

GLADSTONE COMMERCIAL CORP
Form 10-K/A
May 15, 2008

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-K/A
(Amendment No. 1)**

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED DECEMBER 31, 2007
OR**

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

**COMMISSION FILE NUMBER: 0-50363
GLADSTONE COMMERCIAL CORPORATION
(Exact name of registrant as specified in its charter)**

MARYLAND

*(State or other jurisdiction of incorporation or
organization)*

02-0681276

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

**1521 WESTBRANCH DRIVE, SUITE 200
MCLEAN, VIRGINIA 22102**

(Address of principal executive office)

(703) 287-5800

(Registrant's telephone number, including area code)

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

| | |
|--|----------------------|
| Common Stock, par value \$0.001 per share | NASDAQ Global Market |
| 7.75% Series A Cumulative Redeemable Preferred Stock, par value \$0.001 per share | NASDAQ Global Market |
| 7.50% Series B Cumulative Redeemable Preferred Stock, par value \$0.001 per share | NASDAQ Global Market |

(Title of Each Class)

*(Name of exchange on which
registered)*

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

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

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

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

Indicate by check mark 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 10-K or any amendment to this Form 10-K.

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

Large accelerated
filer

Accelerated filer

Non-accelerated filer

Smaller reporting
company

(Do not check if a smaller reporting company)

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

The aggregate market value of the voting stock held by non-affiliates of the registrant on June 30, 2007, based on the closing price on that date of \$19.60 on the Nasdaq Global Market, was \$156,540,552. For the purposes of calculating this amount only, all directors and executive officers of the registrant have been treated as affiliates.

The number of shares of the registrant's Common Stock, \$0.001 par value, outstanding as of February 22, 2008 was 8,565,264.

Documents Incorporated by Reference: Portions of the registrant's Proxy Statement relating to the Registrant's 2008 Annual Meeting of Stockholders are incorporated by reference into Part III of this Report.

EXPLANATORY NOTE

This Amendment No. 1 on form 10-K/A (this Amendment) amends the Registrant's Annual Report on Form 10-K for the year ended December 31, 2007, which the Registrant previously filed with the Securities and Exchange Commission on February 27, 2008 (the Original Filing). The Registrant is filing this Amendment for the sole purpose of correcting a typographical error which resulted in a transposition within the columns in the table in Footnote No. 9 to the Consolidated Financial Statements. The percentages for the tax status of distributions for ordinary income and return of capital for the year ended December 31, 2007, as it related to common stock, were inadvertently transposed. In addition, as required by Rule 12b-15 under the Securities Exchange Act of 1934, new certifications by our principal executive officer and principal financial officer are filed as exhibits to this Amendment. Except as described above, the Original Filing has not been amended, updated or otherwise modified.

PART II

Item 8. Financial Statements and Supplementary Data

Index to Consolidated Financial Statements

Report of Independent Registered Public Accounting Firm

Consolidated Balance Sheets as of December 31, 2007 and December 31, 2006

Consolidated Statements of Operations for the years ended December 31, 2007, 2006 and 2005

Consolidated Statements of Stockholders' Equity for the years ended December 31, 2007, 2006 and 2005

Consolidated Statements of Cash Flows for the years ended December 31, 2007, 2006 and 2005

Notes to Financial Statements

Schedule III Real Estate and Accumulated Depreciation

Schedule IV Mortgage Loans on Real Estate

Report of Independent Registered Public Accounting Firm

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

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of Gladstone Commercial Corporation and its subsidiaries at December 31, 2007 and December 31, 2006, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2007 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedules listed in the accompanying index present fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007 based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements and financial statement schedules, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management's Annual Report on Internal Control Over Financial Reporting appearing under Item 9A. Our responsibility is to express opinions on these financial statements, on the financial statement schedules, and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

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

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

PricewaterhouseCoopers LLP

McLean, VA

February 27, 2008

GLADSTONE COMMERCIAL CORPORATION
CONSOLIDATED BALANCE SHEETS

| | December 31, 2007 | December 31, 2006 |
|---|-----------------------|-----------------------|
| ASSETS | | |
| Real estate, net of accumulated depreciation of \$15,738,634 and \$8,595,419, respectively | \$ 324,761,772 | \$ 235,118,123 |
| Lease intangibles, net of accumulated amortization of \$7,560,928 and \$4,175,685, respectively | 28,989,556 | 23,416,696 |
| Mortgage notes receivable | 10,000,000 | 10,000,000 |
| Cash and cash equivalents | 1,356,408 | 36,005,686 |
| Restricted cash | 1,914,067 | 1,225,162 |
| Funds held in escrow | 1,401,695 | 1,635,819 |
| Interest receivable mortgage note | 86,111 | |
| Interest receivable employees | 39,280 | 43,716 |
| Deferred rent receivable | 5,094,799 | 3,607,279 |
| Deferred financing costs, net of accumulated amortization of \$2,184,492 and \$1,467,297, respectively | 4,405,129 | 3,713,004 |
| Prepaid expenses | 522,348 | 521,290 |
| Deposits on real estate | 300,000 | 300,000 |
| Accounts receivable | 31,524 | 179,247 |
| TOTAL ASSETS | \$ 378,902,689 | \$ 315,766,022 |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| LIABILITIES | | |
| Mortgage notes payable | \$ 202,120,471 | \$ 154,494,438 |
| Short-term loan and borrowings under line of credit | 24,400,000 | |
| Deferred rent liability | 3,933,035 | 4,718,599 |
| Asset retirement obligation liability | 1,811,752 | 1,631,294 |
| Accounts payable and accrued expenses | 778,949 | 673,410 |
| Due to adviser | 784,301 | 183,042 |
| Rent received in advance, security deposits and funds held in escrow | 2,706,113 | 1,841,063 |
| Total Liabilities | 236,534,621 | 163,541,846 |
| STOCKHOLDERS EQUITY | | |
| Redeemable preferred stock, \$0.001 par value; \$25 liquidation preference; 2,300,000 shares authorized and 2,150,000 shares issued and outstanding | 2,150 | 2,150 |
| Common stock, \$0.001 par value, 17,700,000 shares authorized and 8,565,264 shares issued and outstanding | 8,565 | 8,565 |
| Additional paid in capital | 170,640,979 | 170,640,979 |

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| | | |
|--|-----------------------|-----------------------|
| Notes receivable - employees | (2,769,923) | (3,201,322) |
| Distributions in excess of accumulated earnings | (25,513,703) | (15,226,196) |
| Total Stockholders Equity | 142,368,068 | 152,224,176 |
| TOTAL LIABILITIES AND STOCKHOLDERS EQUITY | \$ 378,902,689 | \$ 315,766,022 |

