EASTGROUP PROPERTIES INC
Form 10-K
February 14, 2019

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

FORM 10-K

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2018

OR

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

For the transition period from to

COMMISSION FILE NUMBER 1-07094

EASTGROUP PROPERTIES, INC.
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

MARYLAND	13-2711135
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

400 W PARKWAY PLACE SUITE 100 RIDGELAND, MISSISSIPPI	39157
(Address of principal executive offices)	(Zip code)

Registrant’s telephone number: (601) 354-3555

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of each class	Name of exchange on which registered
Common Stock, $.0001 par value	New York Stock Exchange

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: NONE

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES (x) NO ( )
Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. YES ( ) NO (x)

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

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

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 definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer (x)	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. ( )

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

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of June 29, 2018, the last business day of the Registrant's most recently completed second fiscal quarter: $3,331,265,000.

The number of shares of common stock, $.0001 par value, outstanding as of February 13, 2019 was 36,479,324.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant’s Proxy Statement relating to its 2019 Annual Meeting of Stockholders are incorporated by reference into Part III. The Registrant intends to file such Proxy Statement with the Securities and Exchange Commission not later than 120 days after the end of the fiscal year ended December 31, 2018.

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FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K includes “forward-looking statements” (within the meaning of the federal securities laws, Section 27A of the Securities Act of 1933, as amended (the “Securities Act”), and Section 21E of the Exchange Act of 1934, as amended (the “Exchange Act”)) that reflect EastGroup Properties, Inc.'s (the "Company" or "EastGroup") expectations and projections about the Company’s future results, performance, prospects and opportunities. The Company has attempted to identify these forward-looking statements by the use of words such as “may,” “will,” “seek,” “expects,” “anticipates,” “believes,” “targets,” “intends,” “should,” “estimates,” “could,” “continue,” “a “plans” or similar expressions. These forward-looking statements are based on information currently available to the Company and are subject to a number of known and unknown risks, uncertainties and other factors that may cause the Company’s actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. These factors include, among other things, those discussed below. The Company intends for all such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in Section 27A of the Securities Act and Section 21E of the Exchange Act, as applicable by law. The Company does not undertake publicly to update or revise any forward-looking statements, whether as a result of changes in underlying assumptions or new information, future events or otherwise, except as may be required to satisfy the Company’s obligations under federal securities law.

The following are some, but not all, of the risks, uncertainties and other factors that could cause the Company’s actual results to differ materially from those presented in the Company’s forward-looking statements (the Company refers to itself as "we," "us" or "our" in the following):

- international, national, regional and local economic conditions;
- the general level of interest rates and ability to raise equity capital on attractive terms;
- financing risks, including the risks that our cash flows from operations may be insufficient to meet required payments of principal and interest and we may be unable to refinance our existing debt upon maturity or obtain new financing on attractive terms or at all;
- the competitive environment in which the Company operates;
- fluctuations of occupancy or rental rates;
- potential defaults (including bankruptcies or insolvency) on or non-renewal of leases by tenants;
- potential changes in the law or governmental regulations and interpretations of those laws and regulations, including changes in real estate laws or real estate investment trust (“REIT”) or corporate income tax laws, and potential increases in real property tax rates;
- our ability to maintain our qualification as a REIT;
- acquisition and development risks, including failure of such acquisitions and development projects to perform in accordance with projections;
- natural disasters such as fires, floods, tornadoes, hurricanes and earthquakes;
- the terms of governmental regulations that affect us and interpretations of those regulations, including the costs of compliance with those regulations, changes in real estate and zoning laws and increases in real property tax rates;
- credit risk in the event of non-performance by the counterparties to the interest rate swaps;
- lack of or insufficient amounts of insurance;
- litigation, including costs associated with prosecuting or defending claims and any adverse outcomes;
- our ability to retain key personnel;
- the consequences of future terrorist attacks or civil unrest; and
- environmental liabilities, including costs, fines or penalties that may be incurred due to necessary remediation of contamination of properties presently owned or previously owned by us.

All forward-looking statements should be read in light of the risks identified in Part I, Item 1A. Risk Factors within the Company's Annual Report on Form 10-K for the year ended December 31, 2018. In addition, the Company's current and continuing qualification as a real estate investment trust, or REIT, involves the application of highly technical and complex provisions of the Internal Revenue Code of 1986, as amended, or the Code, and depends on the Company's ability to meet the various requirements imposed by the Code through actual operating results, distribution levels and diversity of stock ownership.

PART I

ITEM 1. BUSINESS.

The Company
EastGroup Properties, Inc., which we refer to in this Annual Report as the "Company" or "EastGroup," is an internally-managed equity real estate investment trust ("REIT") first organized in 1969. EastGroup is focused on the development, acquisition and operation of industrial properties in major Sunbelt markets throughout the United States, primarily in the states of Florida, Texas, Arizona, California and North Carolina. EastGroup’s strategy for growth is based on ownership of premier distribution facilities generally clustered near major transportation features in supply-constrained submarkets. EastGroup is a Maryland corporation, and its common stock is publicly traded on the New York Stock Exchange (“NYSE”) under the symbol “EGP.” The Company has elected to be taxed and intends to continue to qualify as a REIT under the Internal Revenue Code of 1986, as amended (the "Code").

Available Information
The Company maintains a website at www.eastgroup.net. The Company posts its annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) of the Securities Exchange Act of 1934, as amended, as soon as reasonably practicable after it electronically files or furnishes such materials to the Securities and Exchange Commission (the "SEC"). In addition, the Company's website includes items related to corporate governance matters, including, among other things, the Company's corporate governance guidelines, charters of various committees of the Board of Directors, and the Company's code of business conduct and ethics applicable to all employees, officers and directors. The Company intends to disclose on its website any amendment to, or waiver of, any provision of this code of business conduct and ethics applicable to the Company's directors and executive officers that would otherwise be required to be disclosed under the rules of the SEC or the New York Stock Exchange. Copies of these reports and corporate governance documents may be obtained, free of charge, from the Company's website. Any shareholder also may obtain copies of these documents, free of charge, by sending a request in writing to: Investor Relations, EastGroup Properties, Inc., 400 W. Parkway Place, Suite 100, Ridgeland, MS 39157.

The SEC also maintains a website that contains reports, proxy and information statements, and other information we file with the SEC at www.sec.gov.

Administration
EastGroup maintains its principal executive office and headquarters in Ridgeland, Mississippi. The Company also has regional offices in Atlanta, Dallas and Los Angeles and asset management offices in Orlando, Charlotte, Houston and Phoenix. EastGroup has property management offices in Jacksonville, Tampa, Ft. Lauderdale and San Antonio. Offices at these locations allow the Company to provide property management services to all of its Florida, Texas (except Austin and El Paso), Arizona and North Carolina properties, which together account for 77% of the Company’s total portfolio on a square foot basis. In addition, the Company currently provides property administration (accounting of operations) for its entire portfolio. The regional offices in Georgia, Texas and California provide oversight of the Company's development program. As of February 13, 2019, EastGroup had 72 full-time employees and 3 part-time employees.

Business Overview
EastGroup's goal is to maximize shareholder value by being a leading provider in its markets of functional, flexible and quality business distribution space for location sensitive customers (primarily in the 15,000 to 50,000 square foot range). The Company develops, acquires and operates distribution facilities, the majority of which are clustered around major transportation features in supply-constrained submarkets in major Sunbelt regions. The Company's core markets are in the states of Florida, Texas, Arizona, California and North Carolina.

As of December 31, 2018, EastGroup owned 377 industrial properties and one office building in 10 states. As of that same date, the Company's portfolio, including development projects and value-add properties in lease-up and under construction, included approximately 41.5 million square feet consisting of 335 business distribution buildings containing 36.4 million square feet, 14 bulk distribution buildings containing 3.7 million square feet, and 28 business service buildings containing 1.4 million square feet. As of December 31, 2018, EastGroup's operating portfolio was 97.3% leased to approximately 1,500 tenants, with no single tenant accounting for more than approximately 1.1% of the Company's income from real estate operations. As of February 13, 2019, the properties development and value-add program at year-end were approximately 45% leased.

During 2018, EastGroup increased its holdings in real estate properties through its acquisition and development programs. The Company purchased 627,000 square feet of operating and value-add properties and 83 acres of land for a total of $87 million. Also during 2018, the Company began construction of 12 development projects containing 1.7 million square feet and transferred 14

projects, which contain 1.7 million square feet and had costs of $135.0 million at the date of transfer, from its development and value-add program to real estate properties.

During 2018, EastGroup completed dispositions including 339,000 square feet of operating properties and 11 acres of land, which generated gross proceeds of $25.4 million.

Typically, the Company initially funds its development and acquisition programs through its unsecured bank credit facilities. In June 2018, the Company expanded the borrowing capacity under its credit facilities from $335 million to $395 million. As market conditions permit, EastGroup also issues equity or employs fixed-rate debt, including variable-rate debt that has been swapped to an effectively fixed rate through the use of interest rate swaps, to replace short-term bank borrowings. In June 2018, Moody's Investors Service affirmed the Company's issuer rating of Baa2 with a stable outlook. A security rating is not a recommendation to buy, sell, or hold securities and may be subject to revision or withdrawal at any time by the assigning rating agency. Each rating should be evaluated independently of any other rating. For future debt issuances, the Company intends to issue primarily unsecured fixed-rate debt, including variable-rate debt that has been swapped to an effectively fixed rate through the use of interest rate swaps. The Company may also access the public debt market in the future as a means to raise capital.

EastGroup holds its properties as long-term investments but may determine to sell certain properties that no longer meet its investment criteria. The Company may provide financing to a prospective purchaser in connection with such sales of property if market conditions require. In addition, the Company may provide financing to a partner or co-owner in connection with an acquisition of real estate in certain situations.

Subject to the requirements necessary to maintain EastGroup’s qualifications as a REIT, the Company may acquire securities of entities engaged in real estate activities or securities of other issuers, including for the purpose of exercising control over those entities.

The Company intends to continue to qualify as a REIT under the Code. To maintain its status as a REIT, the Company is required to, among other things, distribute at least 90% of its ordinary taxable income to its stockholders. If the Company has a capital gain, it has the option of (i) deferring recognition of the capital gain through a tax-deferred exchange, (ii) declaring and paying a capital gain dividend on any recognized net capital gain resulting in no corporate level tax, or (iii) retaining and paying corporate income tax on its net long-term capital gain, with shareholders reporting their proportional share of the undistributed long-term capital gain and receiving a credit or refund of their share of the tax paid by the Company.

EastGroup has no present intention of acting as an underwriter of offerings of securities of other issuers. The strategies and policies set forth above were determined and are subject to review by EastGroup's Board of Directors, which may change such strategies or policies based upon its evaluation of the state of the real estate market, the performance of EastGroup's assets, capital and credit market conditions, and other relevant factors. EastGroup provides annual reports to its stockholders, which contain financial statements audited by the Company’s independent registered public accounting firm.

Competition
The market for the leasing of industrial real estate is competitive. We experience competition for tenants from other existing assets in proximity to our buildings as well as from new development. Institutional investors, other REITs and local real estate operators generally own such properties; however, no single competitor or small group of competitors is dominant in our current markets. Even so, as a result of competition, we may have to provide concessions, incur charges for tenant improvements or offer other inducements, all of which may have an adverse impact on our results of operations. The market for the acquisition of industrial real estate is also competitive. We compete for real property investments with other REITs and institutional investors such as pension funds and their advisors, private real estate

investment funds, insurance company investment accounts, private investment companies, individuals and other entities engaged in real estate investment activities.

Environmental Property Matters

Under various federal, state and local laws, ordinances and regulations, an owner of real estate may be liable for the costs of removal or remediation of certain hazardous or toxic substances on or in such property. Many such laws impose liability without regard to whether the owner knows of, or was responsible for, the presence of such hazardous or toxic substances. The presence of such substances, or the failure to properly remediate such substances, may adversely affect the owner's ability to sell or rent such property or to use such property as collateral in its borrowings. EastGroup's properties have been subjected to Phase I Environmental Site Assessments (ESAs) by independent environmental consultants and, as necessary, have been subjected to Phase II ESAs. These reports have not revealed any potential significant environmental liability. Management of EastGroup is not aware of any environmental liability that would have a material adverse effect on EastGroup's business, assets, financial position or results of operations. See "Item 1A. Risk Factors" in this Annual Report for additional information.

Environmental, Social and Governance (ESG) Matters
At EastGroup, protecting the environment is important to the Company's employees, families, customers and communities. The Company strives to support sustainability through its commitment to build high performance and environmentally responsible properties. Through EastGroup's continued efforts, numerous properties have been Leadership in Energy and Environmental Design (LEED) and ENERGY STAR certified with the remainder reflecting the Company's commitment to pursue environmentally conscious performance and standards. The Company's continued commitment to sustainability best practices creates long-term value for the environment, the Company and shareholders.

EastGroup and its employees are committed to social responsibility and participate in various charitable service organizations in the Company's business communities. EastGroup's employees volunteer for numerous charities, and the Company coordinates volunteer opportunities for its employees and allows time away from work in order to encourage participation and increase social engagement in all of the communities in which we operate.

SUPPLEMENTAL MATERIAL U.S. FEDERAL INCOME TAX CONSIDERATIONS

This summary updates and supersedes the discussion contained under the caption "Material United States Federal Income Tax Considerations" in (i) the prospectus within our Registration Statement on Form S-3 filed with the SEC on March 6, 2017 (the "Prospectus") and (ii) the prospectus supplement that supplements the Prospectus filed with the SEC on February 15, 2018, and should be read in conjunction therewith and is subject to qualifications set forth therein.
The following summary addresses U.S. federal income tax considerations related to our election to be subject to taxation as a REIT and the ownership and disposition of our common stock or preferred stock that we anticipate being material to holders of such securities. Except to the limited extent discussed below, this summary does not address any foreign, state, or local tax consequences of holding our common stock, or preferred stock. The provisions of the Internal Revenue Code of 1986, as amended (the "Code") concerning the U.S. federal income tax treatment of a REIT and its shareholders and security holders are highly technical and complex; the following discussion sets forth only certain aspects of those provisions. This summary is intended to provide you with general information only, it is not intended as a substitute for careful tax planning, and it is not tax advice.
This summary is based on provisions of the Code, applicable final and temporary Treasury Regulations, judicial decisions, and administrative rulings and practice, all in effect as of the date of this prospectus, and should not be construed as legal or tax advice. No assurance can be given that future legislative or administrative changes or judicial decisions will not affect the accuracy of the descriptions or conclusions contained in this summary. In addition, any such changes may be retroactive and apply to transactions entered into prior to the date of their enactment, promulgation or release. We do not expect to seek a ruling from the IRS regarding any of the U.S. federal income tax issues discussed in this prospectus, and no assurance can be given that the IRS will not challenge any of the positions we take and that such a challenge will not succeed. This discussion does not purport to address all aspects of U.S. federal income taxation that may be relevant to you in light of your particular investment circumstances, or if you are a type of investor subject to special tax rules. This discussion also does not consider tax considerations that may be relevant with respect to securities we may issue, or selling security holders may sell, other than our common stock and preferred stock described below. Each time we or selling security holders sell securities, we will provide a prospectus supplement that will contain specific information about the terms of that sale and may add to or update the discussion below as appropriate.
PROSPECTIVE PURCHASERS OF OUR SECURITIES ARE URGED TO CONSULT THEIR TAX ADVISORS PRIOR TO ANY INVESTMENT IN OUR COMMON STOCK OR PREFERRED STOCK CONCERNING THE POTENTIAL U.S. FEDERAL, STATE, LOCAL AND FOREIGN TAX CONSEQUENCES OF THE INVESTMENT WITH SPECIFIC REFERENCE TO THEIR OWN TAX SITUATIONS. PROSPECTIVE PURCHASERS ALSO ARE URGED TO REFER TO THE APPLICABLE PROSPECTUS SUPPLEMENT FOR ANY AMENDMENTS OR CHANGES TO THIS SUMMARY.

Except as otherwise noted, references in this discussion of "Supplemental Material U.S. Federal Income Tax Considerations" to "we," "our," "us" and "our company" refer to EastGroup Properties, Inc.

Taxation of our Company

We have elected to be taxed as a REIT under Sections 856 through 860 of the Code. We believe that we have been organized and operated in conformity with the requirements for qualification and taxation as a REIT under the Code beginning with our taxable year ended November 30, 1969 and that our intended manner of operation will enable us to continue to meet the requirements for qualification and taxation as a REIT for U.S. federal income tax purposes.

In connection with the filing of this prospectus, our tax counsel, Goodwin Procter LLP, is rendering an opinion to us to the effect that, commencing with our taxable year ended December 31, 2014, we have been organized in conformity with the requirements for qualification and taxation as a REIT under the Code and our prior, current and proposed ownership, organization and method of operations have allowed and will continue to allow us to satisfy the requirements for qualification and taxation as a REIT under the Code commencing with our taxable year ended December 31, 2014 and for subsequent taxable years. The opinion of Goodwin Procter LLP is based upon various assumptions and our representations as to our past and contemplated future ownership, investments, distributions, share valuations and operations, among other things. The opinion of Goodwin Procter LLP is expressly conditioned upon the accuracy of these and other assumptions and upon our representations, which Goodwin Procter LLP has not verified and will not verify. Moreover, our qualification and taxation as a REIT will depend upon our ability to meet, through actual annual operating results, distribution levels, and diversity of stock ownership, the various and complex REIT qualification tests imposed under the Code, the results of which have not been and will not be reviewed or verified by Goodwin Procter LLP. See “-Qualification as a REIT” below. Accordingly, no assurance can be given that we have satisfied or will satisfy the requirements for qualification and taxation as a REIT. The opinion of Goodwin Procter LLP is based upon the law in effect as of the date of the opinion (or, with respect to past years, the law in effect for such years), which is subject to change either prospectively or retroactively. Opinions of counsel impose no obligation on counsel to advise us or the holders of our stock of any subsequent change in the matters stated, represented or assumed, or of any subsequent change in the applicable law. Changes in applicable law could modify the conclusions expressed in the opinion. Unlike a ruling from the IRS, an opinion of Goodwin Procter LLP is not binding on the IRS and no assurance can be given that the IRS could not successfully challenge our qualification as a REIT.

If we qualify as a REIT, we generally will be allowed to deduct dividends paid to our shareholders, and, as a result, we generally will not be subject to U.S. federal income tax on that portion of our ordinary income and net capital gain that we currently distribute to our shareholders. We intend to make distributions to our shareholders on a regular basis as necessary to avoid material U.S. federal income tax and to comply with the REIT requirements. See “—Qualification as a REIT—Annual Distribution Requirements” below.

Notwithstanding the foregoing, even if we qualify for taxation as a REIT, we nonetheless may be subject to U.S. federal income tax or excise tax in certain circumstances, including the following:

we will be required to pay U.S. federal income tax on our undistributed REIT taxable income, including net capital gain;

we may be subject to tax at the highest U.S. federal corporate income tax rate on certain income from “foreclosure property” (generally, property acquired by reason of default on a lease or indebtedness held by us);

we will be subject to a 100% U.S. federal income tax on net income from “prohibited transactions” (generally, certain sales or other dispositions of property, sometimes referred to as “dealer property,” held primarily for sale to customers in the ordinary course of business, other than foreclosure property) unless the gain is realized in a “taxable REIT subsidiary,” or TRS, or such property has been held by us for at least two years and certain other requirements are satisfied;

if we fail to satisfy either the 75% gross income test or the 95% gross income test (discussed below), but nonetheless maintain our qualification as a REIT pursuant to certain relief provisions, we will be subject to a 100% U.S. federal income tax on the greater of (i) the amount by which we fail the 75% gross income test or (ii) the amount by which we fail the 95% gross income test, in either case, multiplied by a fraction intended to reflect our profitability;

if we fail to satisfy any of the asset tests, and the failure is not a failure of the 5% or the 10% asset test that qualifies under the De Minimis Exception but the failure does qualify under the General Exception, both as described below under “-Qualification as a REIT-Asset Tests,” then we will have to pay an excise tax equal to the greater of (i) $50,000 and (ii) an amount determined by multiplying the net income generated during a specified period by the assets that

caused the failure by the highest U.S. federal corporate income tax rate;

if we fail to satisfy any REIT requirements other than the gross income test or asset test requirements, described below under “-Qualification as a REIT-Income Tests” and “-Qualification as a REIT-Asset Tests,” respectively, and we qualify for a reasonable cause exception, then we will have to pay a penalty equal to $50,000 for each such failure;
we will be subject to a 4% excise tax on certain undistributed amounts if certain distribution requirements are not satisfied;

we may be required to pay monetary penalties to the IRS in certain circumstances, including if we fail to meet record-keeping requirements intended to monitor our compliance with rules relating to the composition of a REIT's shareholders, as described below in "-Recordkeeping Requirements;"

if we dispose of an asset acquired by us from a C corporation in a transaction in which we took the C corporation's tax basis in the asset, we may be subject to tax at the highest U.S. federal corporate income tax rate on the appreciation inherent in such asset as of the date of acquisition by us;

we will be required to pay a 100% tax on any redetermined rents, redetermined deductions, excess interest and redetermined TRS service income. In general, redetermined rents are rents from real property that are overstated as a result of services furnished by our TRS. Redetermined deductions and excess interest generally represent amounts that are deducted by a TRS for amounts paid to us that are in excess of the amounts that would have been deducted based on arm's-length negotiations. Redetermined TRS service income generally means the additional gross income a TRS would recognize if it were paid an arm's length fee for services provided to, or on behalf of, us; and

income earned by our TRS or any other subsidiaries that are taxable as C corporations will be subject to regular U.S. federal corporate income tax.

