Spirit Heat Map and where we believe we are underweight. On the disposition side, we intend to reduce industry concentration based on the Spirit Heat Map and where we believe we are overweight. The Spirit Heat Map is used to analyze tenant industries across Porter's Five Forces and potential causes of technological disruption to identify tenant industries that we believe to have good fundamentals for future performance. The Spirit Heat Map is updated regularly to factor for changes in business and market conditions, changes in technology and other trends. Desirable tenants have attractive credit characteristics and stable operating histories. This strategy offers us the opportunity to achieve superior risk-adjusted returns when coupled with our intensive credit and real estate analysis, lease structuring and ongoing portfolio management. We also monitor and manage the diversification of our real estate investment portfolio in order to reduce the risks associated with adverse developments affecting a particular tenant, property, or region. Our strategy emphasizes a portfolio that (1) derives no more than 10.0% of its annual rent from any single tenant and no more than 2.0% of its annual rent from any single property, (2) is leased to tenants operating in various industries aligned with our Spirit Heat Map and (3) is located across the U.S. without significant



geographic concentration. While we consider the foregoing when making investments, we have made, and may make investments in the future that do not meet one or more of these criteria, and we may make additional investments that do not meet one or more of these criteria if we believe the opportunity is sufficiently attractive.

**Focus on Active Portfolio Management Decisions.** We use our proprietary Spirit Property Ranking Model to rank all properties in our portfolio, across twelve factors and weightings consisting of both real estate quality scores and credit underwriting criteria, in order to benchmark property quality, identify asset recycling opportunities and to enhance acquisition and disposition decisions. The Spirit Property Ranking Model is a key component of both the acquisition and disposition process, as well as the process for identifying asset recycling opportunities.

We selectively make acquisitions that we believe will contribute to our business objectives. We believe there will be ample acquisition opportunities in the single-tenant market fitting our underwriting and acquisition criteria. This criteria includes, but is not limited to, evaluation of the rank from our Spirit Property Ranking Model and impact on our portfolio's tenant, industry and geographic diversification.

We typically retain and manage real estate assets that fit within our investment criteria, which criteria are subject to change without notice to or vote by our stockholders. Additionally, management may elect to dispose of assets when it believes appropriate in view of our business objective, considering criteria including, but not limited to, the Spirit Heat Map, the rank from the Spirit Property Ranking Model, tenant concentration, tenant credit quality, unit financial performance, associated indebtedness, and asset zoning, as well as potential capital appreciation, potential uses of proceeds and tax considerations, among others.

#### **Execute Leases with Optimal Structures**

We seek to maintain the stability of our rental revenue and the long-term return on our investments by entering into leases with structures we deem to be aligned with our business and growth strategies:

**Leases for Operationally Essential Real Estate.** We seek to own properties that are operationally essential to our tenants, thereby reducing the risk that the tenant would choose not to renew an expiring lease or reject a lease in bankruptcy.

**Enhance Our Portfolio through Contractual Rental Growth.** Approximately 85.3% of our single-tenant properties (based on Contractual Rent) contain contractual provisions that increase the rental revenue over the term of the lease. Generally, our rent escalators increase rent at specified dates by: (1) a fixed amount; or (2) the lesser of (a) 1 to 2 times any increase in the CPI over a specified period, (b) a fixed percentage, or (c) a fixed schedule.

**Leases with Relatively Long Terms.** We seek to enter into leases with relatively long terms, typically with non-cancelable initial terms of 15 to 20 years and tenant renewal options for additional terms with attractive rent escalation provisions.

**Leases with a Master Lease Structure.** Where appropriate, we seek to enter into master leases whereby we lease multiple properties to a single tenant on an "all or none" basis. In a master lease structure, a tenant is responsible for a single lease payment relating to the entire portfolio of leased properties, as opposed to separate lease payments relating to each individually leased property. The master lease structure hinders a tenant's ability to "cherry pick" locations, where it unilaterally gives up underperforming properties while maintaining its leasehold interest in well-performing properties.

#### **FINANCING STRATEGY**

Our long-term financing strategy is to maintain a leverage profile that creates operational flexibility and generates superior risk-adjusted returns for our stockholders. We finance our operations and investments using a variety of methods, including available unrestricted cash balances, property operating revenue, proceeds from property dispositions, available borrowings under our credit facilities, common and preferred stock issuances, and debt securities issuances, including mortgage indebtedness and senior unsecured debt. We determine the amount of equity and debt financing to be used when acquiring an asset by evaluating our cost of equity capital, terms available in the credit markets (such as interest rate, repayment provisions and maturity) and our assessment of the particular asset's risk.

We may issue common stock when we believe that our share price is at a level that allows the offering proceeds to be accretively invested into additional properties, to permanently finance properties that were financed by our credit facilities, or to repay outstanding debt at or before maturity.

In September 2017, we filed a shelf registration statement with the SEC, which became immediately effective upon filing and will remain effective for a term of three years with an expiration in September 2020. Under this shelf registration statement, we may offer shares of our common or preferred stock or debt securities from time to time in amounts, at prices and on terms to be announced when and if such shares are offered. The specifics of any future offerings, along with the use of proceeds from any such offerings, will be described in detail in a prospectus supplement or other offering materials at the time of such offerings.

We have issued senior unsecured debt securities and have obtained other senior unsecured debt at the Operating Partnership level. In addition, our debt historically has also consisted of long-term borrowings secured by specific real estate assets or, more typically, pools of real estate assets. These secured borrowings include the issuance of non-recourse net-lease mortgage notes under Master Trust 2013, as well as non-recourse loans which have been securitized into CMBS debt. To the extent practicable, we expect to maintain a well-balanced debt profile with manageable and balanced maturities.

We expect to fund our operating expenses and other short-term liquidity requirements, including property acquisitions, payment of principal and interest on our outstanding indebtedness, property improvements, re-leasing costs, and cash distributions to common and preferred stockholders, primarily through cash provided by operating activities, borrowings under our available credit facilities and periodically through issuances of public securities. We anticipate that we will continue to use a number of different sources to finance our acquisitions and operations going forward; however, we cannot assure you that we will have access to the capital and credit markets at times and at terms that are acceptable to us.

## RECENT DEVELOPMENTS

### Financing Activities

#### 2019 Facilities Agreement

On January 14, 2019, the Operating Partnership entered into a new 2019 Revolving Credit and Term Loan Agreement with JPMorgan Chase Bank, N.A., as administrative agent, and various lenders, comprised of the 2019 Credit Facility and the A-1 Term Loans.

The 2019 Credit Facility is comprised of \$800.0 million of aggregate revolving commitments with a maturity date of March 31, 2023. The outstanding loans under the 2019 Credit Facility currently bear interest at LIBOR plus an applicable margin of 1.10% per annum and the aggregate revolving commitments incur a facility fee of 0.25% per annum, in each case, based on the Operating Partnership's credit rating. The 2019 Revolving Credit and Term Loan Agreement includes an accordion feature providing for an additional \$400.0 million of revolving borrowing capacity, subject to the satisfaction of certain requirements and obtaining additional lender commitments.

The A-1 Term Loans have an aggregate borrowing amount of \$420.0 million with a maturity date of March 31, 2024. The A-1 Term Loans currently bear interest at LIBOR plus an applicable margin of 1.25% per annum based on the Operating Partnership's credit rating. The Revolving Credit and Term Loan Agreement includes an accordion feature providing for an additional \$200.0 million of term loans, subject to satisfying certain requirements and obtaining additional lender commitments.

In addition, on January 14, 2019, the Operating Partnership entered into new A-2 Term Loans with Bank of America, N.A., as administrative agent, and various lenders, comprised of \$400 million of delayed draw term loans with a maturity date of March 31, 2022. The A-2 Term Loans currently bear interest at LIBOR plus an applicable margin of 1.25% per annum based on the Operating Partnership's credit rating. In addition, a ticking fee accrues on the unused portion of the commitments at a rate of 0.20% until the earlier of July 12, 2019 and the termination of the commitments. There are currently no borrowings outstanding under the A-2 Term Loans. The A-2 Term Loans include an accordion feature providing for an additional \$200.0 million of term loans, subject to the satisfaction of certain requirements and obtaining additional lender commitments.

The 2019 Facilities Agreements replaced the existing 2015 Credit Agreement and 2015 Term Loan Agreement.



See Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources - Description of Certain Debt" for further information on our debt and equity financings.

#### Real Estate Portfolio Activities

##### Concentration

During the month ended December 31, 2018, no tenant exceeded 5.0% of our Contractual Rent, and no one single property contributed more than 2.0% of our Contractual Rent. See Item 2. "Properties - Our Real Estate Investment Portfolio" for further information on our ten largest tenants and the composition of our tenant base.

##### Acquisitions and Dispositions

During the year ended December 31, 2018, we purchased 17 properties which are included in continuing operations, representing an aggregate gross investment of \$250.8 million, and invested \$36.2 million in revenue producing capital expenditures to fund improvements on properties the Company currently owns. During the same period, we sold 29 properties from continuing operations for \$103.3 million in gross sales proceeds. See Note 3 to our consolidated financial statements included in this Annual Report on Form 10-K for additional discussion of our investments.

##### Other Activities

##### Haggen Settlement

In 2015, Haggen Holdings, LLC and a number of its affiliates, including Haggen Operations Holdings, LLC ("Haggen"), filed petitions for bankruptcy. At the time of the filing, Haggen leased 20 properties from a subsidiary of the Company under a master lease. The Company and Haggen restructured the master lease in an initial settlement agreement with approved claims of \$21.0 million. In 2016, the Company entered into a second settlement agreement with both Haggen and Albertsons, LLC for \$3.4 million and \$3.0 million, respectively. Prior to 2018, the Company collected \$5.5 million of the total claims. In December 2018, the Company received final settlement proceeds of \$19.7 million and no other claims related to the Haggen settlement remain outstanding.

#### COMPETITION

We face competition for acquisitions from investors, including traded and non-traded public REITs, and private equity and institutional investment funds, some of which have greater financial resources than we do, a greater ability to borrow funds to acquire properties and the ability to accept more risk than we can prudently manage. This competition may increase the demand for the types of properties in which we typically invest and, therefore, reduce the number of suitable acquisition opportunities available to us and increase the prices paid for such. This competition will increase if investments in real estate become more attractive relative to other forms of investment.

As a landlord, we compete in the multi-billion dollar commercial real estate market with numerous developers and owners of properties, many of which own properties similar to ours in the same markets in which our properties are located. In operating and managing our portfolio, we compete for tenants based on a number of factors, including location, rental rates and flexibility. Some of our competitors have greater economies of scale, have lower cost of capital, have access to more resources and have greater name recognition than we do. If our competitors offer space at rental rates below current market rates or below the rental rates we currently charge our tenants, we may lose our tenants or prospective tenants and we may be pressured to reduce our rental rates or to offer substantial rent abatements, tenant improvement allowances, early termination rights or below-market renewal options in order to retain tenants when our leases expire.

#### REGULATION

##### General

Our properties are subject to various covenants, laws, ordinances and regulations, including regulations relating to common areas and fire and safety requirements. We believe that each of our properties has the necessary permits and approvals.

##### Americans With Disabilities Act

Pursuant to the ADA, our properties are required to meet federal requirements related to access and use by persons with disabilities. Compliance with the ADA, as well as a number of additional federal, state and local laws and regulations, may require modifications to properties we currently own and any properties we purchase, or may restrict renovations





of those properties. Noncompliance with these laws or regulations could result in the imposition of fines or an award of damages to private litigants, as well as the incurrence of the costs of making modifications to attain compliance, and future legislation could impose additional financial obligations or restrictions on our properties. Although our tenants are generally responsible for all maintenance and repair costs pursuant to triple-net leases, including compliance with the ADA and other similar laws or regulations, we could be held liable as the owner of the property for a failure of one of our tenants to comply with such laws or regulations.

#### Environmental Matters

Federal, state and local environmental laws and regulations regulate, and impose liability for, releases of hazardous or toxic substances into the environment. Under various of these laws and regulations, a current or previous owner, operator or tenant of real estate may be required to investigate and clean up hazardous or toxic substances, hazardous wastes or petroleum product releases or threats of releases at the property, and may be held liable to a government entity or to third parties for property damage and for investigation, clean-up and monitoring costs incurred by those parties in connection with actual or threatened contamination. These laws typically impose clean-up responsibility and liability without regard to fault, or whether or not the owner, operator or tenant knew of or caused the presence of the contamination. The liability under these laws may be joint and several for the full amount of the investigation, clean-up and monitoring costs incurred or to be incurred or actions to be undertaken, although a party held jointly and severally liable may seek contributions from other identified, solvent, responsible parties for their fair share toward these costs. These costs may be substantial, and can exceed the value of the property. The presence of contamination, or the failure to properly remediate contamination, on a property may adversely affect the ability of the owner, operator or tenant to sell or rent that property or to borrow using the property as collateral and may adversely impact our investment in that property.

Some of our properties contain, 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. Similarly, some of our properties are or were used for commercial or industrial purposes that involve or involved the use of petroleum products or other hazardous or toxic substances, or are adjacent to or near properties that have been or are used for similar commercial or industrial purposes. These operations create a potential for the release of petroleum products or other hazardous or toxic substances, and we could potentially be required to pay to clean up any contamination. In addition, strict environmental laws regulate a variety of activities that can occur on a property, including the storage of petroleum products or other hazardous or toxic substances, air emissions and water discharges. Such laws may impose fines or penalties for violations. As a result of the foregoing, we could be materially and adversely affected.

Environmental laws also govern the presence, maintenance and removal of ACM. Federal regulations require building owners and those exercising control over a building's management to identify and warn, through signs and labels, of potential hazards posed by workplace exposure to installed ACM in their building. The regulations also have employee training, record keeping and due diligence requirements pertaining to ACM. Significant fines can be assessed for violation of these regulations. As a result of these regulations, building owners and those exercising control over a building's management may be subject to an increased risk of personal injury lawsuits by workers and others exposed to ACM. The regulations may affect the value of a building containing ACM in which we have invested. Federal, state and local laws and regulations also govern the removal, encapsulation, disturbance, handling and/or disposal of ACM when those materials are in poor condition or in the event of construction, remodeling, renovation or demolition of a building. These laws may impose liability for improper handling or a release into the environment of ACM and may provide for fines to, and for third parties to seek recovery from, owners or operators of real properties for personal injury or improper work exposure associated with ACM.

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. Indoor air quality issues can also stem from inadequate ventilation, chemical contamination from indoor or outdoor sources, and other biological contaminants such as pollen, viruses and bacteria. Indoor exposure to airborne toxins or irritants above certain levels can be alleged to cause a variety of adverse health effects and symptoms, including allergic or other reactions. As a result, the presence of significant mold or other airborne contaminants at any of our properties could require us to undertake a costly remediation program to contain

or remove the mold or other airborne contaminants from the affected property or increase indoor ventilation. In addition, the presence of significant mold or other airborne contaminants could expose us to liability from our tenants, employees of our tenants or others if property damage or personal injury occurs. We are not presently aware of any material adverse indoor air quality issues at our properties that have not been previously addressed or remediated by us.

Before completing any property acquisition, we obtain environmental assessments in order to identify potential environmental concerns at the property. These assessments are carried out in accordance with the Standard Practice for Environmental Site Assessments (ASTM Practice E 1527-05) as set by ASTM International, formerly known as the American Society for Testing and Materials, and generally include a physical site inspection, a review of relevant federal, state and local environmental and health agency database records, one or more interviews with appropriate site-related personnel, review of the property's chain of title and review of historical aerial photographs and other information on past uses of the property. These assessments are limited in scope, however, if recommended in the initial assessments, we may undertake additional assessments such as soil and/or groundwater samplings or other limited subsurface investigations and ACM or mold surveys to test for substances of concern. A prior owner or operator of a property or historic operations at our properties may have created a material environmental condition that is not known to us or the independent consultants preparing the site assessments. Material environmental conditions may have arisen after the review was completed or may arise in the future, and future laws, ordinances or regulations may impose material additional environmental liability. If environmental concerns are not satisfactorily resolved in any initial or additional assessments, we may obtain environment insurance policies to insure against potential environmental risk or loss depending on the type of property, the availability and cost of the insurance and various other factors we deem relevant (i.e., an environmental occurrence affects one of our properties where our lessee may not have the financial capability to honor its indemnification obligations to us).

Generally, our leases provide that the lessee will indemnify us for any loss or expense we incur as a result of the presence, use or release of hazardous materials on our property. However, our ultimate liability for environmental conditions may exceed the policy limits on any environmental insurance policies we obtain, if any. If we are unable to enforce the indemnification obligations of our lessees or if the amount of environmental insurance we carry is inadequate, our results of operations would be adversely affected.

#### INSURANCE

Our tenants are generally required to maintain liability and property insurance coverage for the properties they lease from us pursuant to triple-net leases. Under such leases, our tenants are generally required to name us (and any of our lenders that have a mortgage on the property leased by the tenant) as additional insureds on their liability policies and additional insured and/or loss payee (or mortgagee, in the case of our lenders) on their property policies. Tenants are required to maintain casualty coverage and most carry limits at 100% of replacement cost. Depending on the location of the property, losses of a catastrophic nature, such as those caused by earthquakes and floods, may be covered by insurance policies that are held by our tenant with limitations such as large deductibles or co-payments that a tenant may not be able to meet. In addition, losses of a catastrophic nature, such as those caused by wind/hail, hurricanes, terrorism or acts of war, may be uninsurable or not economically insurable. In the event there is damage to our properties that is not covered by insurance and such properties are subject to recourse indebtedness, we will continue to be liable for the indebtedness, even if these properties are irreparably damaged. See Item 1A. "Risk Factors - Risks Related to Our Business and Properties - Insurance on our properties may not adequately cover all losses, which could materially and adversely affect us."

In addition to being generally named as additional insureds on our tenants' liability policies, we separately maintain commercial general liability coverage with limits of \$1.0 million for each occurrence and \$2.0 million general aggregate. We also maintain primary property coverage on (i) all unleased properties, (ii) all properties for which such coverage is not required to be carried by a tenant and (iii) all properties for which we obtain such coverage but the costs of which are reimbursed by tenants. In addition, we maintain excess property coverage on all remaining properties and other property coverage as may be required by our lenders.

#### Item 1A. Risk Factors

#### SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. When used in this Annual Report on Form 10-K, the words "estimate," "anticipate," "expect," "believe," "intend," "may," "will," "should," "seek," "approximately" or "plan," or the negative words or similar words or phrases that are predictions of or indicate future events or trends and which do not relate solely to historical matters are intended to identify forward-looking statements. You can also identify forward-looking statements by discussions of strategy, plans or intentions of management.

Forward-looking statements involve numerous risks and uncertainties and you should not rely on them as predictions of future events. Forward-looking statements depend on assumptions, data or methods which may be incorrect or

imprecise and we may not be able to realize them. We do not guarantee that the transactions and events described will happen as described (or that they will happen at all).

The following risks and uncertainties, among others, could cause actual results and future events to differ materially from those set forth or contemplated in the forward-looking statements:

- industry and economic conditions;
- volatility and uncertainty in the financial markets, including potential fluctuations in the CPI;
- our success in implementing our business strategy and our ability to identify, underwrite, finance, consummate, integrate and manage diversifying acquisitions or investments;
- the financial performance of our retail tenants and the demand for retail space, particularly with respect to challenges being experienced by general merchandise retailers;
- our ability to diversify our tenant base;
- the nature and extent of future competition;
- increases in our costs of borrowing as a result of changes in interest rates and other factors;
- our ability to access debt and equity capital markets;
- our ability to pay down, refinance, restructure and/or extend our indebtedness as it becomes due;
- our ability and willingness to renew our leases upon expiration and to reposition our properties on the same or better terms upon expiration in the event such properties are not renewed by tenants or we exercise our rights to replace existing tenants upon default;
- the impact of any financial, accounting, legal or regulatory issues or litigation that may affect us or our major tenants;
- our ability to manage our expanded operations;
- our ability and willingness to maintain our qualification as a REIT;
- the impact of Shopko's bankruptcy filing on SMTA;
- the impact of SMTA's board of trustees' decision to accelerate its strategic plan, including our ability to collect amounts to which we are contractually entitled under the Asset Management Agreement or SMTA Preferred Stock (defined below) upon a resolution of SMTA and/or a termination of the Asset Management Agreement;
- our ability to perform as an external manager for SMTA; and
- other risks inherent in the real estate business, including tenant defaults, potential liability relating to environmental matters, illiquidity of real estate investments and potential damages from natural disasters.