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

GLADSTONE COMMERCIAL CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS

| | For the year ended December 31, | | |
|---|---------------------------------|-----------------|-----------------|
| | 2007 | 2006 | 2005 |
| Operating revenues | | | |
| Rental income | \$ 31,469,297 | \$ 23,964,035 | \$ 10,853,903 |
| Interest income from mortgage notes receivable | 1,013,889 | 1,845,231 | 1,915,795 |
| Tenant recovery revenue | 310,353 | 136,280 | 111,808 |
| Total operating revenues | 32,793,539 | 25,945,546 | 12,881,506 |
| Operating expenses | | | |
| Depreciation and amortization | 10,528,458 | 8,297,174 | 3,521,128 |
| Property operating expenses | 821,790 | 645,792 | 406,277 |
| Base management fee | 1,858,120 | 2,902,053 | 2,118,040 |
| Incentive fee | 2,564,365 | | |
| Administration fee | 837,898 | | |
| Professional fees | 625,349 | 953,066 | 563,205 |
| Insurance | 214,141 | 211,562 | 196,657 |
| Directors fees | 229,000 | 140,000 | 96,219 |
| Stockholder related expenses | 244,629 | 311,049 | 215,907 |
| Asset retirement obligation expense | 116,478 | 129,142 | |
| General and administrative | 102,999 | 82,847 | 67,607 |
| Stock option compensation expense | | 394,411 | |
| Total operating expenses before credit from Adviser | 18,143,227 | 14,067,096 | 7,185,040 |
| Credit to incentive fee | (2,321,597) | | |
| Total operating expenses | 15,821,630 | 14,067,096 | 7,185,040 |
| Other income (expense) | | | |
| Interest income from temporary investments | 354,249 | 76,772 | 126,826 |
| Interest income - employee loans | 222,051 | 125,788 | 21,041 |
| Other income | 47,847 | 380,915 | |
| Interest expense | (11,564,541) | (9,104,894) | (2,333,376) |
| Total other expense | (10,940,394) | (8,521,419) | (2,185,509) |
| Income from continuing operations | 6,031,515 | 3,357,031 | 3,510,957 |
| Discontinued operations | | | |
| (Loss) income from discontinued operations | (3,312) | 112,145 | 309,545 |

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| | | | |
|--|--------------|--------------|--------------|
| Net realized income (loss) from foreign currency transactions | 33,359 | (202,938) | (6,278) |
| Net unrealized loss from foreign currency transactions | | | (212,279) |
| Gain on sale of real estate | | 1,422,026 | |
| Taxes refunded (paid) on sale of real estate | 78,667 | (315,436) | |
| Total discontinued operations | 108,714 | 1,015,797 | 90,988 |
| Net income | 6,140,229 | 4,372,828 | 3,601,945 |
| Dividends attributable to preferred stock | (4,093,750) | (2,186,890) | |
| Net income available to common stockholders | \$ 2,046,479 | \$ 2,185,938 | \$ 3,601,945 |
| Earnings per weighted average common share - basic | | | |
| Income from continuing operations (net of dividends attributable to preferred stock) | \$ 0.23 | \$ 0.15 | \$ 0.46 |
| Discontinued operations | 0.01 | 0.13 | 0.01 |
| Net income available to common stockholders | \$ 0.24 | \$ 0.28 | \$ 0.47 |
| Earnings per weighted average common share - diluted | | | |
| Income from continuing operations (net of dividends attributable to preferred stock) | \$ 0.23 | \$ 0.14 | \$ 0.46 |
| Discontinued operations | 0.01 | 0.13 | 0.01 |
| Net income available to common stockholders | \$ 0.24 | \$ 0.27 | \$ 0.47 |
| Weighted average shares outstanding | | | |
| Basic | 8,565,264 | 7,827,781 | 7,670,219 |
| Diluted | 8,565,264 | 7,986,690 | 7,723,220 |

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

GLADSTONE COMMERCIAL CORPORATION
CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

| | Common Stock | Preferred Stock | Capital in Excess of Par Value | Notes Receivable From Sale of Common Stock | Distributions in Excess of Accumulated Earnings | Total Stockholders Equity |
|--|-----------------|--------------------|--------------------------------------|--|---|---------------------------------|
| Issuance of Common Stock Under Stock Option Plan | 5 | | 74,995 | (75,000) | | |
| Repayment of Principal on Notes Receivable | | | | 17,718 | | 17,718 |
| Distributions Declared to Common Stockholders | | | | | (7,363,820) | (7,363,820) |
| Net income | | | | | 3,601,945 | 3,601,945 |
| Balance at December 31, 2005 | \$ 7,672 | \$ | \$ 105,502,544 | \$ (432,282) | \$ (6,129,398) | \$ 98,948,536 |
| Issuance of Common Stock Under Stock Option Plan | 893 | | 13,650,453 | (2,769,954) | | 10,881,392 |
| Issuance of Preferred Stock | | 2,150 | 53,747,850 | | | 53,750,000 |
| Public Offering Costs | | | (2,654,279) | | | (2,654,279) |
| Stock Option Compensation Expense | | | 394,411 | | | 394,411 |
| Repayment of Principal on Notes Receivable | | | | 914 | | 914 |
| Distributions Declared to Common and Preferred Stockholders | | | | | (13,469,626) | (13,469,626) |

| | | | | | | |
|--|----------|----------|----------------|----------------|-----------------|----------------|
| Net income | | | | | 4,372,828 | 4,372,828 |
| Balance at December 31, 2006 | \$ 8,565 | \$ 2,150 | \$ 170,640,979 | \$ (3,201,322) | \$ (15,226,196) | \$ 152,224,176 |
| Repayment of Principal on Notes Receivable | | | | 431,399 | | 431,399 |
| Distributions Declared to Common and Preferred Stockholders | | | | | (16,427,736) | (16,427,736) |
| Net income | | | | | 6,140,229 | 6,140,229 |
| Balance at December 31, 2007 | \$ 8,565 | \$ 2,150 | \$ 170,640,979 | \$ (2,769,923) | \$ (25,513,703) | \$ 142,368,068 |