No assurance can be given that the amount of any such U.S. federal income or excise taxes will not be substantial. In addition, we and our subsidiaries may be subject to a variety of taxes, including payroll taxes and state, local and foreign income, property and other taxes on assets and operations. We could also be subject to tax in situations and on transactions not presently contemplated.

Qualification as a REIT

In General

The REIT provisions of the Code apply to a domestic corporation, trust or association (i) that is managed by one or more trustees or directors, (ii) the beneficial ownership of which is evidenced by transferable shares or by transferable certificates of beneficial interest, (iii) that properly elects to be taxed as a REIT and such election has not been terminated or revoked, (iv) that is neither a financial institution nor an insurance company, (v) that uses a calendar year for U.S. federal income tax purposes, and (vi) that meets the additional requirements discussed below. The discussion below summarizes current law except where expressly noted otherwise. We do not believe any differences between the current requirements for qualification as a REIT and the requirements in effect for any prior year have prevented us from qualifying as a REIT for any period.

Ownership Tests

In order to continue to qualify as a REIT, (i) the beneficial ownership of our stock must be held by 100 or more persons during at least 335 days of a 12-month taxable year (or during a proportionate part of a taxable year of less than 12 months) for each of our taxable years and (ii) during the last half of each taxable year, no more than 50% in value of our stock may be owned, directly or indirectly, by or for five or fewer individuals (the "5/50 Test"). Stock ownership for purposes of the 5/50 Test is determined by applying the constructive ownership provisions of Section 544(a) of the Code, subject to certain modifications. The term "individual" for purposes of the 5/50 Test includes a private foundation, a trust providing for the payment of supplemental unemployment compensation benefits, and a portion of a trust permanently set aside or to be used exclusively for charitable purposes. A "qualified trust" described in Section 401(a) of the Code and exempt from tax under Section 501(a) of the Code generally is not treated as an individual; rather, stock held by it is generally treated as owned proportionately by its beneficiaries.

We believe that we have satisfied and will continue to satisfy the above ownership requirements. In addition, our charter restricts ownership and transfers of our stock that would violate these requirements, although these restrictions may not be effective in all circumstances to prevent a violation. We will be deemed to
have satisfied the 5/50 Test for a particular taxable year if we have complied with all the requirements for ascertaining the ownership of our outstanding stock in that taxable year and have no reason to know that we have violated the 5/50 Test.

Income Tests

In order to maintain qualification as a REIT, we must annually satisfy two gross income requirements:

(1) First, at least 75% of our gross income (excluding gross income from prohibited transactions and certain other income and gains as described below) for each taxable year must be derived, directly or indirectly, from investments relating to real property or mortgages on real property or from certain types of temporary investments (or any combination thereof). Qualifying income for purposes of this 75% gross income test generally includes: (a) rents from real property, (b) interest on obligations secured by mortgages on real property or on interests in real property, (c) dividends or other distributions on, and gain from the sale of, shares

in other REITs, (d) gain from the sale of real estate assets (but not including certain debt instruments of publicly offered REITs that are not secured by mortgages on real property or interests on real property and gain from prohibited transactions), (e) income and gain derived from foreclosure property, and (f) income from certain types of temporary investments; and
(2) Second, in general, at least 95% of our gross income (excluding gross income from prohibited transactions and certain other income and gains as described below) for each taxable year must be derived from the real property investments described above and from other types of dividends and interest, gain from the sale or disposition of stock or securities that are not dealer property, or any combination of the above.
Rents we receive will qualify as rents from real property in satisfying the gross income requirements for a REIT described above only if several conditions are met. First, the amount of rent generally must not be based in whole or in part on the income or profits of any person. However, an amount received or accrued generally will not be excluded from the term “rents from real property” solely by reason of being based on a fixed percentage or percentages of receipts or sales. Second, rents received from a “related party tenant” will not qualify as rents from real property in satisfying the gross income tests unless the tenant is a TRS and either (i) at least 90% of the property is leased to unrelated tenants and the rent paid by the TRS is substantially comparable to the rent paid by the unrelated tenants for comparable space, or (ii) the property leased is a “qualified lodging facility,” as defined in Section 856(d)(9)(D) of the Code, or a “qualified health care property,” as defined in Section 856(e)(6)(D)(i), and certain other conditions are satisfied. A tenant is a related party tenant if the REIT, or an actual or constructive owner of 10% or more of the REIT, actually or constructively owns 10% or more of the tenant. Third, if rent attributable to personal property, leased in connection with a lease of real property, is greater than 15% of the total rent received under the lease (determined based on the fair market value as of the beginning and end of the taxable year), then the portion of rent attributable to the personal property will not qualify as rents from real property.
Generally, for rents to qualify as rents from real property for the purpose of satisfying the gross income tests, we may provide directly only an insignificant amount of services, unless those services are “usually or customarily rendered” in connection with the rental of real property and not otherwise considered “rendered to the occupant” under the applicable tax rules. Accordingly, we may not provide “impermissible services” to tenants (except through an independent contractor from whom we derive no revenue and that meets other requirements or through a TRS) without giving rise to “impermissible tenant service income.” Impermissible tenant service income is deemed to be at least 150% of the direct cost to us of providing the service. If the impermissible tenant service income exceeds 1% of our total income from a property, then all of the income from that property will fail to qualify as rents from real property. If the total amount of impermissible tenant service income from a property does not exceed 1% of our total income from the property, the services will not disqualify any other income from the property that qualifies as rents from real property, but the impermissible tenant service income will not qualify as rents from real property.

We do not intend to charge significant rent that is based in whole or in part on the income or profits of any person, derive significant rents from related party tenants, derive rent attributable to personal property leased in connection with real property that exceeds 15% of the total rents from that property, or derive impermissible tenant service income that exceeds 1% of our total income from any property if the treatment of the rents from such property as nonqualified rents could cause us to fail to qualify as a REIT.
Distributions that we receive from a TRS will be classified as dividend income to the extent of the earnings and profits of the TRS. Such distributions will generally constitute qualifying income for purposes of the 95% gross income test, but not under the 75% gross income test unless attributable to investments of certain new capital during the one-year period beginning on the date of receipt of the new capital (as described below under “Qualification as a REIT-Income Tests-Qualified temporary investment income”). Any dividends received by us from a REIT will be qualifying income for purposes of both the 75% and 95% gross income tests.
If we fail to satisfy one or both of the 75% or the 95% gross income tests, we may nevertheless qualify as a REIT for a particular year if we are entitled to relief under certain provisions of the Code. Those relief provisions generally will be available if our failure to meet such tests is due to reasonable cause and not due to willful neglect and we file a schedule describing each item of our gross income for such year(s) in accordance with the applicable Treasury

Regulations. It is not possible, however, to state whether in all circumstances we would be entitled to the benefit of these relief provisions. As discussed above in "-Taxation of Our Company," even if these relief provisions were to apply, we would be subject to U.S. federal corporate income tax to the extent we fail to meet the 75% or 95% gross income tests.

Foreclosure property. Foreclosure property is real property (including interests in real property) and any personal property incident to such real property (1) that is acquired by a REIT as a result of the REIT having bid on the property at foreclosure, or having otherwise reduced the property to ownership or possession by agreement or process of law, after there was a default (or default was imminent) on a lease of the property or a mortgage loan held by the REIT and secured by the property, (2) for which the related loan or lease was made, entered into or acquired by the REIT at a time when default was not imminent or anticipated and

(3) for which such REIT makes an election to treat the property as foreclosure property. REITs generally are subject to tax at the highest U.S. federal corporate income tax rate on any net income from foreclosure property, including any gain from the disposition of the foreclosure property, other than income that would otherwise be qualifying income for purposes of the 75% gross income test. Any gain from the sale of property for which a foreclosure property election has been made will not be subject to the 100% tax on gains from prohibited transactions described above, even if the property is held primarily for sale to customers in the ordinary course of a trade or business.

Hedging transactions. We may enter into hedging transactions with respect to one or more of our assets or liabilities. Hedging transactions could take a variety of forms, including interest rate swaps or cap agreements, options, futures contracts, forward rate agreements or similar financial instruments. Except to the extent as may be provided by future Treasury Regulations, any income from a hedging transaction which is (1) clearly identified as such before the close of the day on which it was acquired, originated or entered into, and (2) accompanied by a substantially contemporaneous identification of the item being hedged, including gain from the disposition or termination of such a transaction, will not constitute gross income for purposes of the 75% and 95% gross income tests, provided that the hedging transaction is entered into (i) in the normal course of our business primarily to manage risk of interest rate or price changes or currency fluctuations with respect to indebtedness incurred or to be incurred by us to acquire or carry real estate assets, (ii) primarily to manage the risk of currency fluctuations with respect to any item of income or gain that would be qualifying income under the 75% or 95% gross income tests (or any property which generates such income or gain), or (iii) to hedge against transactions described in clause (i) or (ii) and is entered into in connection with the extinguishment of debt or a sale of property that is being hedged against by the transaction described in clause (i) or (ii). To the extent we enter into other types of hedging transactions or do not make proper identifications, as applicable, the income from those transactions is likely to be treated as non-qualifying income for purposes of both the 75% and 95% gross income tests. We intend to structure, monitor and document our hedging transactions so that such transactions do not jeopardize our ability to qualify as a REIT. No assurances can be given, however, that our hedging activities will not give rise to income that does not qualify for purposes of either or both of the gross income tests and that such income will not adversely affect our ability to satisfy REIT qualification requirements.

Qualified temporary investment income. Income derived from certain types of temporary stock and debt investments made with the proceeds of certain stock and debt offerings (but not including proceeds received pursuant to a dividend reinvestment plan), not otherwise treated as qualifying income for the 75% gross income test, generally will nonetheless constitute qualifying income for purposes of the 75% gross income test for the year following such an offering. More specifically, qualifying income for purposes of the 75% gross income test includes “qualified temporary investment income,” which generally means any income that is attributable to stock or a debt instrument, is attributable to the temporary investment of new equity capital and certain debt capital, and is received or accrued during the one-year period beginning on the date on which the REIT receives such new capital. After the one-year period following a qualifying equity or debt offering, income from investments of the proceeds of such offering will be qualifying income for purposes of the 75% gross income test only if derived from one of the other qualifying sources enumerated above.

Asset Tests

At the close of each quarter of each taxable year, we must also satisfy five tests relating to the nature of our assets. First, real estate assets, cash and cash items, and government securities must represent at least 75% of the value of our total assets. Real estate assets include interests in real property (such as land, buildings, leasehold interests in real property and personal property leased with real property if the rents attributable to the personal property would be rents from real property under the income tests discussed above), interests in mortgages on real property or on interest in real property, shares in other qualifying REITs, debt instruments issued by publicly offered REITs, and stock or debt instruments held for less than one year that are purchased with the proceeds from an offering of shares of our stock or certain long-term debt. Second, not more than 25% of our total assets may be represented by securities other than those in the 75% asset class. Third, of the investments that are not included in the 75% asset class and are not securities of our TRSs, (i) the value of any one issuer’s securities owned by us may not exceed 5% of the value of our total assets and (ii) we may not own more than 10% by vote or by value of any one issuer’s outstanding securities. For

purposes of the 10% value test, debt instruments issued by a partnership are not classified as "securities" to the extent of our interest as a partner in such partnership (based on our proportionate share of the partnership's equity interests and certain debt securities) or if at least 75% of the partnership's gross income, excluding income from prohibited transactions, is qualifying income for purposes of the 75% gross income test. For purposes of the 10% value test, the term "securities" also does not include certain instruments, such as debt securities issued by another REIT, certain "straight debt" securities (for example, qualifying debt securities of a corporation of which we own no more than a de minimis amount of equity interest), loans to individuals or estates, and accrued obligations to pay rent. Fourth, securities of our TRSs cannot represent more than 20% of the value of our total assets. Fifth, not more than 25% of the value of our total assets may be represented by debt instruments of publicly offered REITs that are not secured by mortgages on real property or interest in real property. Although we believe we have met these asset tests and we intend to continue to meet them, no assurance can be given that we have met them or will be able to do so. For purposes of these asset tests, we are treated as holding our proportionate share of our subsidiary partnerships' assets. Also, for purposes of these asset tests, pursuant to an IRS ruling, we generally may treat shares of certain money market mutual funds as "cash items."

We will monitor the status of our assets for purposes of the various asset tests and will endeavor to manage our portfolio in order to comply at all times with such tests. If we fail to satisfy the asset tests at the end of a calendar quarter, other than our first calendar quarter as a REIT, we will not lose our REIT status if one of the following exceptions applies:

we satisfied the asset tests at the end of the preceding calendar quarter and the discrepancy between the value of our assets and the asset test requirements arose from changes in the market values of our assets and was not wholly or partly caused by the acquisition of one or more non-qualifying assets; or

we eliminate any discrepancy within 30 days after the close of the calendar quarter in which it arose.

Moreover, if we fail to satisfy the asset tests at the end of a calendar quarter during a taxable year, we will not lose our REIT status if one of the following additional exceptions applies:

De Minimis Exception: the failure is due to a violation of the 5% or 10% asset tests referenced above and is “de minimis” (meaning that the failure is one that arises from our ownership of assets the total value of which does not exceed the lesser of 1% of the total value of our assets at the end of the quarter in which the failure occurred and $10 million), and we either dispose of the assets that caused the failure or otherwise satisfy the asset tests within six months after the last day of the quarter in which our identification of the failure occurred; or

General Exception: all of the following requirements are satisfied: (i) the failure does not qualify for the above De Minimis Exception, (ii) the failure is due to reasonable cause and not willful neglect, (iii) we file a schedule in accordance with the applicable Treasury Regulations providing a description of each asset that caused the failure, and (iv) we either dispose of the assets that caused the failure or otherwise satisfy the asset tests within six months after the last day of the quarter in which our identification of the failure occurred. A REIT that utilizes this general relief provision must pay an excise tax equal to the greater of (a) $50,000 or (b) the product of the net income generated during a specified period by the asset that caused the failure and the highest U.S. federal corporate income tax rate.

Annual Distribution Requirements

In order to qualify as a REIT, each taxable year we must distribute dividends (other than capital gain dividends) to our shareholders in an amount at least equal to (A) the sum of (i) 90% of our “REIT taxable income” (determined without regard to the dividends paid deduction and excluding net capital gains), and (ii) 90% of the net income (after tax), if any, from foreclosure property, minus (B) the sum of certain items of non-cash income. We generally must pay such distributions in the taxable year to which they relate (or be treated as having paid such distributions in such year, as described further below under “Taxation of U.S. Shareholders -- Distributions”), or in the following taxable year if declared before we timely file our tax return for such year and if paid on or before the first regular dividend payment after such declaration. Subject to certain requirements, we may satisfy all or part of our distribution requirement by paying taxable stock dividends.

To the extent that we do not distribute all of our net capital gain and REIT taxable income, we will be subject to regular U.S. federal corporate income tax, and potentially, state and local tax, on these retained amounts. Furthermore, if we should fail to distribute during each calendar year at least the sum of (i) 85% of our “ordinary income,” as defined in Section 4981(e)(1) of the Code, for such year, (ii) 95% of our “capital gain net income,” as defined in Section 4981(e)(2) of the Code, for such year, and (iii) 100% of any corresponding undistributed amounts from prior periods, we will be subject to a 4% nondeductible federal excise tax on the excess of such required distribution over the sum of amounts actually distributed plus retained income from such taxable year on which we paid corporate income tax.

Under certain circumstances, we may be able to rectify a failure to meet the distribution requirement for a year by paying “deficiency dividends” to our shareholders in a later year that may be included in our deduction for dividends paid for the earlier year. Thus, we may be able to avoid being taxed on amounts distributed as deficiency dividends; however, we will be required to pay interest based upon the amount of any deduction taken for deficiency dividends.

For taxable years beginning before January 1, 2015, in order for our distributions to have satisfied the annual distribution requirements for REITs and provided us with a REIT-level tax deduction, the distributions must not have been "preferential dividends." A dividend is not a preferential dividend if the distribution is (i) pro rata among all outstanding shares of stock within a particular class, and (ii) in accordance with the preferences among different classes of stock as set forth in our organizational documents. The preferential dividend rule for publicly offered REITs was repealed for distributions made in taxable years beginning after December 31, 2014. As such, we are no longer subject to these preferential dividend requirements. Any non-publicly offered REIT in which we invest would be subject to the preferential dividend rule regardless of the date of the distribution.

Pursuant to an IRS ruling, the prohibition on preferential dividends applicable to taxable years beginning before January 1, 2015 did not prohibit REITs from offering shares under a distribution reinvestment plan at discounts of up to 5% of fair market value, but a discount in excess of 5% of the fair market value of the shares would have been considered a preferential dividend. We believe that our distribution reinvestment plan has complied with those requirements.

We may retain and pay income tax on net long-term capital gains we received during the tax year. To the extent we so elect, (i) each shareholder must include in its income (as long-term capital gain) its proportionate share of our undistributed long-term capital gains, (ii) each shareholder is deemed to have paid, and receives a credit for, its proportionate share of the tax paid by us on the undistributed long-term capital gains, and (iii) each shareholder's basis in its stock is increased by the included amount of the undistributed long-term capital gains less their share of the tax paid by us.

To qualify as a REIT, we may not have, at the end of any taxable year, any undistributed earnings and profits accumulated in any non-REIT taxable year. We believe that we have not had any non-REIT earnings and profits at the end of any taxable year covered by this rule, and we intend to distribute any non-REIT earnings and profits that we accumulate before the end of any taxable year in which we accumulate such earnings and profits.

Failure to Qualify

If we fail to qualify as a REIT and such failure is not an asset test or gross income test failure subject to the cure provisions described above, or for taxable years beginning before January 1, 2015 the result of preferential dividends, we generally will be eligible for a relief provision if the failure is due to reasonable cause and not willful neglect and we pay a penalty of $50,000 with respect to such failure.

If we fail to qualify for taxation as a REIT in any taxable year and no relief provisions apply, we generally will be subject to regular U.S. federal corporate income tax on our taxable income. Distributions to our shareholders in any year in which we fail to qualify as a REIT will not be deductible by us nor will they be required to be made. In such event, to the extent of our current or accumulated earnings and profits, all distributions to our shareholders will be taxable as dividend income. Subject to certain limitations in the Code, corporate shareholders may be eligible for the dividends received deduction, and individual, trust and estate shareholders may be eligible to treat the dividends received from us as qualified dividend income taxable as net capital gains, under the provisions of Section 1(h)(11) of the Code. However, non-corporate shareholders (including individuals) will not be able to deduct 20% of certain dividends they receive from us. Unless entitled to relief under specific statutory provisions, we also will be ineligible to elect to be taxed as a REIT again prior to the fifth taxable year following the first year in which we failed to qualify as a REIT under the Code.

Our qualification as a REIT for U.S. federal income tax purposes will depend on our continuing to meet the various requirements summarized above governing the ownership of our outstanding stock, the nature of our assets, the sources of our income, and the amount of our distributions to our shareholders. Although we intend to operate in a manner that will enable us to comply with such requirements, there can be no certainty that such intention will be realized. In addition, because the relevant laws may change, compliance with one or more of the REIT requirements may become impossible or impracticable for us.