You are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date of this Annual Report on Form 10-K. While forward-looking statements reflect our good faith beliefs, they are not guarantees of future performance. We disclaim any obligation to publicly update or revise any forward-looking statement to reflect changes in underlying assumptions or factors, new information, data or methods, future events or other changes, except as required by law.

Set forth below are some (but not all) of the risk factors that could adversely affect our business and financial performance. Because we operate in a highly competitive and rapidly changing environment, new risk factors emerge from time to time, and it is not possible for management to predict all such risk factors, nor can management assess the impact of all such risk factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements. Given these risks and uncertainties, investors should not place undue reliance on forward-looking statements as a prediction of actual results.

#### RISKS RELATED TO OUR BUSINESS AND PROPERTIES

Risks related to commercial real estate ownership could reduce the value of our properties.

Our core business is the ownership of real estate that is leased to retail, service and distribution companies on a triple-net basis. Accordingly, our performance is subject to risks inherent to the ownership of commercial real estate, including:

- inability to collect rent from tenants due to financial hardship, including bankruptcy;
- changes in local real estate markets resulting in the lack of availability or demand for single-tenant retail space;
- changes in consumer trends and preferences that reduce the demand for products/services of our tenants;



- inability to lease or sell properties upon expiration or termination of existing leases;
- environmental risks related to the presence of hazardous or toxic substances or materials on our properties;
- subjectivity of real estate valuations and changes in such valuations over time;
- illiquid nature of real estate compared to most other financial assets;
- changes in laws and regulations, including those governing real estate usage and zoning;
- changes in interest rates and the availability of financing; and
- changes in the general economic and business climate.

The occurrence of any of the risks described above may cause the value of our real estate to decline, which could materially and adversely affect us.

Credit and capital market conditions may adversely affect our access to and/or the cost of capital.

Periods of volatility in the credit and capital markets negatively affect the amounts, sources and cost of capital available to us. We primarily use external financing to fund acquisitions and to refinance indebtedness as it matures. If sufficient sources of external financing are not available to us on cost effective terms, we could be forced to limit our acquisition activity and/or to take other actions to fund our business activities and repayment of debt, such as selling assets. To the extent that we access capital at a higher cost (reflected in higher interest rates for debt financing or lower stock price for equity financing), our acquisition yields, earnings per share and cash flow could be adversely affected.

Our tenants may fail to successfully operate their businesses, which could adversely affect us.

The success of our investments is materially dependent on the financial stability of our tenants' financial condition and leasing practices. Adverse economic conditions such as high unemployment levels, interest rates, tax rates and fuel and energy costs may have an impact on the results of operations and financial condition of our tenants and result in a decline in rent or an increased incidence of default under existing leases. Such adverse economic conditions may also reduce overall demand for rental space, which could adversely affect our ability to maintain our current tenants and attract new tenants.

At any given time, our tenants may experience a downturn in their business that may weaken the operating results and financial condition of individual properties or of their business as whole. As a result, a tenant may delay lease commencement, decline to extend a lease upon its expiration, fail to make rental payments when due, become insolvent or declare bankruptcy. We depend on our tenants to operate the properties we own in a manner which generates revenues sufficient to allow them to meet their obligations to us, including their obligations to pay rent, maintain certain insurance coverage and pay real estate taxes and maintain the properties in a manner so as not to jeopardize their operating licenses or regulatory status. The ability of our tenants to fulfill their obligations under our leases may depend, in part, upon the overall profitability of their operations. Cash flow generated by certain tenant businesses may not be sufficient for a tenant to meet its obligations to us. Although our occupied properties are generally operationally essential to our tenants, meaning the property is essential to the tenant's generation of sales and profits, this does not guarantee that a tenant's operations at a particular property will be successful or that the tenant will be able to meet all of its obligations to us. Our tenants' failure to successfully operate their businesses could materially and adversely affect us.

Single-tenant leases involve particular and significant risks related to tenant default.

Our strategy focuses primarily on investing in single-tenant triple-net leased properties throughout the U.S. The financial failure of, or default in payment by, a single tenant under its lease is likely to cause a significant reduction in, or elimination of, our rental revenue from that property and a reduction in the value of the property. We may also experience difficulty or a significant delay in re-leasing or selling such property. This risk is magnified in situations where we lease multiple properties to a single tenant under a master lease. The failure or default of a tenant under a master lease could reduce or eliminate rental revenue from multiple properties and reduce the value of such properties. Although the master lease structure may be beneficial to us because it restricts the ability of tenants to individually remove underperforming properties from the portfolio of properties leased from us, there is no guarantee that a tenant will not default in its obligations to us or decline to renew its master lease upon expiration. The default of a tenant that leases multiple properties from us could materially and adversely affect us.





A substantial portion of our properties are leased to unrated tenants and the tools we use to measure the credit quality of such tenants may not be accurate.

A substantial portion our properties are leased to unrated tenants whom we determine, through our internal underwriting and credit analysis, to be credit worthy. Many of our tenants are required to provide financial information, which includes balance sheet, income statement and cash flow statement data, on a quarterly and/or annual basis, and, as of December 31, 2018, approximately 52.8% of our lease investment portfolio required the tenant to provide property-level performance information, which includes income statement data on a quarterly and/or annual basis. To assist in our determination of a tenant's credit quality, we license a product from Moody's Analytics that provides an EDF and a "shadow rating," and we evaluate a lease's property-level rent coverage ratio. An EDF is only an estimate of default probability based, in part, on assumptions incorporated into the product. A shadow rating does not constitute a published credit rating and lacks the extensive company participation that is typically involved when a rating agency publishes a rating; accordingly, a shadow rating may not be as indicative of creditworthiness as a rating published by Moody's, S&P, or another nationally recognized statistical rating organization. Our calculations of EDFs, shadow ratings and rent coverage ratios are based on financial information provided to us by our tenants and prospective tenants without independent verification on our part, and we must assume the appropriateness of estimates and judgments that were made by the party preparing the financial information. If our measurement of credit quality proves to be inaccurate, we may be subject to defaults, and investors may view our cash flows as less stable.

Decrease in demand for retail and restaurant space may materially and adversely affect us.

As of December 31, 2018, leases representing approximately 33.3% and 13.2% of our Contractual Rent were with tenants in the retail and restaurant industries, respectively, and we may acquire additional retail and restaurant properties in the future. Accordingly, decreases in the demand for retail and/or restaurant spaces adversely impact us. The market for retail and restaurant space has previously been, and could continue to be, adversely affected by weakness in the national, regional and local economies, the adverse financial condition of some large retail and restaurant companies, the ongoing consolidation in the retail and restaurant industries, the excess amount of retail and restaurant space in a number of markets and, in the case of the retail industry, increasing consumer purchases through catalogs or over the Internet. To the extent that these conditions continue, they are likely to negatively affect market rents for retail and restaurant space, which could materially and adversely affect us.

High geographic concentration of our properties could magnify the effects of adverse economic or regulatory developments in such geographic areas on our operations and financial condition.

As of December 31, 2018, 11.9% of our portfolio (as a percentage of Contractual Rent) was located in Texas, representing the highest concentration of our assets. Geographic concentration exposes us to greater economic or regulatory risks than if we owned a more geographically diverse portfolio. We are susceptible to adverse developments in the economic or regulatory environments of the geographic areas in which we concentrate (or in which we may develop a substantial concentration of assets in the future), such as business layoffs or downsizing, industry slowdowns, relocations of businesses, increases in real estate and other taxes or costs of complying with governmental regulations.

We may be unable to renew leases, lease vacant space or re-lease space as leases expire on favorable terms or at all.

Our results of operations depend on our ability to strategically lease space in our properties (by renewing or re-leasing expiring leases and leasing vacant space), optimize our tenant mix or lease properties on more economically favorable terms. As of December 31, 2018, leases representing approximately 1.5% of our rental revenue will expire during 2019. As of December 31, 2018, five of our properties, representing approximately 0.3% of our total economically yielding owned properties, were vacant. Current tenants may decline, or may not have the financial resources available, to renew current leases and we cannot guarantee that leases that are renewed will have terms that are as economically favorable to us as the expiring lease terms. If tenants do not renew the leases as they expire, we will have to find new tenants to lease our properties and there is no guarantee that we will be able to find new tenants or that our properties will be re-leased at rental rates equal to or above the current average rental rates or that substantial rent abatements, tenant improvement allowances, early termination rights, below-market renewal options or other lease incentive payments will not be offered to attract new tenants. We may experience significant costs in connection with renewing, leasing or re-leasing a significant number of our properties, which could materially and adversely affect us.



Our ability to realize future rent increases will vary depending on changes in the CPI.

Most of our leases contain rent escalators, or provisions that periodically increase the base rent payable by the tenant under the lease. Although 66.6% of our rent escalators increase rent at a fixed amount on fixed dates, as of December 31, 2018, approximately 18.7% (excluding leases on multi-tenant properties) of our rent escalators increase rent by a multiple of any increases in the CPI or the lesser of (a) a multiple of any increase in the CPI over a specified period or (b) a fixed percentage. If the product of any increase in the CPI multiplied by the applicable factor is less than the fixed percentage, the increased rent we are entitled to receive will be less than what we otherwise would have been entitled to receive if the rent escalator was based solely on a fixed percentage. Therefore, during periods of low inflation or deflation, small increases or decreases in the CPI will subject us to the risk of receiving lower rental revenue than we otherwise would have been entitled to receive if our rent escalators were based solely on fixed percentages or amounts. Conversely, if the product of any increase in the CPI multiplied by the applicable factor is more than the fixed percentage, the increased rent we are entitled to receive will be less than what we otherwise would have been entitled to receive if the rent escalator was based solely on an increase in CPI. Therefore, periods of high inflation will subject us to the risk of receiving lower rental revenue than we otherwise would have been entitled to receive if our rent escalators were based solely on CPI increases.

The bankruptcy or insolvency of any of our tenants could result in the termination of such tenant's lease and material losses to us.

The occurrence of a tenant bankruptcy or insolvency could diminish the income we receive from that tenant's lease or leases. In particular, the retail industry is facing reductions in sales revenues and increased bankruptcies throughout the United States, and revenues generated from retail tenants represented approximately 33.3% of our Contractual Rent for the month ended December 31, 2018. If a tenant becomes bankrupt or insolvent, federal law may prohibit us from evicting such tenant based solely upon such bankruptcy or insolvency. In addition, a bankrupt or insolvent tenant may be authorized to reject and terminate its lease or leases with us. Any claims against such bankrupt tenant for unpaid future rent would be subject to statutory limitations that would likely result in our receipt of rental revenues that are substantially less than the contractually specified rent we are owed under the lease or leases. In addition, any claim we have for unpaid past rent, if any, may not be paid in full. We may also be unable to re-lease a terminated or rejected space or to re-lease it on comparable or more favorable terms.

Moreover, tenants who are considering filing for bankruptcy protection may request that we agree to amendments of their master leases to remove certain of the properties they lease from us under such master leases. We cannot guarantee that we will be able to sell or re-lease such properties or that lease termination fees, if any, received in exchange for such releases will be sufficient to make up for the rental revenues lost as a result of such lease amendments. As a result, tenant bankruptcies may materially and adversely affect us.

Property vacancies could result in significant capital expenditures and illiquidity.

The loss of a tenant, either through lease expiration or tenant bankruptcy or insolvency, may require us to spend significant amounts of capital to renovate the property before it is suitable for a new tenant. Many of the leases we enter into or acquire are for properties that are specially suited to the particular business of our tenants. Because these properties have been designed or physically modified for a particular tenant, if the current lease is terminated or not renewed, we may be required to renovate the property at substantial costs, decrease the rent we charge or provide other concessions in order to lease the property to another tenant. In the event we are required to sell the property, we may have difficulty selling it to a party other than the tenant due to the special purpose for which the property may have been designed or modified. This potential illiquidity may limit our ability to quickly modify our portfolio in response to changes in economic or other conditions, including tenant demand. These limitations may materially and adversely affect us.

Our future results will suffer if we do not effectively manage our expanded operations.

We may continue to expand our operations through additional acquisitions and other strategic transactions, and modernize our information technology and management systems through new systems implementations, some of which may involve complex challenges. Our future success will depend, in part, upon our ability to manage our expansion opportunities, integrate new operations into our existing business in an efficient and timely manner, successfully monitor our operations, costs and regulatory compliance, and develop and maintain other necessary systems, processes and internal controls. We cannot guarantee that our expansion or acquisition opportunities will



be successful or that we will realize their expected operating efficiencies, cost savings, revenue enhancements, synergies or other benefits.

We may be unable to identify and complete acquisitions of suitable properties, which may impede our growth, or our future acquisitions may not yield the returns we expect.

Our ability to expand through acquisitions requires us to identify and complete acquisitions or investment opportunities that are compatible with our growth strategy and to successfully integrate newly acquired properties into our portfolio. We continually evaluate investment opportunities and may acquire properties when strategic opportunities exist. Our ability to acquire properties on favorable terms and successfully operate them may be constrained by the following significant risks:

- we face competition from other real estate investors with significant capital, including REITs and institutional investment funds, which may be able to accept more risk than we can prudently manage, including risks associated with paying higher acquisition prices;
- we face competition from other potential acquirers which may significantly increase the purchase price for a property we acquire, which could reduce our growth prospects;
- we may incur significant costs and divert management attention in connection with evaluating and negotiating potential acquisitions, including ones that we are subsequently unable to complete;
- we may acquire properties that are not accretive to our results upon acquisition, and we may be unsuccessful in managing and leasing such properties in accordance with our expectations;
- our cash flow from an acquired property may be insufficient to meet our required principal and interest payments with respect to debt used to finance the acquisition of such property;
- we may discover unexpected items, such as unknown liabilities, during our due diligence investigation of a potential acquisition or other customary closing conditions may not be satisfied, causing us to abandon an acquisition opportunity after incurring expenses related thereto;
- we may fail to obtain financing for an acquisition on favorable terms or at all;
- we may spend more than budgeted amounts to make necessary improvements or renovations to acquired properties;
- market conditions may result in higher than expected vacancy rates and lower than expected rental rates; or
- we may acquire properties subject to liabilities and without any recourse, or with only limited recourse, with respect to unknown liabilities such as liabilities for clean-up of undisclosed environmental contamination, claims by tenants, vendors or other persons dealing with the former owners of the properties, liabilities incurred in the ordinary course of business and claims for indemnification by general partners, directors, officers and others indemnified by the former owners of the properties.

If any of these risks are realized, we may be materially and adversely affected.

Any material failure, weakness, interruption or breach in security of our information systems could prevent us from effectively operating our business.

We rely on information systems across our operations and corporate functions, including finance and accounting, and depend on such systems to ensure payment of obligations, collection of cash, data warehousing to support analytics, and other various processes and procedures. Our ability to efficiently manage our business depends significantly on the reliability and capacity of these systems. The failure of these systems to operate effectively, maintenance problems, upgrading or transitioning to new platforms, or a breach in security of these systems, such as in the event of cyber-attacks, could result in the theft of intellectual property, personal information or personal property, damage to our reputation and third-party claims, as well as reduced efficiency in our operations and in the accuracy in our internal and external financial reporting. The remediation of such problems could result in significant unplanned expenditures.

Illiquidity of real estate investments could significantly impede our ability to respond to adverse changes in the performance of our properties and harm our financial condition.

The real estate investments made, and expected to be made, by us are relatively difficult to sell quickly. As a result, our ability to promptly sell one or more properties in our portfolio in response to changing economic, financial or investment conditions is limited. Return of capital and realization of gains, if any, from an investment generally will occur upon disposition or refinancing of the underlying property. We may be unable to realize our investment objective



by sale, other disposition or refinancing at attractive prices within any given period of time or may otherwise be unable to complete any exit strategy. In particular, these risks could arise from weakness in or even the lack of an established market for a property, changes in the financial condition or prospects of prospective purchasers, changes in national or international economic conditions and changes in laws, regulations or fiscal policies of the jurisdiction in which a property is located.

In addition, the Code imposes restrictions on a REIT's ability to dispose of properties that are not applicable to other types of real estate companies. In particular, the tax laws applicable to REITs effectively require that we hold our properties for investment, rather than primarily for sale in the ordinary course of business, which may cause us to forgo or defer sales of properties that otherwise would be in our best interest. Therefore, we may not be able to vary our portfolio in response to economic or other conditions promptly or on favorable terms, which may materially and adversely affect us.

We face significant competition for tenants, which may decrease or prevent increases of the occupancy and rental rates of our properties, and competition for acquisitions may reduce the number of acquisitions we are able to complete and increase the costs of these acquisitions.

We compete with numerous developers, owners and operators of properties, many of which own properties similar to ours in the same markets in which our properties are located. If our competitors offer space at rental rates below current market rates or below the rental rates we currently charge our tenants, we may lose existing or potential tenants and we may be pressured to reduce our rental rates or to offer more substantial rent abatements, tenant improvements, early termination rights, below-market renewal options or other lease incentive payments in order to retain tenants when our leases expire. Competition for tenants could decrease or prevent increases of the occupancy and rental rates of our properties, which could materially and adversely affect us.

We also face competition for acquisitions of real property from investors, including traded and non-traded public REITs, private equity investors and institutional investment funds, some of which have greater financial resources than we do, a greater ability to borrow funds to acquire properties and the ability to accept more risk than we can prudently manage. This competition may increase the demand for the types of properties in which we typically invest and, therefore, reduce the number of suitable acquisition opportunities available to us and increase the prices paid for such acquisition properties. This competition will increase if investments in real estate become more attractive relative to other types of investment. Accordingly, competition for the acquisition of real property could materially and adversely affect us.

The loss of a borrower or the failure of a borrower to make loan payments on a timely basis will reduce our revenues, which could lead to losses on our investments and reduced returns to our stockholders.

We have originated or acquired long-term, commercial mortgage and other loans. The success of our loan investments is materially dependent on the financial stability of our borrowers. The success of our borrowers is dependent on each of their individual businesses and their industries, which could be affected by economic conditions in general, changes in consumer trends and preferences and other factors over which neither they nor we have control. A default of a borrower on its loan payments to us that would prevent us from earning interest or receiving a return of the principal of our loan could materially and adversely affect us. In the event of a default, we may also experience delays in enforcing our rights as lender and may incur substantial costs in collecting the amounts owed to us and in liquidating any collateral.

Foreclosure and other similar proceedings used to enforce payment of real estate loans are generally subject to principles of equity, which are designed to relieve the indebted party from the legal effect of that party's default. Foreclosure and other similar laws may limit our right to obtain a deficiency judgment against the defaulting party after a foreclosure or sale. The application of any of these principles may lead to a loss or delay in the payment on loans we hold, which in turn could reduce the amounts we have available to make distributions. Further, in the event we have to foreclose on a property, the amount we receive from the foreclosure sale of the property may be inadequate to fully pay the amounts owed to us by the borrower and our costs incurred to foreclose, repossess and sell the property which could materially and adversely affect us.

Our investments in mortgage loans may be affected by unfavorable real estate market conditions, including interest rate fluctuations, which could decrease the value of those loans.



Our investments in mortgage loans are subject to risk of default by the borrowers and to interest rate risks. To the extent we incur delays in liquidating defaulted mortgage loans, we may not be able to obtain all amounts due to us

under such 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 or the dates of our investment in the loans. If the values of the underlying properties decline, the value of the collateral securing our mortgage loans will also decline and if we were to foreclose on any of the properties securing the mortgage loans, we may not be able to sell or lease them for an amount equal to the unpaid amounts due to us under the mortgage loans. As such, defaults on mortgage loans in which we invest may materially and adversely affect us.