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

GLADSTONE COMMERCIAL CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS

| | For the year ended December 31, | | |
|---|---------------------------------|--------------|---------------|
| | 2007 | 2006 | 2005 |
| Cash flows from operating activities: | | | |
| Net income | \$ 6,140,229 | \$ 4,372,828 | \$ 3,601,945 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Depreciation and amortization, including discontinued operations | 10,528,458 | 8,349,474 | 3,651,119 |
| Amortization of deferred financing costs, including discontinued operations | 717,195 | 1,207,198 | 260,099 |
| Amortization of deferred rent asset | 253,496 | 253,496 | 178,070 |
| Amortization of deferred rent liability | (785,564) | (696,261) | |
| Asset retirement obligation expense, including discontinued operations | 116,478 | 139,074 | |
| Stock compensation | | 394,411 | |
| Increase in mortgage notes payable due to change in value of foreign currency | | 202,066 | 209,395 |
| Value of building acquired in excess of mortgage note satisfied, applied to interest income | | (335,701) | |
| Gain on sale of real estate | | (1,422,026) | |
| (Increase) decrease in mortgage interest receivable | (86,111) | 70,749 | (5,954) |
| Decrease (increase) in employee interest receivable | 4,436 | (43,716) | 4,792 |
| Increase in deferred rent receivable | (1,741,016) | (1,270,159) | (562,133) |
| Decrease (increase) in prepaid expenses and other assets | 146,665 | (89,913) | (425,120) |
| Increase in accounts payable, accrued expenses, and amount due adviser | 625,398 | 196,294 | 359,537 |
| Increase in rent received in advance | 176,145 | 268,037 | 133,798 |
| Net cash provided by operating activities | 16,095,809 | 11,595,851 | 7,405,548 |
| Cash flows from investing activities: | | | |
| Real estate investments | (105,599,587) | (48,339,307) | (117,531,731) |
| Proceeds from sales of real estate | | 2,102,567 | |
| Issuance of mortgage note receivable | | | (10,000,000) |
| Principal repayments on mortgage notes receivable | | 44,742 | 81,902 |
| Net payments to lenders for reserves held in escrow | (1,338,904) | (3,346,216) | (1,041,292) |
| (Decrease) increase in restricted cash | (688,905) | 749,274 | (513,761) |
| Deposits on future acquisitions | (2,110,000) | (900,000) | (2,686,000) |
| Deposits applied against real estate investments | 2,110,000 | 1,200,000 | 1,986,000 |
| Refunds of deposits on real estate | | | 150,000 |
| Net cash used in investing activities | (107,627,396) | (48,488,940) | (129,554,882) |
| Cash flows from financing activities: | | | |

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| | | | |
|---|---------------|---------------|--------------|
| Proceeds from share issuance | | 65,089,026 | |
| Redemption of shares for payment of taxes | | (457,634) | |
| Offering costs | | (2,654,279) | |
| Borrowings under mortgage notes payable | 48,521,690 | 68,055,000 | 61,419,179 |
| Principal repayments on mortgage notes payable | (895,657) | (604,318) | (70,479) |
| Principal repayments on employee notes receivable from sale of common stock | 431,399 | 914 | 17,718 |
| Borrowings from short-term loan and line of credit | 65,500,000 | 71,400,400 | 85,460,000 |
| Repayments on line of credit | (41,100,000) | (114,960,400) | (41,900,000) |
| Increase in reserves from tenants | 1,885,361 | 1,574,464 | 158,646 |
| Increase in security deposits | 376,572 | 427,951 | 355,115 |
| Payments for deferred financing costs | (1,409,320) | (3,242,881) | (2,021,115) |
| Dividends paid for common and preferred | (16,427,736) | (13,469,627) | (8,283,860) |
| Net cash provided by financing activities | 56,882,309 | 71,158,616 | 95,135,204 |
| Net (decrease) increase in cash and cash equivalents | (34,649,278) | 34,265,527 | (27,014,130) |
| Cash and cash equivalents, beginning of period | 36,005,686 | 1,740,159 | 28,754,289 |
| Cash and cash equivalents, end of period | \$ 1,356,408 | \$ 36,005,686 | \$ 1,740,159 |
| Cash paid during period for interest | \$ 10,693,440 | \$ 8,045,342 | \$ 2,014,236 |
| NON-CASH INVESTING ACTIVITIES | | | |
| Increase in asset retirement obligation | \$ 180,458 | \$ 1,631,294 | \$ |
| Additions to real estate included in accounts payable, accrued expenses, and amount due adviser | \$ 81,400 | \$ | \$ |
| NON-CASH FINANCING ACTIVITIES | | | |
| Fixed rate debt assumed in connection with acquisitions | \$ 4,506,689 | \$ 30,129,654 | \$ |
| Assumption of mortgage notes payable by buyer | \$ | \$ 4,846,925 | \$ |
| Notes receivable issued in exchange for common stock associated with the exercise of employee stock options | \$ | \$ 2,769,954 | \$ 75,000 |
| Acquisition of building in satisfaction of mortgage note receivable | \$ | \$ 11,316,774 | \$ |

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

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GLADSTONE COMMERCIAL CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Organization and Significant Accounting Policies

Gladstone Commercial Corporation (the Company) is a Maryland corporation that operates in a manner so as to qualify as a real estate investment trust (REIT) for federal income tax purposes and was incorporated on February 14, 2003 under the General Corporation Law of Maryland for the purpose of engaging in the business of investing in real estate properties net leased to creditworthy entities and making mortgage loans to creditworthy entities. Subject to certain restrictions and limitations, the business of the Company is managed by Gladstone Management Corporation, a Delaware corporation (the Adviser).

Subsidiaries

The Company conducts substantially all of its operations through a subsidiary, Gladstone Commercial Limited Partnership, a Delaware limited partnership, (the Operating Partnership). As the Company currently owns all of the general and limited partnership interests of the Operating Partnership through GCLP Business Trust I and II as disclosed below, the financial position and results of operations of the Operating Partnership are consolidated with those of the Company.

Gladstone Commercial Partners, LLC, a Delaware limited liability company (Commercial Partners) and a subsidiary of the Company, was organized to engage in any lawful act or activity for which a limited liability company may be organized in Delaware. Commercial Partners has the power to make and perform all contracts and to engage in all activities to carry out the purposes of the Company, and all other powers available to it as a limited liability company. As the Company currently owns all of the membership interests of Commercial Partners, the financial position and results of operations of Commercial Partners are consolidated with those of the Company.

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

Gladstone Commercial Advisers, Inc., a Delaware corporation (Commercial Advisers) and a subsidiary of the Company, is a taxable REIT subsidiary (TRS), which was created to collect all non-qualifying income related to the Company's real estate portfolio. It is currently anticipated that this income will predominately consist of fees received by the Company related to the leasing of real estate. There have been no such fees earned to date. Since the Company owns 100% of the voting securities of Commercial Advisers, the financial position and results of operations of Commercial Advisers are consolidated with those of the Company.

GCLP Business Trust I and GCLP Business Trust II, subsidiaries of the Company, each are business trusts formed under the laws of the Commonwealth of Massachusetts on December 28, 2005. The Company transferred its 99% limited partnership interest in the Operating Partnership to GCLP Business Trust I in exchange for 100 trust shares. Commercial Partners transferred its 1% general partnership interest in the Operating Partnership to GCLP Business Trust II in exchange for 100 trust shares.