Prohibited Transaction Tax

Any gain realized by us on the sale of any property held (other than foreclosure property) as inventory or other property held primarily for sale to customers in the ordinary course of business, including our share of any such gain realized by our subsidiary partnerships, will be treated as income from a "prohibited transaction" that is subject to a 100% penalty tax. Whether property is held as inventory or primarily for sale to customers in the ordinary course of a trade or business depends upon all the facts and circumstances with respect to the particular transaction. However, the Code provides a "safe harbor" pursuant to which sales of properties held for at least two years and meeting certain other requirements will not give rise to prohibited transaction income.

We generally intend to hold properties for investment, but we have made and will make sales of properties consistent with our strategic objectives. We believe our past sales in open tax years are not considered prohibited transactions.

However, we have made and we may make sales at a gain that do not satisfy the safe harbor requirements described above. There can be no assurance that the IRS will not contend that one or more of these sales are subject to the 100% penalty tax. The 100% penalty tax will not apply to gains from the sale of property realized through a U.S. TRS or other U.S. taxable corporation, although such income will be subject to regular U.S. federal corporate income tax.

Recordkeeping Requirements

To avoid a monetary penalty, we must request on an annual basis information from certain of our shareholders designed to disclose the actual ownership of our outstanding stock. We intend to comply with these requirements.

Qualified REIT Subsidiaries and Disregarded Entities

If a REIT owns a subsidiary that is a "qualified REIT subsidiary," or QRS, or if a REIT owns 100% of the membership interests in a domestic limited liability company or other domestic unincorporated entity that does not elect to be treated as a corporation for U.S. federal income tax purposes, the separate existence of the QRS, limited liability company or other unincorporated entity generally will be disregarded for U.S. federal income tax purposes. Generally, a QRS is a corporation, other than a TRS, all of the stock of which is owned by a REIT. All assets, liabilities, and items of income, deduction, and credit of the QRS or disregarded entity will be treated as assets, liabilities, and items of income, deduction, and credit of its owner. To the extent we own a QRS or a disregarded entity, neither will be subject to U.S. federal corporate income taxation, although such entities may be subject to state and local taxation in some states or foreign taxes if they do business or own property outside the United States.

Taxation of Subsidiary Partnerships

We have held and may in the future hold investments through entities that are classified as partnerships for U.S. federal income tax purposes. Under the Code, a partnership generally is not subject to U.S. federal income tax, but is required to file a partnership tax information return each year. In general, the character of each partner's share of each item of income, gain, loss, deduction, credit, and tax preference is determined at the partnership level. Each partner is then allocated a distributive share of such items and is required to take such items into account in determining the partner's income. Each partner includes such amount in income for any taxable year of the partnership ending within or with the taxable year of the partner, without regard to whether the partner has received or will receive any cash distributions from the partnership. Cash distributions, if any, from a partnership to a partner generally are not taxable unless and to the extent they exceed the partner's basis in its partnership interest immediately before the distribution. Any amounts in excess of such tax basis will generally be treated as a sale of such partner's interest in the partnership. While generally the rules described above mean that a partnership is not subject to U.S. federal income tax, new rules applicable to U.S. federal income tax audits of partnerships effective for taxable years beginning after December 31, 2017 may require the partnership to pay the hypothetical increase in partner-level taxes (including interest and penalties) resulting from an adjustment of partnership tax items on audit or in other tax proceedings (an "imputed underpayment"), unless the partnership elects an alternative method under which the taxes resulting from the adjustment (and interest and penalties) are assessed at the partner level (often referred to as a "push-out election"), subject to a higher rate of interest than otherwise would apply. Treasury Regulations provide that when a push-out election affects a partner that is a REIT, such REIT may be able to use deficiency dividend procedures with respect to adjustments resulting from such election. It is possible that partnerships in which we directly and indirectly invest may be subject to U.S. federal income tax, interest and penalties in the event of a U.S. federal income tax audit as a result of these law changes, and as a result, we could be required to bear the economic costs of taxes attributable to our partners.

For purposes of the REIT income and assets tests, a REIT that is a partner in a partnership will be deemed to own its proportionate share of the assets of the partnership and will be deemed to earn its proportionate share of the partnership's income. The assets and gross income of the partnership retain the same character in the hands of the REIT for purposes of the gross income and asset tests applicable to REITs. Our proportionate share of the assets and items of income of any subsidiary partnership, including such partnership's share of the assets and liabilities and items of income with respect to any partnership or disregarded entity in which it holds an interest, will be treated as our assets and liabilities and items of income for purposes of applying the REIT asset and income tests.

We may form joint ventures taxed as partnerships and our joint venture partners may contribute property to such subsidiary partnerships. If our partner contributes appreciated property (i.e., property with a value in excess of adjusted tax basis) in exchange for a partnership interest, the subsidiary partnership's initial tax basis in the property acquired generally will be less than the purchase price of the property. Although the partnership tax rules of Section 704(c) of the Code would generally attempt to provide us as the non-contributing partner with the depreciation deductions comparable to what we would receive if the subsidiary partnership purchased the appreciated assets for cash in a taxable transaction (and obtained an initial tax basis equal to the purchase price), absent certain elections, which would accelerate income to the contributor, the depreciation would be limited to tax basis. Consequently, our

depreciation deductions for such properties may be less, and our tax gain on a sale of such properties may be more, than the deductions or gain, respectively, that we would have if the subsidiary partnership acquired these properties in taxable transactions. Alternatively, if we contribute appreciated property to a subsidiary partnership, such partnership may elect to use a method of allocation under Section 704(c) of the Code that accelerates income to us.

The discussion above assumes that any subsidiary partnerships in which we invest will be treated as "partnerships" for U.S. federal income tax purposes. Generally, a domestic unincorporated entity with two or more owners is treated as a partnership for U.S. federal income tax purposes unless it affirmatively elects to be treated as a corporation. However, certain "publicly traded partnerships" are treated as corporations for U.S. federal income tax purposes. Pursuant to Section 7704 of the Code, a partnership that does not elect to be treated as a corporation nevertheless will be treated as a corporation for U.S. federal income tax purposes if it is a "publicly traded partnership," it does not derive at least 90% of its gross income from certain specified sources of "qualifying income" within the meaning of that provision and it meets certain other requirements. A "publicly traded partnership" is any

partnership (i) the interests in which are traded on an established securities market or (ii) the interests in which are readily tradable on a "secondary market or the substantial equivalent thereof." Under the relevant Treasury Regulations, interests in a partnership will not be considered readily tradable on a secondary market or on the substantial equivalent of a secondary market if the partnership qualifies for specified "safe harbors," which are based on the specific facts and circumstances relating to the partnership. For example, interests in a partnership are not readily tradable on a secondary market or the substantial equivalent thereof if (i) all interests in the partnership were issued in a transaction (or transactions) that was not required to be registered under the Securities Act, and (ii) the partnership does not have more than 100 partners at any time during the taxable year of the partnership (determined by counting indirect partners who held their partnership interest through certain flow-through entities). If any subsidiary partnership were a publicly traded partnership, it would be taxed as a corporation unless at least 90% of its gross income consists of "qualifying income" under Section 7704 of the Code. Qualifying income is generally real property rents and other types of passive income, and the income requirements applicable to us to qualify as a REIT under the Code and the definition of qualifying income under the publicly traded partnership rules are very similar. We intend to operate so that any subsidiary partnerships in which we invest will satisfy at least one of the above-mentioned safe harbors, and/or comply with the qualifying income exception, so as to avoid being taxed as a corporation under these rules. However, we may not control all of the subsidiary partnerships in which we may invest, and treatment of a subsidiary partnership as a corporation could prevent us from qualifying as a REIT.

Investments in Certain Debt Instruments

We may acquire mortgage, mezzanine, bridge loans and other debt investments. If a mortgage loan is secured by both real property and personal property, then such mortgage shall be treated as a wholly qualifying real estate asset and all interest shall be treated as mortgage interest for purposes of the 75% gross income test, provided that the fair market value of such personal property does not exceed 15% of the total fair market value of all such property on the date that we committed to acquire or modify the loan (or on the date of disposition for purposes of whether gain from a disposition of the mortgage is qualifying income for purposes of the 75% gross income test), even if the real property collateral value is less than the outstanding balance of the loan. However, if a mortgage loan that is secured by both real property and personal property does not satisfy the 15% test articulated in the previous sentence or if such mortgage loan is entered into or acquired in taxable years beginning before January 1, 2016, then such mortgage may not be a qualifying real estate asset in its entirety for purposes of the 75% asset test and/or a portion of the interest income from such mortgage may not constitute qualifying mortgage interest for purposes of the 75% gross income test if the amount of the loan outstanding exceeds the fair market value of the real property collateral on the date that we committed to acquire or modify the loan.

To the extent that we derive interest income from a mortgage loan where all or a portion of the amount of interest payable is contingent, such income generally will qualify for purposes of the gross income tests only if it is based upon the gross receipts or sales, and not the net income or profits, of the borrower. This limitation does not apply, however, where the borrower leases substantially all of its interest in the property to tenants or subtenants, to the extent that the rental income derived by the borrower would qualify as rents from real property had we earned the income directly.

The application of the REIT provisions of the Code to certain mezzanine loans, which are loans secured by equity interests in an entity that directly or indirectly owns real property rather than by a direct mortgage of the real property, is not entirely clear. A safe harbor in IRS Revenue Procedure 2003-65 provides that if a mezzanine loan meets certain requirements then it will be treated by the IRS as a qualifying real estate asset for purposes of the REIT asset tests and interest income derived from it will be treated as qualifying mortgage interest for purposes of the 75% gross income test. However, to the extent that mezzanine loans do not meet all of the requirements for reliance on the safe harbor set forth in IRS Revenue Procedure 2003-65, all or a portion of such mezzanine loans may not qualify as real estate assets for purposes of the REIT asset tests and the interest income derived therefrom may not be qualifying income for purposes of the 75% gross income test, which could adversely affect our REIT qualification if we acquired such loans. As such, the REIT provisions of the Code may limit our ability to acquire mortgage, mezzanine or other loans that we might otherwise desire to acquire.

Investments in debt instruments may require recognition of taxable income prior to receipt of cash from such investments and may cause portions of gain to be treated as ordinary income. For example, we may purchase debt instruments at a discount from face value. To the extent we purchase any instruments at a discount in connection with their original issuances, the discount will be “original issue discount,” or OID, if it exceeds certain de minimis amounts, which must be accrued on a constant yield method even though we may not receive the corresponding cash payment until maturity. To the extent debt instruments are purchased by us at a discount after their original issuances, the discount may represent “market discount.” Unlike OID, market discount is not required to be included in income on a constant yield method. However, if we sell a debt instrument with market discount, we will be required to treat gain up to an amount equal to the market discount that has accrued while we held the debt instrument as ordinary income. Additionally, any principal payments we receive in respect of our debt instruments must be treated as ordinary income to the extent of any accrued market discount. If we ultimately collect less on a debt instrument than our purchase price and any OID or accrued market discount that we have included in income, there may be limitations on our ability to use any losses resulting from that debt instrument. We may acquire distressed debt instruments that are subsequently modified by agreement with

the borrower. Under applicable Treasury Regulations, these modifications may be treated as a taxable event in which we exchange the old debt instrument for a new debt instrument, the value of which may be treated as equal to the face amount of the new debt instrument. Because distressed debt instruments are often acquired at a substantial discount from face value, the difference between our amount realized and our tax basis in the old note could be significant, resulting in significant income without any corresponding receipt of cash. Similarly, if we acquire a distressed debt instrument and subsequently foreclose, we could have taxable income to the extent that the fair market value of the property we receive exceeds our tax basis in the debt instrument. Such a scenario could also result in significant taxable income without any receipt of cash. In the event that any debt instruments acquired by us are delinquent as to mandatory principal and interest payments, or in the event payments with respect to a particular debt instrument are not made when due, we may nonetheless be required to continue to recognize the unpaid interest as taxable income. We generally will be required to include certain amounts in income for U.S. federal income tax purposes no later than the time such amounts are reflected on certain financial statements. The application of this rule may require the accrual of income with respect to our debt instruments earlier than would be the case under the general tax rules described in the preceding paragraph.

Investments in TRSs

We own a subsidiary that has elected to be treated as a TRS for U.S. federal income tax purposes, and we may form additional TRSs. A TRS of ours is a corporation in which we directly or indirectly own stock and that jointly elects with us to be treated as a TRS under Section 856(l) of the Code. In addition, if a TRS owns, directly or indirectly, securities representing 35% or more of the vote or value of a subsidiary corporation, that subsidiary will also be treated as a TRS of ours. A domestic TRS (or a foreign TRS with income from a U.S. business) pays U.S. federal, state, and local income taxes at the full applicable corporate rates on its taxable income prior to payment of any dividends. A TRS owning property outside of the U.S. may pay foreign taxes. The taxes owed by a TRS could be substantial. To the extent that any of our TRSs is required to pay U.S. federal, state, local or foreign taxes, the cash available for distribution by us will be reduced accordingly.

A TRS is permitted to engage in certain kinds of activities that cannot be performed directly by us without jeopardizing our qualification as a REIT. However, several provisions regarding the arrangements between a REIT and its TRS ensure that a TRS will be subject to an appropriate level of U.S. federal income taxation. For example, we will be obligated to pay a 100% penalty tax on some payments that we receive or on certain expenses deducted by the TRS if the economic arrangements among us, our tenants, and/or the TRS are not comparable to similar arrangements among unrelated parties.

Taxation of U.S. Shareholders

The term “U.S. shareholder” means a beneficial owner of our common stock or preferred stock that, for U.S. federal income tax purposes, is (i) a citizen or resident of the United States, (ii) a corporation or other entity treated as a corporation for U.S. federal income tax purposes, created or organized in or under the laws of the United States, any of its states or the District of Columbia, (iii) an estate, the income of which is subject to U.S. federal income taxation regardless of its source, or (iv) a trust (a) that is subject to the primary supervision of a United States court and the control of one or more U.S. persons or (b) that has a valid election in effect under the applicable Treasury Regulations to be treated as a U.S. person under the Code.

In addition, as used herein, the term U.S. shareholder does not include any individuals or entities that are subject to special treatment under the Code, such as (i) insurance companies; (ii) tax-exempt organizations (except to the limited extent discussed below); (iii) financial institutions or broker-dealers; (iv) U.S. expatriates; (v) persons who mark-to-market our common stock or preferred stock; (vi) subchapter S corporations; (vii) U.S. shareholders whose functional currency is not the U.S. dollar; (viii) regulated investment companies; (ix) holders who receive our common stock or preferred stock through the exercise of employee stock options or otherwise as compensation; (x) persons holding shares of our common stock or preferred stock as part of a “straddle,” “hedge,” “conversion transaction,” “synthetic security” or other integrated investment; (xi) persons subject to the alternative minimum tax provisions of the Code; (xii) persons holding our common stock or preferred stock through a partnership or similar pass-through entity;

and (xiii) persons holding a 10% or more (by vote or value) beneficial interest in our stock. If a partnership, including any entity treated as a partnership for U.S. federal income tax purposes, holds our stock, the U.S. federal income tax treatment of a partner in the partnership will generally depend on the status of the partner and the activities of the partnership. If you are a partner in a partnership holding our stock, you are urged to consult your tax advisor regarding the consequences of the ownership and disposition of shares of our stock by the partnership. This summary assumes that shareholders hold our stock as capital assets for U.S. federal income tax purposes, which generally means property held for investment.

Certain accrual method taxpayers are required to include certain amounts in income for U.S. federal income tax purposes no later than the time such amounts are reflected on certain financial statements. This summary does not address the impact of those rules.

Distributions

Distributions by us, other than capital gain dividends, will constitute ordinary dividends to the extent of our current or accumulated earnings and profits as determined for U.S. federal income tax purposes. Distributions on our preferred stock will be treated as

made out of any available earnings and profits in priority to distributions on our common stock. In general, these dividends will be taxable as ordinary income and will not be eligible for the dividends-received deduction for corporate shareholders. However, for taxable years beginning after December 31, 2017 and before January 1, 2026, individuals and other non-corporate taxpayers generally may deduct 20% of dividends received from us, other than capital gain dividends or dividends treated as qualified dividend income, subject to certain limitations. Our ordinary dividends generally will not qualify as "qualified dividend income" currently taxed as net capital gain for U.S. shareholders that are individuals, trusts or estates. However, provided we properly designate the distributions, distributions to U.S. shareholders that are individuals, trusts or estates generally will constitute qualified dividend income taxed as net capital gains to the extent the U.S. shareholder satisfies certain holding period requirements and to the extent the dividends are attributable to (i) qualified dividend income we receive from other corporations during the taxable year, including from our TRSs, and (ii) our undistributed earnings or built-in gains taxed at the corporate level during the immediately preceding taxable year. We do not anticipate distributing a significant amount of qualified dividend income.

The discussion in this section applies equally to distributions payable in cash and taxable stock distributions. The Code provides that certain distributions payable in stock will be treated as taxable stock dividends. In addition, shares acquired through a distribution reinvestment plan are treated as taxable stock dividends. Certain features, typically with respect to preferred stock, such as certain redemption premiums and conversion ratio adjustments that have the effect of increasing the affected shareholders' interest in our earnings or assets, also may be treated as taxable stock dividends for U.S. federal income tax purposes. Taxable U.S. shareholders receiving taxable dividends of stock will be required to include as dividend income the fair market value of the stock received plus any cash or other property received in the distribution, to the extent of our current and accumulated earnings and profits for U.S. federal income tax purposes. As a result, a U.S. shareholder may be required to pay tax with respect to such dividends in excess of the cash received. If a U.S. shareholder sells the stock it receives as a dividend, the sales proceeds may be less than the amount included in income with respect to the dividend, depending on the market price of the stock at the time of the sale.

To the extent that we make a distribution in excess of our current and accumulated earnings and profits (a "return of capital distribution"), a U.S. shareholder will first apply the distribution to reduce the shareholder's tax basis in our stock, and the return of capital distribution will be tax-free to that extent. To the extent that a return of capital distribution exceeds a U.S. shareholder's tax basis in its stock, the distribution will be taxable as capital gain realized from the sale of such stock. Under proposed Treasury Regulations, a shareholder would apply a return of capital distribution pro rata, on a share-by-share basis, to each share of stock held by the shareholder with the class of stock upon which the return of capital distribution is made.

Dividends declared by us in October, November or December and payable to a shareholder of record on a specified date in any such month shall be treated both as paid by us and as received by the shareholder on December 31 of the year to the extent of our remaining current and accumulated earnings and profits for such year, provided that the dividend is actually paid by us during January of the following calendar year.

We will be treated as having sufficient earnings and profits to treat as a dividend any distribution up to the amount required to be distributed in order to avoid imposition of the 4% excise tax generally applicable to REITs if certain distribution requirements are not met. Moreover, any deficiency dividend will be treated as an ordinary or a capital gain dividend, as the case may be, regardless of our earnings and profits at the time the distribution is actually made. As a result, shareholders may be required to treat certain distributions as taxable dividends that would otherwise result in a tax-free return of capital.

Distributions that are properly designated as capital gain dividends will be taxed as long-term capital gains (to the extent they do not exceed our actual net capital gain for the taxable year) without regard to the period for which the shareholder has held its stock. However, corporate shareholders may be required to treat up to 20% of certain capital gain dividends as ordinary income. In addition, U.S. shareholders may be required to treat a portion of any capital gain dividend as "unrecaptured Section 1250 gain," taxable at a maximum rate of 25%, if we incur such gain. Capital gain dividends are not eligible for the dividends-received deduction for corporations.

The REIT provisions of the Code do not require us to distribute our long-term capital gain, and we may elect to retain and pay income tax on our net long-term capital gains received during the taxable year. If we so elect for a taxable year, our shareholders would include in income as long-term capital gains their proportionate share of retained net long-term capital gains for the taxable year as we may designate. A U.S. shareholder would be deemed to have paid its share of the tax paid by us on such undistributed capital gains, which would be credited or refunded to the shareholder. The U.S. shareholder’s basis in its stock would be increased by the amount of undistributed long-term capital gains (less the capital gains tax paid by us) included in the U.S. shareholder’s long-term capital gains.