Inflation may materially and adversely affect us and our tenants.

Increased inflation could have a negative impact on variable-rate debt we currently have or that we may incur in the future. Our leases typically contain provisions designed to mitigate the adverse impact of inflation on our results of operations. Because tenants are typically required to pay all property operating expenses, increases in property-level expenses at our leased properties generally do not affect us. However, increased operating expenses at vacant properties and the limited number of properties that are not subject to full triple-net leases could cause us to incur additional operating expenses, which could increase our exposure to inflation. Additionally, the increases in rent provided by many of our leases may not keep up with the rate of inflation. Increased costs may also have an adverse impact on our tenants if increases in their operating expenses exceed increases in revenue, which may adversely affect the tenants' ability to pay rent owed to us.

Changes in market interest rates may adversely impact the value of our common stock.

The market price of shares of our common stock will generally be influenced by the distribution yield on shares of our common stock (as a percentage of the price of shares of our common stock) relative to market interest rates. Further increases in market interest rates, which are currently at low levels relative to historical rates, may lead prospective purchasers of shares of our common stock to expect a higher distribution yield. In addition, higher market interest rates would likely increase our borrowing costs and potentially decrease funds available for distribution. Thus, higher market interest rates could cause the market price of shares of our common stock to decrease.

The market price and trading volume of shares of our common stock may fluctuate or decline.

The market price and trading volume of our common stock may fluctuate widely due to various factors, including:

- actual or anticipated variations in our or our competitors' quarterly operating results or distributions;

- publication of research reports about us, our competitors or the real estate industry;

- adverse market reaction to any additional indebtedness we incur or debt or equity securities we or the Operating Partnership issue in the future;

- additions or departures of key management personnel;

- changes in our credit ratings;

- the financial condition, performance and prospects of our tenants; and

- the realization of any of the other risk factors presented in this Annual Report on Form 10-K.

We may issue shares of our common stock or other securities without stockholder approval, including shares issued to satisfy REIT dividend distribution requirements. The Operating Partnership may issue partnership interests to third parties, and such partnership interests would be exchangeable for cash or, at our election, shares of our common stock at specified ratios set when partnership interests in the Operating Partnership are issued. Our existing stockholders have no preemptive rights to acquire any of these securities, and any issuance of equity securities by us or the Operating Partnership may dilute stockholder investment.

Broad market fluctuations could negatively impact the market price of shares of our common stock.

The stock market has experienced extreme price and volume fluctuations that have affected the market price of the common equity of many companies in industries similar or related to ours and that have been unrelated to these companies' operating performances. These broad market fluctuations could reduce the market price of shares of our common stock. Furthermore, our operating results and prospects may be below the expectations of public market analysts and investors or may be lower than those of companies with comparable market capitalizations. Either of these factors could lead to a material decline in the market price of our common stock.



If we fail to maintain effective internal controls over financial reporting, we may not be able to accurately and timely report our financial results.

Effective internal controls over financial reporting are necessary for us to provide reliable financial reports, effectively prevent fraud and operate successfully as a public company. If we cannot provide reliable financial reports or prevent fraud, our reputation and operating results would be harmed. We are required to perform system and process evaluation and testing of our internal control over financial reporting to allow management to report on, and our independent registered public accounting firm to attest to, the effectiveness of our internal control over financial reporting, as required by Section 404 of the Sarbanes-Oxley Act of 2002.

As a result of material weaknesses or significant deficiencies that may be identified in our internal control over financial reporting in the future, we may also identify certain deficiencies in some of our disclosure controls and procedures that we believe require remediation. If we or our independent registered public accounting firm discover any such weaknesses or deficiencies, we will make efforts to further improve our internal control over financial reporting controls. However, there is no assurance that we will be successful. Any failure to maintain effective controls or timely effect any necessary improvement of our internal control over financial reporting controls could harm operating results or cause us to fail to meet our reporting obligations, which could affect the listing of our common stock on the NYSE. Ineffective internal control over financial reporting and disclosure controls could also cause investors to lose confidence in our reported financial information, which would likely have a negative effect on the per share trading price of our common stock.

Our growth depends on external sources of capital that are outside of our control and may not be available to us on commercially reasonable terms or at all.

In order to maintain our qualification as a REIT, we are required under the Code to distribute annually at least 90% of our REIT taxable income, determined without regard to the dividends paid deduction and excluding any net capital gain. In addition, we will be subject to income tax at regular corporate rates to the extent that we distribute less than 100% of our REIT taxable income, determined without regard to the dividends paid deduction and including any net capital gain. Because of these distribution requirements, we may not be able to fund future capital needs, including any necessary acquisition financing, from operating cash flow. Consequently, we may rely on third-party sources to fund our capital needs. We may not be able to obtain the financing on favorable terms or at all. Any additional debt we incur will increase our leverage and likelihood of default. Our access to third-party sources of capital depends, in part, on:

- general market conditions;
- the market's perception of our growth potential;
- our current debt levels;
- our current and expected future earnings;
- our cash flow and cash distributions; and
- the market price per share of our common stock.

If we cannot obtain capital from third-party sources, we may not be able to acquire properties when strategic opportunities exist, meet the capital and operating needs of our existing properties, satisfy our debt service obligations or make the cash distributions to our stockholders necessary to maintain our qualification as a REIT.

Historically, we have raised a significant amount of debt capital through our asset-backed securitization program and the CMBS market. We have generally used the proceeds from these financings to repay debt and fund real estate acquisitions. On May 31, 2018, in conjunction with the Spin-Off, we contributed Master Trust 2014 to SMTA. As of December 31, 2018, we had issued notes under our asset-backed securitization program in one class (Series 2013-2 Class A) with an outstanding principal balance of \$167.9 million. These Master Trust Notes had a maturity of 5.0 years as of December 31, 2018. In addition, we had CMBS loans with an aggregate outstanding principal balance of \$274.8 million and an average maturity of 4.5 years as of December 31, 2018. Our obligations under these loans are generally secured by liens on certain of our properties. No assurance can be given that the CMBS market will be available to us in the future, whether to refinance existing debt or to raise additional debt capital. Moreover, we view our ability to substitute collateral under our asset-backed securitization program favorably, and no assurance can be given that financing facilities offering similar flexibility will be available to us in the future.



Dispositions of real estate assets could change the holding period assumption in our valuation analyses, which could result in material impairment losses and adversely affect our financial results.

We evaluate real estate assets for impairment based on the projected cash flow of the asset over our anticipated holding period. If we change our intended holding period due to our intention to sell or otherwise dispose of an asset, we must reevaluate whether that asset is impaired under GAAP. Depending on the carrying value of the property at the time we change our intention and the amount that we estimate we would receive on disposal, we may record an impairment loss that would adversely affect our financial results. This loss could be material to our assets in the period that it is recognized.

Loss of our key personnel with long-standing business relationships could materially impair our ability to operate successfully.

Our continued success and our ability to manage anticipated future growth depend, in large part, upon the efforts of key personnel, particularly our President and Chief Executive Officer, Jackson Hsieh, who has extensive market knowledge and relationships and exercises substantial influence over our operational, financing, acquisition and disposition activity.

Many of our other key executive personnel, particularly our executive and senior vice presidents, also have extensive experience and strong reputations in the real estate industry and have been instrumental in setting our strategic direction, operating our business, identifying, recruiting and training key personnel and arranging necessary financing. In particular, the extent and nature of the relationships that these individuals have developed with financial institutions and existing and prospective tenants is critically important to the success of our business. The loss of services of one or more members of our senior management team, or our inability to attract and retain highly qualified personnel, could adversely affect our business, diminish our investment opportunities and weaken our relationships with lenders, business partners, existing and prospective tenants and industry personnel, which could materially and adversely affect us.

We may become subject to litigation, which could materially and adversely affect us.

In the ordinary course of business, we may become subject to litigation, including claims relating to our operations, security offerings and otherwise. Some of these claims may result in significant defense costs and potentially significant judgments against us, some of which are not, or cannot be, insured against. We generally intend to vigorously defend ourselves. However, we cannot be certain of the ultimate outcomes of any claims that may arise in the future. Resolution of these types of matters against us may result in our having to pay significant fines, judgments, or settlements, which, if uninsured, or if the fines, judgments, and settlements exceed insured levels, could adversely impact our earnings and cash flows, thereby materially and adversely affecting us. Certain litigation or the resolution of certain litigation may affect the availability or cost of some of our insurance coverage, which could materially and adversely impact us, expose us to increased risks that would be uninsured, and materially and adversely impact our ability to attract directors and officers.

Costs of compliance with, or liabilities related to, environmental laws may materially and adversely affect us.

The properties we own or have owned in the past may subject us to known and unknown environmental liabilities.

Under various federal, state and local laws and regulations relating to the environment, as a current or former owner or operator of real property, we may be liable for costs and damages resulting from the presence or discharge of hazardous or toxic substances, waste or petroleum products at, on, in, under or migrating from such property, including costs to investigate, clean up such contamination and liability for harm to natural resources. We may face liability regardless of:

- our knowledge of the contamination;
- the timing of the contamination;
- the cause of the contamination; or
- the party responsible for the contamination of the property.

There may be environmental liabilities associated with our properties of which we are unaware. We obtain Phase I environmental site assessments on all properties we finance or acquire. The Phase I environmental site assessments are limited in scope and therefore may not reveal all environmental conditions affecting a property. Therefore, there could be undiscovered environmental liabilities on the properties we own. Some of our properties use, or may have



used in the past, underground tanks for the storage of petroleum-based products or waste products that could create a potential for release of hazardous substances or penalties if tanks do not comply with legal standards. If environmental contamination exists on our properties, we could be subject to strict, joint and/or several liability for the contamination by virtue of our ownership interest. Some of our properties may contain ACM. Strict environmental laws govern the presence, maintenance and removal of ACM and such laws may impose fines and penalties for failure to comply with these requirements or expose us to third-party liability (e.g., liability for personal injury associated with exposure to asbestos). Strict environmental laws also apply to other activities that can occur on a property, such as air emissions and water discharges, and such laws may impose fines and penalties for violations.

The presence of hazardous substances on a property may adversely affect our ability to sell, lease or improve the property or to borrow using the property as collateral. In addition, environmental laws may create liens on contaminated properties in favor of the government for damages and costs it incurs to address such contamination. Moreover, if contamination is discovered on our properties, environmental laws may impose restrictions on the manner in which they may be used or businesses may be operated, and these restrictions may require substantial expenditures.

In addition, although our leases generally require our tenants to operate in compliance with all applicable laws and to indemnify us against any environmental liabilities arising from a tenant's activities on the property, we could be subject to strict liability by virtue of our ownership interest. We cannot be sure that our tenants will, or will be able to, satisfy their indemnification obligations, if any, under our leases. Furthermore, the discovery of environmental liabilities on any of our properties could lead to significant remediation costs or to other liabilities or obligations attributable to the tenant of that property, which may affect such tenant's ability to make payments to us, including rental payments and, where applicable, indemnification payments.

Our environmental liabilities may include property damage, personal injury, investigation and clean-up costs. These costs could be substantial. Although we may obtain insurance for environmental liability for certain properties that are deemed to warrant coverage, our insurance may be insufficient to address any particular environmental situation and we may be unable to continue to obtain insurance for environmental matters, at a reasonable cost or at all, in the future. If our environmental liability insurance is inadequate, we may become subject to material losses for environmental liabilities. Our ability to receive the benefits of any environmental liability insurance policy will depend on the financial stability of our insurance company and the position it takes with respect to our insurance policies. If we were to become subject to significant environmental liabilities, we could be materially and adversely affected.

Most of the environmental risks discussed above refer to properties that we own or may acquire in the future. However, each of the risks identified also applies to the owners (and potentially, the lessees) of the properties that secure each of the loans we have made and any loans we may acquire or make in the future. Therefore, the existence of environmental conditions could diminish the value of each of the loans and the abilities of the borrowers to repay the loans and could materially and adversely affect us.

Our properties may contain or develop harmful mold, which could lead to liability for adverse health effects and costs of remediation.

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. 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. As a result, should our tenants or their employees or customers be exposed to mold at any of our properties we could be required to undertake a costly remediation program to contain or remove the mold from the affected property. In addition, exposure to mold by our tenants or others could subject us to liability if property damage or health concerns arise. If we were to become subject to significant mold-related liabilities, we could be materially and adversely affected.

Insurance on our properties may not adequately cover all losses, which could materially and adversely affect us.

Our tenants are required to maintain liability and property insurance coverage for the properties they lease from us pursuant to triple-net leases. Pursuant to such leases, our tenants are generally required to name us (and any of our lenders that have a mortgage on the property leased by the tenant) as additional insureds on their liability policies and additional insured and/or loss payee (or mortgagee, in the case of our lenders) on their property policies. All tenants



are required to maintain casualty coverage and most carry limits at 100% of replacement cost. Depending on the location of the property, losses of a catastrophic nature, such as those caused by earthquakes and floods, may be

covered by insurance policies that are held by our tenant with limitations such as large deductibles or co-payments that a tenant may not be able to meet. In addition, losses of a catastrophic nature, such as those caused by wind/hail, hurricanes, terrorism or acts of war, may be uninsurable or not economically insurable. In the event there is damage to our properties that is not covered by insurance and such properties are subject to recourse indebtedness, we will continue to be liable for the indebtedness, even if these properties are irreparably damaged.

Inflation, changes in building codes and ordinances, environmental considerations, and other factors, including terrorism or acts of war, may make any insurance proceeds we receive insufficient to repair or replace a property if it is damaged or destroyed. In that situation, the insurance proceeds received may not be adequate to restore our economic position with respect to the affected real property. Furthermore, in the event we experience a substantial or comprehensive loss of one of our properties, we may not be able to rebuild such property to its existing specifications without significant capital expenditures which may exceed any amounts received pursuant to insurance policies, as reconstruction or improvement of such a property would likely require significant upgrades to meet zoning and building code requirements. The loss of our capital investment in or anticipated future returns from our properties due to material uninsured losses could materially and adversely affect us.

Compliance with the ADA and fire, safety and other regulations may require us to make unanticipated expenditures that materially and adversely affect us.

Our properties are subject to the ADA. Under the ADA, all public accommodations must meet federal requirements related to access and use by disabled persons. Compliance with the ADA requirements could require removal of access barriers and non-compliance could result in imposition of fines by the U.S. government or an award of damages to private litigants, or both. While our tenants are obligated by law to comply with the ADA and typically obligated under our leases and financing agreements to cover costs associated with compliance, if required changes involve greater expenditures than anticipated or if the changes must be made on a more accelerated basis than anticipated, our tenants' ability to cover the costs could be adversely affected. We may be required to expend our own funds to comply with the provisions of the ADA, which could materially and adversely affect us.

In addition, we are required to operate our properties in compliance with fire and safety regulations, building codes and other land use regulations, as they may be adopted by governmental agencies and bodies and become applicable to our properties. We may be required to make substantial capital expenditures to comply with those requirements and may be required to obtain approvals from various authorities with respect to our properties, including prior to acquiring a property or when undertaking renovations of any of our existing properties. There can be no assurance that existing laws and regulatory policies will not adversely affect us or the timing or cost of any future acquisitions or renovations, or that additional regulations will not be adopted that increase such delays or result in additional costs. Additionally, failure to comply with any of these requirements could result in the imposition of fines by governmental authorities or awards of damages to private litigants. While we intend to only acquire properties that we believe are currently in substantial compliance with all regulatory requirements, these requirements may change and new requirements may be imposed which would require significant unanticipated expenditures by us and could materially and adversely affect us.

Changes in accounting standards may materially and adversely affect us.

From time to time the FASB, and the SEC, who create and interpret appropriate accounting standards, may change the financial accounting and reporting standards or their interpretation and application of these standards that will govern the preparation of our financial statements. These changes could materially and adversely affect our reported financial condition and results of operations. In some cases, we could be required to apply a new or revised standard retroactively, resulting in restating prior period financial statements. Similarly, these changes could materially and adversely affect our tenants' reported financial condition or results of operations and affect their preferences regarding leasing real estate.

The SEC is currently considering whether issuers in the U.S. should be required to prepare financial statements in accordance with IFRS instead of GAAP. IFRS is a comprehensive set of accounting standards promulgated by the IASB, which are rapidly gaining worldwide acceptance. The SEC currently has not finalized the time frame it expects that U.S. issuers would first report under the new standards. If IFRS is adopted, the potential changes associated with the adoption or convergence with IFRS, may materially and adversely affect us.

Additionally, the FASB is considering various changes to GAAP, some of which may be significant, as part of a joint effort with the IASB to converge accounting standards. In particular, FASB issued a new accounting standard that

requires companies to capitalize all leases on their balance sheets by recognizing a lessee's rights and obligations. For public companies, this new standard will be effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Many companies that account for certain leases on an "off balance sheet" basis would be required to account for such leases "on balance sheet" upon adoption of this rule. This change removes many of the differences in the way companies account for owned property and leased property, and could have a material effect on various aspects of our tenants' businesses, including their credit quality and the factors they consider in deciding whether to own or lease properties. Additionally, it could cause companies that lease properties to prefer shorter lease terms in an effort to reduce the leasing liability required to be recorded on the balance sheet. This new standard could also make lease renewal options less attractive, because, under certain circumstances, the rule would require a tenant to assume that a renewal right will be exercised and accrue a liability relating to the longer lease term. In the future, we may choose to acquire properties or portfolios of properties through tax deferred contribution transactions, which could result in stockholder dilution and limit our ability to sell such assets.

In the future we may acquire properties or portfolios of properties through tax deferred contribution transactions in exchange for partnership interests in the Operating Partnership, which may result in stockholder dilution. This acquisition structure may have the effect of, among other things, reducing the amount of tax depreciation we could deduct over the tax life of the acquired properties, and may require that we agree to protect the contributors' ability to defer recognition of taxable gain through restrictions on our ability to dispose of the acquired properties and/or the allocation of partnership debt to the contributors to maintain their tax bases. These restrictions could limit our ability to sell an asset at a time, or on terms, that would be favorable absent such restrictions.

#### RISKS RELATED TO OUR RELATIONSHIP WITH SMTA

A substantial number of SMTA's properties are leased to one tenant, Shopko, which has filed for bankruptcy protection.

On January 16, 2019, Shopko and its affiliates filed petitions for relief under Chapter 11 of the Bankruptcy Code. SMTA reported that, as of September 30, 2018, it leased 90 properties to Shopko, primarily pursuant to four master leases (relating to 33, 31, 21 and 4 properties, respectively) and one single site lease, under which SMTA received approximately \$3.6 million in contractual rent per month. SMTA reported that revenues generated from Shopko represented 18.3% of SMTA's Contractual Rent for the month ended September 30, 2018, and a significant portion of SMTA's estimated cash available for distribution is derived from rental revenues received from Shopko. Additionally, in January 2018, Spirit Realty, L.P. extended a senior secured term loan to Shopko in the amount of \$35.0 million, which was contributed to SMTA prior to the Spin-Off. The senior secured term loan matures in June 2020, bears interest at a rate of 12% per annum and requires repayment in consecutive quarterly installments of \$583,625, the first of which was paid in the fourth quarter 2018.

SMTA has reported that it does not expect to receive any additional rent payments from any of the properties leased to Shopko. Furthermore, the senior secured term loan extended to Shopko has been accelerated. Although SMTA intends to exercise and pursue all of its rights and remedies with respect to the senior secured term loan, there can be no assurances that there will be a recovery in whole or in part with respect to the \$34.4 million outstanding balance. As a result, SMTA's results of operations and financial condition will be significantly impacted by Shopko's bankruptcy. As of September 30, 2018, SMTA's Adjusted Debt to Annualized Adjusted EBITDA ratio was 9.6x and its Fixed Charge Coverage Ratio was 1.8x. SMTA's Fixed Charge Coverage Ratio does not reflect the impact of its amortizing debt principal payments. Had Shopko completely defaulted on its payments to SMTA at the beginning of the third quarter 2018, SMTA's Adjusted Debt to Annualized Adjusted EBITDA ratio as of September 30, 2018 would have been 12.4x and its Fixed Charge Coverage Ratio would have been 1.4x.