Investments in real estate

The Company records investments in real estate at cost and capitalizes improvements and replacements when they extend the useful life or improve the efficiency of the asset. The Company expenses costs of repairs and maintenance as incurred. The Company computes depreciation using the straight-line method over the estimated useful life of 39 years for buildings and improvements, five to seven years for equipment and fixtures and the shorter of the useful life or the remaining lease term for tenant improvements and leasehold interests.

The Company accounts for its acquisitions of real estate in accordance with Statement of Financial Accounting Standards (SFAS) No. 141, Business Combinations, which requires the purchase price of real estate to be allocated to the acquired tangible assets and liabilities, consisting of land, building, tenant improvements, long-term debt and identified intangible assets and liabilities, consisting of the value of above-market and below-market leases, the value of in-place leases, the value of unamortized lease origination costs and the value of tenant relationships, based in each case on their fair values.

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

The Company allocates purchase price to the fair value of the tangible assets of an acquired property by valuing the property as if it were vacant. The as-if-vacant value is allocated to land, building, and tenant improvements based on management's determination of the relative fair values of these assets. Real estate depreciation expense on these tangible assets, including discontinued operations, was \$7,143,215, \$5,351,412 and \$2,623,753 for the years ended December 31, 2007, 2006, and 2005 respectively.

Above-market and below-market in-place lease values for owned properties are recorded based on the present value (using an interest rate which reflects the risks associated with the leases acquired) of the difference between (i) the contractual amounts to be paid pursuant to the in-place leases and (ii) management's estimate of fair market lease rates for the corresponding in-place leases, measured over a period equal to the remaining non-cancelable term of the lease. The capitalized above-market lease values, included in the accompanying balance sheet as part of deferred rent receivable, are amortized as a reduction of rental income over the remaining non-cancelable terms of the respective leases. Total amortization related to above-market lease values was \$253,496, \$253,496 and \$178,070 for the years ended December 31, 2007, 2006, and 2005 respectively. The capitalized below-market lease values, included in the accompanying balance sheet as deferred rent liability, are amortized as an increase to rental income over the remaining non-cancelable terms of the respective leases. Total amortization related to below-market lease values was \$785,564 and \$696,261 for the years ended December 31, 2007 and 2006 respectively. There was no amortization related to below-market lease values in 2005.

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

The value of in-place leases and unamortized lease origination costs are amortized to expense over the remaining term of the respective leases, which generally range from five to twenty years. The value of customer relationship intangibles, which is the benefit to the Company resulting from the likelihood of an existing tenant renewing its lease, are amortized to expense over the remaining term and any anticipated renewal periods in the respective leases, but in no event does the amortization period for intangible assets exceed the remaining depreciable life of the building. Should a tenant terminate its lease, the unamortized portion of the above-market and below-market lease values, in-place lease values, unamortized lease origination costs and customer relationship intangibles will be charged to expense. Total amortization expense related to these intangible assets, including discontinued operations, was \$3,385,243, \$2,998,062 and \$1,027,367 for the years ended December 31, 2007, 2006, and 2005 respectively. The following table summarizes the net value of other intangible assets and the accumulated amortization for each intangible asset class:

| | December 31, 2007 | | December 31, 2006 | |
|------------------------|-------------------|--------------------------|-------------------|--------------------------|
| | Lease Intangibles | Accumulated Amortization | Lease Intangibles | Accumulated Amortization |
| In-place leases | \$ 12,660,732 | \$ (3,414,868) | \$ 10,738,319 | \$ (1,907,668) |
| Leasing costs | 9,290,026 | (2,114,233) | 5,891,099 | (1,267,829) |
| Customer relationships | 14,599,726 | (2,031,827) | 10,962,963 | (1,000,188) |
| | \$ 36,550,484 | \$ (7,560,928) | \$ 27,592,381 | \$ (4,175,685) |

The estimated aggregate amortization expense for the next five fiscal years is as follows:

| Year | Estimated Amortization Expense |
|------|--------------------------------|
| 2008 | \$ 3,442,888 |
| 2009 | 3,314,527 |
| 2010 | 3,232,433 |
| 2011 | 3,089,169 |
| 2012 | 2,736,211 |

Impairment

Investments in Real Estate

The Company accounts for the impairment of real estate in accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, which requires that the Company periodically review the carrying value of each property to determine if circumstances that indicate impairment in the carrying value of the investment exist or that depreciation periods should be modified. If circumstances support the possibility of impairment, the Company prepares a projection of the undiscounted future cash flows, without interest charges, of the specific property and determines if the investment in such property is recoverable. If impairment is indicated, the carrying value of the property would be written down to its estimated fair value based on the Company's best estimate of the property's discounted future cash flows. There have been no impairments recognized on the Company's real estate assets at December 31, 2007.

Provision for Loan Losses

The Company's accounting policies require that it reflect in its financial statements an allowance for estimated credit losses with respect to mortgage loans it has made based upon its evaluation of known and inherent risks associated with its private lending assets. Management reflects provisions for loan losses based upon its assessment of general market conditions, its internal risk management policies and credit risk rating system, industry loss experience, its assessment of the likelihood of delinquencies or defaults, and the value of the collateral underlying its investments. Actual losses, if any, could ultimately differ from these estimates. There have been no provisions for loan losses in the Company's history.

Cash and cash equivalents

The Company considers all short-term, highly liquid investments that are both readily convertible to cash and have a maturity of three months or less at the time of purchase to be cash equivalents; except that any such investments purchased with funds held in escrow or similar accounts are classified as restricted cash. Items classified as cash equivalents include commercial paper and money-market funds. All of the Company's cash and cash equivalents at December 31, 2007 were held in the custody of two financial institutions, and the Company's balance at times may exceed federally insurable limits. The Company mitigates this risk by depositing funds with major financial institutions.

Restricted cash

Restricted cash consists of security deposits and funds held in escrow for certain tenants. The funds held in escrow are for capital improvements, taxes, insurance and other replacement reserves for certain of our tenants. These funds will be released to the tenants upon completion of agreed upon tasks as specified in the lease agreements, mainly consisting of maintenance and repairs on the buildings, and when evidence of insurance and tax payments has been submitted to the Company.

Funds held in escrow

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

Deferred financing costs

Deferred financing costs consist of costs incurred to obtain long-term financing, including legal fees, origination fees, and administrative fees. The costs are deferred and amortized using the straight-line method, which approximates the effective interest method, over the term of the financing secured. The Company incurred \$1,409,320, \$3,242,881, and \$2,021,115 in deferred financing costs during the years ended December 31, 2007, 2006 and 2005, respectively. Total amortization expense related to deferred financing costs, including discontinued operations, was \$717,195, \$1,207,198 and \$260,099 for the years ended December 31, 2007, 2006, and 2005 respectively. Amortization of financing costs are included in the interest expense line item in the consolidated financial statements.