Passive Activity Loss and Investment Interest Limitations; No Pass-Through of Losses

Dividends paid by us and gain from the disposition of our common stock or preferred stock will not be treated as passive activity income and, therefore, U.S. shareholders will not be able to apply any "passive losses" against such income. With respect to non-corporate U.S. shareholders, our dividends (to the extent they do not constitute a return of capital) that are taxed at ordinary income rates will generally be treated as investment income for purposes of the investment interest limitation; however, net capital gain from the disposition of our common stock or preferred stock (or distributions treated as such), capital gain dividends, and dividends taxed at net capital gains rates generally will be excluded from investment income except to the extent the U.S. shareholder elects to treat such amounts as ordinary income for U.S. federal income tax purposes. U.S. shareholders may not include in their own U.S. federal income tax returns any of our net operating or net capital losses.

Sale or Disposition of Stock

In general, any gain or loss realized upon a taxable disposition of shares of our common stock or preferred stock by a shareholder that is not a dealer in securities will be a long-term capital gain or loss if the stock has been held for more than one year; otherwise it will be a short-term capital gain or loss. However, any loss upon a sale or exchange of the stock by a shareholder who has held such stock for six months or less (after applying certain holding period rules) will be treated as a long-term capital loss to the extent of our distributions or undistributed capital gains required to be treated by such shareholder as long-term capital gain. All or a portion of any loss realized upon a taxable disposition of shares of our common stock or preferred stock may be disallowed if the taxpayer purchases other shares of our common stock within 30 days before or after the disposition.

A redemption by us of any redeemable preferred stock we may issue could be treated either as a taxable disposition of shares or as a dividend, depending on the applicable facts and circumstances. In the event we issue any redeemable preferred stock, the prospectus supplement will discuss the tax consequences of owning such securities in greater detail.

Taxation of U.S. Tax-Exempt Shareholders

In General

In general, a tax-exempt organization is exempt from U.S. federal income tax on its income, except to the extent of its "unrelated business taxable income" or UBTI, which is defined by the Code as the gross income derived from any trade or business which is regularly carried on by a tax-exempt entity and unrelated to its exempt purposes, less any directly connected deductions and subject to certain modifications. For this purpose, the Code generally excludes from UBTI any gain or loss from the sale or other disposition of property (other than stock in trade or property held primarily for sale in the ordinary course of a trade or business), dividends, interest, rents from real property, and certain other items. However, a portion of any such gains, dividends, interest, rents, and other items generally is UBTI to the extent derived from debt-financed property not related to the tax-exempt entity's exempt purpose, based on the amount of "acquisition indebtedness" with respect to such debt-financed property. A U.S. tax-exempt shareholder that is subject to tax on its UBTI will be required to separately compute its taxable income and loss for each unrelated trade or business activity for purposes of determining its UBTI. Before making an investment in shares of our common stock or preferred stock, a tax-exempt shareholder should consult its tax advisors with regard to UBTI and the suitability of the investment in our stock.

Distributions we make to a tax-exempt employee pension trust or other domestic tax-exempt shareholder or gains from the disposition of our common stock or preferred stock held as capital assets generally will not constitute UBTI unless the exempt organization's stock is debt-financed property (e.g., the shareholder has incurred "acquisition indebtedness" with respect to such stock). However, if we are a "pension-held REIT," this general rule may not apply to distributions to certain pension trusts that are qualified trusts (as defined above) and that hold more than 10% (by value) of our stock. We will be treated as a "pension-held REIT" if (i) treating qualified trusts as individuals would cause us to fail the 5/50 Test (as defined above) and (ii) we are "predominantly held" by qualified trusts. We will be "predominantly held" by qualified trusts if either (i) a single qualified trust holds more than 25% by value of our stock or (ii) one or more qualified trusts, each owning more than 10% by value of our stock, hold in the aggregate more than

50% by value of our stock. In the event we are a pension-held REIT, the percentage of any dividend received from us treated as UBTI would be equal to the ratio of (a) the gross UBTI (less certain associated expenses) earned by us (treating us as if we were a qualified trust and, therefore, subject to tax on UBTI) to (b) our total gross income (less certain associated expenses). A de minimis exception applies where the ratio set forth in the preceding sentence is less than 5% for any year; in that case, no dividends are treated as UBTI. We cannot assure you that we will not be treated as a pension-held REIT.

Special Issues

Social clubs, voluntary employee benefit associations and supplemental unemployment benefit trusts that are exempt from taxation under paragraphs (7), (9) and (17), respectively, of Section 501(c) of the Code are subject to different UBTI rules, which generally will require them to characterize distributions from us as UBTI.

Taxation of Non-U.S. Shareholders

The rules governing U.S. federal income taxation of beneficial owners of our stock who are not U.S. persons, such as nonresident alien individuals, foreign corporations, and foreign trusts and estates ("non-U.S. shareholders"), are complex. This section is only a partial discussion of such rules. This discussion does not attempt to address the considerations that may be relevant for non-U.S. shareholders that are partnerships or other pass-through entities, that hold their common stock or preferred stock through intermediate entities, that have special statuses (such as sovereigns), or that otherwise are subject to special rules under the Code. This discussion also generally is limited to investments in classes of our stock that are regularly traded on an established securities market.

Distributions

A non-U.S. shareholder that receives a distribution that is not attributable to gain from our sale or exchange of "United States real property interests" (as defined below) and that we do not designate as a capital gain dividend or retained capital gain generally will recognize ordinary dividend income to the extent that we pay the distribution out of our current or accumulated earnings and profits. A U.S. federal withholding tax equal to 30% of the gross amount of the distribution ordinarily will apply unless an applicable tax treaty reduces or eliminates the tax. Under many treaties, lower withholding rates do not apply to dividends from REITs or are available in limited circumstances. However, if a distribution is treated as effectively connected with the non-U.S. shareholder's conduct of a U.S. trade or business, the non-U.S. shareholder generally will be subject to U.S. federal income tax on the distribution at graduated rates (in the same manner as U.S. shareholders are taxed on distributions) and also may be subject to the 30% branch profits tax in the case of a corporate non-U.S. shareholder. We generally plan to withhold U.S. income tax at the rate of 30% on the gross amount of any distribution paid to a non-U.S. shareholder (including any portion of any dividend that is payable in our stock) unless either (i) a lower treaty rate or special provision of the Code (e.g., Section 892) applies and the non-U.S. shareholder provides to us any required IRS Form W-8 (for example, an IRS Form W-8BEN) evidencing eligibility for that reduced rate or (ii) the non-U.S. shareholder provides with us an IRS Form W-8ECI claiming that the distribution is effectively connected income, or (iii) we determined that a different withholding rate is appropriate (such as because we can determine at the time of distribution that the distribution is a capital gain dividend or is attributable to gain from the sale or exchange of "United States real property interests").

A non-U.S. shareholder generally will not incur U.S. federal income tax (but will be subject to withholding as described below) on a return of capital distribution in excess of our current and accumulated earnings and profits that is not attributable to the gain from our disposition of a "United States real property interest" if the excess portion of the distribution does not exceed the adjusted basis of the non-U.S. shareholder's stock. Instead, the excess portion of the distribution will reduce the adjusted basis of the stock. However, a non-U.S. shareholder will be subject to tax on such a distribution that exceeds both our current and accumulated earnings and profits and the non-U.S. shareholder's adjusted basis in the stock if the non-U.S. shareholder otherwise would be subject to tax on gain from the sale or disposition of its stock, as described below. Because we generally cannot determine at the time we make a distribution whether or not the distribution will exceed our current and accumulated earnings and profits, we normally will withhold tax on the entire amount of any distribution at the same rate as we would withhold on a dividend.

We may be required to withhold 15% of any distribution that exceeds our current and accumulated earnings and profits even if a lower treaty rate applies to dividends or the non-U.S. shareholder is not liable for tax on the receipt of that distribution. Consequently, to the extent that we do not withhold at a rate of 30% on the entire amount of any distribution, we generally expect to withhold at a rate of 15% on the portion of the distribution that we do not withhold at a rate of 30%,. unless we conclude that an exemption or different rate applies.

A non-U.S. shareholder may seek a refund from the IRS if the non-U.S. shareholder's withholdings and any other tax payments exceed its U.S. federal income tax liability for the year.

Subject to the exception discussed below for 10% or smaller holders of classes of stock of a corporation that are regularly traded on an established securities market located in the United States and the special rules for "qualified shareholders" or "qualified foreign pension funds" discussed below, a non-U.S. shareholder will incur tax on distributions that are attributable to gain from our sale or exchange of "United States real property interests" under special provisions of the Foreign Investment in Real Property Tax Act of 1980, or FIRPTA, regardless of whether we designate such

distributions as capital gain dividend. The term “United States real property interests” includes interests in U.S. real property and stock in U.S. corporations at least 50% of whose assets consist of interests in U.S. real property. Under those rules, a non-U.S. shareholder is taxed on distributions attributable to gain from sales of United States real property interests as if the gain were effectively connected with the non-U.S. shareholder’s conduct of a U.S. trade or business. A non-U.S. shareholder thus would be taxed on such a distribution at the normal capital gain rates applicable to U.S. shareholders, subject to any applicable alternative minimum tax. A corporate non-U.S. shareholder not entitled to treaty relief or exemption also may be subject to the 30% branch profits tax on such a distribution. We will be required to withhold and remit to the IRS 21% of any distributions to non-U.S. shareholders attributable to gain from our sale or exchange

of United States real property interests ("FIRPTA Withholding"). A non-U.S. shareholder may receive a credit against its tax liability for the amount we withhold.

A non-U.S. shareholder that owns, actually or constructively, no more than 10% of our common stock (or preferred stock) at all times during the one-year period ending on the date of a distribution with respect to such stock should not be subject to FIRPTA, branch profits tax or FIRPTA Withholding with respect to a distribution on that stock that is attributable to gain from our sale or exchange of United States real property interests, provided that the class of stock in question continues to be regularly traded on an established securities market located in the United States. In the case of any such distribution that was a capital gain dividend made to such non-U.S. shareholder, the distribution will be treated as an ordinary dividend subject to the general withholding rules discussed above, which generally impose a withholding tax equal to 30% of the gross amount of each dividend distribution (unless reduced by treaty).

Distributions that are designated by us as capital gain dividends but that are not attributable to the disposition of a United States real property interest, generally should not be subject to U.S. federal income taxation unless:

(i) such distribution is effectively connected with the non-U.S. shareholder's U.S. trade or business and, if certain treaties apply, is attributable to a U.S. permanent establishment maintained by the non-U.S. shareholder, in which case the non-U.S. shareholder will be subject to tax on a net basis in a manner similar to the taxation of U.S. shareholders with respect to such gain, except that a holder that is a foreign corporation may also be subject to the additional 30% branch profits tax; or

(ii) the non-U.S. shareholder is a nonresident alien individual who is present in the United States for 183 days or more during the taxable year and meets certain other criteria, in which case such nonresident alien individual generally will be subject to a 30% tax on the individual's net U.S. source capital gain.

Notwithstanding that such non-FIRPTA capital gain dividend may not be subject to U.S. federal income taxation, as noted above we generally plan to withhold U.S. federal income tax at the rate of 30% on the gross amount of any dividend distribution paid to a non-U.S. shareholder and we may be required to withhold not less than 21% of any such capital gain dividends (or amounts we could have designated as such). Distributions can be designated as capital gain dividends to the extent of our net capital gain for the taxable year of the distribution. The amount withheld is creditable against the non-U.S. shareholder's U.S. federal income tax liability.

Although the law is not clear on the matter, it appears that amounts designated by us as undistributed capital gains generally should be treated with respect to non-U.S. shareholders in the same manner as actual distributions by us of capital gain dividends. Under that approach, non-U.S. shareholders would be able to offset as a credit against their U.S. federal income tax liability resulting therefrom an amount equal to their proportionate share of the tax paid by us on the undistributed capital gains and to receive from the IRS a refund to the extent their proportionate share of this tax paid by us exceeds their actual U.S. federal income tax liability.

Dispositions

If gain on the sale of our common stock or preferred stock were taxed under FIRPTA, a non-U.S. shareholder would be taxed on that gain in the same manner as U.S. shareholders with respect to that gain, subject to any applicable alternative minimum tax. A non-U.S. shareholder generally will not incur tax under FIRPTA on a sale or other disposition of our common stock or preferred stock if we are a "domestically controlled qualified investment entity," which requires that, during the five-year period ending on the date of the distribution or disposition, non-U.S. shareholders hold, directly or indirectly, less than 50% in value of our stock and we are qualified as a REIT. For such testing periods that end on or after December 18, 2015, a person holding less than 5% of our regularly traded classes of stock for five years has been, and will be, treated as a U.S. person unless we have actual knowledge that such person is not a U.S. person. Because our common stock is publicly traded, we cannot assure you that we are or will be in the future a domestically controlled qualified investment entity. However, gain recognized by a non-U.S. shareholder from a sale of our common stock or preferred stock that is regularly traded on an established securities market will not be subject to tax under FIRPTA if (i) our stock is considered regularly traded under applicable Treasury Regulations on an established securities market, such as the NYSE, and (ii) the non-U.S. shareholder owned,

actually and constructively, 10% or less of the value of such class of stock at all times during the specified testing period ending on the date of the disposition. The testing period referred to in the previous sentence is the shorter of (x) the period during which the non-U.S. shareholder held the stock and (y) the five-year period ending on the date of the disposition. We believe that our common stock is currently regularly traded on an established securities market. Non-U.S. shareholders should consult their tax advisors as to the availability of the exception for holders of less than 10% of our stock in the case of a class of our stock that is not regularly traded on an established securities market.

In addition, even if we are a domestically controlled qualified investment entity, upon a disposition of our common stock or preferred stock, a non-U.S. shareholder may be treated as having gain from the sale or exchange of a United States real property

interest if the non-U.S. shareholder (i) disposes of an interest in our common stock or preferred stock during the 30-day period preceding the ex-dividend date of a distribution, any portion of which, but for the disposition, would have been treated as gain from the sale or exchange of a United States real property interest, and (ii) directly or indirectly acquires, enters into a contract or option to acquire, or is deemed to acquire, other shares of our common stock or preferred stock within 30 days before or after such ex-dividend date. The foregoing rule does not apply if the exception described above for dispositions by 10% or smaller holders of regularly traded classes of stock is satisfied. Furthermore, a non-U.S. shareholder generally will incur tax on gain not subject to FIRPTA if (i) the gain is effectively connected with the non-U.S. shareholder's U.S. trade or business and, if certain treaties apply, is attributable to a U.S. permanent establishment maintained by the non-U.S. shareholder, in which case the non-U.S. shareholder will be subject to the same treatment as U.S. shareholders with respect to such gain and may be subject to the 30% branch profits tax in the case of a non-U.S. corporation, or (ii) the non-U.S. shareholder is a nonresident alien individual who was present in the United States for 183 days or more during the taxable year and has a "tax home" in the United States, in which case the non-U.S. shareholder will generally incur a 30% tax on his or her net U.S. source capital gains.

Purchasers of our common stock or preferred stock from a non-U.S. shareholder generally will be required to withhold and remit to the IRS 15% of the purchase price unless at the time of purchase (i) any class of our stock is regularly traded on an established securities market (subject to certain limits if the shares of stock sold are not themselves part of such a regularly traded class) or (ii) we are a domestically controlled qualified investment entity. The non-U.S. shareholder may receive a credit against his or her U.S. tax liability for the amount withheld.

Special FIRPTA Rules

To the extent our stock is held directly (or indirectly through one or more partnerships) by a "qualified shareholder," it will not be treated as a United States real property interest for such qualified shareholder. Thus, gain treated as gain from the sale or exchange of our stock (including distributions treated as gain from the sale or exchange of our stock) will not be subject to tax unless such gain is treated as effectively connected with the qualified shareholder's conduct of a U.S. trade or business. Further, to the extent such treatment applies, any distribution to such shareholder will not be treated as gain recognized from the sale or exchange of a United States real property interest (and capital gain dividends and non-dividend distributions to such shareholder may be treated as ordinary dividends). For these purposes, a qualified shareholder is generally a non-U.S. shareholder that (i)(A) is eligible for treaty benefits under an income tax treaty with the United States that includes an exchange of information program and the principal class of interests of which is listed and regularly traded on one or more stock exchanges as defined by the treaty, or (B) is a foreign limited partnership organized in a jurisdiction with an exchange of information agreement with the United States and that has a class of regularly traded limited partnership units (having a value greater than 50% of the value of all partnership units) on the NYSE or Nasdaq, (ii) is a "qualified collective investment vehicle" (within the meaning of Section 897(k)(3)(B) of the Code) and (iii) maintains records of persons holding 5% or more of the class of interests described in clauses (i)(A) or (i)(B) above. However, in the case of a qualified shareholder having one or more "applicable investors," the exception described in the first sentence of this paragraph will not apply to the applicable percentage of the qualified shareholder's stock (with "applicable percentage" generally meaning the percentage of the value of the interests in the qualified shareholder held by applicable investors after applying certain constructive ownership rules). The applicable percentage of the amount realized by a qualified shareholder on the disposition of our stock or with respect to a distribution from us attributable to gain from the sale or exchange of a United States real property interest will be treated as amounts realized from the disposition of United States real property interest. Such treatment shall also apply to applicable investors in respect of distributions treated as a sale or exchange of stock with respect to a qualified shareholder. For these purposes, an "applicable investor" is a person (other than a qualified shareholder) who generally holds an interest in the qualified shareholder and holds more than 10% of our stock applying certain constructive ownership rules.

For FIRPTA purposes, neither a "qualified foreign pension fund" nor an entity all of the interests of which are held by a qualified foreign pension fund is treated as a non-U.S. shareholder. Accordingly, the U.S. federal income tax treatment of ordinary dividends received by qualified foreign pension funds and their wholly owned non-U.S.

subsidiaries will be determined without regard to the FIRPTA rules discussed above, and their gain from the sale or exchange of our stock, as well as our capital gain dividends and distributions treated as gain from the sale or exchange of our stock, will not be subject to U.S. federal income tax unless such gain is treated as effectively connected with the qualified foreign pension fund's (or the wholly owned subsidiary's) conduct of a U.S. trade or business. A "qualified foreign pension fund" is an organization or arrangement (i) created or organized in a foreign country, (ii) established to provide retirement or pension benefits to current or former employees (including self-employed individuals) or their designees by either (A) a foreign country as a result of services rendered by such employees to their employers, or (B) one or more employers in consideration for services rendered by such employees to such employers, (iii) which does not have a single participant or beneficiary that has a right to more than 5% of its assets or income, (iv) which is subject to government regulation and with respect to which annual information about its beneficiaries is provided, or is otherwise available, to relevant local tax authorities, and (v) with respect to which, under its local laws, (A) contributions that would otherwise be subject to tax are deductible

or excluded from its gross income or taxed at a reduced rate, or (B) taxation of its investment income is deferred, or such income is excluded from its gross income or taxed at a reduced rate.

U.S. Federal Income Tax Returns
If a non-U.S. shareholder is subject to taxation under FIRPTA on proceeds from the sale of our common stock or preferred stock or on distributions, the non-U.S. shareholder will be required to file a U.S. federal income tax return.

Information Reporting Requirements and Backup Withholding Tax Applicable to Shareholders
U.S. Shareholders. In general, information reporting requirements will apply to payments of distributions on our stock and payments of the proceeds of the sale of our stock to some shareholders. Further, the payor will be required to backup withhold on any payments at the current rate of 24% if:
(1) the payee fails to furnish a taxpayer identification number, or TIN, to the payor or establish an exemption from backup withholding;
(2) the IRS notifies the payor that the TIN furnished by the payee is incorrect; or
(3) the payee fails to certify under the penalty of perjury that the payee is not subject to backup withholding under the Code; or
(4) there has been a notified payee underreporting with respect to dividends described in Code Section 3406(c).
Some U.S. shareholders, including corporations and tax-exempt organizations, will be exempt from backup withholding. Any amounts withheld under the backup withholding rules from a payment to a shareholder will be allowed as a credit against the shareholder's U.S. federal income tax and may entitle the shareholder to a refund, provided that the required information is furnished to the IRS on a timely basis.
Non-U.S. Shareholders. Information reporting requirements and backup withholding may apply to (i) payments of distributions on our stock to a non-U.S. shareholder and (ii) proceeds a non-U.S. shareholder receives upon the sale, exchange, redemption, retirement or other disposition of our stock. Information reporting and backup withholding will generally not apply if an appropriate IRS Form W-8 is duly provided by such non-U.S. shareholder or the shareholder otherwise establishes an exemption, provided that the withholding agent does not have actual knowledge or reason to know that the shareholder is a U.S. person or that the claimed exemption is not in fact satisfied. Even without having executed an appropriate IRS Form W-8 or substantially similar form, however, in some cases information reporting and backup withholding will not apply to proceeds received through a broker's foreign office that a non-U.S. shareholder receives upon the sale, exchange, redemption, retirement or other disposition of our stock. However, this exemption does not apply to brokers that are U.S. persons and certain foreign brokers with substantial U.S. ownership or operations. Any amount withheld under the backup withholding rules is allowable as a credit against such shareholder's U.S. federal income tax liability (which might entitle such holder to a refund), provided that such holder furnishes the required information to the IRS. Payments not subject to information reporting requirements may nonetheless be subject to other reporting requirements.