Because a significant portion of SMTA's estimated cash available for distribution is derived from rental revenues received from Shopko, Shopko's bankruptcy could limit or eliminate SMTA's ability to make distributions to its common stockholders, which could limit or eliminate SMTA's obligation and/or ability to make cash payments or distributions to us, as holders of 10% series A preferred shares of beneficial interest of SMTA ("SMTA Preferred Stock"), and could cause us to lose all or a part of the value of our investment in SMTA Preferred Stock. In addition, Shopko's bankruptcy could limit or eliminate SMTA's ability to make cash payments to us under the Asset Management Agreement, which could cause us to receive SMTA Preferred Stock in lieu of cash payment of the management fee, which would exacerbate the risks associated with our investment in SMTA Preferred Stock. See

“-Under certain circumstances, SMTA may pay us the management fee due under the Asset Management Agreement in SMTA Preferred Stock rather than cash, which

would adversely affect our cash flow, AFFO and AFFO per share, as well as increase the risks related to our ownership of SMTA Preferred Stock.”

We may not be able to collect amounts to which we are contractually entitled under the Asset Management Agreement or SMTA Preferred Stock upon a resolution of SMTA and/or a termination of the Asset Management Agreement.

On January 16, 2019, SMTA announced that its board of trustees has elected to accelerate SMTA’s previously announced strategic plan and has engaged advisors to explore strategic alternatives focused on maximizing shareholder value, including a sale of SMTA or Master Trust 2014, a merger or other potential alternatives. SMTA has not set a timetable for completion of the process.

There can be no assurance that SMTA’s exploration of strategic alternatives will result in any transaction or other alternative. Additionally, there can be no assurance that we will be able to collect amounts to which we are contractually entitled under the Asset Management Agreement or SMTA Preferred Stock in the event of a resolution of SMTA and/or a termination of the Asset Management Agreement.

Asset Management Agreement. Pursuant to the Asset Management Agreement, we are entitled to a termination fee upon occurrence of certain events and, if applicable thresholds are met, a promote payment in the event that the Asset Management Agreement is terminated (a) by SMTA without cause or (b) by us for cause (including upon a change in control of SMTA). Although SMTA has announced that its board of trustees has elected to accelerate its previously announced strategic plan, we cannot control a decision by SMTA’s board of trustees to terminate the Asset Management Agreement without cause or effect a change of control of SMTA. As a result, such termination could occur at a time when SMTA does not have sufficient cash to pay us the termination fee or a promote that we would otherwise be entitled to or at a time when the SMTA stockholder return threshold for the promote has not been met. Additionally, should the Asset Management Agreement be terminated without cause by us, or for cause by SMTA, we are not entitled to the termination fee or any otherwise applicable promote payment.

SMTA Preferred Stock. Pursuant to the terms of the SMTA Preferred Stock, SMTA must offer to purchase our shares of SMTA Preferred Stock at the liquidation preference, plus any accrued and unpaid dividends to, but not including, the payment date, upon the occurrence of a certain change of control events. However, if a change of control were to occur, SMTA may not have sufficient funds available at such time to pay the purchase price of our shares of SMTA Preferred Stock. Moreover, the payment of accrued dividends on the SMTA Preferred Stock will be subordinated to all of SMTA’s existing and future debt. SMTA reported that, as of September 30, 2018, it had approximately \$2.03 billion aggregate principal amount of indebtedness outstanding that would rank senior to the SMTA Preferred Stock. In the event of any liquidation, dissolution or winding up of SMTA, SMTA may have insufficient assets available to make distributions or payments of accrued dividends on the SMTA Preferred Stock. Additionally, SMTA may have insufficient assets to repay our investment in SMTA Preferred Stock.

Furthermore, if SMTA’s business, financial condition, liquidity and results of operations further deteriorate prior to any resolution of SMTA and/or a termination of the Asset Management Agreement, SMTA’s obligation and/or ability to make cash payments or distributions to us, including under the Asset Management Agreement and as holders of SMTA Preferred Stock, may be limited or eliminated and we could lose all or a part of the value of our investment in the SMTA Preferred Stock. See “Our relationship with SMTA involves certain risks and uncertainties, many of which are beyond our control” and the risk factors that follow.

Our relationship with SMTA involves certain risks and uncertainties, many of which are beyond our control.

Our relationship with SMTA involves certain risks and uncertainties, many of which are beyond our control. If any of the following risks, as well as others described in this report (including the risks and uncertainty associated with the reduction in rental revenues received by SMTA from Shopko), occur, SMTA’s business, financial condition, liquidity and results of operations could further deteriorate. As discussed in the risk factors that follow, if this were to happen, SMTA’s obligation and/or ability to make cash payments or distributions to us, including under the Asset Management Agreement and as holders of SMTA Preferred Stock, may be limited or eliminated and we could lose all or a part of the value of our investment in the SMTA Preferred Stock.

• SMTA may be unable to maintain sufficient liquidity to meet its obligations to us prior to the consummation of a strategic or alternative transaction, if any.

• SMTA’s tenants may fail to successfully operate their businesses, which could adversely affect SMTA.



A substantial portion of SMTA's properties are leased to unrated tenants, and the tools we, as external manager, use to measure the credit quality of such tenants may not be accurate.

Decrease in demand for retail and restaurant space may materially and adversely affect SMTA.

SMTA faces significant competition for tenants, which may decrease or prevent increases of the occupancy and rental rates of its properties.

SMTA reported that, as of September 30, 2018, it had approximately \$2.03 billion aggregate principal amount of indebtedness outstanding, which may expose it to the risk of default under its debt obligations, limit its ability to obtain additional financing and affect the market price of shares of SMTA's common stock and, consequently, our ability to earn a cash promote payment.

Although SMTA's board of trustees has elected to accelerate SMTA's previously announced strategic plan and explore strategic alternatives, it may change that decision without stockholder approval, and SMTA may pursue other objectives, including those that would increase SMTA's leverage, which may increase SMTA's risk of default under its debt obligations.

Although SMTA intends to exercise and pursue all of its rights and remedies with respect to the senior secured term loan extended to Shopko, there can be no assurances that there will be a recovery in whole or in part.

Current market conditions could adversely affect SMTA's ability to refinance existing indebtedness or obtain additional financing for growth on acceptable terms or at all.

Failure to maintain SMTA's qualification as a REIT would have significant adverse consequences to SMTA, the market price of shares of SMTA's common stock and, consequently, our ability to earn a cash promote payment.

Under certain circumstances, SMTA may pay us the management fee due under the Asset Management Agreement in SMTA Preferred Stock rather than cash, which would adversely affect our cash flow, AFFO and AFFO per share, as well as increase the risks related to our ownership of SMTA Preferred Stock.

Pursuant to the Asset Management Agreement, SMTA is required to pay us an annual management fee of \$20.0 million, payable in equal monthly installments, in arrears. However, in the event of a "Management Fee PIK Event," all or a portion of such fee may be paid in SMTA Preferred Stock. A "Management Fee PIK Event" means (i) a good faith determination by SMTA's board of trustees that forgoing the payment of all or any portion of the monthly installment of the management fee is necessary for SMTA to have sufficient funds to declare and pay dividends required to be paid in cash in order for it to maintain its status as a REIT under the Internal Revenue Code of 1986, as amended, and to avoid incurring income or excise taxes, in which case such necessary portion shall be paid in SMTA Preferred Stock, or (ii) the occurrence and continuation of an "Early Amortization Event," "Event of Default" or "Sweep Period," in each case as defined pursuant under the Second Amended and Restated Master Indenture, dated as of May 20, 2014, among Spirit Master Funding, LLC, Spirit Master Funding II, LLC, Spirit Master Funding III, LLC and Citibank, N.A., as amended and supplemented from time to time, in which case our entire monthly installment will be paid in SMTA Preferred Stock. Receiving payment of the management fee in SMTA Preferred Stock, rather than cash, would adversely affect our cash flow, AFFO and AFFO per share, as well as increase the risks related to our ownership of SMTA Preferred Stock.

Many of the factors that could trigger a Management Fee PIK Event are beyond our control, including the ability of SMTA's tenants to successfully operate their businesses. As is the case with our investments, the success of SMTA's investments is materially dependent on the financial stability of its tenants' financial condition and leasing practices. See "-Our tenants may fail to successfully operate their businesses, which could adversely affect us." At any given time, SMTA's tenants may experience a downturn in their business that causes them to delay lease commencement, decline to extend a lease upon its expiration, fail to make rental payments when due, become insolvent or declare bankruptcy. A substantial number of SMTA's properties are leased to one tenant, Shopko, and rental revenues received from Shopko represent a significant portion of SMTA's estimated cash available for distribution. See "-A substantial number of SMTA's properties are leased to one tenant, Shopko, which has filed for bankruptcy protection." Because a significant portion of SMTA's estimated cash available for distribution are derived from rental revenues received from Shopko, Shopko's bankruptcy could limit or eliminate SMTA's ability to make distributions to its common stockholders, which could trigger a Management Fee PIK Event.





Additionally, SMTA has a substantial amount of debt. Payments of principal and cash interest expense and financial covenants relating to SMTA's indebtedness may limit or eliminate its ability and/or obligation to make cash distributions to us as holders of SMTA Preferred Stock and, if a Management Fee PIK Event is triggered, pay us the asset management fee due under the Asset Management Agreement in cash. See "-SMTA has significant indebtedness outstanding."

SMTA has significant indebtedness outstanding.

SMTA reported that, as of September 30, 2018, it had approximately \$2.03 billion aggregate principal amount of indebtedness outstanding, all of which incurs interest at a fixed rate. SMTA may also incur significant additional debt to finance future investment activities. As of September 31, 2018, SMTA's Adjusted Debt to Annualized Adjusted EBITDA ratio was 9.6x and its Fixed Charge Coverage Ratio was 1.8x. SMTA's Fixed Charge Coverage Ratio does not reflect the impact of its amortizing debt principal payments. As noted above, as a result of Shopko's bankruptcy filing, SMTA does not expect to receive any additional rent payments from any of the properties leased to Shopko. Had Shopko completely defaulted on its payments to SMTA at the beginning of the third quarter of 2018, SMTA's Adjusted Debt to Annualized Adjusted EBITDA ratio as of September 30, 2018 would have been 12.4x and its Fixed Charge Coverage Ratio would have been 1.4x. Payments of principal and cash interest expense and financial covenants relating to SMTA's indebtedness may limit or eliminate its ability and/or obligation to make cash distributions to us as holders of SMTA Preferred Stock and, if a Management Fee PIK event is triggered, pay us the asset management fee due under the Asset Management Agreement in cash. SMTA's level of debt and the limitations imposed on SMTA by its debt agreements could have various other significant adverse consequences.

SMTA's ability to pay dividends is limited by the requirements of Maryland law.

SMTA's ability to pay dividends on the SMTA Preferred Stock is limited by the laws of Maryland. Under applicable Maryland law, a Maryland real estate investment trust generally may not make a distribution if, after giving effect to the distribution, the trust would not be able to pay its debts as the debts become due in the usual course of business, or the trust's total assets would be less than the sum of its total liabilities plus, unless the trust's declaration of trust provides otherwise, the amount that would be needed, if the trust were dissolved at the time of the distribution, to satisfy the preferential rights upon dissolution of shareholders whose preferential rights are superior to those receiving the distribution. Accordingly, SMTA generally may not make a distribution on the SMTA Preferred Stock if, after giving effect to the distribution, SMTA would not be able to pay its debts as they become due in the usual course of business or SMTA's total assets would be less than the sum of its 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 any class or series of preferred shares then outstanding, if any, with preferences senior to those of the SMTA Preferred Stock.

In the event of a non-payment of dividends on our SMTA Preferred Stock, we have limited rights and our cash flow, AFFO and AFFO per share would be adversely affected.

Our rights in the event of a non-payment of dividends on our SMTA Preferred Stock are limited to being granted the ability to elect (voting separately as a class together with holders of all classes and series of parity preferred shares upon which like voting rights have been conferred and are exercisable) two additional trustees to SMTA's board of trustees in the event that six quarterly dividends (whether or not consecutive) payable on the SMTA Preferred Stock are in arrears. In addition, in the event of a non-payment of dividends on our SMTA Preferred Stock, our cash flow, AFFO and AFFO per share would be adversely affected.

The SMTA Preferred Stock is illiquid.

The SMTA Preferred Stock is not traded on any securities exchange or other market, and there is no established public trading market for the SMTA Preferred Stock, nor is there any assurance that one may develop. Therefore, it will be difficult for us to sell our shares of SMTA Preferred Stock promptly, or at all, and if we are able to sell such shares, we may have to sell them at a substantial discount.

We have no history operating as an external manager to another entity, and our inability to do so successfully could impact our business and reputation.

In connection with the Spin-Off, we entered into an Asset Management Agreement with SMTA, pursuant to which we agreed to act as the external manager for SMTA. We have no history operating as an external manger to another entity. SMTA has no employees and is completely reliant on us for the effective operation of its business. The officers and

other individuals who perform services for SMTA are our employees, including certain of our key employees. Such employees may dedicate substantial time to and become distracted by financial or operational developments related to SMTA, including in connection with Shopko's bankruptcy filing and SMTA's board of trustees' decision to accelerate its strategic plan, and we may experience difficulties in appropriately allocating resources between us and SMTA, which could materially and adversely affect our business and our ability to achieve our objectives. Additionally, the base management fee that we receive under the Asset Management Agreement is fixed for the first three years, and such fee may not reflect our actual expenses or time spent externally managing SMTA.

Alternatively, we may dedicate substantial time to and become distracted by financial or operational developments related to our business and activities unrelated to SMTA. Should we fail to allocate sufficient resources to perform our responsibilities to SMTA for any reason, SMTA may be unable to achieve its objectives, which could, among other things, impact our ability to receive fees, including a promote payment, under the Asset Management Agreement. Any potentially negative matters concerning SMTA could harm our reputation and business and materially and adversely affect the trading price of our common stock.

Under the Asset Management Agreement, SMTA has a license to use the name "Spirit." Because news coverage of events often fail to appropriately distinguish between legal entities with similar names, investors may impute to us any unfavorable information about SMTA, including financial or operational developments related to SMTA and/or the trading price of SMTA's common stock that are unrelated to our economic relationship with and interest in SMTA, that could harm our reputation and business and materially and adversely affect the trading price of our common stock.

Following the Spin-Off, we retained certain obligations and liabilities related to assets now owned by SMTA.

**Master Trust 2014 Performance Undertaking.** Following the Spin-Off, we have agreed to act as the "support provider" under Master Trust 2014, which was contributed to SMTA in connection with the Spin-Off, undertaking contingent financial and other liability, both relating to asset transfers that occurred in the past and to asset transfers that may occur in the future. Pursuant to this performance undertaking, we (i) guarantee the payment and performance of the cure, repurchase, exchange and indemnification obligations of the applicable originators under property transfer agreements, (ii) are deemed to have made the same representations each issuer made on each series closing date with respect to the assets that were in the collateral pool as of such date, (iii) are deemed to make the same representations each issuer is required to make with respect to each transfer of assets from time to time and (iv) agree to perform all covenants, agreements, terms, conditions and indemnities to be performed and observed by each issuer pursuant to the applicable environmental indemnity agreement with respect to environmental violations arising or existing on or prior to the date of the transfer of the relevant property to the collateral pool. In the case of a breach of a deemed representation relating to (ii) or (iii) above, or if there is another defect relating to the affected property (e.g., missing documentation) and such breach or defect materially and adversely affects the value of the related property, we are required to cure such defect or repurchase the property. With respect to the obligations described under (iv), the obligation to remedy any environmental violations are our direct obligations. We have the right to transfer these obligations to an eligible successor support provider, which can include SMTA, two years after the Spin-Off, or upon the occurrence of certain events. Prior to the time of such transfer, SMTA is required to reimburse us for any liability related to these obligations. However, SMTA may not have the resources or cash available to satisfy such indemnification and reimbursement obligations.

**Asset Management Agreement.** Pursuant to the Asset Management Agreement, we are required, to the full extent lawful, to reimburse, indemnify and hold SMTA, its stockholders, trustees, officers and employees and each other person, if any, controlling SMTA, harmless of and from any and all expenses, losses, damages, liabilities, demands, charges and claims of any nature whatsoever (including attorneys' fees) in respect of or arising from any of our acts or omissions of constituting bad faith, willful misconduct or gross negligence. SMTA must, to the full extent lawful, reimburse, indemnify and hold harmless us, our affiliates, members, managers, officers and employees, sub-advisers and each other person, if any, controlling us, from any and all expenses, losses, damages, liabilities, demands, charges and claims of any nature whatsoever (including attorneys' fees) in respect of or arising from any acts or omissions of such indemnified party made in good faith in the performance of our duties under the Asset Management Agreement and not constituting such indemnified party's bad faith, willful misconduct or gross negligence. Additionally, SMTA is required to reimburse us for certain expenses incurred in connection with the performance of our duties under the

Asset Management Agreement. However, SMTA may not have the resources or cash available to satisfy such indemnification and reimbursement obligations.

Property Management and Servicing Agreement. Pursuant to the Second Amended and Restated Property Management and Servicing Agreement dated May 20, 2014, by and among Spirit Realty, L.P., Spirit Master Funding, LLC, Spirit Master Funding II, LLC, Spirit Master Funding III, LLC and Midland Loan Services, a division of PNC Bank, National Association (as amended, the "Property Management and Servicing Agreement") related to the assets under Master Trust 2014, we, as property manager, are required to make certain advances in the case of shortfalls in amounts available to pay principal and interest or with respect to customary out-of-pocket expenses in order to protect the mortgaged properties of the note issuers, such as insurance premiums, tenant eviction costs and expenses necessary to preserve the security interest of the indenture trustee.

We may not continue to receive fees under the Property Management and Servicing Agreement with SMTA.

We provide property and management services and special services for Master Trust 2014. We may be terminated as property manager and special servicer for cause following the occurrence of certain property manager replacement events. Additionally, due to the risks described above, SMTA may be unable to pay our fees.

There are conflicts of interest in our relationship with SMTA.

There are conflicts of interest in our relationship with SMTA insofar as we have investment objectives that overlap with those of SMTA. We have instituted a proprietary Spirit Property Ranking Model that we also apply to SMTA's portfolio. The Spirit Property Ranking Model is used annually to rank all properties across twelve factors and weightings, consisting of both real estate quality scores and credit underwriting criteria, in order to benchmark property quality, identify asset recycling opportunities and to enhance acquisition or disposition decisions. We also update the Spirit Heat Map that is used for us and SMTA, which analyzes tenant industries across Porter's Five Forces and potential causes of technological disruption to identify tenant industries which Spirit believes to have good fundamentals for future performance. We use a rotation system when considering potential acquisitions by SMTA and us, subject to available liquidity and certain other criteria. As a result, we may not be presented with certain investment opportunities that may be appropriate for us. Additionally, we own real estate assets in the same geographic regions as SMTA and may compete with it for tenants. This competition may affect our ability to attract and retain tenants and may reduce the rent we are able to charge.

In addition, we may engage (subject to our investment manual and conflicts of interest policy) in material transactions with SMTA, which may present an actual, potential or perceived conflict of interest. It is possible that actual, potential or perceived conflicts of interest could give rise to investor dissatisfaction, litigation or regulatory enforcement actions. Appropriately dealing with conflicts of interest is complex and difficult, and our reputation could be damaged if we fail, or appear to fail, to deal appropriately with one or more potential, actual or perceived conflicts of interest. Regulatory scrutiny of, or litigation in connection with, conflicts of interest could have a material adverse effect on our reputation, which could materially adversely affect our business in a number of ways, including difficulty in raising additional funds, a reluctance of counterparties to do business with us, a decrease in the prices of our equity securities and a resulting risk of litigation and regulatory enforcement actions.

Our interests could be diluted by the issuance of additional preferred shares, including additional SMTA Preferred Stock, and by other transactions.