Revenue recognition

Rental revenue includes rents that each tenant pays in accordance with the terms of its respective lease reported on a straight-line basis over the non-cancelable term of the lease. Certain of the Company's leases currently contain rental increases at specified intervals, and straight-line basis accounting requires the Company to record an asset, and include in revenues, deferred rent receivable that will be received if the tenant makes all rent payments required through the expiration of the initial term of the lease. Deferred rent receivable in the accompanying balance sheet includes the cumulative difference between rental revenue as recorded on a straight line basis and rents received from the tenants in accordance with the lease terms, along with the capitalized above-market lease values of certain acquired properties.

Accordingly, the Company determines, in its judgment, to what extent the deferred rent receivable applicable to each specific tenant is collectible. The Company reviews deferred rent receivable, as it relates to straight line rents, on a quarterly basis and takes into consideration the tenant's payment history, the financial condition of the tenant, business conditions in the industry in which the tenant operates and economic conditions in the area in which the property is located. In the event that the collectibility of deferred rent with respect to any given tenant is in doubt, the Company records an increase in the allowance for uncollectible accounts or records a direct write-off of the specific rent receivable, which would have an adverse effect on the net income for the year in which the reserve is increased or the direct write-off is recorded and would decrease total assets and stockholders' equity. No such reserves have been recorded as of December 31, 2007.

Management considers its loans and other lending investments to be held-for-investment. The Company reflects held-for-investment investments at amortized cost less allowance for loan losses, acquisition premiums or discounts, and deferred loan fees. On occasion, the Company may acquire loans at small premiums or discounts based on the credit characteristics of such loans. These premiums or discounts are recognized as yield adjustments over the lives of the related loans. Loan origination or exit fees, as well as direct loan origination costs, are also deferred and recognized over the lives of the related loans as yield adjustments. If loans with premiums, discounts, loan origination or exit fees are prepaid, the Company immediately recognizes the unamortized portion as a decrease or increase in the prepayment gain or loss. Interest income is recognized using the effective interest method applied on a loan-by-loan basis. Prepayment penalties or yield maintenance payments from borrowers are recognized as additional income when received.

Certain of our mortgage loans and leases have embedded derivatives in the form of interest rate floors and ceilings. These embedded derivatives do not require separate accounting under SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities.

Income taxes

The Company has operated and intends to continue to operate in a manner that will allow it to qualify as a REIT under the Internal Revenue Code of 1986, as amended, and accordingly will not be subject to federal income taxes on amounts distributed to stockholders (except income from foreclosure property), provided it distributes at least 90% of its REIT taxable income to its stockholders and meets certain other conditions. To the extent that the Company satisfies the distribution requirement but distributes less than 100% of its taxable income, the Company will be subject to federal corporate income tax on its undistributed income.

Commercial Advisers is a wholly-owned TRS that is subject to federal and state income taxes. Though Commercial Advisers has had no activity to date, the Company would account for any future income taxes in accordance with the provisions of SFAS No. 109, Accounting for Income Taxes. Under SFAS No. 109, the Company accounts for income taxes using the asset and liability method under which deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases.

In July of 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109 (FIN 48). FIN 48 provides guidance for the financial statement recognition and measurement of a tax position taken or expected to be taken on a tax return, and provides guidance on recognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition of tax positions. This Interpretation is effective for fiscal years beginning after December 15, 2006. The Company adopted FIN 48 effective for the fiscal year beginning January 1, 2007, and the adoption had no impact on the Company's results of operations.

Segment information

SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information provides standards for public companies relating to the reporting of financial and descriptive information about their operating segments in financial statements. Operating segments are defined as components of an enterprise for which separate financial information is available and is evaluated regularly by the chief operating decision maker or decision making group in determining how to allocate resources and in assessing performance. Company management is the chief decision making group. As discussed in Note 10, the Company's operations are derived from two operating segments, one segment purchases real estate (land, buildings and other improvements), which is simultaneously leased to existing users, and the other segment originates mortgage loans and collects principal and interest payments.

Foreign Currency Transactions

The Company purchased two properties in Canada in October of 2004. These properties were classified as held for sale as of June 30, 2006, and were sold in July 2006. All gains and losses from foreign currency transactions are reflected in discontinued operations in the Company's consolidated financial statements. Rental payments from these properties were received in Canadian dollars. In accordance with SFAS No. 52, Foreign Currency Translation, the rental revenue received was recorded using the exchange rate as of the transaction date, which was the first day of each month. In addition to rental payments that were denominated in Canadian dollars, the Company also had a bank account in Canada and the long-term financings on the two Canadian properties were also issued in Canadian dollars. All cash, deferred rent assets and mortgage notes payable related to the Canadian properties were re-valued at each balance sheet date to reflect the then current exchange rate. The gains or losses from the valuation of the cash were recorded on the income statement as a realized gain or loss, and the valuation of the deferred rent assets and mortgage notes payable was recorded on the income statement as unrealized gains or losses on the translation of assets and liabilities. A realized foreign currency gain of \$33,359 was recorded for the year ended December 31, 2007. Realized foreign currency losses of \$202,938 and \$6,278 were recorded for the years ended December 31, 2006, and 2005, respectively. A realized gain of \$1,422,026 related to the sale of the Canadian properties was recognized for the year ended December 31, 2006. An unrealized foreign currency loss of \$212,279 was recorded for the year ended December 31, 2005. There were no unrealized foreign currency losses during the years ended December 31, 2007 and 2006, respectively. These realized gains and losses were from the valuation of cash, tax payments made to the Canadian government, and the previously unrealized foreign currency losses associated with the valuation of the deferred rent assets and mortgage notes payable that became realized foreign currency losses as of the date of sale.

Asset retirement obligations

In March of 2005, the FASB issued Interpretation No. 47, Accounting for Conditional Asset Retirement Obligations (FIN 47). FIN 47 requires an entity to recognize a liability for a conditional asset retirement obligation when incurred if the liability can be reasonably estimated. FIN 47 clarifies that the term Conditional Asset Retirement Obligation refers to a legal obligation (pursuant to existing laws or by contract) to perform an asset retirement activity in which the timing and/or method of settlement are conditional on a future event that may or may not be within the control of the entity. FIN 47 also clarifies when an entity would have sufficient information to reasonably estimate the fair value of an asset retirement obligation. The Company has accrued a liability and corresponding increase to the cost of the related properties for disposal related to all properties constructed prior to 1985 that have, or may have, asbestos present in the building. The Company accrued a liability during the year ended December 31, 2007 of \$63,980 related to properties acquired during the period. The Company also recorded expense of \$116,478 and \$139,074, during the years ended December 31, 2007 and 2006 respectively, including discontinued operations, related to the cumulative accretion of the obligation. The Company adopted FIN 47 as of December 31, 2005, but did not record the liability and the related cumulative effect as of December 31, 2005 because the Company deemed the impact of its initial estimates immaterial and worked to further refine these estimates.