Foreign Account Tax Compliance Act Withholding Rules
The Foreign Account Tax Compliance Act, or FATCA, provisions of the Code, subject to administrative guidance and certain intergovernmental agreements entered into thereunder, impose a 30% withholding tax on certain types of payments made to ''foreign financial institutions'' (as specifically defined in the Code) and certain other non-U.S. entities unless (i) the foreign financial institution (as the beneficial owner or as an intermediary for the beneficial owners) undertakes certain diligence and reporting obligations or (ii) the foreign non-financial entity (as the beneficial owner or, in certain cases, as an intermediary for the beneficial owners) either certifies it does not have any substantial United States owners or furnishes identifying information regarding each substantial United States owner. If the payee is a foreign financial institution that is not subject to special treatment under certain intergovernmental agreements, it must enter into an agreement with the United States Treasury requiring, among other things, that it undertakes to identify accounts held by certain United States persons or United States-owned foreign entities, annually report certain information about such accounts, and withhold 30% on payments to account holders whose actions prevent them from complying with these reporting and other requirements. The compliance requirements under FATCA are complex and

special requirements may apply to certain categories of payees. Withholding under this legislation may apply with respect to certain types of passive income from sources within the United States, which include dividend income from our stock. However, FATCA withholding will not apply to amounts treated as income effectively connected with the conduct of a trade or business within the United States or (ii) distributions and proceeds from a sale or other disposition of our stock.

Medicare Tax

A U.S. shareholder that is an individual is subject to a 3.8% tax on the lesser of (1) his or her "net investment income" for the relevant taxable year and (2) the excess of his or her modified adjusted gross income for the taxable year over a certain threshold (currently between $125,000 and $250,000, depending on the individual's U.S. federal income tax filing status). A similar regime applies to certain estates and trusts. Net investment income generally would include dividends on our common stock and preferred stock (without regard to the 20% deduction allowed by Section 199A of the Code) and gain from the sale of our common stock and preferred stock. If you are a U.S. person that is an individual, an estate or a trust, you are urged to consult your tax advisors regarding the applicability of this tax to your income and gains in respect of your investment in our common stock and preferred stock.

Recent Tax Legislation

The recently enacted legislation informally knows as the Tax Cuts and Jobs Act, or TCJA, is generally applicable for tax years beginning after December 31, 2017 and made significant changes to the Code, including a number of provisions of the Code that affect the taxation of businesses and their owners, including REITs, their shareholders and holders of their debt securities. Among other changes not reflected in the discussion above, the TCJA (i) reduces the U.S. federal income tax rates on ordinary income of individuals, trusts and estates for taxable years beginning before January 1, 2026 and on corporations indefinitely, (ii) limits the deductibility of interest expense, and (iii) limits the use of net operating losses. The effect of the TCJA on us and our shareholders is still uncertain, and administrative guidance will be required in order to fully evaluate the effect of many provisions. Any technical corrections with respect to the TCJA could have an adverse effect on us or our shareholders.

Additional Legislative or Other Actions Affecting REITs

The rules dealing with U.S. federal income taxation are constantly under review by persons involved in the legislative process and by the IRS and the U.S. Treasury Department and it is possible that there could be future changes that could adversely impact our shareholders. No assurance can be given as to whether, when, or in what form the U.S. federal income tax laws applicable to us and our shareholders may be enacted. Changes to the U.S. federal tax laws and interpretations of federal tax laws could adversely affect an investment in our common stock or preferred stock.

State, Local and Foreign Tax

We may be subject to state, local and foreign tax in states, localities and foreign countries in which we do business or own property. The tax treatment applicable to us and our shareholders in such jurisdictions may differ from the U.S. federal income tax treatment described above. The TCJA also disallows itemized deductions for taxable years beginning before January 1, 2026 for individuals for state and local income, property and sales taxes in excess of a combined limit of $10,000 ($5,000 for a married individual filing a separate return) per year.

ITEM 1A. RISK FACTORS.

In addition to the other information contained or incorporated by reference in this document, readers should carefully consider the following risk factors. Any of these risks or the occurrence of any one or more of the uncertainties described below could have a material adverse effect on the Company's financial condition and the performance of its business. Additional risks and uncertainties not presently known to the Company or that the Company currently deems immaterial also may impair its business operations. The Company refers to itself as "we", "us" or "our" in the following risk factors.

Real Estate Industry Risks

We face risks associated with local real estate conditions in areas where we own properties. We may be adversely affected by general economic conditions and local real estate conditions. For example, an oversupply of industrial properties in a local area or a decline in the attractiveness of our properties to tenants would have a negative effect on

us. Other factors that may affect general economic conditions or local real estate conditions include:

- population and demographic trends;
- employment and personal income trends;
- income and other tax laws;
- changes in interest rates and availability and costs of financing;
- increased operating costs, including insurance premiums, utilities and real estate taxes, due to inflation and other factors which may not necessarily be offset by increased rents;
- changes in the price of oil; and
- construction costs.

We may be unable to compete for properties and tenants. The real estate business is highly competitive. We compete for interests in properties with other real estate investors and purchasers, some of whom have greater financial resources, revenues and geographical diversity than we have. Furthermore, we compete for tenants with other property owners. All of our industrial properties are subject to significant local competition. We also compete with a wide variety of institutions and other investors for capital funds necessary to support our investment activities and asset growth.

We are subject to significant regulation that constrains our activities. Local zoning and land use laws, environmental statutes and other governmental requirements restrict our expansion, rehabilitation and reconstruction activities. These regulations may prevent us from taking advantage of economic opportunities. Legislation such as the Americans with Disabilities Act may require us to modify our properties, and noncompliance could result in the imposition of fines or an award of damages to private litigants. Future legislation may impose additional requirements. We cannot predict what requirements may be enacted or what changes may be implemented to existing legislation.

Risks Associated with Our Properties

We may be unable to lease space on favorable terms or at all. When a lease expires, a tenant may elect not to renew it. We may not be able to re-lease the property on favorable terms, if we are able to re-lease the property at all. The terms of renewal or re-lease (including the cost of required renovations and/or concessions to tenants) may be less favorable to us than the prior lease. We also routinely develop properties with no pre-leasing. If we are unable to lease all or a substantial portion of our properties, or if the rental rates upon such leasing are significantly lower than expected rates, our cash generated before debt repayments and capital expenditures and our ability to make expected distributions to stockholders may be adversely affected.

We have been and may continue to be affected negatively by tenant bankruptcies and leasing delays. At any time, a tenant may experience a downturn in its business that may weaken its financial condition. Similarly, a general decline in the economy may result in a decline in the demand for space at our industrial properties. As a result, our tenants may delay lease commencement, fail to make rental payments when due, or declare bankruptcy. Any such event could result in the termination of that tenant’s lease and losses to us, and distributions to investors may decrease. We receive a substantial portion of our income as rents under mid-term and long-term leases. If tenants are unable to comply with the terms of their leases for any reason, including because of rising costs or falling sales, we may deem it advisable to modify lease terms to allow tenants to pay a lower rent or a smaller share of taxes, insurance and other operating costs. If a tenant becomes insolvent or bankrupt, we cannot be sure that we could recover the premises from the tenant promptly or from a trustee or debtor-in-possession in any bankruptcy proceeding relating to the tenant. We also cannot be sure that we would receive rent in the proceeding sufficient to cover our expenses with respect to the premises. If a tenant becomes bankrupt, the federal bankruptcy code will apply and, in some instances, may restrict the amount and recoverability of our claims against the tenant. A tenant’s default on its obligations to us could adversely affect our financial condition and the cash we have available for distribution.

We face risks associated with our property development. We intend to continue to develop properties where market conditions warrant such investment. Once made, our investments may not produce results in accordance with our expectations. Risks associated with our current and future development and construction activities include:

- the availability of favorable financing alternatives;
- the risk that we may not be able to obtain land on which to develop or that due to the increased cost of land, our activities may not be as profitable;
- construction costs exceeding original estimates due to rising interest rates and increases in the costs of materials and labor;
- construction and lease-up delays resulting in increased debt service, fixed expenses and construction costs;

- expenditure of funds and devotion of management's time to projects that we do not complete;
- fluctuations of occupancy and rental rates at newly completed properties, which depend on a number of factors, including market and economic conditions, resulting in lower than projected rental rates and a corresponding lower return on our investment; and
- complications (including building moratoriums and anti-growth legislation) in obtaining necessary zoning, occupancy and other governmental permits.

We face risks associated with property acquisitions. We acquire individual properties and portfolios of properties and intend to continue to do so. Our acquisition activities and their success are subject to the following risks:

- when we are able to locate a desired property, competition from other real estate investors may significantly increase the purchase price;
- acquired properties may fail to perform as expected;
- the actual costs of repositioning or redeveloping acquired properties may be higher than our estimates;

- acquired properties may be located in new markets where we face risks associated with an incomplete knowledge or understanding of the local market, a limited number of established business relationships in the area and a relative unfamiliarity with local governmental and permitting procedures;
- we may be unable to quickly and efficiently integrate new acquisitions, particularly acquisitions of portfolios of properties, into our existing operations, and as a result, our results of operations and financial condition could be adversely affected; and
- we may acquire properties subject to liabilities and without any recourse, or with only limited recourse, to the transferor with respect to unknown liabilities. As a result, if a claim were asserted against us based upon ownership of those properties, we might have to pay substantial sums to settle it, which could adversely affect our cash flow.

Coverage under our existing insurance policies may be inadequate to cover losses. We generally maintain insurance policies related to our business, including casualty, general liability and other policies, covering our business operations, employees and assets as appropriate for the markets where our properties and business operations are located. However, we would be required to bear all losses that are not adequately covered by insurance. In addition, there may be certain losses that are not generally insured against or that are not generally fully insured against because it is not deemed economically feasible or prudent to do so, including losses due to floods, wind, earthquakes, acts of war, acts of terrorism or riots. If an uninsured loss or a loss in excess of insured limits occurs with respect to one or more of our properties, then we could lose the capital we invested in the properties, as well as the anticipated future revenue from the properties. In addition, if the damaged properties are subject to recourse indebtedness, we would continue to be liable for the indebtedness, even if these properties were irreparably damaged.

We face risks due to lack of geographic and real estate sector diversity. Substantially all of our properties are located in the Sunbelt region of the United States with an emphasis in the states of Florida, Texas, Arizona, California and North Carolina. As of December 31, 2018, our two largest markets were Houston and Tampa. We owned operating properties totaling 5.5 million square feet in Houston and 4.2 million square feet in Tampa, which represent 14.1% and 10.7%, respectively, of the Company's total Real estate properties on a square foot basis. A downturn in general economic conditions and local real estate conditions in these geographic regions, as a result of oversupply of or reduced demand for industrial properties, local business climate, business layoffs and changing demographics, would have a particularly strong adverse effect on us. Our investments in real estate assets are concentrated in the industrial distribution sector. This concentration may expose us to the risk of economic downturns in this sector to a greater extent than if our business activities included other sectors of the real estate industry.

We face risks due to the illiquidity of real estate which may limit our ability to vary our portfolio. Real estate investments are relatively illiquid. Our ability to vary our portfolio in response to changes in economic and other conditions will therefore be limited. In addition, because of our status as a REIT, the Internal Revenue Code limits our ability to sell our properties. If we must sell an investment, we cannot ensure that we will be able to dispose of the investment on terms favorable to the Company.

We are subject to environmental laws and regulations. Current and previous real estate owners and operators may be required under various federal, state and local laws, ordinances and regulations to investigate and clean up hazardous substances released at the properties they own or operate. They may also be liable to the government or to third parties for substantial property or natural resource damage, investigation costs and cleanup costs. Such laws often impose liability without regard to whether the owner or operator knew of, or was responsible for, the release or presence of such hazardous substances. In addition, some environmental laws create a lien on the contaminated site in favor of the government for damages and costs the government incurs in connection with the contamination. Contamination may adversely affect the owner’s ability to use, sell or lease real estate or to borrow using the real estate as collateral. We have no way of determining at this time the magnitude of any potential liability to which we may be subject arising out of environmental conditions or violations with respect to the properties we currently or formerly owned. Environmental laws today can impose liability on a previous owner or operator of a

property that owned or operated the property at a time when hazardous or toxic substances were disposed of, released from, or present at the property. A conveyance of the property, therefore, may not relieve the owner or operator from liability. Although ESAs have been conducted at our properties to identify potential sources of contamination at the properties, such ESAs do not reveal all environmental liabilities or compliance concerns that could arise from the properties. Moreover, material environmental liabilities or compliance concerns may exist, of which we are currently unaware, that in the future may have a material adverse effect on our business, assets or results of operations.

Compliance with new laws or regulations related to climate change, including compliance with "green" building codes, may require us to make improvements to our existing properties. Proposed legislation could also increase the costs of energy and utilities. The cost of the proposed legislation may adversely affect our financial position, results of operations and cash flows. We may be adversely affected by floods, hurricanes and other climate related events.

Financing Risks

We face risks associated with the use of debt to fund acquisitions and developments, including refinancing risk. We are subject to the risks normally associated with debt financing, including the risk that our cash flow will be insufficient to meet required payments of principal and interest. In addition, certain of our debt will have significant outstanding principal balances on their maturity dates, commonly known as "balloon payments." Therefore, we will likely need to refinance at least a portion of our outstanding debt as it matures. There is a risk that we may not be able to refinance existing debt or that the terms of any refinancing will not be as favorable as the terms of the existing debt.

We face risks associated with our dependence on external sources of capital. In order to qualify as a REIT, we are required each year to distribute to our stockholders at least 90% of our ordinary taxable income, and we are subject to tax on our income to the extent it is not distributed. Because of this distribution requirement, we may not be able to fund all future capital needs from cash retained from operations. As a result, to fund capital needs, we rely on third-party sources of capital, which we may not be able to obtain on favorable terms, if at all. Our access to third-party sources of capital depends upon a number of factors, including (i) general market conditions; (ii) the market's perception of our growth potential; (iii) our current and potential future earnings and cash distributions; and (iv) the market price of our capital stock. Additional debt financing may substantially increase our debt-to-total market capitalization ratio. Additional equity financing may dilute the holdings of our current stockholders.

Covenants in our credit agreements could limit our flexibility and adversely affect our financial condition. The terms of our various credit agreements and other indebtedness require us to comply with a number of customary financial and other covenants, such as maintaining debt service coverage and leverage ratios and maintaining insurance coverage. These covenants may limit our flexibility in our operations, and breaches of these covenants could result in defaults under the instruments governing the applicable indebtedness even if we had satisfied our payment obligations. If we are unable to refinance our indebtedness at maturity or meet our payment obligations, the amount of our distributable cash flow and our financial condition would be adversely affected.

Adverse changes in our credit ratings could impair our ability to obtain additional debt and equity financing on favorable terms, if at all. Our credit ratings are based on our operating performance, liquidity and leverage ratios, overall financial position and other factors employed by the credit rating agencies in their rating analysis of us. Our credit ratings can affect the amount and type of capital we can access, as well as the terms of any financings we may obtain. There can be no assurance that we will be able to maintain our current credit ratings. In the event our current credit ratings deteriorate, it may be more difficult or expensive to obtain additional financing or refinance existing obligations and commitments. Also, a downgrade in our credit ratings would trigger additional costs or other potentially negative consequences under our current and future credit facilities and debt instruments.

Increases in interest rates would increase our interest expense. At December 31, 2018, we had $195.7 million of variable-rate debt outstanding not protected by interest rate hedge contracts. We may incur additional variable-rate debt in the future. If interest rates increase, then so would the interest expense on our unhedged variable-rate debt, which would adversely affect our financial condition and results of operations. From time to time, we manage our exposure to interest rate risk with interest rate hedge contracts that effectively fix or cap a portion of our variable-rate debt. In addition, we refinance fixed-rate debt at times when we believe rates and terms are appropriate. Our efforts to manage these exposures may not be successful. Our use of interest rate hedge contracts to manage risk associated with interest rate volatility may expose us to additional risks, including a risk that a counterparty to a hedge contract may fail to honor its obligations. Developing an effective interest rate risk strategy is complex and no strategy can completely insulate us from risks associated with interest rate fluctuations. There can be no assurance that our hedging activities will have the desired beneficial impact on our results of operations or financial condition. Termination of interest rate hedge contracts typically involves costs, such as transaction fees or breakage costs.

A lack of any limitation on our debt could result in our becoming more highly leveraged. Our governing documents do not limit the amount of indebtedness we may incur. Accordingly, we may incur additional debt and would do so, for example, if it were necessary to maintain our status as a REIT. We might become more highly leveraged as a result, and our financial condition and cash available for distribution to stockholders might be negatively affected and the risk of default on our indebtedness could increase.

Other Risks

The market value of our common stock could decrease based on our performance and market perception and conditions. The market value of our common stock may be affected by the market's perception of our operating results, growth potential, and current and future cash dividends and may also be affected by the real estate market value of our underlying assets. The market price of our common stock may be influenced by the dividend on our common stock relative to market interest rates. Rising interest rates may lead potential buyers of our common stock to expect a higher dividend rate, which would adversely affect the market price of our common stock. In addition, rising interest rates would result in increased expense, thereby adversely affecting cash flow and our ability to service our indebtedness and pay dividends.

The state of the economy or other adverse changes in general or local economic conditions may adversely affect our operating results and financial condition. Turmoil in the global financial markets may have an adverse impact on the availability of credit to businesses generally and could lead to a further weakening of the U.S. and global economies. Currently these conditions have not impaired our ability to access credit markets and finance our operations. However, our ability to access the capital markets may be restricted at a time when we would like, or need, to raise financing, which could have an impact on our flexibility to react to changing economic and business conditions. Furthermore, deteriorating economic conditions including business layoffs, downsizing, industry slowdowns and other similar factors that affect our customers could continue to negatively impact commercial real estate fundamentals and result in lower occupancy, lower rental rates and declining values in our real estate portfolio and in the collateral securing any loan investments we may make. Additionally, an adverse economic situation could have an impact on our lenders or customers, causing them to fail to meet their obligations to us. No assurances can be given that the effects of an adverse economic situation will not have a material adverse effect on our business, financial condition and results of operations.

We may fail to qualify as a REIT. If we fail to qualify as a REIT, we will not be allowed to deduct distributions to stockholders in computing our taxable income and will be subject to federal income tax at regular corporate rates. In addition, we may be barred from qualification as a REIT for the four years following disqualification. The additional tax incurred at regular corporate rates would significantly reduce the cash flow available for distribution to stockholders and for debt service. Furthermore, we would no longer be required by the Internal Revenue Code to make any distributions to our stockholders as a condition of REIT qualification. Any distributions to stockholders would be taxable as ordinary income to the extent of our current and accumulated earnings and profits. Corporate distributees, however, may be eligible for the dividends received deduction on the distributions, subject to limitations under the Internal Revenue Code. To qualify as a REIT, we must comply with certain highly technical and complex requirements. We cannot be certain we have complied with these requirements because there are few judicial and administrative interpretations of these provisions. In addition, facts and circumstances that may be beyond our control may affect our ability to qualify as a REIT. We cannot assure you that new legislation, regulations, administrative interpretations or court decisions will not change the tax laws significantly with respect to our qualification as a REIT or with respect to the federal income tax consequences of qualification. We cannot assure you that we will remain qualified as a REIT.