SMTA may issue additional SMTA Preferred Stock or shares of another class or series of preferred shares ranking on parity with (or, upon the affirmative vote or consent of the holders of at least two-thirds of the outstanding SMTA Preferred Stock and each other class or series of parity preferred shares with which the holders of SMTA Preferred Stock are entitled to vote together as a single class, voting together as a single class, senior to) the SMTA Preferred Stock with respect to the payment of dividends and the distribution of assets upon liquidation, dissolution or winding up. None of the provisions relating to the SMTA Preferred Stock relate to or limit SMTA's indebtedness, nor provide us protection, as a holder of the SMTA Preferred Stock, in the event of a highly leveraged or other transaction, including a merger or the sale, lease or conveyance of all or substantially all of SMTA's assets or business, that might adversely affect us as a holders of the SMTA Preferred Stock. These factors may affect the recovery value or market price of the SMTA Preferred Stock.



## RISKS RELATED TO OUR INDEBTEDNESS

We have approximately \$2.08 billion principal balance of indebtedness outstanding, which may expose us to the risk of default under our debt obligations, limit our ability to obtain additional financing or affect the market price of our common stock or debt securities.

As of December 31, 2018, the total principal balance outstanding on our indebtedness was approximately \$2.08 billion, of which the \$566.3 million outstanding under the 2015 Credit Facility and 2015 Term Loan incurs interest at a variable rate. We may also incur significant additional debt to finance future investment activities. Payments of principal and interest on borrowings may leave us with insufficient cash resources to meet our cash needs or make the distributions to our common stockholders necessary to maintain our REIT qualification. Our level of debt and the limitations imposed on us by our debt agreements could have significant adverse consequences, including the following:

- our cash flow may be insufficient to meet our required principal and interest payments;
- cash interest expense and financial covenants relating to our indebtedness may limit or eliminate our ability to make distributions to our common stockholders;
- we may be unable to borrow additional funds as needed or on favorable terms, which could, among other things, adversely affect our ability to capitalize upon acquisition opportunities or meet operational needs;
- we may be unable to refinance our indebtedness at maturity or the refinancing terms may be less favorable than the terms of our original indebtedness;
- for our variable interest rate debt, increases in interest rates could increase our interest expense;
- we may be unable to hedge floating rate debt, counterparties may fail to honor their obligations under any hedge agreements we enter into, such agreements may not effectively hedge interest rate fluctuation risk, and, upon the expiration of any hedge agreements we enter into, we would be exposed to then-existing market rates of interest and future interest rate volatility;
- we may be forced to dispose of properties, possibly on unfavorable terms or in violation of certain covenants to which we may be subject;
- we may default on our obligations and the lenders or mortgagees may foreclose on our properties or our interests in the entities that own the properties that secure their loans and receive an assignment of rents and leases;
- we may be restricted from accessing some of our excess cash flow after debt service if certain of our tenants fail to meet certain financial performance metric thresholds;
- we may violate restrictive covenants in our loan documents, which would entitle the lenders to accelerate our debt obligations; and
- our default under any loan with cross-default provisions could result in a default on other indebtedness.

Changes in our leverage ratios may also negatively impact the market price of our equity or debt securities.

Furthermore, foreclosures could create taxable income without accompanying cash proceeds, which could hinder our ability to meet the REIT distribution requirements imposed by the Code.

Current market conditions could adversely affect our ability to refinance existing indebtedness or obtain additional financing for growth on acceptable terms or at all.

The credit markets can experience significant price volatility, displacement and liquidity disruptions, including the bankruptcy, insolvency or restructuring of certain financial institutions. These circumstances could materially impact liquidity in the financial markets, making financing terms for borrowers less attractive, and in certain cases, result in the unavailability of various types of debt financing. As a result, we may be unable to obtain debt financing on favorable terms or at all or fully refinance maturing indebtedness with new indebtedness. Reductions in our available borrowing capacity or inability to obtain credit when required or when business conditions warrant could materially and adversely affect us.

Furthermore, if prevailing interest rates or other factors at the time of refinancing result in higher interest rates upon refinancing, then the interest expense relating to that refinanced indebtedness would increase. Higher interest rates on newly incurred debt may negatively impact us as well. If interest rates increase, our interest costs and overall costs of capital will increase, which could materially and adversely affect us. Total debt service, including scheduled principal maturities and interest, for 2019 and 2020 is \$1.06 billion and \$61.2 million, respectively. Debt service for 2019 includes \$10.1 million for the acceleration of principal payable following an event of default under one CMBS loan



with a stated

30

---

maturity in 2018. Debt service for 2019 also includes principal on the 2015 Credit Facility and 2015 Term Loan, which were paid-off in conjunction with the execution of the 2019 Facilities Agreement.

Some of our financing arrangements involve balloon payment obligations.

Some of our financings require us to make a lump-sum or “balloon” payment at maturity. Our ability to make any balloon payment is uncertain and may depend on our ability to obtain additional financing or our ability to sell our properties. At the time the balloon payment is due, we may or may not be able to refinance the balloon payment on terms as favorable as the original loan or sell our properties at a price sufficient to make the balloon payment, if at all. If the balloon payment is refinanced at a higher rate, it will reduce or eliminate any income from our properties. Our inability to meet a balloon payment obligation, through refinancing or sale proceeds, or refinancing on less attractive terms could materially and adversely affect us. We have balloon maturities, excluding debt extendible at our option, of \$412.6 million in 2019, including \$10.1 million on a defaulted loan, and none in 2020. If we are unable to refinance these maturities or otherwise retire the indebtedness by that time, we could be materially adversely affected, and could be forced to relinquish the related collateral.

The agreements governing our indebtedness contain restrictions and covenants which may limit our ability to enter into or obtain funding for certain transactions, operate our business or make distributions to our preferred and common stockholders.

The agreements governing our indebtedness contain restrictions and covenants that limit or will limit our ability to operate our business. These covenants, as well as any additional covenants to which we may be subject in the future because of additional indebtedness, could cause us to forgo investment opportunities, reduce or eliminate distributions to our preferred and common stockholders or obtain financing that is more expensive than financing we could obtain if we were not subject to the covenants. In addition, the agreements may have cross default provisions, which provide that a default under one of our financing agreements would lead to a default on some or all of our debt financing agreements.

If an event of default occurs under certain of our CMBS loans, if the master tenants at the properties that secure the CMBS loans fail to maintain certain EBITDAR ratios or if an uncured monetary default exists under the master leases, then a portion of or all of the cash which would otherwise be distributed to us may be restricted by the lenders and unavailable to us until the terms are cured or the debt refinanced. If the financial performance of the collateral for our indebtedness under our asset-backed securitization program fails to achieve certain financial performance criteria, cash from such collateral may be unavailable to us until the terms are cured or the debt refinanced. Such cash sweep triggering events have occurred previously and may be ongoing from time to time. The occurrence of these events limit the amount of cash available to us for use in our business and could limit or eliminate our ability to make distributions to our common stockholders.

The covenants and other restrictions under our debt agreements affect, among other things, our ability to:

- incur indebtedness;
- create liens on assets;
- sell or substitute assets;
- modify certain terms of our leases;
- prepay debt with higher interest rates;
- manage our cash flows; and
- make distributions to equity holders.

Additionally, these restrictions may adversely affect our operating and financial flexibility and may limit our ability to respond to changes in our business or competitive environment, all of which may materially and adversely affect us.

#### RISKS RELATED TO OUR ORGANIZATIONAL STRUCTURE

Our charter and bylaws and Maryland law contain provisions that may delay, defer or prevent a change of control transaction, even if such a change in control may be in the interest of our stockholders.

Our charter contains certain restrictions on ownership and transfer of our stock. Our charter contains various provisions that are intended to preserve our qualification as a REIT and, subject to certain exceptions, authorize our directors to



take such actions as are necessary or appropriate to preserve our qualification as a REIT. For example, our charter prohibits the actual, beneficial or constructive ownership by any person of more than 9.8% in value or number of shares, whichever is more restrictive, of the outstanding shares of our common stock or more than 9.8% in value of the aggregate of the outstanding shares of all classes and series of our stock. Our Board of Directors, in its sole and absolute discretion, may exempt a person, prospectively or retroactively, from these ownership limits if certain conditions are satisfied. The restrictions on ownership and transfer of our stock may:

- discourage a tender offer or other transactions or a change in management or of control that might involve a premium price for our common stock or that our stockholders otherwise believe to be in their best interests; or
- result in the transfer of shares acquired in excess of the restrictions to a trust for the benefit of a charitable beneficiary and, as a result, the forfeiture by the acquirer of the benefits of owning the additional shares.

We could increase the number of authorized shares of stock, classify and reclassify un-issued stock and issue stock without stockholder approval. Our Board of Directors, without stockholder approval, has the power under our charter to amend our charter to increase the aggregate number of shares of stock or the number of shares of stock of any class or series that we are authorized to issue, to authorize us to issue authorized but un-issued shares of our common stock or preferred stock and to classify or reclassify any un-issued shares of our common stock or preferred stock into one or more classes or series of stock and to set the terms of such newly classified or reclassified shares. As a result, we may issue one or more series or classes of common stock or preferred stock with preferences, dividends, powers and rights, voting or otherwise, that are senior to, or otherwise conflict with, the rights of our common stockholders. Although our Board of Directors has no such intention at the present time, it could establish a class or series of common stock or preferred stock that could, depending on the terms of such series, delay, defer or prevent a transaction or a change of control that might involve a premium price for our common stock or otherwise be in the best interest of our stockholders.

Certain provisions of Maryland law could inhibit changes in control, which may discourage third parties from conducting a tender offer or seeking other change of control transactions that could involve a premium price for our common stock or that our stockholders otherwise believe to be in their best interest. Certain provisions of the MGCL may have the effect of inhibiting a third party from making a proposal to acquire us or of impeding a change of control under circumstances that otherwise could provide our common stockholders with the opportunity to realize a premium over the then-prevailing market price of such shares, including:

- “business combination” provisions that, subject to certain limitations, prohibit certain business combinations between us and an “interested stockholder” (defined generally as any person who beneficially owns 10% or more of the voting power of our shares or of an affiliate of ours or an affiliate or associate of ours who was the beneficial owner, directly or indirectly, of 10% or more of the voting power of our then outstanding voting stock at any time within a two-year period immediately prior to the date in question) or any affiliate of an interested stockholder for five years after the most recent date on which the stockholder becomes an interested stockholder, and thereafter impose fair price and/or super-majority and stockholder voting requirements on these combinations; and
- “control share” provisions that provide that a holder of “control shares” of our Company (defined as shares that, when aggregated with other shares controlled by the stockholder, entitle the stockholder to exercise one of three increasing ranges of voting power in electing directors) acquired in a “control share acquisition” (defined as the direct or indirect acquisition of ownership or control of outstanding “control shares”) has no voting rights with respect to those shares except to the extent approved by our stockholders by the affirmative vote of at least two-thirds of all the votes entitled to be cast on the matter, excluding all interested shares.

As permitted by the MGCL, we have elected, by resolution of our Board of Directors, to opt out of the business combination provisions of the MGCL and, pursuant to a provision in our bylaws, to exempt any acquisition of our stock from the control share provisions of the MGCL. However, our Board of Directors may by resolution elect to repeal the exemption from the business combination provisions of the MGCL and may by amendment to our bylaws opt into the control share provisions of the MGCL at any time in the future, whether before or after an acquisition of control shares.

Certain provisions of the MGCL permit our Board of Directors, without stockholder approval and regardless of what is currently provided in our charter or bylaws, to implement certain corporate governance provisions, some of which (for example, a classified board) are not currently applicable to us. These provisions may have the effect of limiting or

precluding a third party from making an unsolicited acquisition proposal for us or of delaying, deferring or preventing a change in control of us under circumstances that otherwise could be in the best interests of our stockholders. Our

charter contains a provision whereby we elect, at such time as we become eligible to do so, to be subject to the provisions of Title 3, Subtitle 8 of the MGCL relating to the filling of vacancies on our Board of Directors.

Termination of the employment agreements with certain members of our senior management team could be costly and prevent a change in control of our company.

The employment agreements with certain members of our senior management team provide that if their employment with us terminates under certain circumstances (including in connection with a change in control of our company), we may be required to pay them significant amounts of severance compensation, thereby making it costly to terminate their employment. Furthermore, these provisions could delay or prevent a transaction or a change in control of our Company that might involve a premium paid for shares of our common stock or otherwise be in the best interests of our stockholders.

Our Board of Directors may change our investment and financing policies without stockholder approval and we may become more highly leveraged, which may increase our risk of default under our debt obligations.

Our investment and financing policies are exclusively determined by our Board of Directors. Accordingly, our stockholders do not control these policies. Further, our organizational documents do not limit the amount or percentage of indebtedness, funded or otherwise, that we may incur. Our Board of Directors may alter or eliminate our current policy on borrowing at any time without stockholder approval. If this policy changed, we could become more highly leveraged, which could result in an increase in our debt service. Higher leverage also increases the risk of default on our obligations. In addition, a change in our investment policies, including the manner in which we allocate our resources across our portfolio or the types of assets in which we seek to invest, may increase our exposure to interest rate risk, real estate market fluctuations and liquidity risk. Changes to our policies with regards to the foregoing could materially and adversely affect us.

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

As permitted by Maryland law, our charter limits the liability of our directors and officers to us and our stockholders for money damages, except for liability resulting from:

- actual receipt of an improper benefit or profit in money, property or services; or
- active and deliberate dishonesty by the director or officer that was established by a final judgment as being material to the cause of action adjudicated.

As a result, we and our stockholders have rights against our directors and officers that are more limited than might otherwise exist. Accordingly, in the event that actions taken in good faith by any of our directors or officers impede the performance of our company, our stockholders' and our ability to recover damages from such director or officer will be limited. In addition, our charter authorizes us to obligate our company, and our bylaws require us, to indemnify our directors and officers for actions taken by them in those and certain other capacities to the maximum extent permitted by Maryland law.

We are a holding company with no direct operations and will rely on funds received from the Operating Partnership to pay liabilities.

We are a holding company and conduct substantially all of our operations through the Operating Partnership. We do not have, apart from an interest in the Operating Partnership, any independent operations. As a result, we rely on distributions from the Operating Partnership to pay any dividends we might declare on shares of our common stock. We also rely on distributions from the Operating Partnership to meet any of our obligations, including any tax liability on taxable income allocated to us from the Operating Partnership. In addition, because we are a holding company, stockholder claims will be structurally subordinated to all existing and future liabilities and obligations (whether or not for borrowed money) of the Operating Partnership and its subsidiaries. Therefore, in the event of our bankruptcy, liquidation or reorganization, our assets and those of the Operating Partnership and its subsidiaries will be able to satisfy the claims of our stockholders only after all of our and the Operating Partnership's and its subsidiaries' liabilities and obligations have been paid in full.

We own directly or indirectly 100% of the interests in the Operating Partnership. However, in connection with our future acquisition of properties or otherwise, we may issue partnership interests of the Operating Partnership to third parties. Such issuances would reduce our ownership in the Operating Partnership. Because our stockholders will not directly



own partnership interests of the Operating Partnership, they will not have any voting rights with respect to any such issuances or other partnership level activities of the Operating Partnership.

Conflicts of interest could arise in the future between the interests of our stockholders and the interests of holders of partnership interests in the Operating Partnership, which may impede business decisions that could benefit our stockholders.

Conflicts of interest could arise in the future as a result of the relationships between us and our affiliates, on the one hand, and the Operating Partnership or any future partner thereof, on the other. Our directors and officers have duties to our company under applicable Maryland law in connection with the management of our company. At the same time, one of our wholly-owned subsidiaries, OP Holdings, as the general partner of the Operating Partnership, has fiduciary duties and obligations to the Operating Partnership and its future limited partners under Delaware law and the partnership agreement of the Operating Partnership in connection with the management of the Operating Partnership. The fiduciary duties and obligations of OP Holdings, as general partner of the Operating Partnership, and its future partners may come into conflict with the duties of the directors and officers of our company.

Under the terms of the partnership agreement of the Operating Partnership, if there is a conflict between the interests of our stockholders on one hand and any future limited partners on the other, we will endeavor in good faith to resolve the conflict in a manner not adverse to either our stockholders or any future limited partners; provided, however, that for so long as we own a controlling interest in the Operating Partnership, any conflict that cannot be resolved in a manner not adverse to either our stockholders or any future limited partners shall be resolved in favor of our stockholders.

The partnership agreement also provides that the general partner will not be liable to the Operating Partnership, its partners or any other person bound by the partnership agreement for monetary damages for losses sustained, liabilities incurred or benefits not derived by the Operating Partnership or any future limited partner, except for liability for the general partner's intentional harm or gross negligence. Moreover, the partnership agreement provides that the Operating Partnership is required to indemnify the general partner and its members, managers, managing members, officers, employees, agents and designees from and against any and all claims that relate to the operations of the Operating Partnership, except (1) if the act or omission of the person was material to the matter giving rise to the action and either was committed in bad faith or was the result of active or deliberate dishonesty, (2) for any transaction for which the indemnified party received an improper personal benefit, in money, property or services or otherwise in violation or breach of any provision of the partnership agreement or (3) in the case of a criminal proceeding, if the indemnified person had reasonable cause to believe that the act or omission was unlawful.

#### RISKS RELATED TO TAXES AND OUR STATUS AS A REIT

Failure to qualify as a REIT would materially and adversely affect us and the value of our common stock.

We believe that we have been organized and have operated in a manner that has allowed us to qualify as a REIT for U.S. federal income tax purposes commencing with our taxable year ended December 31, 2005 and we intend to continue operating in such a manner. We have not requested and do not plan to request a ruling from the IRS that we qualify as a REIT and the statements in this Annual Report on Form 10-K are not binding on the IRS or any court. Therefore, we cannot guarantee that we have qualified as a REIT or that we will remain qualified as such in the future. If we lose our REIT status, we will face significant tax consequences that would substantially reduce our cash available for distribution to our stockholders for each of the years involved because:

- we would not be allowed a deduction for distributions to stockholders in computing our taxable income and would be subject to regular U.S. federal corporate income tax;

- we could be subject to the federal alternative minimum tax for tax years prior to 2018 and increased state and local taxes; and

- unless we are entitled to relief under applicable statutory provisions, we could not elect to be taxed as a REIT for four taxable years following the year during which we were disqualified.

Any such corporate tax liability could be substantial and would reduce our cash available for, among other things, our operations and distributions to stockholders. In addition, if we fail to qualify as a REIT, we will not be required to make distributions to our stockholders. As a result of all these factors, our failure to qualify as a REIT also could impair our ability to expand our business and raise capital, and could materially and adversely affect the trading price of our common stock.





Qualification as a REIT involves the application of highly technical and complex Code provisions for which there are only limited judicial and administrative interpretations. The determination of various factual matters and circumstances not entirely within our control may affect our ability to qualify as a REIT. In order to qualify as a REIT, we must satisfy a number of requirements, including requirements regarding the ownership of our stock, requirements regarding the composition of our assets and a requirement that at least 95% of our gross income in any year must be derived from qualifying sources, such as “rents from real property.” Also, we must make distributions to stockholders aggregating annually at least 90% of our REIT taxable income, determined without regard to the dividends paid deduction and excluding any net capital gains. In addition, legislation, new regulations, administrative interpretations or court decisions may materially and adversely affect our investors, our ability to qualify as a REIT for federal income tax purposes or the desirability of an investment in a REIT relative to other investments.

Even if we qualify as a REIT for federal income tax purposes, we may be subject to some federal, state and local income, property and excise taxes on our income or property and, in certain cases, a 100% penalty tax, in the event we sell property as a dealer. In addition, our TRSs will be subject to income tax as regular corporations in the jurisdictions in which they operate.

If SMTA fails to qualify as a REIT, we could cease to qualify as a REIT and suffer other adverse consequences. SMTA’s failure to qualify as a REIT could adversely affect our ability to qualify as a REIT. If SMTA failed to qualify as a REIT during the year of the Spin-Off, the income recognized by us in connection with the Spin-Off would not have constituted qualifying income for purposes of the 75% gross income test, which could have adversely affected our ability to qualify as a REIT for such year. In addition, if SMTA did not qualify as a REIT, or if SMTA’s REIT election terminates, the SMTA Preferred Stock would not qualify as a real estate asset for purposes of the REIT asset tests or produce qualifying income for purposes of the REIT 75% gross income test. In such case, we would need to restructure or otherwise dispose of our investment in the SMTA Preferred Stock to comply with the REIT requirements.