Real estate held for sale and discontinued operations

SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, requires that the results of operations of any properties which have been sold, or are held for sale, be presented as discontinued operations in the Company's consolidated financial statements in both current and prior periods presented. Income items related to held for sale properties are listed separately on the Company's consolidated income statement. Real estate assets held for sale are measured at the lower of the carrying amount or the fair value, less the cost to sell, and are listed separately on the Company's consolidated balance sheet for the current period. Once properties are listed as held for sale, no further depreciation is recorded.

Recently Issued Accounting Pronouncements

In September 2006, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin No. 108 (SAB 108). SAB 108 addresses how the effects of prior year uncorrected misstatements should be considered when quantifying misstatements in current year financial statements and requires registrants to consider the effect of all carry over and reversing effects of prior year misstatements when quantifying errors in current year financial statements. SAB 108 does not change the SEC's previous guidance in SAB No. 99, Materiality, on evaluating the materiality of misstatements. A registrant applying the new guidance for the first time that identifies material errors in existence at the beginning of the first fiscal year ending after November 15, 2006, may correct those errors through a one-time cumulative effect adjustment to beginning-of-year retained earnings. The cumulative effect alternative is available only if the application of the new guidance results in a conclusion that a material error exists as of the beginning of the first fiscal year ending after November 15, 2006, and those misstatements were determined to be immaterial based on a proper application of the registrant's previous method for quantifying misstatements. The Company adopted SAB 108 effective for the fiscal year beginning January 1, 2007, and the adoption had no impact on the Company's results of operations.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value in GAAP and expands disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is required to adopt the provisions of SFAS 157 beginning with the fiscal year beginning January 1, 2008. The Company believes there will be no impact of the adoption on its results of operations.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS 159). SFAS 159 allows entities to measure at fair value many financial instruments and certain other assets and liabilities that are not otherwise required to be measured at fair value. SFAS 159 is effective for fiscal years beginning after November 15, 2007. The Company adopted SFAS 159 effective for the fiscal year beginning January 1, 2007, and the adoption had no impact on the Company's results of operations. The Company believes there will be no impact of the adoption on its results of operations.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), Business Combinations, SFAS No. 141(R), which replaces SFAS No. 141, Business Combinations (SFAS 141R). SFAS 141R significantly changes the accounting for acquisitions involving business combinations, as it requires that the assets and liabilities of all business combinations be recorded at fair value, with limited exceptions. SFAS 141R also requires that all expenses related to the acquisition be expensed as incurred, rather than capitalized into the cost of the acquisition as had been the previous accounting under SFAS 141. SFAS 141R is effective on a prospective basis for all business combinations for which the acquisition date is on or after the beginning of the first annual period subsequent to December 15, 2008.

Use of estimates

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

Reclassifications

Certain amounts from prior years' financial statements have been reclassified to conform to the current year presentation. These reclassifications had no effect on previously reported net income or stockholders' equity.

2. Management Advisory Fee

The Company has been externally managed pursuant to a contractual investment advisory arrangement with its Adviser, under which its Adviser has directly employed all of the Company's personnel and paid its payroll, benefits, and general expenses directly. The Company's initial investment advisory agreement with its Adviser was in place from August 12, 2003 through December 31, 2006 (the "Initial Advisory Agreement"). On January 1, 2007, the Company entered into an amended and restated investment advisory agreement with its Adviser (the "Amended Advisory Agreement") and an administration agreement (the "Administration Agreement") with Gladstone Administration, LLC (the "Administrator"). The management services and fees in effect under the Initial Advisory, Amended Advisory and Administration Agreements are described below.

Initial Advisory Agreement

Under the Initial Advisory Agreement, the Company was required to reimburse its Adviser for its pro rata share of its Adviser's payroll and benefits expenses on an employee-by-employee basis, based on the percentage of each employee's time devoted to the Company's matters. During the years ended December 31, 2006 and 2005, these expenses were approximately \$2,266,000 and \$1,547,000, respectively.

The Company was also required to reimburse its Adviser for its pro rata portion of all other expenses of its Adviser not reimbursed under the Initial Advisory Agreement (overhead expenses), equal to the total overhead expenses of its Adviser, multiplied by the ratio of hours worked by its Adviser's employees on the Company's projects to the total hours worked by its Adviser's employees. However, the Company was only required to reimburse its Adviser for its portion of its overhead expenses if the amount of payroll and benefits the Company reimbursed to its Adviser was less than 2.0% of the Company's average invested assets for the year. Additionally, the Company was only required to reimburse its Adviser for overhead expenses up to the point that reimbursed overhead expenses and payroll and benefits expenses, on a combined basis, equaled 2.0% of the Company's average invested assets for the year. The Adviser billed the Company on a monthly basis for these amounts. The Adviser was required to reimburse the Company annually for the amount by which overhead expenses billed to and paid by the Company exceeded this combined 2.0% limit during a given year. The overhead expenses never exceeded the combined 2.0% limit and, consequently, the Company never received any reimbursement. During the years ended December 31, 2006 and 2005, the Company reimbursed its Adviser approximately \$636,000 and \$571,000, respectively, of overhead expenses.

Amended Advisory Agreement

The Amended Advisory Agreement provides for an annual base management fee equal to 2% of the Company's total stockholders' equity, less the recorded value of any preferred stock, and an incentive fee based on funds from operations (FFO). For the year ended December 31, 2007, the Company recorded a base management fee of \$1,858,120. For purposes of calculating the incentive fee, FFO includes any realized capital gains and capital losses, less any dividends paid on preferred stock, but FFO does not include any unrealized capital gains or losses. The incentive fee will reward the Adviser if the Company's quarterly FFO, before giving effect to any incentive fee (pre-incentive fee FFO), exceeds 1.75%, or 7% annualized, (the "hurdle rate") of total stockholders' equity, less the recorded value of any preferred stock. The Adviser will receive 100% of the amount of the pre-incentive fee FFO that exceeds the hurdle rate, but is less than 2.1875% of the Company's pre-incentive fee FFO. The Adviser will also receive an incentive fee of 20% of the amount of the Company's pre-incentive fee FFO that exceeds 2.1875%.