Legislative or regulatory action with respect to tax laws and regulations could adversely affect the Company and our stockholders. On December 22, 2017, H.R. 1, informally titled the Tax Cuts and Jobs Act, was enacted. The TCJA made major changes to the Code, including a number of provisions of the Code that affect the taxation of REITs and their stockholders. The long-term effect of the significant changes made by the TCJA remains uncertain, and additional administrative guidance will be required in order to fully evaluate the effect of many provisions. The effect of any technical corrections with respect to the TCJA could have an adverse effect on the Company and our stockholders. We are also subject to state and local tax laws and regulations. Changes in state and local tax laws or regulations may result in an increase in our tax liability. A shortfall in tax revenues for states and municipalities in which we operate may lead to an increase in the frequency and size of such changes. If such changes occur, we may be required to pay additional taxes on our assets or income. These increased tax costs could adversely affect our financial condition, results of operations and the amount of cash available for the payment of dividends.
In addition, in recent years, numerous legislative, judicial and administrative changes have been made to the federal income tax laws applicable to investments in REITs and similar entities. Additional changes to tax laws are likely to continue to occur in the future, and we cannot assure our stockholders that any such changes will not adversely affect the taxation of a stockholder. We cannot assure you that future changes to tax laws and regulations will not have an adverse effect on an investment in our stock.
To maintain our status as a REIT, we limit the amount of shares any one stockholder can own. The Internal Revenue Code imposes certain limitations on the ownership of the stock of a REIT. For example, not more than 50% in value of our outstanding shares of capital stock may be owned, directly or indirectly, by five or fewer individuals (as defined

in the Code) during the last half of any taxable year. To protect our REIT status, our charter prohibits any holder from acquiring more than 9.8% (in value or in number, whichever is more restrictive) of our outstanding equity stock (defined as all of our classes of capital stock, except our excess stock (of which there is none outstanding)) unless our Board of Directors grants a waiver. The ownership limit may limit the opportunity for stockholders to receive a premium for their shares of common stock that might otherwise exist if an investor were attempting to assemble a block of shares in excess of 9.8% of the outstanding shares of equity stock or otherwise effect a change in control.

Certain tax and anti-takeover provisions of our charter and bylaws may inhibit a change of our control. Certain provisions contained in our charter and bylaws and the Maryland General Corporation Law may discourage a third party from making a tender offer or acquisition proposal to us. If this were to happen, it could delay, deter or prevent a change in control or the removal of existing management. These provisions also may delay or prevent our stockholders from receiving a premium for their common shares over then-prevailing market prices. These provisions include:

- the REIT ownership limit described above;

- special meetings of our stockholders may be called only by the chairman of the board, the chief executive officer, the president, a majority of the board or by stockholders possessing a majority of all the votes entitled to be cast at the meeting;
- our Board of Directors may authorize and issue securities without stockholder approval; and
- advance-notice requirements for proposals to be presented at stockholder meetings.

In addition, Maryland law provides protection for Maryland corporations against unsolicited takeovers by limiting, among other things, the duties of the directors in unsolicited takeover situations. The duties of directors of Maryland corporations do not require them to (a) accept, recommend or respond to any proposal by a person seeking to acquire control of the corporation, (b) authorize the corporation to redeem any rights under, or modify or render inapplicable, any stockholders rights plan, (c) make a determination under the Maryland Business Combination Act or the Maryland Control Share Acquisition Act, or (d) act or fail to act solely because of the effect of the act or failure to act may have on an acquisition or potential acquisition of control of the corporation or the amount or type of consideration that may be offered or paid to the stockholders in an acquisition. Moreover, under Maryland law the act of a director of a Maryland corporation relating to or affecting an acquisition or potential acquisition of control is not subject to any higher duty or greater scrutiny than is applied to any other act of a director. Maryland law also contains a statutory presumption that an act of a director of a Maryland corporation satisfies the applicable standards of conduct for directors under Maryland law.

The Maryland Business Combination Act provides that unless exempted, a Maryland corporation may not engage in business combinations, including mergers, dispositions of 10 percent or more of its assets, certain issuances of shares of stock and other specified transactions, with an "interested stockholder" or an affiliate of an interested stockholder for five years after the most recent date on which the interested stockholder became an interested stockholder, and thereafter unless specified criteria are met. An interested stockholder is generally a person owning or controlling, directly or indirectly, 10 percent or more of the voting power of the outstanding stock of the Maryland corporation. These provisions of Maryland law do not apply, however, to business combinations that are approved or exempted by a board of directors prior to the time that the interested stockholder becomes an interested stockholder. Pursuant to the statute, our Board of Directors has by resolution exempted business combinations between us and any other person and such resolution may not be revoked, altered or amended without prior stockholder approval.

The Maryland Control Share Acquisition Act provides that "control shares" of a corporation acquired in a "control share acquisition" shall have no voting rights except to the extent approved by a vote of two-thirds of the votes eligible to cast on the matter. "Control Shares" means shares of stock that, if aggregated with all other shares of stock previously acquired by the acquirer, would entitle the acquirer to exercise voting power in electing directors within one of the following ranges of the voting power: one-tenth or more but less than one-third, one-third or more but less than a majority, or a majority or more of all voting power. A "control share acquisition" means the acquisition of control shares, subject to certain exceptions.

If voting rights of control shares acquired in a control share acquisition are not approved at a stockholders' meeting, then subject to certain conditions and limitations, the issuer may redeem any or all of the control shares for fair value. If voting rights of such control shares are approved at a stockholders' meeting and the acquirer becomes entitled to vote a majority of the shares of stock entitled to vote, all other stockholders may exercise appraisal rights. Our bylaws contain a provision exempting from the Maryland Control Share Acquisition Act any and all acquisitions by any person of our stock. Our bylaws prohibit the repeal, amendment or alteration of this provision without the approval by the Company's stockholders; however, there can be no assurance that this provision will not be amended or eliminated at some time in the future.

The Company faces risks in attracting and retaining key personnel. Many of our senior executives have strong industry reputations, which aid us in identifying acquisition and development opportunities and negotiating with

tenants and sellers of properties. The loss of the services of these key personnel could affect our operations because of diminished relationships with existing and prospective tenants, property sellers and industry personnel. In addition, attracting new or replacement personnel may be difficult in a competitive market.

We have severance and change in control agreements with certain of our officers that may deter changes in control of the Company. If, within a certain time period (as set in the officer's agreement) following a change in control, we terminate the officer's employment other than for cause, or if the officer elects to terminate his or her employment with us for reasons specified in the agreement, we will make a severance payment equal to the officer's average annual compensation times an amount specified in the officer's agreement, together with the officer's base salary and vacation pay that have accrued but are unpaid through the date of termination. These agreements may deter a change in control because of the increased cost for a third party to acquire control of us.

We rely on information technology in our operations, and any material failure, inadequacy, interruption or security failure of that technology could harm our business. We rely on information technology networks and systems, including the internet, to process,

transmit and store electronic information, and to manage or support a variety of business processes, including financial transactions and records, and maintaining personal identifying information and customer and lease data. We purchase some of our information technology from vendors, on whom our systems depend. We rely on commercially available systems, software, tools and monitoring to provide security for the processing, transmission and storage of confidential customer data, including individually identifiable information relating to financial accounts. Although we have taken steps to protect the security of our information systems and the data maintained in those systems, it is possible that our safety and security measures will not prevent the systems' improper functioning or damage, or the improper access or disclosure of personally identifiable information such as in the event of cyber-attacks. Security breaches, including physical or electronic break-ins, computer viruses, attacks by hackers and similar breaches, can create system disruptions, shutdowns or unauthorized disclosure of confidential information. In some cases, it may be difficult to anticipate or immediately detect such incidents and the damage they cause. Any failure to maintain proper function, security and availability of our information systems could interrupt our operations, damage our reputation, subject us to liability claims or regulatory penalties and could have a materially adverse effect on our business, financial condition and results of operations.

We may be impacted by changes in U.S. social, political, regulatory and economic conditions or laws and policies. Any changes to U.S. tax laws, foreign trade, manufacturing, and development and investment in the territories and countries where our customers operate could adversely affect our operating results and our business.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

None.

ITEM 2. PROPERTIES.

EastGroup owned 377 industrial properties and one office building at December 31, 2018. These properties are located primarily in the Sunbelt states of Florida, Texas, Arizona, California and North Carolina, and the majority are clustered around major transportation features in supply constrained submarkets. As of February 13, 2019, EastGroup’s portfolio was 97.3% leased and 96.8% occupied by approximately 1,500 tenants, with no single tenant accounting for more than approximately 1.1% of the Company's income from real estate operations. The Company has developed approximately 46% of its total portfolio (on a square foot basis), including real estate properties and development and value-add properties in lease-up and under construction. The Company’s focus is the ownership of business distribution space (88% of the total portfolio) with the remainder in bulk distribution space (9%) and business service space (3%). Business distribution space properties are typically multi-tenant buildings with a building depth of 200 feet or less, clear height of 24-30 feet, office finish of 10-25% and truck courts with a depth of 100-120 feet. See Consolidated Financial Statement Schedule III – Real Estate Properties and Accumulated Depreciation for a detailed listing of the Company’s properties.

At December 31, 2018, EastGroup did not own any single property with a book value that was 10% or more of total book value or with gross revenues that were 10% or more of total gross revenues.

The Company's lease expirations for the next ten years are detailed below:

Years Ending December 31,	Number of Leases Expiring	Total Area of Leases Expiring (in Square Feet)	Annualized Current Base Rent of Leases Expiring [(1)]	% of Total Base Rent of Leases Expiring

2019 [2]	296	4,429,000	$28,660,000	12.6%
2020	300	6,243,000	$37,247,000	16.3%
2021	296	7,340,000	$44,134,000	19.3%
2022	206	5,618,000	$34,081,000	14.9%
2023	179	4,544,000	$27,361,000	12.0%
2024	110	4,180,000	$22,504,000	9.9%
2025	36	2,057,000	$12,329,000	5.4%
2026	30	1,054,000	$6,295,000	2.8%
2027	16	848,000	$5,790,000	2.5%
2028 and beyond	34	1,860,000	$9,891,000	4.3%

(1) Represents the monthly cash rental rates, excluding tenant expense reimbursements, as of December 31, 2018, multiplied by 12 months.

(2) Includes month-to-month leases.

ITEM 3. LEGAL PROCEEDINGS.

The Company is not presently involved in any material litigation nor, to its knowledge, is any material litigation threatened against the Company or its properties, other than routine litigation arising in the ordinary course of business or which is expected to be covered by the Company’s liability insurance. The Company cannot predict the outcome of any litigation with certainty, and some lawsuits, claims or proceedings may be disposed of unfavorably to the Company, which could materially affect its financial condition or results of operations.

ITEM 4. MINE SAFETY DISCLOSURES.

Not applicable.

PART II. OTHER INFORMATION

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.

The Company’s shares of common stock are listed for trading on the NYSE under the symbol “EGP.” As of February 13, 2019, there were 450 holders of record of the Company's 36,479,324 outstanding shares of common stock. The Company distributed all of its 2018 and 2017 taxable income to its stockholders. Accordingly, no significant provisions for income taxes were necessary. The following table summarizes the federal income tax treatment for all distributions by the Company for the years 2018 and 2017.

Federal Income Tax Treatment of Share Distributions

	Years Ended December 31,	
	2018	2017
Common Share Distributions:	(Per share)	
Ordinary dividends	$2.14305	2.49146
Nondividend distributions	—	0.02686
Unrecaptured Section 1250 capital gain	—	—
Other capital gain	—	0.00168
Total Common Distributions	$2.14305	2.52000

Purchases of Equity Securities by the Issuer and Affiliated Purchasers

No shares of common stock were purchased by the Company or withheld by the Company to satisfy any tax withholding obligations during the three-month period ended December 31, 2018.

Performance Graph

The following graph compares, over the five years ended December 31, 2018, the cumulative total shareholder return on EastGroup's common stock with the cumulative total return of the Standard & Poor's 500 Total Return Index (S&P 500 Total Return) and the FTSE Equity REIT index prepared by the National Association of Real Estate Investment Trusts (FTSE Nareit Equity REITs).

The performance graph and related information shall not be deemed "soliciting material" or be deemed to be "filed" with the SEC, nor shall such information be incorporated by reference into any future filing, except to the extent that the Company specifically incorporates it by reference into such filing.

	Fiscal years ended December 31,					
	2013	2014	2015	2016	2017	2018
EastGroup	$100.00	113.22	103.61	142.51	175.79	187.97
FTSE Nareit Equity REITs	100.00	130.14	134.30	145.74	153.36	146.27
S&P 500 Total Return	100.00	113.69	115.26	129.05	157.22	150.33

The information above assumes that the value of the investment in shares of EastGroup's common stock and each index was $100 on December 31, 2013, and that all dividends were reinvested.

ITEM 6. SELECTED FINANCIAL DATA.

The following table sets forth selected financial and operating data on a historical basis for the Company. The following data should be read in conjunction with the Company's financial statements and notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations included elsewhere in this Annual Report on Form 10-K. The Company's historical operating results may not be comparable to the Company's future operating results.

	Years Ended December 31,				
	2018	2017	2016	2015	2014
OPERATING DATA	(In thousands, except per share data)				
REVENUES					
Income from real estate operations	$299,018	274,031	252,961	234,918	219,706
Other revenue	1,374	119	86	90	123
	300,392	274,150	253,047	235,008	219,829
Expenses					
Expenses from real estate operations	86,394	80,108	74,347	67,402	62,797
Depreciation and amortization	91,704	83,874	77,935	73,290	70,314
General and administrative	13,738	14,972	13,232	15,091	12,726
Acquisition costs	—	—	161	164	210
	191,836	178,954	165,675	155,947	146,047
Operating income	108,556	95,196	87,372	79,061	73,782
Other income (expense)					
Interest expense	(35,106)	(34,775)	(35,213)	(34,666)	(35,486)
Gain, net of loss, on sales of real estate investments	14,273	21,855	42,170	2,903	9,188
Other	913	1,313	1,765	1,101	989
Net income	88,636	83,589	96,094	48,399	48,473
Net income attributable to noncontrolling interest in joint ventures	(130)	(406)	(585)	(533)	(532)
Net income attributable to EastGroup Properties, Inc. common stockholders	88,506	83,183	95,509	47,866	47,941
Other comprehensive income (loss) - Cash flow hedges	1,353	3,353	5,451	(1,099)	(3,986)
TOTAL COMPREHENSIVE INCOME	$89,859	86,536	100,960	46,767	43,955
BASIC PER COMMON SHARE DATA FOR NET INCOME ATTRIBUTABLE TO EASTGROUP PROPERTIES, INC. COMMON STOCKHOLDERS					
Net income attributable to common stockholders	$2.50	2.45	2.93	1.49	1.53
Weighted average shares outstanding	35,439	33,996	32,563	32,091	31,341
DILUTED PER COMMON SHARE DATA FOR NET INCOME ATTRIBUTABLE TO EASTGROUP PROPERTIES, INC. COMMON STOCKHOLDERS					
Net income attributable to common stockholders	$2.49	2.44	2.93	1.49	1.52
Weighted average shares outstanding	35,506	34,047	32,628	32,196	31,452
OTHER PER SHARE DATA					
Book value, at end of year	$24.74	21.56	19.13	17.11	17.72
Common distributions declared	2.72	2.52	2.44	2.34	2.22
Common distributions paid	2.00	2.52	2.44	2.34	2.22

BALANCE SHEET DATA (AT END OF YEAR)					
Real estate investments, at cost [(1)]	$2,827,609	2,591,358	2,419,461	2,232,344	2,087,821
Real estate investments, net of accumulated depreciation [(1)]	2,012,694	1,841,757	1,725,211	1,574,890	1,487,295
Total assets	2,131,705	1,953,221	1,825,764	1,661,904	1,572,112
Unsecured bank credit facilities, unsecured debt and secured debt	1,105,787	1,108,282	1,101,333	1,027,909	929,465
Total liabilities	1,227,002	1,202,091	1,183,898	1,102,703	996,497
Noncontrolling interest in joint ventures	1,644	1,658	4,205	4,339	4,486
Total stockholders' equity	903,059	749,472	637,661	554,862	571,129

(1) Includes mortgage loans receivable and unconsolidated investment. See Notes 3 and 4 in the Notes to Consolidated Financial Statements.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The following discussion and analysis of results of operations and financial condition should be read in conjunction with the consolidated financial statements and notes thereto appearing elsewhere in this Annual Report on Form 10-K.

OVERVIEW
EastGroup’s goal is to maximize shareholder value by being a leading provider in its markets of functional, flexible and quality business distribution space for location sensitive customers (primarily in the 15,000 to 50,000 square foot range). The Company develops, acquires and operates distribution facilities, the majority of which are clustered around major transportation features in supply-constrained submarkets in major Sunbelt regions. The Company’s core markets are in the states of Florida, Texas, Arizona, California and North Carolina.

The Company believes its current operating cash flow and unsecured bank credit facilities provide the capacity to fund the operations of the Company, and the Company also believes it can issue common and/or preferred equity and obtain debt financing. During 2018, EastGroup issued 1,706,474 shares of common stock through its continuous common equity program, providing net proceeds to the Company of $157 million. Also during 2018, the Company closed $60 million of senior unsecured private placement notes and replaced its $300 million and $35 million unsecured bank credit facilities with new $350 million and $45 million facilities. EastGroup's financing and equity issuances are further described in Liquidity and Capital Resources.

The Company’s primary revenue is rental income. During 2018, the Company executed leases on 7,365,000 square feet, which represents 18.8% of EastGroup’s total of 39,231,000 square feet as of December 31, 2018. For new and renewal leases signed during 2018, average rental rates increased by 15.8% as compared to the former leases on the same spaces.

Property net operating income (PNOI) excluding income from lease terminations from same properties, defined as operating properties owned during the entire current and prior year reporting periods (January 1, 2017 through December 31, 2018), increased 3.8% for 2018 compared to 2017.

EastGroup’s portfolio was 97.3% leased at December 31, 2018 compared to 97.0% at December 31, 2017. Leases scheduled to expire in 2019 were 11.3% of the portfolio on a square foot basis at December 31, 2018. As of February 13, 2019, leases scheduled to expire during the remainder of 2019 were 9.4% of the portfolio on a square foot basis.

The Company generates new sources of leasing revenue through its development and acquisition programs. The Company mitigates risks associated with development through a Board-approved maximum level of land held for development and by adjusting development start dates according to leasing activity.

During 2018, EastGroup acquired 627,000 square feet of operating and value-add properties in Atlanta, Chino (Los Angeles), San Diego, Austin and Dallas and 83 acres of land in Dallas, San Antonio and Phoenix for a total of $87 million. The Company began construction of 12 development projects containing 1,697,000 square feet in Miami, Orlando, Ft. Myers, Atlanta, Dallas, Houston, San Antonio and Charlotte. Also in 2018, the Company transferred 14 development projects and value-add acquisitions (1,719,000 square feet) in Orlando, Tampa, Ft. Lauderdale, Ft. Myers, Charlotte, Atlanta, Houston, San Antonio, Phoenix and Tucson from its development and value-add program to real estate properties with costs of $135.0 million at the date of transfer. As of December 31, 2018, EastGroup's development program consisted of 17 projects (2,264,000 square feet) located in 11 cities. The projected total cost for the development projects, which were collectively 45% leased as of February 13, 2019, is $206 million, of which $56 million remained to be invested as of December 31, 2018.

During 2018, EastGroup sold 339,000 square feet of operating properties and 11 acres of land, generating gross sales proceeds of $25.4 million. The Company recognized $14,273,000 in Gain, net of loss, on sales of real estate investments and $86,000 in Gain, net of loss, on sales of non-operating real estate (included in Other on the Consolidated Statements of Income and Comprehensive Income) during 2018.

Typically, the Company initially funds its development and acquisition programs through its $395 million unsecured bank credit facilities (as discussed in Liquidity and Capital Resources). As market conditions permit, EastGroup issues equity and/or employs fixed-rate debt, including variable-rate debt that has been swapped to an effectively fixed rate through the use of interest rate swaps, to replace short-term bank borrowings. In June 2018, Moody's Investors Service affirmed the Company's issuer rating of Baa2 with a stable outlook. A security rating is not a recommendation to buy, sell or hold securities and may be subject to revision or withdrawal at any time by the assigning rating agency. Each rating should be evaluated independently of any other rating. For future debt issuances, the Company intends to issue primarily unsecured fixed-rate debt, including variable-rate debt that has been

swapped to an effectively fixed rate through the use of interest rate swaps. The Company may also access the public debt market in the future as a means to raise capital.

EastGroup has one reportable segment–industrial properties. These properties are primarily located in major Sunbelt regions of the United States. The Company's properties have similar economic characteristics and as a result, have been aggregated into one reportable segment.