If the Operating Partnership fails to qualify as a partnership for federal income tax purposes, we would cease to qualify as a REIT and suffer other adverse consequences.

The Operating Partnership is currently treated as a partnership for federal income tax purposes and, therefore, is not subject to federal income tax on its income. Instead, each of its partners, including us, is allocated, and may be required to pay tax with respect to, such partner’s share of its income. We cannot assure you that the IRS will not challenge the status of the Operating Partnership or any other subsidiary partnership or limited liability company in which we own an interest as a disregarded entity or partnership for federal income tax purposes, or that a court would not sustain such a challenge. If the IRS were successful in treating the Operating Partnership or any such other subsidiary partnership or limited liability company as an entity taxable as a corporation for federal income tax purposes, we would fail to meet the gross income tests and certain of the asset tests applicable to REITs and, accordingly, we would likely cease to qualify as a REIT. Also, the failure of the Operating Partnership or any subsidiary partnerships or limited liability company to qualify as a disregarded entity or partnership for applicable income tax purposes could cause it to become subject to federal and state corporate income tax, which would reduce significantly the amount of cash available for debt service and for distribution to its partners or members, including us. Our ownership of TRSs is subject to certain restrictions, and we will be required to pay a 100% penalty tax on certain income or deductions if our transactions with our TRSs are not conducted on arm’s-length terms.

We own securities in TRSs and may acquire securities in additional TRSs in the future. If a TRS owns more than 35% of the total voting power or value of the outstanding securities of another corporation, such other corporation will also be treated as a TRS. Other than some activities relating to lodging and health care facilities, a TRS may generally engage in any business, including the provision of customary or non-customary services to tenants of its parent REIT. A TRS is subject to federal income tax as a regular C corporation. In addition, a 100% excise tax will be imposed on certain transactions between a TRS and its parent REIT that are not conducted on an arm’s length basis.

A REIT’s ownership of securities of a TRS is not subject to the 5% or 10% asset tests applicable to REITs. Not more than 25% of the value of our total assets may be represented by securities (including securities of TRSs), other than those securities includable in the 75% asset test, and not more than 20% of the value of our total assets may be represented by securities of TRSs. We anticipate that the aggregate value of the stock and securities of any TRS and other nonqualifying assets that we own will be less than 25% (or 20%, as applicable) of the value of our total assets,

and we will monitor the value of these investments to ensure compliance with applicable ownership limitations. In addition, we intend to structure our transactions with any TRSs that we own to ensure that they are entered into on

arm's length terms to avoid incurring the 100% excise tax described above. There can be no assurance, however, that we will be able to comply with the above limitations or to avoid application of the 100% excise tax discussed above. We may be forced to borrow funds to maintain our REIT status, and the unavailability of such capital on favorable terms at the desired times, or at all, may cause us to curtail our investment activities and/or to dispose of assets at inopportune times, which could materially and adversely affect us.

To qualify as a REIT, we generally must distribute to our stockholders at least 90% of our REIT taxable income each year, determined without regard to the dividends paid deduction and excluding any net capital gains, and we will be subject to regular corporate income taxes on our undistributed taxable income to the extent that we distribute less than 100% of our REIT taxable income, determined without regard to the dividends paid deduction and including any net capital gains, each year. In addition, we will be subject to a 4% nondeductible excise tax on the amount, if any, by which distributions paid by us in any calendar year are less than the sum of 85% of our ordinary income, 95% of our capital gain net income and 100% of our undistributed income from prior years. In order to maintain our REIT status and avoid the payment of income and excise taxes, we may need to borrow funds to meet the REIT distribution requirements even if the then prevailing market conditions are not favorable for these borrowings. These borrowing needs could result from, among other things, differences in timing between the actual receipt of cash and recognition of income for federal income tax purposes, or the effect of non-deductible capital expenditures, the creation of reserves or required debt or amortization payments. These sources, however, may not be available on favorable terms or at all. Our access to third-party sources of capital depends on a number of factors, including the market's perception of our growth potential, our current debt levels, the market price of our common stock, and our current and potential future earnings. We cannot assure you that we will have access to such capital on favorable terms at the desired times, or at all, which may cause us to curtail our investment activities and/or to dispose of assets at inopportune times, and could materially and adversely affect us.

The IRS may treat sale-leaseback transactions as loans, which could jeopardize our REIT status or require us to make an unexpected distribution.

The IRS may take the position that specific sale-leaseback transactions that we treat as leases are not true leases for federal income tax purposes but are, instead, financing arrangements or loans. If a sale-leaseback transaction were so re-characterized, we might fail to satisfy the REIT asset tests, the income tests or distribution requirements and consequently lose our REIT status effective with the year of re-characterization unless we elect to make an additional distribution to maintain our REIT status. The primary risk relates to our loss of previously incurred depreciation expenses, which could affect the calculation of our REIT taxable income and could cause us to fail the REIT distribution test that requires a REIT to distribute at least 90% of its REIT taxable income, determined without regard to the dividends paid deduction and excluding any net capital gain. In this circumstance, we may elect to distribute an additional dividend of the increased taxable income so as not to fail the REIT distribution test. This distribution would be paid to all stockholders at the time of declaration rather than the stockholders existing in the taxable year affected by the re-characterization.

Dividends payable by REITs generally do not qualify for the reduced tax rates available for some dividends, which may negatively affect the value of our shares.

Income from "qualified dividends" payable to U.S. stockholders that are individuals, trusts and estates are generally subject to tax at preferential rates, currently at a maximum federal rate of 20%. Dividends payable by REITs, however, generally are not eligible for the preferential tax rates applicable to qualified dividend income. Under the 2017 Tax Legislation, however, U.S. stockholders that are individuals, trusts and estates generally may deduct up to 20% of the ordinary dividends (e.g., dividends not designated as capital gain dividends or qualified dividend income) received from a REIT for taxable years beginning after December 31, 2017 and before January 1, 2026. Although this deduction reduces the effective tax rate applicable to certain dividends paid by REITs (generally to 29.6% assuming the shareholder is subject to the 37% maximum rate), such tax rate is still higher than the tax rate applicable to corporate dividends that constitute qualified dividend income. Accordingly, investors who are individuals, trusts and estates may perceive investments in REITs to be relatively less attractive than investments in the stocks of non-REIT corporations that pay dividends, which could materially and adversely affect the value of the shares of REITs, including the per share trading price of our common stock.



The tax imposed on REITs engaging in “prohibited transactions” may limit our ability to engage in transactions which would be treated as sales for federal income tax purposes.

A REIT’s net income from prohibited transactions is subject to a 100% penalty tax. In general, prohibited transactions are sales or other dispositions of property, other than foreclosure property, held primarily for sale to customers in the ordinary course of business. Although we do not intend to hold any properties that would be characterized as held for sale to customers in the ordinary course of our business, unless a sale or disposition qualifies under certain statutory safe harbors, such characterization is a factual determination and no guarantee can be given that the IRS would agree with our characterization of our properties or that we will always be able to make use of the available safe harbors. Complying with REIT requirements may affect our profitability and may force us to liquidate or forgo otherwise attractive investments.

To qualify as a REIT, we must continually satisfy tests concerning, among other things, the nature and diversification of our assets, the sources of our income and the amounts we distribute to our stockholders. We may be required to liquidate or forgo otherwise attractive investments in order to satisfy the asset and income tests or to qualify under certain statutory relief provisions. We also may be required to make distributions to stockholders at disadvantageous times or when we do not have funds readily available for distribution. As a result, having to comply with the distribution requirement could cause us to: (1) sell assets in adverse market conditions; (2) borrow on unfavorable terms; or (3) distribute amounts that would otherwise be invested in future acquisitions, capital expenditures or repayment of debt. Accordingly, satisfying the REIT requirements could materially and adversely affect us. Moreover, if we are compelled to liquidate our investments to meet any of these asset, income or distribution tests, or to repay obligations to our lenders, we may be unable to comply with one or more of the requirements applicable to REITs or may be subject to a 100% tax on any resulting gain if such sales constitute prohibited transactions.

As a result of acquiring C corporations in carry-over basis transactions, we may inherit material tax liabilities and other tax attributes from such acquired corporations, and we may be required to distribute earnings and profits. From time to time, we have and may continue to acquire C corporations in transactions in which the basis of the corporations’ assets in our hands is determined by reference to the basis of the assets in the hands of the acquired corporations, or carry-over basis transactions.

If we acquire any asset from a corporation that is or has been a C corporation in a carry-over basis transaction, and we subsequently recognize gain on the disposition of the asset during the five-year period beginning on the date on which we acquired the asset, then we will be required to pay tax at the regular corporate tax rate on this gain to the extent of the excess of (1) the fair market value of the asset over (2) our adjusted basis in the asset, in each case determined as of the date on which we acquired the asset. Any taxes we pay as a result of such gain would reduce the amount available for distribution to our stockholders. The imposition of such tax may require us to forgo an otherwise attractive disposition of any assets we acquire from a C corporation in a carry-over basis transaction, and as a result may reduce the liquidity of our portfolio of investments. In addition, in such a carry-over basis transaction, we will succeed to any tax liabilities and earnings and profits of the acquired C corporation. To qualify as a REIT, we must distribute any non-REIT earnings and profits by the close of the taxable year in which such transaction occurs. Any adjustments to the acquired corporation’s income for taxable years ending on or before the date of the transaction, including as a result of an examination of the corporation’s tax returns by the IRS, could affect the calculation of the corporation’s earnings and profits. If the IRS were to determine that we acquired non-REIT earnings and profits from a corporation that we failed to distribute prior to the end of the taxable year in which the carry-over basis transaction occurred, we could avoid disqualification as a REIT by paying a “deficiency dividend.” Under these procedures, we generally would be required to distribute any such non-REIT earnings and profits to our stockholders within 90 days of the determination and pay a statutory interest charge at a specified rate to the IRS. Such a distribution would be in addition to the distribution of REIT taxable income necessary to satisfy the REIT distribution requirement and may require that we borrow funds to make the distribution even if the then-prevailing market conditions are not favorable for borrowings. In addition, payment of the statutory interest charge could materially and adversely affect us. Legislative or other actions affecting REITs could have a negative effect on us.

The rules dealing with federal income taxation are constantly under review by persons involved in the legislative process and by the IRS and the U.S. Department of the Treasury. Changes to the tax laws, with or without retroactive application, could materially and adversely affect our investors or us. We cannot predict how changes in the tax laws

might affect

37

---

our investors or us. New legislation, Treasury Regulations, administrative interpretations or court decisions could significantly and negatively affect our ability to qualify as a REIT or the federal income tax consequences of such qualification, or the federal income tax consequences of an investment in us. Also, the law relating to the tax treatment of other entities, or an investment in other entities, could change, making an investment in such other entities more attractive relative to an investment in a REIT.

The 2017 Tax Legislation has significantly changed the U.S. federal income taxation of U.S. businesses and their owners, including REITs and their stockholders. Changes made by the 2017 Tax Legislation that could affect the Company and its stockholders include:

- temporarily reducing individual U.S. federal income tax rates on ordinary income; the highest individual U.S. federal income tax rate has been reduced from 39.6% to 37% for taxable years beginning after December 31, 2017 and before January 1, 2026;

- permanently eliminating the progressive corporate tax rate structure, which previously imposed a maximum corporate tax rate of 35%, and replacing it with a flat corporate tax rate of 21%;

- permitting a deduction for certain pass-through business income, including dividends received by our stockholders from us that are not designated by us as capital gain dividends or qualified dividend income, which will allow individuals, trusts, and estates to deduct up to 20% of such amounts for taxable years beginning after December 31, 2017 and before January 1, 2026;

- reducing the highest rate of withholding with respect to our distributions to non-U.S. stockholders that are treated as attributable to gains from the sale or exchange of U.S. real property interests from 35% to 21%;

- limiting our deduction for net operating losses arising in taxable years beginning after December 31, 2017 to 80% of our REIT taxable income (determined without regard to the dividends paid deduction);

- generally limiting the deduction for net business interest expense in excess of 30% of a business's "adjusted taxable income," except for taxpayers that engage in certain real estate businesses (including most equity REITs) and elect out of this rule (provided that such electing taxpayers must use an alternative depreciation system with longer depreciation periods); and

- eliminating the corporate alternative minimum tax.

Many of these changes that are applicable to us are effective with our 2018 taxable year, without any transition periods or grandfathering for existing transactions. The legislation is unclear in many respects and could be subject to potential amendments and technical corrections, as well as interpretations and implementing regulations by the Treasury and IRS, any of which could lessen or increase the impact of the legislation. In addition, it is unclear how these U.S. federal income tax changes will affect state and local taxation, which often uses federal taxable income as a starting point for computing state and local tax liabilities.

While some of the changes made by the tax legislation may adversely affect the Company in one or more reporting periods and prospectively, other changes may be beneficial on a going forward basis. The Company continues to work with its tax advisers and auditors to determine the full impact that the recent tax legislation as a whole will have on the Company.

Item 1B. Unresolved Staff Comments

None.



## Item 2. Properties

## PROPERTY PORTFOLIO DIVERSIFICATION

1,462 99.7% 49 252 32

Properties Occupancy States Tenants Industries

## Diversification By Tenant

Tenant concentration represents the tenant's contribution to Contractual Rent of our owned real estate properties as of December 31, 2018:

Tenant <sup>(1)</sup>	Number of Properties	Total Square Feet (in thousands)	Percent of Contractual Rent	
Walgreen Company	39	575	3.4	%
Cajun Global, LLC	170	243	3.4	
The Home Depot, Inc.	7	821	2.9	
Alimentation Couche-Tard, Inc.	77	232	2.8	
CVS Caremark Corporation	34	422	2.4	
Life Time Fitness, Inc.	5	588	2.3	
GPM Investments, LLC	104	271	2.2	
Ferguson Enterprises, Inc.	7	1,003	1.7	
PetSmart, Inc.	4	1,016	1.7	
AB Acquisition, LLC	15	686	1.6	
Other	995	21,463	75.6	
Vacant	5	957	—	
Total	1,462	28,277	100.0	%

<sup>(1)</sup> Tenants represent legal entities ultimately responsible for obligations under the lease agreements or affiliated entities. Other tenants may operate the same or similar business concepts or brands as those set forth above.

## Diversification By Asset Type

Asset type concentration represents the type of asset's contribution to Contractual Rent of our owned real estate properties among different asset types as of December 31, 2018:

Asset Type	Number of Properties	Total Square Feet (in thousands)
Retail	1,395	21,185
Industrial	27	5,543
Office	37	1,120
Data Center	3	429
Total	1,462	28,277

## Diversification By Industry

Industry concentration represents the industry's contribution to Contractual Rent of our owned real estate properties as of December 31, 2018:

Industry	Number of Properties	Total Square Feet (in thousands)	Percent of Contractual Rent	
Convenience Stores	306	946	10.0	%
Health and Fitness	41	2,162	8.4	
Restaurants - Quick Service	332	686	7.3	
Drug Stores / Pharmacies	85	1,156	6.8	
Movie Theaters	32	1,636	6.5	
Restaurants - Casual Dining	102	732	5.9	
Grocery	40	1,839	4.8	
Home Improvement	14	1,653	4.3	
Specialty Retail	62	1,682	3.9	
Medical Office	36	620	3.9	
Home Furnishings	19	1,869	3.6	
Entertainment	23	897	3.3	
Manufacturing	13	1,875	2.8	
Professional Services	6	684	2.5	
Car Washes	35	183	2.4	
Warehouse Club/Supercenters	9	883	2.2	
Automotive Service	54	419	2.1	
Sporting Goods	13	667	2.0	
Building Materials	9	1,047	1.9	
Dollar Stores	70	718	1.7	
Pet Supplies & Service	4	1,016	1.7	
Education	37	390	1.6	
Distribution	6	677	1.6	
Automotive Dealers	10	297	1.5	
Automotive Parts	54	383	1.4	
Discount Department Stores	7	571	1.2	
Office Supplies	17	458	1.2	
Apparel	5	507	1.0	
Travel Plaza	3	48	0.8	
Other	6	243	0.8	
Consumer Electronics	4	188	0.6	
Discount Retailer	3	188	0.3	
Vacant	5	957	—	
Total	1,462	28,277	100.0	%

## Diversification By Geography

Geographic concentration represents the geographic region's contribution to Contractual Rent of our owned real estate properties as of December 31, 2018:

Location	Number of Properties	Total Square Feet (in thousands)	Percent of Contractual Rent		Location	Number of Properties	Total Square Feet (in thousands)	Percent of Contractual Rent	
Texas	230	3,116	11.9	%	Louisiana	18	244	1.3	%
Florida	106	1,254	7.5	%	Arkansas	33	283	1.2	%
Georgia	106	1,484	6.6	%	Mississippi	30	295	1.2	%
California	21	1,147	5.6	%	Nevada	2	934	1.1	%
Ohio	73	1,119	4.9	%	Kansas	16	397	1.0	%
Illinois	37	1,299	4.1	%	Idaho	11	236	1.0	%
Tennessee	52	1,240	3.9	%	Maryland	7	201	1.0	%
Michigan	73	1,018	3.7	%	Connecticut	5	686	1.0	%
Arizona	40	727	3.5	%	Iowa	11	186	0.8	%
Virginia	44	1,264	3.2	%	Utah	5	568	0.7	%
Missouri	54	939	3.0	%	North Dakota	5	234	0.7	%
South Carolina	28	535	2.5	%	Washington	7	114	0.7	%
Alabama	73	509	2.5	%	Maine	24	63	0.6	%
Colorado	22	851	2.4	%	Oregon	4	144	0.5	%
North Carolina	47	850	2.4	%	Montana	3	152	0.5	%
Minnesota	24	764	2.4	%	Massachusetts	2	131	0.5	%
Indiana	35	501	2.0	%	Wisconsin	7	137	0.3	%
Kentucky	31	448	1.9	%	Rhode Island	3	95	0.3	%
New York	24	704	1.9	%	West Virginia	10	64	0.3	%
New Mexico	26	440	1.8	%	Nebraska	5	136	0.2	%
New Jersey	11	590	1.5	%	U.S. V.I.	1	38	0.2	%
Oklahoma	48	410	1.5	%	Wyoming	1	35	0.1	%
Alaska	9	319	1.3	%	South Dakota	1	20	0.1	%
New Hampshire	16	640	1.3	%	Delaware	1	5	0.1	%
Pennsylvania	19	709	1.3	%	Vermont	1	2	—	

## Lease Expirations

The following table sets forth a summary schedule of expiration dates for leases in place as of December 31, 2018. As of December 31, 2018, the weighted average remaining non-cancelable initial term of our leases (based on Contractual Rent) was 9.6 years. The information set forth in the table assumes that tenants do not exercise renewal options or any early termination rights:

Leases Expiring In:	Number of Properties	Contractual Rent Annualized (in thousands) (1)	Total Square Feet (in thousands)	Percent of Contractual Rent	
2019	15	\$ 5,914	528	1.5	%
2020	35	12,353	1,010	3.2	
2021	115	30,072	2,312	7.9	
2022	43	19,160	1,778	5.0	
2023	112	38,422	3,919	10.0	
2024	33	16,924	1,484	4.4	
2025	36	16,346	1,272	4.3	
2026	78	22,536	1,686	5.9	
2027	112	32,572	2,225	8.5	
2028	85	17,601	984	4.6	
Thereafter	793	170,639	10,122	44.7	
Vacant	5	—	957	—	
Total owned properties	1,462	382,539	28,277	100.0	%

(1) Contractual Rent for the month ended December 31, 2018 for properties owned at December 31, 2018, multiplied by twelve.