For the year ended December 31, 2007, the Company recorded an incentive fee of \$2,564,365 offset by a credit from an unconditional and irrevocable voluntary waiver issued by the Adviser of \$2,321,597, for a net incentive fee for the year ended December 31, 2007 of \$242,768. The board of directors of the Company accepted the Adviser's offer to waive a portion of the incentive fee for the year ended December 31, 2007 in order to maintain the current level of distributions to the Company's stockholders.

Administration Agreement

Under the Administration Agreement, the Company pays separately for its allocable portion of the Administrator's overhead expenses in performing its obligations including, but not limited to, rent for employees of the Administrator, and its allocable portion of the salaries and benefits expenses of its chief financial officer, chief compliance officer, controller, treasurer and their respective staffs. The amount of overhead expenses allocated to the Company is determined by calculating the percentage of total assets of the Company to the total assets managed by the Administrator. For the year ended December 31, 2007, the Company recorded an administration fee of \$837,898.

3. Stock Options

In December of 2004, FASB issued SFAS No. 123(R), *Share-Based Payment*. The new standard was effective for awards that are granted, modified, or settled in cash for annual periods beginning after June 15, 2005. The Company previously accounted for its stock option plans under the recognition and measurement principles of APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations and disclosure requirements established by SFAS No. 123, *Accounting for Stock-Based Compensation*. In this regard, the options under the plan had been granted to individuals who are the Company's officers, and who would qualify as leased employees under FASB Interpretation No. 44 (FIN 44), *Accounting for Certain Transactions Involving Stock Compensation*, an Interpretation of APB Opinion No. 25. Under APB Opinion No. 25, no expense was recorded in the income statement for the Company's stock options. The pro forma effects on income for stock options were instead disclosed in a footnote to the financial statements. Under SFAS No. 123(R), all share-based compensation cost was measured at the grant date, based on the fair value of the award, and was recognized as an expense in the income statement over an employee's requisite service period.

The Company adopted SFAS No. 123(R) on January 1, 2006 using the modified prospective approach. Under the modified prospective approach, stock-based compensation expense was recorded for the unvested portion of previously issued awards that remained outstanding at January 1, 2006 using the same estimate of the grant date fair value and the same attribution method used to determine the pro forma disclosure under SFAS No. 123. SFAS No. 123(R) also requires that all share-based payments to employees after January 1, 2006, including employee stock options, be recognized in the financial statements as stock-based compensation expense based on the fair value on the date of grant. The Company recorded total stock option compensation expense of \$394,411 for the year ended December 31, 2006. As the Company terminated its stock option plan on December 31, 2006 there were no stock options outstanding, and therefore, no stock option compensation expense was recorded for the year ended December 31, 2007.

The following table illustrates the effect on net income and earnings per share as if the Company had applied the fair-value recognition provisions of SFAS No. 123(R) to stock options, stock appreciation rights, performance units and restricted stock units for periods prior to adoption of SFAS No. 123(R).

| | For the year ended December 31, 2005 |
|---|--|
| Net income, as reported | \$ 3,601,945 |
| Less: Stock-based compensation expense determined using the fair value based method | (187,483) |
| Net income, pro-forma | \$ 3,414,462 |
| Basic, as reported | \$ 0.47 |
| Basic, pro-forma | \$ 0.45 |
| Diluted, as reported | \$ 0.47 |
| Diluted, pro-forma | \$ 0.44 |

The stock-based compensation expense under the fair value method, as reported in the above table, was computed using an estimated weighted average fair value of \$1.26 using the Black-Scholes option-pricing model, based on options issued from date of inception forward, and the following weighted-average assumptions: dividend yield of 5.07%, risk-free interest rate of 2.61%, expected volatility factor of 18.15%, and expected lives of 3 years.

A summary of the status of the Company's 2003 Equity Incentive Plan from February 14, 2003 (inception) through December 31, 2006 (termination) is as follows:

| | Shares | Weighted Average Exercise Price |
|--|----------|---------------------------------------|
| Options outstanding at February 14, 2003 | | |
| Granted | 629,000 | \$ 15.00 |
| Exercised | | |
| Options outstanding at December 31, 2003, of which 629,000 shares were exercisable | 629,000 | \$ 15.00 |
| Granted | 280,000 | \$ 16.22 |
| Exercised | (25,000) | \$ 15.00 |
| Forfeited | (15,000) | \$ 15.73 |
| Options outstanding at December 31, 2004, of which 599,000 shares were exercisable | 869,000 | \$ 15.39 |
| Granted | 64,500 | \$ 15.47 |
| Exercised | (5,000) | \$ 15.00 |
| Forfeited | (12,500) | \$ 15.48 |

| | | |
|--|-----------|----------|
| Options outstanding at December 31, 2005, of which 744,250 shares were exercisable | 916,000 | \$ 15.39 |
| Granted | | \$ |
| Exercised | (916,000) | \$ 15.40 |
| Forfeited | | \$ |
| Options outstanding and exercisable at December 31, 2006 | | \$ |

The following table is a summary of all outstanding notes issued to employees of the Adviser for the exercise of stock options:

| Date Issued | Number of Options Exercised | Strike Price of Options Exercised | Amount of Promissory Note Issued to Employees | Outstanding | Term of Note | Interest Rate on Note |
|-------------|-----------------------------|-----------------------------------|---|---------------------------------------|--------------|-----------------------|
| | | | | Balance of Employee Loans at 12/31/07 | | |
| Sep-04 | 25,000 | \$ 15.00 | \$ 375,000 | \$ 368,161 | 9 years | 5.00% |
| May-05 | 5,000 | 15.00 | 75,000 | 57,796 | 9 years | 6.00% |
| Apr-06 | 12,422 | 16.10 | 199,994 | 199,994 | 9 years | 7.77% |
| May-06 | 50,000 | 16.85 | 842,500 | 842,500 | 10 years | 7.87% |
| May-06 | 15,000 | 16.10 | 241,500 | 241,500 | 10 years | 7.87% |
| May-06 | 2,500 | 16.01 | 40,000 | 39,012 | 10 years | 7.87% |
| May-06 | 2,000 | 16.10 | 32,200 | 32,200 | 10 years | 7.87% |
| May-06 | 2,000 | 16.10 | 32,200 | 32,200 | 10 years | 7.87% |
| May-06 | 2,000 | 16.68 | 33,360 | 33,360 | 10 years | 7.87% |
| May-06 | 2,000 | 15.00 | 30,000 | 30,000 | 10 years | 7.87% |
| Oct-06 | 12,000 | 16.10 | 193,200 | 193,200 | 9 years | 8.17% |
| Nov-06 | 25,000 | 15.00 | 375,000 | 325,000 | 9 years | 8.15% |
| Dec-06 | 25,000 | 15.00 | 375,000 | 375,000 | 10 years | 8.12% |
| | 204,922 | | \$ 3,219,954 | \$ 2,769,923 | | |

In accordance with Emerging Issues Task Force No. 85-1, Classifying Notes Received for Sale of Stock, receivables from employees for the issuance of capital stock to employees prior to the receipt of cash payment should be reflected in the balance sheet as a reduction to stockholders' equity. Therefore, these notes were recorded as loans to employees and are included in the equity section of the accompanying consolidated balance sheets.