The Company's chief decision makers use two primary measures of operating results in making decisions: (1) property net operating income (PNOI), defined as Income from real estate operations less Expenses from real estate operations (including market-based internal management fee expense) plus the Company's share of income and property operating expenses from its less-than-wholly-owned real estate investments, and (2) funds from operations attributable to common stockholders (FFO), defined as net income (loss) attributable to common stockholders computed in accordance with U.S. generally accepted accounting principles (GAAP), excluding gains or losses from sales of depreciable real estate property and impairment losses, plus real estate related depreciation and amortization, and after adjustments for unconsolidated partnerships and joint ventures. The Company calculates FFO based on the National Association of Real Estate Investment Trusts' (Nareit) definition.

PNOI is a supplemental industry reporting measurement used to evaluate the performance of the Company's real estate investments. The Company believes the exclusion of depreciation and amortization in the industry's calculation of PNOI provides a supplemental indicator of the properties' performance since real estate values have historically risen or fallen with market conditions. PNOI as calculated by the Company may not be comparable to similarly titled but differently calculated measures for other real estate investment trusts (REITs). The major factors influencing PNOI are occupancy levels, acquisitions and sales, development projects that achieve stabilized operations, rental rate increases or decreases, and the recoverability of operating expenses. The Company's success depends largely upon its ability to lease space and to recover from tenants the operating costs associated with those leases.

PNOI was calculated as follows for the three fiscal years ended December 31, 2018, 2017 and 2016.

	Years Ended December 31,		
	2018	2017	2016
	(In thousands)		
Income from real estate operations	$299,018	274,031	252,961
Expenses from real estate operations	(86,394)	(80,108)	(74,347)
Noncontrolling interest in PNOI of consolidated 80% joint ventures	(314)	(633)	(823)
PNOI from 50% owned unconsolidated investment	869	897	906
PROPERTY NET OPERATING INCOME (PNOI)	$213,179	194,187	178,697

Income from real estate operations is comprised of rental income, expense reimbursement pass-through income and other real estate income including lease termination fees. Expenses from real estate operations is comprised of property taxes, insurance, utilities, repair and maintenance expenses, management fees, other operating costs and bad debt expense. Generally, the Company's most significant operating expenses are property taxes and insurance. Tenant leases may be net leases in which the total operating expenses are recoverable, modified gross leases in which some of the operating expenses are recoverable, or gross leases in which no expenses are recoverable (gross leases represent only a small portion of the Company's total leases). Increases in property operating expenses are fully recoverable under net leases and recoverable to a high degree under modified gross leases. Modified gross leases often include base year amounts and expense increases over these amounts are recoverable. The Company's exposure to property operating expenses is primarily due to vacancies and leases for occupied space that limit the amount of expenses that

can be recovered.

The following table presents reconciliations of Net Income to PNOI for the three fiscal years ended December 31, 2018, 2017 and 2016.

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	Years Ended December 31,		
	2018	2017	2016
		(In thousands)	
NET INCOME	$88,636	83,589	96,094
Net (gain) on sales of real estate investments	(14,273)	(21,855)	(42,170)
Net (gain) on sales of non-operating real estate	(86)	(293)	(733)
Net loss on other	70	—	—
Interest income	(156)	(247)	(255)
Other revenue	(1,374)	(119)	(86)
Interest rate swap ineffectiveness	—	—	5
Depreciation and amortization	91,704	83,874	77,935
Company's share of depreciation from unconsolidated investment	128	124	124
Interest expense	35,106	34,775	35,213
General and administrative expense	13,738	14,972	13,232
Acquisition costs	—	—	161
Noncontrolling interest in PNOI of consolidated 80% joint ventures	(314)	(633)	(823)
PROPERTY NET OPERATING INCOME (PNOI)	$213,179	194,187	178,697

The Company believes FFO is a meaningful supplemental measure of operating performance for equity REITs. The Company believes excluding depreciation and amortization in the calculation of FFO is appropriate since real estate values have historically increased or decreased based on market conditions. FFO is not considered as an alternative to net income (determined in accordance with GAAP) as an indication of the Company's financial performance, nor is it a measure of the Company's liquidity or indicative of funds available to provide for the Company's cash needs, including its ability to make distributions. In addition, FFO, as reported by the Company, may not be comparable to FFO reported by other REITs that do not define the term in accordance with the current Nareit definition. The Company's key drivers affecting FFO are changes in PNOI (as discussed above), interest rates, the amount of leverage the Company employs and general and administrative expenses. The following table presents reconciliations of Net Income Attributable to EastGroup Properties, Inc. Common Stockholders to FFO Attributable to Common Stockholders for the three fiscal years ended December 31, 2018, 2017 and 2016.

	Years Ended December 31,		
	2018	2017	2016
	(In thousands, except per share data)		
NET INCOME ATTRIBUTABLE TO EASTGROUP PROPERTIES, INC. COMMON STOCKHOLDERS	$88,506	83,183	95,509
Depreciation and amortization	91,704	83,874	77,935
Company's share of depreciation from unconsolidated investment	128	124	124
Depreciation and amortization from noncontrolling interest	(182)	(224)	(214)
Net (gain) on sales of real estate investments	(14,273)	(21,855)	(42,170)
FUNDS FROM OPERATIONS (FFO) ATTRIBUTABLE TO COMMON STOCKHOLDERS	$165,883	145,102	131,184
Net income attributable to common stockholders per diluted share	$2.49	2.44	2.93
Funds from operations (FFO) attributable to common stockholders	4.67	4.26	4.02

per diluted share			
Diluted shares for earnings per share and funds from operations	35,506	34,047	32,628

The Company analyzes the following performance trends in evaluating the revenues and expenses of the Company:

- The FFO change per share represents the increase or decrease in FFO per share from the current year compared to the prior year. For 2018, FFO was $4.67 per share compared with $4.26 per share for 2017, an increase of 9.6%.

- For the year ended December 31, 2018, PNOI increased by $18,992,000, or 9.8%, compared to 2017. PNOI increased $11,900,000 from newly developed and value-add properties, $6,712,000 from same property operations and $2,134,000

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from 2017 and 2018 acquisitions; PNOI from operating properties sold in 2017 and 2018 decreased $1,831,000 for 2018 compared to 2017.

- The same property net operating income change represents the PNOI increase or decrease for the same operating properties owned during the entire current and prior year reporting periods (January 1, 2017 through December 31, 2018). PNOI, excluding income from lease terminations, from same properties increased 3.8% for the year ended December 31, 2018, compared to 2017.

- Same property average occupancy represents the average month-end percentage of leased square footage for which the lease term has commenced as compared to the total leasable square footage for the same operating properties owned during the entire current and prior year reporting periods (January 1, 2017 through December 31, 2018). Same property average occupancy for the year ended December 31, 2018, was 96.9% compared to 96.6% for 2017.

- Occupancy is the percentage of leased square footage for which the lease term has commenced as compared to the total leasable square footage as of the close of the reporting period. Occupancy at December 31, 2018 was 96.8%. Quarter-end occupancy ranged from 95.7% to 96.4% over the previous four quarters ended December 31, 2017 to September 30, 2018.

- Rental rate change represents the rental rate increase or decrease on new and renewal leases compared to the prior leases on the same space. For the year 2018, rental rate increases on new and renewal leases (18.8% of total square footage) averaged 15.8%.

- Lease termination fee income is included in Income from real estate operations. For the year 2018, lease termination fee income was $294,000 compared to $468,000 for 2017.

- Bad debt expense is included in Expenses from real estate operations. The Company recorded net bad debt expense of $784,000 in 2018 and $499,000 in 2017.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The Company's management considers the following accounting policies and estimates to be critical to the reported operations of the Company.

Real Estate Properties

The Financial Accounting Standards Board (FASB) Codification provides guidance on how to properly determine the allocation of the purchase price among the individual components of both the tangible and intangible assets based on their respective fair values. Goodwill for business combinations is recorded when the purchase price exceeds the fair value of the assets and liabilities acquired. Factors considered by management in allocating the cost of the properties acquired include an estimate of carrying costs during the expected lease-up periods considering current market conditions and costs to execute similar leases. The allocation to tangible assets (land, building and improvements) is based upon management's determination of the value of the property as if it were vacant using discounted cash flow models. The Company determines whether any financing assumed is above or below market based upon comparison to similar financing terms for similar properties. The cost of the properties acquired may be adjusted based on indebtedness assumed from the seller that is determined to be above or below market rates.

The purchase price is also allocated among the following categories of intangible assets: the above or below market component of in-place leases, the value of in-place leases, and the value of customer relationships. The value

allocable to the above or below market component of an acquired in-place lease is determined based upon the present value (using a discount rate reflecting the risks associated with the acquired leases) of the difference between (i) the contractual amounts to be paid pursuant to the lease over its remaining term, and (ii) management's estimate of the amounts that would be paid using fair market rates over the remaining term of the lease. The amounts allocated to above and below market leases are included in Other assets and Other liabilities, respectively, on the Consolidated Balance Sheets and are amortized to rental income over the remaining terms of the respective leases. The total amount of intangible assets is further allocated to in-place lease values and customer relationship values based upon management's assessment of their respective values. These intangible assets are included in Other assets on the Consolidated Balance Sheets and are amortized over the remaining term of the existing lease, or the anticipated life of the customer relationship, as applicable.

For properties under development and value-add properties acquired in the development stage, costs associated with development (i.e., land, construction costs, interest expense, property taxes and other costs associated with development) are aggregated into the total capitalized costs of the property. Included in these costs are management's estimates for the portions of internal costs

(primarily personnel costs) deemed related to such development activities. The internal costs are allocated to specific development projects based on development activity.

FINANCIAL CONDITION

EastGroup's Total Assets were $2,131,705,000 at December 31, 2018, an increase of $178,484,000 from December 31, 2017. Total Liabilities increased $24,911,000 to $1,227,002,000, and Total Equity increased $153,573,000 to $904,703,000 during the same period. The following paragraphs explain these changes in detail.

Assets
Real Estate Properties
Real estate properties increased $216,747,000 during the year ended December 31, 2018. The increase was primarily due to: (i) the transfer of 14 properties from Development and value-add properties to Real estate properties, as detailed under Development and Value-Add Properties below; (ii) the purchase of the operating properties detailed below; and (iii) capital improvements at the Company's properties. These increases were partially offset by the operating property sales discussed below.

During 2018, EastGroup acquired the following operating properties:

REAL ESTATE PROPERTIES ACQUIRED IN 2018	Location	Size	Date Acquired	Cost [(1)]
		(Square feet)		(In thousands)
Gwinnett 316	Atlanta, GA	65,000	04/24/2018	$ 4,147
Eucalyptus Distribution Center	Chino, CA	182,000	06/20/2018	22,890
Allen Station I & II	Dallas, TX	220,000	08/29/2018	23,424
Greenhill Distribution Center	Austin, TX	45,000	12/04/2018	4,076
Total Real Estate Property Acquisitions		512,000		$ 54,537

(1) Total cost of the operating properties acquired was $57,053,000, of which $54,537,000 was allocated to Real estate properties as indicated above. The Company allocated $18,540,000 of the total purchase price to land using third party land valuations for the Atlanta, Dallas, Austin and Chino (Los Angeles) markets. The market values are considered to be Level 3 inputs as defined by ASC 820, Fair Value Measurement (see Note 18 in the Notes to Consolidated Financial Statements for additional information on ASC 820). Intangibles associated with the purchases of real estate were allocated as follows: $4,224,000 to in-place lease intangibles and $21,000 to above market leases (both included in Other assets on the Consolidated Balance Sheets), and $1,729,000 to below market leases (included in Other liabilities on the Consolidated Balance Sheets).

During the year ended December 31, 2018, the Company made capital improvements of $37,920,000 on existing and acquired properties (included in the Capital Expenditures table under Results of Operations). Also, the Company incurred costs of $8,556,000 on development projects subsequent to transfer to Real estate properties; the Company records these expenditures as development costs on the Consolidated Statements of Cash Flows.

EastGroup sold the following operating properties during 2018: World Houston 18 in Houston, 56 Commerce Park in Tampa and 35th Avenue Distribution Center in Phoenix. The properties (339,000 square feet combined) were sold for $22.9 million and the Company recognized gains on the sales of $14.3 million.

Development and Value-Add Properties
EastGroup's investment in Development and value-add properties at December 31, 2018 consisted of properties in lease-up and under construction of $149,860,000 and prospective development (primarily land) of $113,804,000. The

Company's total investment in Development and value-add properties at December 31, 2018 was $263,664,000 compared to $242,014,000 at December 31, 2017. Total capital invested for development and value-add properties during 2018 was $167,667,000, which primarily consisted of costs of $134,957,000 and $21,736,000 as detailed in the Development and Value-Add Properties Activity table below and costs of $8,556,000 on projects subsequent to transfer to Real estate properties. The capitalized costs incurred on development projects subsequent to transfer to Real estate properties include capital improvements at the properties and do not include other capitalized costs associated with development (i.e., interest expense, property taxes and internal personnel costs).

EastGroup capitalized internal development costs of $4,696,000 during the year ended December 31, 2018, compared to $4,754,000 during 2017.

During 2018, the Company acquired one value-add property, Siempre Viva Distribution Center in San Diego. At the time of acquisition, Siempre Viva was classified in the lease-up phase and was occupied by the seller under a short-term lease that expired during the third quarter of 2018. EastGroup successfully re-leased the multi-tenant distribution center, which became 100% occupied on January 1, 2019. The total cost for the property acquired by the Company was $14,033,000, of which $13,934,000 was allocated to Development and value-add properties. EastGroup allocated $4,723,000 of the total purchase price to land using third party land valuations for the San Diego market. The market values are considered to be Level 3 inputs as defined by ASC 820, Fair Value Measurement (see Note 18 for additional information on ASC 820). Intangibles associated with the purchase were allocated as follows: $126,000 to in-place lease intangibles (included in Other assets on the Consolidated Balance Sheets), and $27,000 to below market leases (included in Other liabilities on the Consolidated Balance Sheets). These costs are amortized over the remaining lives of the associated leases in place at the time of acquisition. Costs associated with the value-add property acquisitions, except for the amounts allocated to the acquired lease intangibles, are included in the Development and Value-Add Properties Activity table below.

Also during 2018, EastGroup purchased 83 acres of development land in Dallas, San Antonio and Phoenix for $15,507,000. Costs associated with these acquisitions are included in the Development and Value-Add Properties Activity table. These increases were offset by the sale of 11 acres of land for $2,577,000 and the transfer of 14 development projects to Real estate properties during 2018 with a total investment of $135,043,000 as of the date of transfer.

DEVELOPMENT AND VALUE-ADD PROPERTIES ACTIVITY		Costs Incurred				
		Costs Transferred in 2018 (1)	For the Year Ended 12/31/18	Cumulative as of 12/31/18	Estimated Total Costs (2)	Anticipated Building Conversion Date
		(In thousands)				
LEASE-UP	Building Size (Square feet)					
Siempre Viva, San Diego, CA	115,000	$—	14,075	14,075	14,400	01/19
CreekView 121 3 & 4, Dallas, TX	158,000	—	3,489	13,800	16,200	03/19
Falcon Field, Phoenix, AZ	96,000	—	5,285	8,232	9,400	05/19
Gateway 1, Miami, FL	200,000	9,110	11,131	20,241	25,000	05/19
Broadmoor 2, Atlanta, GA	111,000	705	5,709	6,414	7,400	11/19
Total Lease-Up	680,000	9,815	39,689	62,762	72,400	
UNDER CONSTRUCTION						
Horizon XI, Orlando, FL	135,000	3,171	5,552	8,723	10,400	01/20
Settlers Crossing 1, Austin, TX	77,000	—	4,704	6,260	7,400	01/20
Settlers Crossing 2, Austin, TX	83,000	—	5,442	7,115	8,400	01/20
SunCoast 5, Ft. Myers, FL	81,000	2,704	3,831	6,535	7,700	01/20
Airport Commerce Center 3, Charlotte, NC	96,000	—	4,060	5,793	7,300	02/20
Parc North 5, Dallas, TX	100,000	1,683	5,270	6,953	9,200	02/20
Steele Creek V, Charlotte, NC	54,000	1,366	1,948	3,314	5,800	03/20
Horizon VI, Orlando, FL	148,000	3,418	4,807	8,225	12,700	04/20
Ten West Crossing 8, Houston, TX	132,000	1,947	4,643	6,590	10,900	04/20
Tri-County Crossing 1 & 2, San Antonio, TX	203,000	2,012	6,883	8,895	14,600	04/20
Eisenhauer Point 7 & 8, San Antonio, TX	336,000	4,916	8,174	13,090	24,500	05/20
CreekView 121 5 & 6, Dallas, TX	139,000	3,675	1,930	5,605	14,900	07/20
Total Under Construction	1,584,000	24,892	57,244	87,098	133,800	
PROSPECTIVE DEVELOPMENT (PRIMARILY LAND)	Estimated Building Size (Square feet)					
Phoenix, AZ	315,000	—	6,809	6,809		
Ft. Myers, FL	488,000	(2,704)	1,914	13,322		
Miami, FL	650,000	(9,110)	14,565	36,331		
Orlando, FL	214,000	(6,589)	1,188	5,719		
Tampa, FL	32,000	—	—	1,560		
Atlanta, GA	100,000	(705)	224	726		
Jackson, MS	28,000	—	—	706		
Charlotte, NC	600,000	(1,366)	1,846	7,209		
Austin, TX	180,000	—	722	3,742		
Dallas, TX	612,000	(5,358)	7,954	12,192		
Houston, TX (3)	1,123,000	(2,969)	(1,782)	16,439		
San Antonio, TX	908,000	(6,928)	4,584	9,049		
Total Prospective Development	5,250,000	(35,729)	38,024	113,804		

	7,514,000	$(1,022)	134,957	263,664		
DEVELOPMENT AND VALUE-ADD PROPERTIES TRANSFERRED TO REAL ESTATE PROPERTIES DURING 2018	Building Size (Square feet)					Building Conversion Date
Alamo Ridge IV, San Antonio, TX	97,000	$—	320	7,417		03/18
Oak Creek VII, Tampa, FL	116,000	—	601	6,732		03/18
Weston, Ft. Lauderdale, FL	134,000	—	222	15,742		03/18
Progress Center 1 & 2, Atlanta, GA	132,000	—	143	10,476		04/18
Horizon X, Orlando, FL	104,000	—	3,352	6,902		05/18
SunCoast 4, Ft. Myers, FL	93,000	—	71	9,191		05/18
Country Club V, Tucson, AZ	305,000	—	7,078	21,029		06/18
Eisenhauer Point 3, San Antonio, TX	71,000	—	231	6,390		06/18
Kyrene 202 III, IV & V, Phoenix, AZ	166,000	—	1,146	12,689		09/18
Steele Creek VII, Charlotte, NC	120,000	—	795	8,592		09/18
Eisenhauer Point 6, San Antonio, TX	85,000	—	1,356	5,406		10/18
Horizon XII, Orlando, FL	140,000	—	653	11,883		10/18
Eisenhauer Point 5, San Antonio, TX	98,000	—	2,012	7,816		11/18
West Road 5, Houston, TX	58,000	1,022	3,756	4,778		11/18
Total Transferred to Real Estate Properties	1,719,000	$1,022	21,736	135,043	(4)	

Footnotes for the Development and Value-Add Properties Activity table are on the following page.

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(1) Represents costs transferred from Prospective Development (primarily land) to Under Construction during the period. Negative amounts represent land inventory costs transferred to Under Construction.
(2) Included in these costs are development obligations of $52.4 million and tenant improvement obligations of $13.6 million on properties under development.
(3) Negative amount represents land inventory costs transferred to Under Construction and land sold on 3/28/18.
(4) Represents cumulative costs at the date of transfer.

Accumulated Depreciation

Accumulated depreciation on real estate, development and value-add properties increased $65,314,000 during 2018 due primarily to depreciation expense of $76,007,000, offset by the sale of 339,000 square feet of operating properties during the period.