## Item 3. Legal Proceedings

From time-to-time, we may be subject to certain claims and lawsuits in the ordinary course of business, the outcome of which cannot be determined at this time. In the opinion of management, any liability we might incur upon the resolution of these claims and lawsuits will not, in the aggregate, have a material adverse effect on our consolidated financial position or results of operations.

## Item 4. Mine Safety Disclosure

None.

## PART II

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

#### MARKET INFORMATION FOR COMMON STOCK, HOLDERS OF RECORD AND DIVIDEND POLICY

Spirit Realty Capital, Inc.

Our common stock is traded on the NYSE under the symbol "SRC." As of February 19, 2019, there were approximately 2,365 stockholders of record of our common stock. Because many of our shares of common stock are held by brokers and other institutions on behalf of stockholders, we are unable to estimate the total number of stockholders represented by these record holders.

We intend to pay regular quarterly dividends to our stockholders, although all future distributions will be declared and paid at the discretion of the Board of Directors and will depend upon cash generated by operating activities, our financial condition, capital requirements, annual distribution requirements under the REIT provisions of the Code and such other factors as the Board of Directors deems relevant.

Spirit Realty, L.P.

Spirit Realty Capital, Inc. directly or indirectly owns all of Spirit Realty, L.P.'s partnership units. Therefore, there is no established trading market for Spirit Realty, L.P.'s partnership units.

#### RECENT SALES OF UNREGISTERED SECURITIES; USE OF PROCEEDS FROM REGISTERED SECURITIES

Spirit Realty Capital, Inc.

No sales of unregistered securities. Gross proceeds of \$3.8 million from sales of registered securities were used for operating expenses and payment of interest and principal on current debt financings.

Spirit Realty, L.P.

None.

#### ISSUER PURCHASES OF EQUITY SECURITIES

Spirit Realty Capital, Inc.

During the fourth quarter of 2018, the following shares of stock were withheld for state and federal payroll taxes on the vesting of employee stock awards, as permitted under the Amended Incentive Award Plan:

• 87 shares of stock, at a weighted average price of \$39.28, in October 2018;

• none in November 2018; and

• 20 shares of stock, at a weighted average price of \$38.30, in December 2018.

Spirit Realty, L.P.

None.

#### EQUITY COMPENSATION PLAN INFORMATION

Our equity compensation plan information required by this item will be included in the Proxy Statement to be filed relating to our 2019 Annual Meeting of Stockholders and is incorporated herein by reference.

# PERFORMANCE GRAPH

The information below shall not be deemed to be “soliciting material” or to be “filed” with the SEC or subject to Regulation 14A or 14C, other than as provided in Item 201 of Regulation S-K, or to the liabilities of Section 18 of the Exchange Act, except to the extent we specifically request that such information be treated as soliciting material or specifically incorporate it by reference into a filing under the Securities Act or the Exchange Act.

The following graph shows our cumulative total stockholder return for the period beginning with the initial listing of our common stock on the NYSE on September 20, 2012 and ending on December 31, 2018, with stock prices retroactively adjusted for the Merger Exchange Ratio and the Spin-Off of SMTA. The graph assumes a \$100 investment in each of the indices on September 20, 2012 and the reinvestment of all cash dividends. Our stock price performance shown in the following graph is not indicative of future stock price performance.

	Period Ended							
Index:	9/20/2012	12/31/2012	12/31/2013	12/31/2014	12/31/2015	12/31/2016	12/31/2017	12/31/2018
Spirit Realty Capital, Inc.	\$ 100.00	\$ 121.05	\$ 137.58	\$ 177.78	\$ 161.47	\$ 187.01	\$ 162.21	\$ 161.17
S&P 500	\$ 100.00	\$ 97.67	\$ 126.58	\$ 141.00	\$ 139.97	\$ 153.32	\$ 183.09	\$ 171.68
NAREIT US Equity REIT Index	\$ 100.00	\$ 101.10	\$ 103.59	\$ 134.81	\$ 139.12	\$ 150.98	\$ 158.87	\$ 151.12

## Item 6. Selected Financial Data

The following tables set forth, on a historical basis, selected financial and operating data for the Company. The following data should be read in conjunction with our financial statements and notes thereto and Item 7.

"Management's Discussion and Analysis of Financial Condition and Results of Operations" included in this Annual Report on Form 10-K.

(Dollars in thousands, except share and per share data)	Years Ended December 31,				
	2018	2017	2016	2015	2014
<b>Operating Data:</b>					
<b>Revenues:</b>					
Rental income	\$402,321	\$424,260	\$420,003	\$395,169	\$346,186
Interest income on loans receivable	3,447	3,346	3,399	3,647	3,955
Earned income from direct financing leases	1,814	2,078	2,742	3,024	3,343
Related party fee income	15,838	—	—	—	—
Other income	21,705	1,574	9,196	866	1,787
Total revenues	\$445,125	\$431,258	\$435,340	\$402,706	\$355,271
<b>Expenses:</b>					
General and administrative	\$52,993	\$54,998	\$48,651	\$45,535	\$39,532
Restructuring charges	—	—	6,341	7,056	—
Finance restructuring costs	—	—	—	—	214
Property costs (including reimbursable)	21,066	28,487	26,045	21,507	21,531
Real estate acquisition costs	210	1,434	2,904	2,352	2,565
Interest	97,548	113,394	118,690	139,183	139,333
Depreciation and amortization	162,452	173,686	173,036	166,478	155,137
Impairments	6,725	61,597	61,395	50,381	30,651
Total expenses	\$340,994	\$433,596	\$437,062	\$432,492	\$388,963
<b>Other income (loss):</b>					
Gain (loss) on debt extinguishment	\$27,092	\$579	\$1,605	\$(2,375 )	\$(457 )
Gain (loss) on disposition of assets	14,629	42,698	29,623	(61 )	48
Preferred dividend income from SMTA	8,750	—	—	—	—
Other expense	(5,319 )	—	—	—	—
Total other income (loss)	\$45,152	\$43,277	\$31,228	\$(2,436 )	\$(409 )
Income (loss) from continuing operations before income tax expense	\$149,283	\$40,939	\$29,506	\$(32,222 )	\$(34,101 )
Income tax expense	(792 )	(511 )	(868 )	(479 )	(673 )
Income (loss) from continuing operations	\$148,491	\$40,428	\$28,638	\$(32,701 )	\$(34,774 )
(Loss) income from discontinued operations <sup>(1)</sup>	(16,439 )	36,720	68,808	125,913	(2,171 )
Net income (loss)	\$132,052	\$77,148	\$97,446	\$93,212	\$(36,945 )
Less: preferred dividends	(10,352 )	(2,530 )	—	—	—
Net income (loss) attributable to common stockholders	\$121,700	\$74,618	\$97,446	\$93,212	\$(36,945 )
<b>Net income (loss) per share of common stock—basic:</b>					
Continuing operations	\$1.59	\$0.40	\$0.30	\$(0.39 )	\$(0.46 )
Discontinued operations	(0.19 )	0.39	0.73	1.46	(0.03 )
Net income (loss) per share attributable to common stockholders—basic	\$1.40	\$0.79	\$1.03	\$1.07	\$(0.49 )
<b>Net income (loss) per share of common stock—diluted:</b>					
Continuing operations	\$1.58	\$0.40	\$0.30	\$(0.39 )	\$(0.46 )
Discontinued operations	(0.19 )	0.39	0.73	1.46	(0.03 )
Net income (loss) per share attributable to common stockholders—diluted	\$1.39	\$0.79	\$1.03	\$1.07	\$(0.49 )





Edgar Filing: SPIRIT REALTY CAPITAL, INC. - Form 10-K

(Dollars in thousands, except share and per share data)	Years Ended December 31,				
	2018	2017	2016	2015	2014
Weighted average shares of common stock outstanding:					
Basic common shares <sup>(2)</sup>	86,321,926	86,991	93,843,552	86,444,333	77,361,948
Diluted common shares <sup>(2)</sup>	86,476,934	88,560	93,849,250	86,444,333	77,361,948
Dividends declared per common share issued <sup>(3)</sup>	\$3.05	\$ 3.60	\$ 3.53	\$ 3.43	\$ 3.34

<sup>(1)</sup> Includes gains, losses and results of operations from all property dispositions and from properties classified as held for sale at the end of the period for all periods prior to 2014. During 2015 and 2014, only those properties classified as held for sale as of December 31, 2013 were reported as discontinued operations. Additionally, includes gains, losses and results of operations of SMTA, applied retrospectively to all periods presented, as a result of the Spin-Off completed on May 31, 2018.

<sup>(2)</sup> Historical weighted average number of shares of common stock outstanding (basic and diluted) have been adjusted for the Merger Exchange Ratio and the reverse stock split effected in 2018.

<sup>(3)</sup> Dividends declared per common share issued for the years ended December 31, 2017, 2016, 2015 and 2014 have been adjusted for the reverse stock split effected in 2018.

(Dollars in thousands)	Years Ended December 31,				
	2018	2017 <sup>(1)</sup>	2016 <sup>(1)</sup>	2015 <sup>(1)</sup>	2014 <sup>(1)</sup>
Balance Sheet Data (end of period):					
Gross investments, including related lease intangibles	\$5,123,631	\$7,903,025	\$8,247,654	\$8,302,688	\$8,043,497
Net investments, including related lease intangibles	4,396,098	6,614,025	7,090,335	7,231,816	7,110,726
Cash and cash equivalents	14,493	8,798	10,059	21,790	176,181
Total assets <sup>(2)</sup>	5,096,316	7,263,511	7,677,971	7,891,039	7,964,230
Total debt, net <sup>(2)</sup>	2,054,637	3,639,680	3,664,628	4,092,787	4,323,302
Total liabilities <sup>(2)</sup>	2,294,567	3,943,902	3,995,863	4,429,165	4,652,568
Total stockholders' equity	2,801,749	3,319,609	3,682,108	3,461,874	3,311,662
Other Data:					
FFO <sup>(3)</sup>	\$322,359	\$367,296	\$394,952	\$354,686	\$238,105
AFFO <sup>(3)</sup>	\$346,323	\$398,148	\$412,999	\$378,050	\$322,400
Number of properties in investment portfolio	1,514	2,480	2,615	2,629	2,509
Owned properties occupancy at period end (based on number of properties)	99.7	% 99.2	% 98.2	% 98.6	% 98.4

<sup>(1)</sup> Balances include assets and liabilities of both continuing operations and discontinued operations. Reference Note 12 to the accompanying consolidated financial statements for additional information.

<sup>(2)</sup> During 2015, we elected to early adopt ASU 2015-03, Simplifying the Presentation of Debt Issuance Costs, in which capitalized deferred financing costs, previously recorded in deferred costs and other assets on the consolidated balance sheets, are presented as a direct deduction from the carrying amount of the debt liability to which these costs relate, and this presentation is retrospectively applied to prior periods. Capitalized deferred financing costs incurred in connection with the 2015 Credit Facility continue to be presented in deferred costs and other assets, net on the consolidated balance sheets as amounts can be drawn and repaid periodically, which is in accordance with ASU 2015-15, Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements.

<sup>(3)</sup> See the definition of FFO and AFFO below.

Non-GAAP Financial Measures  
FFO AND AFFO

We calculate FFO in accordance with the standards established by the National Association of Real Estate Investment Trusts (NAREIT). FFO represents net income (loss) attributable to common stockholders (computed in accordance with GAAP), excluding real estate-related depreciation and amortization, impairment charges and net (gains) losses from property dispositions. FFO is a supplemental non-GAAP financial measure. We use FFO as a supplemental performance measure because we believe that FFO is beneficial to investors as a starting point in measuring our operational performance. Specifically, in excluding real estate-related depreciation and amortization, gains and losses from property dispositions and impairment charges, which do not relate to or are not indicative of operating performance, FFO provides a performance measure that, when compared year over year, captures trends in occupancy rates, rental

rates and operating costs. We also believe that, as a widely recognized measure of the performance of equity REITs, FFO will be used by investors as a basis to compare our operating performance with that of other equity REITs. However, because FFO excludes depreciation and amortization and does not capture the changes in the value of our properties that result from use or market conditions, all of which have real economic effects and could materially impact our results from operations, the utility of FFO as a measure of our performance is limited. In addition, other equity REITs may not calculate FFO as we do, and, accordingly, our FFO may not be comparable to such other equity REITs' FFO. Accordingly, FFO should be considered only as a supplement to net income (loss) attributable to common stockholders (computed in accordance with GAAP) as a measure of our performance.

AFFO is a non-GAAP financial measure of operating performance used by many companies in the REIT industry. We adjust FFO to eliminate the impact of certain items that we believe are not indicative of our core operating performance, including restructuring and divestiture costs, other general and administrative costs associated with relocation of the Company's headquarters, transactions costs associated with our Spin-Off, default interest and fees on non-recourse mortgage indebtedness, debt extinguishment gains (losses), transaction costs incurred in connection with the acquisition of real estate investments subject to existing leases, costs associated with performing on a guarantee of a former tenant's debt, and certain non-cash items. These certain non-cash items include non-cash revenues (comprised of straight-line rents, amortization of above- and below-market rent on our leases, amortization of lease incentives, amortization of net premium (discount) on loans receivable, bad debt expense and amortization of capitalized lease transaction costs), non-cash interest expense (comprised of amortization of deferred financing costs and amortization of net debt discount/premium) and non-cash compensation expense (stock-based compensation expense). In addition, other equity REITs may not calculate AFFO as we do, and, accordingly, our AFFO may not be comparable to such other equity REITs' AFFO. AFFO does not represent cash generated from operating activities determined in accordance with GAAP, is not necessarily indicative of cash available to fund cash needs and should only be considered a supplement, and not an alternative, to net income (loss) attributable to common stockholders (computed in accordance with GAAP) as a performance measure.

#### Adjusted Debt

Adjusted Debt represents interest bearing debt (reported in accordance with GAAP) adjusted to exclude unamortized debt discount/premium, deferred financing costs, and reduced by cash and cash equivalents and cash reserves on deposit with lenders as additional security. By excluding these amounts, the result provides an estimate of the contractual amount of borrowed capital to be repaid, net of cash available to repay it. We believe this calculation constitutes a beneficial supplemental non-GAAP financial disclosure to investors in understanding our financial condition.

#### EBITDAre

EBITDAre is a non-GAAP financial measure and is computed in accordance with standards established by NAREIT. EBITDAre is defined as net income (loss) (computed in accordance with GAAP), plus interest expense, plus income tax expense (if any), plus depreciation and amortization, plus (minus) losses and gains on the disposition of depreciated property, plus impairment write-downs of depreciated property and investments in unconsolidated real estate ventures, plus adjustments to reflect the Company's share of EBITDAre of unconsolidated real estate ventures.

#### Adjusted EBITDAre

Adjusted EBITDAre represents EBITDAre as adjusted for transaction costs, revenue producing acquisitions and dispositions for the quarter as if such acquisitions and dispositions had occurred as of the beginning of the quarter, severance charges, real estate acquisition costs, and debt extinguishment gains (losses). We focus our business plans to enable us to sustain increasing shareholder value. Accordingly, we believe that excluding these items, which are not key drivers of our investment decisions and may cause short-term fluctuations in net income, provides a useful supplemental measure to investors and analysts in assessing the net earnings contribution of our real estate portfolio. Because these measures do not represent net income (loss) that is computed in accordance with GAAP, they should only be considered a supplement, and not an alternative, to net income (loss) (computed in accordance with GAAP) as a performance measure.

#### Annualized Adjusted EBITDAre

Annualized Adjusted EBITDAre is calculated as Adjusted EBITDAre for the quarter, adjusted for items where annualization would not be appropriate, multiplied by four. Our computation of Adjusted EBITDAre and Annualized

Adjusted EBITDA may differ from the methodology used by other equity REITs to calculate these measures and, therefore, may not be comparable to such other REITs.

# Adjusted Debt to Annualized Adjusted EBITDA

Adjusted Debt to Annualized Adjusted EBITDA is a supplemental non-GAAP financial measure we use to evaluate the level of borrowed capital being used to increase the potential return of our real estate investments, and a proxy for a measure we believe is used by many lenders and ratings agencies to evaluate our ability to repay and service our debt obligations over time. We believe the ratio is a beneficial disclosure to investors as a supplemental means of evaluating our ability to meet obligations senior to those of our equity holders. Our computation of this ratio may differ from the methodology used by other equity REITs, and, therefore, may not be comparable to such other REITs. A reconciliation of interest bearing debt (computed in accordance with GAAP) to Adjusted Debt is included in the financial information accompanying this report.

## FFO and AFFO

	Years Ended December 31,				
(Dollars in thousands)	2018	2017	2016	2015	2014
Net income attributable to common stockholders <sup>(1)</sup>	\$121,700	\$74,618	\$97,446	\$93,212	\$(36,945 )
Add/(less):					
Portfolio depreciation and amortization	197,346	255,454	261,799	260,257	247,587
Portfolio impairments	17,668	102,330	88,072	70,231	38,009
Gain on disposition of assets	(14,355 )	(65,106 )	(52,365 )	(69,014 )	(10,546 )
FFO attributable to common stockholders	\$322,359	\$367,296	\$394,952	\$354,686	\$238,105
Add/(less):					
(Gain) loss on debt extinguishment	(26,729 )	1,645	(233 )	3,162	64,750
Restructuring charges	—	—	6,341	7,056	—
Other costs in G&A associated with headquarter relocation	—	—	3,629	—	—
Real estate acquisition costs	549	1,356	3,229	2,739	3,631
Transaction costs	21,391	6,361	—	—	—
Master Trust Exchange Costs	—	—	—	—	13,022
Non-cash interest expense	22,866	23,469	15,380	10,367	5,175
Accrued interest and fees on defaulted loans	1,429	4,201	4,740	7,649	3,103
Straight-line rent, net of related bad debt expense	(15,382 )	(19,474 )	(23,496 )	(19,291 )	(12,191 )
Other amortization and non-cash charges	(2,434 )	(3,266 )	(2,837 )	(1,639 )	(4,541 )
Swap termination costs <sup>(2)</sup>	—	—	1,724	—	—
Non-cash compensation expense	15,114	16,560	9,570	13,321	11,346
Other G&A costs associated with Spin-Off	1,841	—	—	—	—
Other expense	5,319	—	—	—	—
AFFO attributable to common stockholders	\$346,323	\$398,148	\$412,999	\$378,050	\$322,400
FFO per share of common stock - diluted <sup>(3)</sup>	\$3.71	\$3.91	\$4.20	\$4.09	\$3.06
AFFO per share of common stock - diluted <sup>(3)</sup>	\$3.99	\$4.24	\$4.39	\$4.36	\$4.14
AFFO per share of common stock, excluding Haggen settlement <sup>(4)</sup>	\$3.78	4.24	4.38	4.36	4.14

## Weighted average shares of common stock outstanding:

Diluted 86,476,449 93,588,560 93,849,250 86,444,333 77,361,948

<sup>(1)</sup> Amount is net of distributions paid to preferred stockholders for the years ended December 31, 2018 and 2017.

<sup>(2)</sup> Included in general and administrative expenses.

<sup>(3)</sup> Assumes the issuance of potentially issuable shares unless the result would be anti-dilutive.

<sup>(4)</sup> AFFO attributable to common stockholders, excluding proceeds from the Haggen settlement of \$19.1 million for the year ended December 31, 2018 and \$1.8 million for the year ended December 31, 2016.



## Adjusted Debt, Adjusted EBITDA and Annualized Adjusted EBITDA

	December 31,	
(Dollars in thousands)	2018	2017
2015 Credit Facility	\$146,300	\$112,000
2015 Term Loan, net	419,560	—
Senior Unsecured Notes, net	295,767	295,321
Mortgages and notes payable, net	463,196	2,516,478
Convertible Notes, net	729,814	715,881
Total debt, net	2,054,637	3,639,680
Add / (less):		
Unamortized debt discount, net	14,733	61,399
Unamortized deferred financing costs	14,932	39,572
Cash and cash equivalents	(14,493 )	(8,798 )
Restricted cash balances held for the benefit of lenders	(62,928 )	(105,909 )
Adjusted Debt	\$2,006,881	\$3,625,944

	Three Months Ended December 31,	
(Dollars in thousands)	2018	2017
Net income	\$54,114	\$35,791
Add/(less):		
Interest	26,163	47,998
Depreciation and amortization	41,437	63,132
Income tax expense (benefit)	317	(25 )
Realized gain on sales of real estate	(13,802 )	(24,909 )
Impairments on real estate assets	471	14,221
EBITDAre	\$108,700	\$136,208
Adjustments to revenue producing acquisitions and dispositions <sup>(1)</sup>	(168 )	—
Transaction costs	460	3,216
Real estate acquisition costs	67	583
Loss on debt extinguishment	—	3,415
Other G&A costs associated with Spin-off	1,841	—
Other expense	5,319	—
Adjusted EBITDAre	\$116,219	\$143,422
Other adjustments for Annualized Adjusted EBITDAre <sup>(1) (2)</sup>	(17,944 )	\$—
Annualized Adjusted EBITDAre	\$393,100	\$573,688
Adjusted Debt / Annualized Adjusted EBITDAre	5.1	6.3

<sup>(1)</sup> In 2018 and going forward, the definition of Adjusted EBITDAre was revised to reflect adjustments made for income producing acquisitions and dispositions made during the quarter. The definition of Annualized Adjusted EBITDAre was also revised to reflect adjustments for items where annualization is not appropriate.

<sup>(2)</sup> Adjustments for which annualization would not be appropriate are composed of the receipt of the Haggen settlement and write-offs related to certain uncollectible accounts receivable and straight-line rent receivables.

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

### OVERVIEW

Spirit Realty Capital, Inc. is a New York Stock Exchange listed company under the ticker symbol "SRC." We are a self-administered and self-managed REIT with in-house capabilities including acquisition, portfolio management, asset management, credit research, real estate research, legal, finance and accounting and capital markets. We primarily invest in single-tenant, operationally essential real estate assets throughout the U.S., which are generally acquired through strategic sale-leaseback transactions and subsequently leased on long-term, triple-net basis to high quality tenants with business operations within predominantly retail, but also office and industrial property types. Single tenant, operationally essential real estate consists of properties that are generally free-standing, commercial real estate facilities where our tenants conduct activities that are essential to the generation of their sales and profits. In support of our primary business of owning and leasing real estate, we have also strategically originated or acquired long-term, commercial mortgage and other loans to provide a range of financing solutions to our tenants.

As of December 31, 2018, our owned real estate represented investments in 1,462 properties. Our properties are leased to 252 tenants across 49 states and 32 industries. As of December 31, 2018, our owned properties were approximately 99.7% occupied (based on number of economically yielding properties). In addition, our investment in real estate includes commercial mortgage and other loans secured by an additional 52 real estate properties or other related assets.

Our operations are carried out through the Operating Partnership. OP Holdings, one of our wholly-owned subsidiaries, is the sole general partner and owns approximately 1% of the Operating Partnership. We and one of our wholly-owned subsidiaries are the only limited partners, and together own the remaining 99% of the Operating Partnership. Although the Operating Partnership is wholly-owned by us, in the future, we may issue partnership interests in the Operating Partnership to third parties in exchange for property owned by such third parties. In general, any partnership interests in the Operating Partnership issued to third parties would be exchangeable for cash or, at our election, shares of our common stock at specified ratios set when such partnership interests in the Operating Partnership are issued.

We have elected to be taxed as a REIT for federal income tax purposes commencing with our taxable year ended December 31, 2005. We believe that we have been organized and have operated in a manner that has allowed us to qualify as a REIT for federal income tax purposes commencing with such taxable year, and we intend to continue operating in such a manner.

On May 31, 2018, we completed a Spin-Off of all of our interests in the assets that collateralize Master Trust 2014, our properties leased to Shopko, and certain other assets into an independent, publicly traded REIT, SMTA. Upon completion of the Spin-Off, our stockholders received a distribution of common shares of beneficial interest in SMTA, which are treated as a taxable distribution to them. Beginning in the second quarter of 2018, the historical financial results of SMTA are reflected in our consolidated financial statements as discontinued operations for all periods presented. See Note 12 to the accompanying consolidated financial statements for further discussion.

### CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our accounting policies are determined in accordance with GAAP. The preparation of our financial statements requires us to make estimates and assumptions that are subjective in nature and, as a result, our actual results could differ materially from our estimates. Estimates and assumptions include, among other things, subjective judgments regarding the fair values and useful lives of our properties for depreciation and lease classification purposes, the collectability of receivables and asset impairment analysis. Set forth below are the more critical accounting policies that require management judgment and estimates in the preparation of our consolidated financial statements. See Notes 2 and 8 to the consolidated financial statements for further details.

#### Purchase Accounting and Acquisition of Real Estate; Lease Intangibles

We use a number of sources to estimate fair value of real estate acquisitions, including building age, building location, building condition, rent comparables from similar properties, and terms of in-place leases, if any. Lease intangibles, if any, acquired in conjunction with the purchase of real estate represent the value of in-place leases and above or below-market leases. In-place lease intangibles are valued based on our estimates of costs related to tenant acquisition and the carrying costs that would be incurred during the time it would take to locate a tenant if the property were vacant, considering current market conditions and costs to execute similar leases at the time of the acquisition. We then





allocate the purchase price (including acquisition and closing costs) to land, building, improvements and equipment based on their relative fair values. For properties acquired with in-place leases, we allocate the purchase price of real estate to the tangible and intangible assets and liabilities acquired based on their estimated fair values. Above and below-market lease intangibles are recorded based on the present value of the difference between the contractual amounts to be paid pursuant to the leases at the time of acquisition of the real estate and our estimate of current market lease rates for the property, measured over a period equal to the remaining initial term of the lease.

#### Impairment

We review our real estate investments and related lease intangibles periodically for indicators of impairment, including the asset being held for sale, vacant or non-operating, tenant bankruptcy or delinquency, and leases expiring in 60 days or less. For assets with indicators of impairment, we then evaluate if its carrying amount may not be recoverable. We consider factors such as expected future undiscounted cash flows, estimated residual value, market trends (such as the effects of leasing demand and competition) and other factors in making this assessment. An asset is considered impaired if its carrying value exceeds its estimated undiscounted cash flows.

Impairment is then calculated as the amount by which the carrying value exceeds the estimated fair value, or for assets held for sale, as the amount by which the carrying value exceeds fair value less costs to sell. Estimating future cash flows and fair values is highly subjective and such estimates could differ materially from actual results. Key assumptions used in estimating future cash flows and fair values include, but are not limited to, revenue growth rates, interest rates, discount rates, capitalization rates, lease renewal probabilities, tenant vacancy rates and other factors.

#### REIT Status

We elected to be taxed as a REIT for federal income tax purposes commencing with our taxable year ended December 31, 2005. We believe that we have been organized and have operated in a manner that has allowed us to qualify as a REIT commencing with such taxable year, and we intend to continue operating in such a manner. To maintain our REIT status, we are required to annually distribute to our stockholders at least 90% of our REIT taxable income, determined without regard to the dividends paid deduction and excluding any net capital gain, and meet the various other requirements imposed by the Code relating to such matters as operating results, asset holdings, distribution levels and diversity of stock ownership. Provided that we qualify for taxation as a REIT, we are generally not subject to corporate level federal income tax on the earnings distributed to our stockholders that we derive from our REIT qualifying activities. We are still subject to state and local income and franchise taxes and to federal income and excise tax on our undistributed income. If we fail to qualify as a REIT in any taxable year and are unable to avail ourselves of certain savings provisions set forth in the Code, all of our taxable income would be subject to federal income tax at regular corporate rates, including any applicable alternative minimum tax for taxable years beginning before January 1, 2018. Unless entitled to relief under specific statutory provisions, we would be ineligible to elect to be treated as a REIT for the four taxable years following the year for which we lose our qualification. It is not possible to state whether in all circumstances we would be entitled to this statutory relief.

## RESULTS OF OPERATIONS: COMPARISON OF THE YEARS ENDED DECEMBER 31, 2018 AND 2017

(In Thousands)	Years Ended December 31,		Change	% Change
	2018	2017		
Revenues:				
Rental income	\$402,321	\$424,260	\$(21,939 )	(5.2 )%
Interest income on loans receivable	3,447	3,346	101	3.0 %
Earned income from direct financing leases	1,814	2,078	(264 )	(12.7 )%
Related party fee income	15,838	—	15,838	100.0 %
Other income	21,705	1,574	20,131	NM
Total revenues	445,125	431,258	13,867	3.2 %
Expenses:				
General and administrative	52,993	54,998	(2,005 )	(3.6 )%
Property costs (including reimbursable)	21,066	28,487	(7,421 )	(26.1 )%
Real estate acquisition costs	210	1,434	(1,224 )	(85.4 )%
Interest	97,548	113,394	(15,846 )	(14.0 )%
Depreciation and amortization	162,452	173,686	(11,234 )	(6.5 )%
Impairments	6,725	61,597	(54,872 )	(89.1 )%
Total expenses	340,994	433,596	(92,602 )	(21.4 )%
Other income:				
Gain on debt extinguishment	27,092	579	26,513	NM
Gain on disposition of assets	14,629	42,698	(28,069 )	(65.7 )%
Preferred dividend income from SMTA	8,750	—	8,750	100.0 %
Other expense	(5,319 )	—	(5,319 )	(100.0)%
Total other income	45,152	43,277	1,875	4.3 %
Income from continuing operations before income tax expense	149,283	40,939	108,344	NM
Income tax expense	(792 )	(511 )	(281 )	(55.0 )%
Income from continuing operations	\$148,491	\$40,428	\$108,063	NM
(Loss) income from discontinued operations	\$(16,439 )	\$36,720	\$(53,159 )	NM

NM - Percentages over 100% are not displayed.

## Revenues

## Rental income

While we were a net acquirer of income producing real estate for the year ended December 31, 2018, our contractual rental revenue between periods decreased 4.9% as a result of the timing of the acquisition/disposition activity, specifically with the majority of acquisitions closing in the second half of 2018. Included in continuing operations for the year ended December 31, 2018 were acquisitions of 17 properties, with a Real Estate Investment Value of \$250.8 million, and dispositions of 29 properties, with a Real Estate Investment Value of \$96.4 million.

The decrease in contractual rental revenues year-over-year was partially offset by fewer tenant credit issues from 2017 to 2018. As of December 31, 2018 and 2017, respectively, five and 11 of our properties in continuing operations were vacant and not generating rent, representing approximately 0.3% and 0.7% of our owned properties.

Also included in rental income are tenant reimbursements, where our tenants are obligated under the lease agreement to reimburse us for certain property costs we incur, and non-cash rental income. Tenant reimbursement income is driven by the tenant reimbursable property costs described below and comprised 3.0% and 3.5% of rental income for the years ended December 31, 2018 and 2017, respectively. Non-cash rental income primarily consists of straight-line rental revenue and amortization of above- and below-market lease intangibles. During the years ended December 31,

2018 and 2017, non-cash rental income was \$20.1 million and \$25.0 million, respectively, representing approximately 5.0% and 5.9%, respectively, of total rental income from continuing operations.

#### Interest income on loans receivable

In conjunction with the Master Trust 2014 Series 2017-1 notes issuance completed in December 2017, the Operating Partnership, as sponsor of the issuance, retained a 5.0% economic interest in the Master Trust 2014 Series 2017-1 notes. Subsequent to the Spin-Off, this holding is reflected as Investment in Master Trust 2014 on the accompanying consolidated balance sheet, and the related interest income resulted in an increase in interest income period-over-period. That increase was offset by a decrease in interest income from mortgage loans during the year ended December 31, 2018, primarily as a result of the pay-off of one \$7.5 million mortgage loan collateralized by 26 properties.

#### Related party fee income

In conjunction with the Spin-Off, we entered into the Asset Management Agreement with SMTA pursuant to which we provide a management team that is responsible for implementing SMTA's business strategy and performing certain services for SMTA. Under this agreement, we recognized \$11.7 million of revenues during the period from the Spin-Off to December 31, 2018.

Additionally, we provide property management services and special services for Master Trust 2014, which was contributed to SMTA as part of the Spin-Off. Therefore, during the period from the Spin-Off to December 31, 2018, we recognized \$4.2 million in revenue under the terms of the Property Management and Servicing Agreement. In January 2019, SMTA announced that due to the bankruptcy of its largest tenant, it would be accelerating its timeline for strategic alternatives. This acceleration may result in the early termination of the Asset Management Agreement and/or the Property Management and Servicing Agreement, in which case we would be entitled to a termination fee. See related discussion in Item 1A. Risk Factors "Risks Related to our Relationship with SMTA."

#### Other income

The driver for the increase in other income was the receipt of the final settlement of \$19.7 million in relation to the Company's claim from 20 properties leased to Haggen at the time of Haggen Operations Holdings, LLC's bankruptcy in 2015. As a result of this settlement, \$19.1 million of other income was recognized in the year ended December 31, 2018. Additionally, we recognized other income of \$1.0 million in the year ended December 31, 2018 for pre-payment penalty income when one of our mortgage loans receivable, which was collateralized by 26 properties, was paid off in 2018 prior to its scheduled maturity.

#### Expenses

##### General and administrative

The year-over-year decrease is a result of decreases in legal fees, primarily as a result of fewer tenant credit issues and internalization of certain legal items, and of decreases in consulting fees, primarily as a result of certain expenses incurred in 2017 related to re-branding and executive team transition, as well as internalization of certain marketing activities.

##### Property costs (including reimbursable)

For the year ended December 31, 2018, property costs excluding bad debt expense were \$20.4 million (including \$15.6 million of tenant reimbursable expenses) compared to \$26.0 million (including \$16.8 million of tenant reimbursable expenses) for the year ended December 31, 2017. The non-reimbursable costs decreased year-over-year as a result of fewer vacancies and tenant credit issues, while the decrease in reimbursable property costs resulted from decreases in reimbursable property taxes and certain property maintenance expenses. Bad debt expense for the year ended December 31, 2018 was \$0.7 million, which reflects the write-off of straight-line rent receivables deemed to be uncollectible, compared to bad debt expense of \$2.5 million for the year ended December 31, 2017.

#### Interest

The decrease in interest expense is primarily related to the extinguishment of \$195.8 million principal outstanding of Master Trust 2013 notes and CMBS debt during the year ended December 31, 2018, with a weighted average interest rate of 5.49%. Additionally, there was a decrease in interest expense for the Term Loan for the year ended December 31, 2018 as the facility was not utilized for the first half of 2018.



The following table summarizes our interest expense on related borrowings:

	Years Ended	
	December 31,	
(In Thousands)	2018	2017
Interest expense – 2015 Credit Facility <sup>(1)</sup>	\$8,220	\$7,957
Interest expense – 2015 Term Loan	6,594	9,793
Interest expense – mortgages and notes payable	26,538	40,385
Interest expense – Convertible Notes	24,509	24,509
Interest expense – Unsecured Senior Notes	13,350	13,351
Non-cash interest expense:		
Amortization of deferred financing costs	7,864	8,416
Amortization of debt discount, net	10,473	8,983
Total interest expense	\$97,548	\$113,394

<sup>(1)</sup> Includes facility fees of approximately \$2.1 million for both the years ended December 31, 2018 and 2017.

#### Depreciation and amortization

During the year ended December 31, 2018, we acquired 17 properties with a Real Estate Investment Value of \$250.8 million, while disposing 29 properties with a Real Estate Investment Value of \$96.4 million. While we were a net acquirer during the period (based on Real Estate Investment Value), depreciation and amortization decreased period-over-period as a result of timing of the acquisition/disposition activity, specifically with the majority of acquisitions closing in the second half of 2018. The following table summarizes our depreciation and amortization expense:

	Years Ended	
	December 31,	
(In Thousands)	2018	2017
Depreciation of real estate assets	\$133,759	\$140,557
Other depreciation	567	563
Amortization of lease intangibles	28,126	32,566
Total depreciation and amortization	\$162,452	\$173,686

#### Impairment

Impairment charges for the year ended December 31, 2018 were \$6.7 million. \$1.9 million of the impairment was recorded on Vacant properties, comprised of \$1.3 million recorded on three Vacant held for use properties and \$0.6 million recorded on one Vacant held for sale property. The remaining \$4.8 million of impairment was recorded on underperforming properties, comprised of \$4.4 million recorded on 17 underperforming held for use properties and \$0.4 million recorded on two underperforming held for sale properties.

Impairment charges for the year ended December 31, 2017 were \$61.6 million. \$45.7 million of the impairment was recorded on Vacant properties, comprised of \$34.5 million recorded on 16 Vacant held for use properties and \$11.2 million recorded on 11 Vacant held for sale properties. The remaining \$15.9 million of impairment was recorded on underperforming properties, comprised of \$14.6 million recorded on 12 underperforming held for use properties and \$1.3 million recorded on five underperforming held for sale properties.

#### Gain on debt extinguishment

During the year ended December 31, 2018, we extinguished \$195.8 million of Master Trust 2013 notes and CMBS debt and recognized a gain on debt extinguishment of \$27.1 million. The gain was primarily attributable to the extinguishment of \$56.2 million of CMBS debt related to six defaulted loans on six underperforming properties, which was partially offset by a loss on the extinguishment of the Master Trust 2013 Series 2013-1 notes and make-whole penalties on early pre-payments of Master Trust 2013 Series 2013-2.

During the year ended December 31, 2017, we extinguished \$195.4 million of mortgage debt and recognized a gain on debt extinguishment of \$0.6 million. The gain was primarily attributable to the partial extinguishment of one defaulted mortgage loan upon the sale of one of the properties collateralizing the loan to a third party, offset by net losses from the prepayment and defeasance fees on mortgage debt related to 25 properties.



Gain on disposition of assets

During the year ended December 31, 2018, we disposed of 29 properties and recorded gains totaling \$14.6 million. There were \$15.5 million in net gains on the sale of 19 active properties. These gains were partially offset by \$0.7 million in net losses on the sale of four Vacant properties and \$0.2 million in net other losses. There were no gains/losses recorded on the transfer of six properties to lenders.

During the year ended December 31, 2017, we disposed of 116 properties and recorded net gains totaling \$42.7 million. There were \$49.7 million in net gains on the sale of 55 active properties. These gains were partially offset by \$6.7 million in net losses on the sale of 61 Vacant properties and \$0.3 million in net other losses.

Preferred dividend income from SMTA

As part of the Spin-Off of SMTA, SMTA issued to us 10% Series A preferred shares with an aggregate liquidation preference of \$150.0 million. During the period from the Spin-Off to December 31, 2018, we recognized preferred dividend income of \$8.8 million from these shares. As noted above, in January 2019, SMTA announced it would be accelerating its timeline for strategic alternatives. This acceleration may result in the early repayment of the Series A preferred shares or other outcomes. See related discussion in Item 1A. Risk Factors "Risks Related to our Relationship with SMTA."

Other expense

We are contingently liable for \$5.7 million of debt owed by one of our former tenants. As a result of the former tenant filing for bankruptcy, we recognized \$5.3 million of debt guarantee expense in the current period to fully reserve for the contingent liability.

(Loss) income from discontinued operations

Subsequent to the completion of the Spin-Off of SMTA on May 31, 2018, the only activity recognized in discontinued operations were transaction costs associated with the Spin-Off. Therefore, the year ended December 31, 2018 only reflects five months of activity for the assets that were included in the Spin-Off. This resulted in a decrease in (loss) income from discontinued operations compared to the year ended December 31, 2017, which reflects a full year of activity for the assets that were included in the Spin-Off.



RESULTS OF OPERATIONS: COMPARISON OF THE YEARS ENDED DECEMBER 31, 2017 AND 2016

(In Thousands)	Years Ended December 31,			
	2017	2016	Change	% Change
Revenues:				
Rental income	\$424,260	\$420,003	\$4,257	1.0 %
Interest income on loans receivable	3,346	3,399	(53 )	(1.6 )%
Earned income from direct financing leases	2,078	2,742	(664 )	(24.2)%
Other income	1,574	9,196	(7,622 )	(82.9)%
Total revenues	431,258	435,340	(4,082 )	(0.9 )%
Expenses:				