Other Assets

Other assets increased $5,202,000 during 2018. A summary of Other assets follows:

	December 31,	
	2018	2017
	(In thousands)	
Leasing costs (principally commissions)	$78,985	72,722
Accumulated amortization of leasing costs	(30,185)	(27,973)
Leasing costs (principally commissions), net of accumulated amortization	48,800	44,749
Straight-line rents receivable	36,365	31,609
Allowance for doubtful accounts on straight-line rents receivable	(343)	(48)
Straight-line rents receivable, net of allowance for doubtful accounts	36,022	31,561
Accounts receivable	6,033	6,004
Allowance for doubtful accounts on accounts receivable	(600)	(577)
Accounts receivable, net of allowance for doubtful accounts	5,433	5,427
Acquired in-place lease intangibles	21,696	20,690
Accumulated amortization of acquired in-place lease intangibles	(9,833)	(8,974)
Acquired in-place lease intangibles, net of accumulated amortization	11,863	11,716
Acquired above market lease intangibles	1,465	1,550
Accumulated amortization of acquired above market lease intangibles	(902)	(794)
Acquired above market lease intangibles, net of accumulated amortization	563	756
Mortgage loans receivable	2,594	4,581
Interest rate swap assets	6,701	6,034
Goodwill	990	990
Prepaid expenses and other assets	8,265	10,215
Total Other assets	$121,231	116,029

Liabilities

Unsecured bank credit facilities decreased $1,783,000 during 2018, mainly due to repayments of $448,709,000 and new debt issuance costs incurred during the period, partially offset by borrowings of $448,100,000 and the amortization of debt issuance costs during the period. The Company’s credit facilities are described in greater detail under Liquidity and Capital Resources.

Unsecured debt increased $10,339,000 during 2018, primarily due to the closing of $60 million of senior unsecured private placement notes in April 2018 and the amortization of debt issuance costs. These increases were offset by the repayment of a $50 million senior unsecured term loan in June 2018 and new debt issuance costs incurred during the period. The borrowings and repayments on Unsecured debt are described in greater detail under Liquidity and Capital Resources.

Secured debt decreased $11,051,000 during the year ended December 31, 2018. The decrease primarily resulted from regularly scheduled principal payments of $11,289,000 and amortization of premiums on Secured debt, offset by the amortization of debt issuance costs during the period.

Accounts payable and accrued expenses increased $21,596,000 during 2018. A summary of the Company's Accounts payable and accrued expenses follows:

	December 31,	
	2018	2017
	(In thousands)	
Property taxes payable	$10,718	12,081
Development costs payable	15,410	9,699
Real estate improvements and capitalized leasing costs payable	3,911	3,957
Interest payable	4,067	3,744
Dividends payable	27,738	1,365
Book overdraft [(1)]	15,048	20,902
Other payables and accrued expenses	9,671	13,219
Total Accounts payable and accrued expenses	$86,563	64,967

[(1)] Represents checks written before the end of the period which have not cleared the bank; therefore, the bank has not yet advanced cash to the Company. When the checks clear the bank, they will be funded through the Company's working cash line of credit. See Note 1(p) in the Notes to Consolidated Financial Statements.

Other liabilities increased $5,810,000 during 2018. A summary of the Company's Other liabilities follows:

	December 31,	
	2018	2017
	(In thousands)	
Security deposits	$18,432	16,668
Prepaid rent and other deferred income	12,728	9,352
Acquired below market lease intangibles	5,891	4,135
Accumulated amortization of acquired below market lease intangibles	(3,028)	(2,147)
Acquired below market lease intangibles, net of accumulated amortization	2,863	1,988
Interest rate swap liabilities	—	695
Prepaid tenant improvement reimbursements	614	124
Other liabilities	15	15
Total Other liabilities	$34,652	28,842

Equity

Additional paid-in capital increased $161,394,000 during 2018 primarily due to the issuance of common stock under the Company's continuous common equity program (as discussed in Liquidity and Capital Resources) and stock-based compensation (as discussed in Note 11 in the Notes to Consolidated Financial Statements). EastGroup issued 1,706,474 shares of common stock under its continuous common equity program with net proceeds to the Company of $157,319,000, which increased Additional paid-in capital by $157,318,000 and Common stock by $1,000.

During 2018, Distributions in excess of earnings increased $9,161,000 as a result of dividends on common stock of $97,667,000 exceeding Net Income Attributable to EastGroup Properties, Inc. Common Stockholders of $88,506,000.

Accumulated other comprehensive income increased $1,353,000 during 2018. The increase resulted from the change in fair value of the Company's interest rate swaps (cash flow hedges) which are further discussed in Notes 12 and 13 in the Notes to Consolidated Financial Statements.

RESULTS OF OPERATIONS

2018 Compared to 2017
Net Income Attributable to EastGroup Properties, Inc. Common Stockholders for 2018 was $88,506,000 ($2.50 per basic and $2.49 per diluted share) compared to $83,183,000 ($2.45 per basic and $2.44 per diluted share) for 2017.

PNOI increased by $18,992,000 ($.53 per diluted share) for 2018 as compared to 2017. EastGroup recognized net gains on sales of real estate investments and non-operating real estate of $14,359,000 ($.40 per diluted share) compared to $22,148,000 ($.65 per diluted share) during 2017. In addition, Depreciation and amortization expense increased by $7,830,000 ($.22 per diluted share), and General and administrative expense decreased by $1,234,000 ($.03 per diluted share) during 2018 compared to 2017. During 2018, EastGroup recognized gain on casualties and involuntary conversion of $1,245,000 ($.04 per diluted share), compared to zero during 2017.

PNOI increased by $18,992,000, or 9.8%, for 2018 compared to 2017. PNOI increased $11,900,000 from newly developed and value-add properties, $6,712,000 from same property operations and $2,134,000 from 2017 and 2018 acquisitions; PNOI from operating properties sold in 2017 and 2018 decreased $1,831,000 for 2018 compared to 2017. For the year 2018, lease termination fee income was $294,000 compared to $468,000 for 2017. The Company recorded net bad debt expense of $784,000 in 2018 and $499,000 in 2017. Straight-lining of rent increased Income from real estate operations by $5,116,000 and $3,723,000 in 2018 and 2017, respectively.

The Company signed 132 leases with certain free rent concessions on 3,800,000 square feet during 2018 with total free rent concessions of $5,944,000 over the lives of the leases, compared to 138 leases with free rent concessions on 3,919,000 square feet with total free rent concessions of $5,672,000 over the lives of the leases in 2017.

The Company’s percentage of leased square footage was 97.3% at December 31, 2018, compared to 97.0% at December 31, 2017. Occupancy at the end of 2018 was 96.8% compared to 96.4% at the end of 2017.

Same property average occupancy represents the average month-end percentage of leased square footage for which the lease term has commenced as compared to the total leasable square footage for the same operating properties owned during the entire current and prior year reporting periods (January 1, 2017 through December 31, 2018). Same property average occupancy for the year ended December 31, 2018, was 96.9% compared to 96.6% for 2017.

The same property average rental rate calculated in accordance with GAAP represents the average annual rental rates of leases in place for the same operating properties owned during the entire current and prior year reporting periods. The same property average rental rate was $5.94 per square foot for the year ended December 31, 2018, compared to $5.74 per square foot for 2017.

Interest Expense increased $331,000 for 2018 compared to 2017. The following table presents the components of Interest Expense for 2018 and 2017:

	Years Ended December 31,		
	2018	2017	Increase (Decrease)
	(In thousands)		
VARIABLE RATE INTEREST EXPENSE			
Unsecured bank credit facilities interest - variable rate (excluding amortization of facility fees and debt issuance costs)	$3,736	2,379	1,357
Amortization of facility fees - unsecured bank credit facilities	736	670	66
Amortization of debt issuance costs - unsecured bank credit facilities	508	451	57
Total variable rate interest expense	4,980	3,500	1,480
FIXED RATE INTEREST EXPENSE			
Unsecured bank credit facilities interest - fixed rate [(1)] [(2)] (excluding amortization of facility fees and debt issuance costs)	1,001	1,616	(615)
Unsecured debt interest [(1)] (excluding amortization of debt issuance costs)	24,544	22,425	2,119
Secured debt interest (excluding amortization of debt issuance costs)	10,071	12,201	(2,130)
Amortization of debt issuance costs - unsecured debt	564	479	85
Amortization of debt issuance costs - secured debt	280	319	(39)
Total fixed rate interest expense	36,460	37,040	(580)
Total interest	41,440	40,540	900
Less capitalized interest	(6,334)	(5,765)	(569)
TOTAL INTEREST EXPENSE	$35,106	34,775	331

(1) Includes interest on the Company's unsecured bank credit facilities and unsecured debt with fixed interest rates per the debt agreements or effectively fixed interest rates due to interest rate swaps, as discussed in Note 13 in the Notes to Consolidated Financial Statements.

(2) The Company had designated an interest rate swap to an $80 million unsecured bank credit facility draw that effectively fixed the interest rate on the $80 million draw to 2.020% through the interest rate swap's maturity date. This swap matured on August 15, 2018, and the $80 million draw has reverted to the variable interest rate associated with the Company's unsecured bank credit facilities.

EastGroup's variable rate interest expense increased by $1,480,000 for 2018 as compared to 2017 primarily due to increases in the Company's weighted average interest rate and average borrowings on its unsecured bank credit facilities as shown in the following table:

	Years Ended December 31,		
	2018	2017	Increase (Decrease)
	(In thousands, except rates of interest)		
Average borrowings on unsecured bank	$ 141,223	114,751	26,472

credit facilities - variable rate				
Weighted average variable interest rates (excluding amortization of facility fees and debt issuance costs)	2.64	%	2.07	%

The Company's fixed rate interest expense decreased by $580,000 for 2018 as compared to 2017 as a result of the secured debt, unsecured debt and fixed rate unsecured bank credit facilities activity described below.

Secured debt interest decreased by $2,130,000 in 2018 as compared to 2017 as a result of regularly scheduled principal payments and debt repayments. Regularly scheduled principal payments on secured debt were $11,289,000 during 2018 and $13,139,000 in 2017. The Company did not repay any secured debt in 2018. The details of the secured debt repaid in 2017 are shown in the following table:

SECURED DEBT REPAID IN 2017	Interest Rate	Date Repaid	Payoff Amount (In thousands)
Arion 16, Broadway VI, Chino, East University I & II, Northpark I-IV, Santan 10 II, 55th Avenue and World Houston 1 & 2, 21 & 23	5.57%	08/07/2017	$ 45,069

EastGroup did not obtain any new secured debt during 2017 or 2018.

Interest expense from fixed rate unsecured debt increased by $2,119,000 during 2018 as compared to 2017 as a result of the Company's unsecured debt activity described below. The details of the unsecured debt obtained in 2017 and 2018 are shown in the following table:

NEW UNSECURED DEBT IN 2017 and 2018	Effective Interest Rate	Date Obtained	Maturity Date	Amount
				(In thousands)
$60 Million Senior Unsecured Notes	3.460%	12/13/2017	12/13/2024	$ 60,000
$60 Million Senior Unsecured Notes	3.930%	04/10/2018	04/10/2028	60,000
Weighted Average/Total Amount for 2017 and 2018	3.695%			$ 120,000

The increase in interest expense from the new unsecured debt was partially offset by the refinancing of two unsecured loans and the repayment of a $50 million unsecured term loan. In December 2017, the Company refinanced a $75 million unsecured term loan, resulting in a 30 basis point reduction in the loan's interest rate. The loan, which has a maturity date of December 20, 2020, now has an effectively fixed interest rate of 3.452%. In February 2018, EastGroup refinanced a $65 million unsecured term loan, resulting in a 55 basis point reduction in the loan's interest rate. The loan, which has a maturity date of April 1, 2023, now has an effectively fixed interest rate of 2.313%. In June 2018, the Company repaid (with no penalty) a $50 million senior unsecured term loan with an effective interest rate of 3.91% and an original maturity date of December 21, 2018.

Interest expense from fixed rate unsecured bank credit facilities decreased by $615,000 during 2018 as compared to 2017 due to the August 15, 2018 maturity of an interest rate swap designated to an $80 million draw on the Company's unsecured bank credit facilities. See footnote (2) in the interest expense summary table above for additional details.

Interest costs during the period of construction of real estate properties are capitalized and offset against interest expense. Capitalized interest increased by $569,000 for 2018 as compared to 2017. The increase is due to changes in development spending and borrowing rates.

Depreciation and amortization expense increased $7,830,000 for 2018 compared to 2017 primarily due to the operating properties acquired by the Company during 2017 and 2018 and the properties transferred from Development and value-add properties in 2017 and 2018, partially offset by operating properties sold in 2017 and 2018.

Gain, net of loss, on sales of real estate investments, which includes gains and losses on the sales of operating properties, decreased $7,582,000 for 2018 as compared to 2017. Net gain on sales of non-operating real estate (included in Other on the Consolidated Statements of Income and Comprehensive Income) decreased $207,000 for 2018 as compared to 2017. The Company's 2017 and 2018 sales transactions are described below in Real Estate Sold and Held for Sale/Discontinued Operations.

Real Estate Improvements

Real estate improvements for EastGroup's operating properties for the years ended December 31, 2018 and 2017 were as follows:

	Estimated Useful Life	Years Ended December 31,	
		2018	2017
		(In thousands)	
Upgrade on Acquisitions	40 yrs	$294	161
Tenant Improvements:			
New Tenants	Lease Life	12,896	11,413
Renewal Tenants	Lease Life	2,926	3,357
Other:			
Building Improvements	5-40 yrs	9,012	3,362
Roofs	5-15 yrs	9,053	6,197
Parking Lots	3-5 yrs	2,878	1,880
Other	5 yrs	861	1,101
Total Real Estate Improvements [1]		$37,920	27,471

(1) Reconciliation of Total Real Estate Improvements to Real Estate Improvements on the Consolidated Statements of Cash Flows:

	Years Ended December 31,	
	2018	2017
	(In thousands)	
Total Real Estate Improvements	$37,920	27,471
Change in Real Estate Property Payables	581	(1,313)
Change in Construction in Progress	(999)	1,227
Real Estate Improvements on the Consolidated Statements of Cash Flows	$37,502	27,385

Capitalized Leasing Costs

The Company's leasing costs (principally commissions) are capitalized and included in Other assets. The costs are amortized over the terms of the associated leases, and the amortization is included in Depreciation and amortization expense. Capitalized leasing costs for the years ended December 31, 2018 and 2017 were as follows:

	Estimated Useful Life	Years Ended December 31,	
		2018	2017
		(In thousands)	
Development and Value-Add	Lease Life	$4,843	5,571
New Tenants	Lease Life	5,880	5,782
Renewal Tenants	Lease Life	5,038	4,907
Total Capitalized Leasing Costs		$15,761	16,260
Amortization of Leasing Costs		$11,493	10,329

Real Estate Sold and Held for Sale/Discontinued Operations

The Company considers a real estate property to be held for sale when it meets the criteria established under ASC 360, Property, Plant and Equipment, including when it is probable that the property will be sold within a year. Real estate properties held for sale are reported at the lower of the carrying amount or fair value less estimated costs to sell and are not depreciated while they are held for sale.

In accordance with FASB Accounting Standards Update (ASU) 2014-08, Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360), Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity, the Company would report a disposal of a component of an entity or a group of components of an entity in discontinued operations if the disposal represents a strategic shift that has (or will have) a major effect on an entity's operations and financial results when the component or group of components meets the criteria to be classified as held for sale or when the component or group of components is disposed of by sale or other than by sale. In addition, the Company would provide additional disclosures

about both discontinued operations and the disposal of an individually significant component of an entity that does not qualify for discontinued operations presentation in the financial statements. EastGroup performs an analysis of properties sold to determine whether the sales qualify for discontinued operations presentation.

The Company did not classify any properties as held for sale as of December 31, 2018 and 2017.

The Company does not consider its sales in 2017 and 2018 to be disposals of a component of an entity or a group of components of an entity representing a strategic shift that has (or will have) a major effect on the entity's operations and financial results.

In 2018, EastGroup sold the following operating properties: World Houston 18 in Houston; 56 Commerce Park in Tampa; and 35th Avenue Distribution Center in Phoenix. The properties contain a combined 339,000 square feet and were sold for $22.9 million. EastGroup recognized gains on the sales of $14.3 million. The Company also sold 11 acres of land in Houston for $2.6 million and recognized a gain on the sale of $86,000.

During 2017, Eastgroup sold Stemmons Circle in Dallas and Techway Southwest I-IV in Houston. The properties, which contain 514,000 square feet, were sold for $38.0 million and the Company recognized gains on the sales of $21.9 million. The Company also sold 19 acres of land in El Paso and Dallas for $3,778,000 and recognized net gains of $293,000.

The gains and losses on the sales of land are included in Other on the Consolidated Statements of Income and Comprehensive Income, and the gains and losses on the sales of operating properties are included in Gain, net of loss, on sales of real estate investments. See Notes 1(f) and 2 in the Notes to Consolidated Financial Statements for more information related to discontinued operations and gains and losses on sales of real estate investments.

2017 Compared to 2016

Net Income Attributable to EastGroup Properties, Inc. Common Stockholders for 2017 was $83,183,000 ($2.45 per basic and $2.44 per diluted share) compared to $95,509,000 ($2.93 per basic and diluted share) for 2016.

PNOI increased by $15,490,000 ($.45 per diluted share) for 2017 as compared to 2016. EastGroup recognized net gains on sales of real estate investments and non-operating real estate of $22,148,000 ($.65 per diluted share) compared to $42,903,000 ($1.31 per diluted share) during 2016. In addition, Depreciation and amortization expense increased by $5,939,000 ($.17 per diluted share), and General and administrative expense increased by $1,740,000 ($.05 per share) during 2017 compared to 2016.

PNOI increased by $15,490,000, or 8.7%, for 2017 compared to 2016. PNOI increased $10,327,000 from newly developed and value-add properties, $4,765,000 from same property operations and $3,355,000 from 2016 and 2017 acquisitions; PNOI decreased $2,767,000 from operating properties sold in 2016 and 2017. For the year 2017, lease termination fee income was $468,000 compared to $812,000 for 2016. The Company recorded net bad debt expense of $499,000 in 2017 and $992,000 in 2016. Straight-lining of rent increased Income from real estate operations by $3,723,000 and $2,839,000 in 2017 and 2016, respectively.

The Company signed 138 leases with certain free rent concessions on 3,919,000 square feet during 2017 with total free rent concessions of $5,672,000 over the lives of the leases, compared to 143 leases with free rent concessions on 4,176,000 square feet with total free rent concessions of $5,286,000 over the lives of the leases in 2016.

The Company’s percentage of leased square footage was 97.0% at December 31, 2017, compared to 97.3% at December 31, 2016. Occupancy at the end of 2017 was 96.4% compared to 96.8% at the end of 2016.

Same property average occupancy for the year ended December 31, 2017, was 96.8% compared to 96.5% for 2016. The same property average rental rate was $5.79 per square foot for the year ended December 31, 2017, compared to $5.57 per square foot for 2016.

Interest expense decreased $438,000 in 2017 compared to 2016. The following table presents the components of Interest expense for 2017 and 2016:

	Years Ended December 31,		
	2017	2016	Increase (Decrease)
	(In thousands)		
VARIABLE RATE INTEREST EXPENSE			
Unsecured bank credit facilities interest - variable rate (excluding amortization of facility fees and debt issuance costs)	$2,379	1,583	796
Amortization of facility fees - unsecured bank credit facilities	670	670	—
Amortization of debt issuance costs - unsecured bank credit facilities	451	450	1
Total variable rate interest expense	3,500	2,703	797
FIXED RATE INTEREST EXPENSE			
Unsecured bank credit facilities interest - fixed rate [(1)] (excluding amortization of facility fees and debt issuance costs)	1,616	614	1,002
Unsecured debt interest [(1)] (excluding amortization of debt issuance costs)	22,425	19,245	3,180
Secured debt interest (excluding amortization of debt issuance costs)	12,201	16,907	(4,706)
Amortization of debt issuance costs - unsecured debt	479	700	(221)
Amortization of debt issuance costs - secured debt	319	384	(65)
Total fixed rate interest expense	37,040	37,850	(810)
Total interest	40,540	40,553	(13)
Less capitalized interest	(5,765)	(5,340)	(425)
TOTAL INTEREST EXPENSE	$34,775	35,213	(438)

(1) Includes interest on the Company's unsecured bank credit facilities and unsecured debt with fixed interest rates per the debt agreements or effectively fixed interest rates due to interest rate swaps, as discussed in Note 13 in the Notes to Consolidated Financial Statements.

EastGroup's variable rate interest expense increased by $797,000 for 2017 as compared to 2016 primarily due to increases in the Company's weighted average interest rate and average borrowings on its unsecured bank credit facilities as shown in the following table:

	Years Ended December 31,		
	2017	2016	Increase (Decrease)
	(In thousands, except rates of interest)		
Average borrowings on unsecured bank credit facilities - variable rate	$114,751	106,352	8,399
Weighted average variable interest rates (excluding amortization of facility fees and debt issuance costs)	2.07		