4. Earnings per Common Share

The following tables set forth the computation of basic and diluted earnings per share for the years ended December 31, 2007, 2006 and 2005:

| | For the year ended December 31, | | |
|---|---------------------------------|--------------|--------------|
| | 2007 | 2006 | 2005 |
| Net income available to common stockholders | \$ 2,046,479 | \$ 2,185,938 | \$ 3,601,945 |
| Denominator for basic weighted average shares | 8,565,264 | 7,827,781 | 7,670,219 |
| Dilutive effect of stock options | | 158,909 | 53,001 |
| Denominator for diluted weighted average shares | 8,565,264 | 7,986,690 | 7,723,220 |
| Basic earnings per common share | \$ 0.24 | \$ 0.28 | \$ 0.47 |
| Diluted earnings per common share | \$ 0.24 | \$ 0.27 | \$ 0.47 |

5. Real Estate

A summary of the 53 properties held by the Company as of December 31, 2007 is as follows:

| Date Acquired | Location | (unaudited) Square Footage | Property Description | Net Real Estate |
|---------------|----------------------------------|----------------------------------|------------------------------|--------------------|
| Dec-03 | Raleigh, North Carolina | 58,926 | Office | \$ 4,628,337 |
| Jan-04 | Canton, Ohio | 54,018 | Office and Warehouse | 2,923,963 |
| Apr-04 | Akron, Ohio | 83,891 | Office and Laboratory | 8,106,036 |
| Jun-04 | Charlotte, North Carolina | 64,500 | Office | 8,451,345 |
| Jul-04 | Canton, North Carolina | 228,000 | Commercial and Manufacturing | 4,749,579 |
| Aug-04 | Snyder Township, Pennsylvania | 290,000 | Commercial and Warehouse | 6,102,338 |
| Aug-04 | Lexington, North Carolina | 154,000 | Commercial and Warehouse | 2,778,380 |
| Sep-04 | Austin, Texas | 51,933 | Flexible Office | 6,803,840 |
| Oct-04 | Norfolk, Virginia | 25,797 | Commercial and Manufacturing | 885,442 |
| Oct-04 | Mt. Pocono, Pennsylvania | 223,275 | Commercial and Manufacturing | 5,699,851 |
| Feb-05 | San Antonio, Texas | 60,245 | Flexible Office | 7,638,439 |
| Feb-05 | Columbus, Ohio | 39,000 | Industrial | 2,615,717 |
| Apr-05 | Big Flats, New York | 120,000 | Industrial | 6,310,146 |
| May-05 | Wichita, Kansas | 69,287 | Office | 10,577,368 |
| May-05 | Arlington, Texas | 64,000 | Warehouse and Bakery | 3,857,133 |
| Jun-05 | Dayton, Ohio | 59,894 | Office | 2,339,980 |
| Jul-05 | Eatontown, New Jersey | 30,268 | Office | 4,606,747 |
| Jul-05 | Franklin Township, New Jersey | 183,000 | Office and Warehouse | 7,439,940 |
| Jul-05 | Duncan, South Carolina | 278,020 | Office and Manufacturing | 15,415,164 |
| Aug-05 | Hazelwood, Missouri | 51,155 | Office and Warehouse | 2,950,754 |
| Sep-05 | Angola, Indiana | 52,080 | Industrial | 1,116,968 |
| Sep-05 | Angola, Indiana | 50,000 | Industrial | 1,116,968 |
| Sep-05 | Rock Falls, Illinois | 52,000 | Industrial | 1,116,969 |
| Oct-05 | Newburyport, Massachusetts | 70,598 | Industrial | 6,798,268 |
| Oct-05 | Clintonville, Wisconsin | 291,142 | Industrial | 4,502,040 |
| Dec-05 | Maple Heights, Ohio | 347,218 | Industrial | 11,099,726 |
| Dec-05 | Richmond, Virginia | 42,213 | Office | 5,809,099 |
| Dec-05 | Toledo, Ohio | 23,368 | Office | 2,939,026 |
| Feb-06 | South Hadley, Massachusetts | 150,000 | Industrial | 3,113,051 |
| Feb-06 | Champaign, Illinois | 108,262 | Office | 13,878,032 |
| Feb-06 | Roseville, Minnesota | 359,540 | Office | 26,408,409 |
| May-06 | Burnsville, Minnesota | 114,100 | Office | 11,768,380 |
| Jun-06 | Menomonee Falls, Wisconsin | 125,692 | Industrial | 7,265,105 |
| Jul-06 | Baytown, Texas | 12,000 | Office | 2,558,544 |
| Sep-06 | Sterling Heights, Michigan | 532,869 | Industrial | 11,072,192 |

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| | | | | |
|--------|-----------------------------|-----------|---------------|----------------|
| Sep-06 | Birmingham, Alabama | 63,514 | Industrial | 1,527,220 |
| Sep-06 | Montgomery, Alabama | 29,472 | Industrial | 1,527,220 |
| Sep-06 | Columbia, Missouri | 16,275 | Industrial | 1,527,220 |
| Jan-07 | Mason, Ohio | 60,000 | Office | 6,856,787 |
| Feb-07 | Raleigh, North Carolina | 115,500 | Industrial | 6,993,551 |
| Mar-07 | Tulsa, Oklahoma | 238,310 | Manufacturing | 13,706,553 |
| Mar-07 | Hialeah, Florida | 132,337 | Industrial | 10,094,438 |
| May-07 | Tewksbury, Massachusetts | 102,200 | Industrial | 10,134,413 |
| Jul-07 | Mason, Ohio | 21,264 | Retail | 6,101,665 |
| Sep-07 | Cicero, New York | 71,880 | Industrial | 5,276,588 |
| Sep-07 | Grand Rapids, Michigan | 63,235 | Office | 12,052,923 |
| Sep-07 | Bolingbrook, Illinois | 55,869 | Industrial | 6,238,674 |
| Dec-07 | Decatur, Georgia | 26,600 | Office | 2,880,207 |
| Dec-07 | Lawrenceville, Georgia | 12,412 | Office | 2,880,207 |
| Dec-07 | Snellville, Georgia | 3,800 | Office | 2,880,207 |
| Dec-07 | Covington, Georgia | 5,000 | Office | 2,880,207 |
| Dec-07 | Cumming, Georgia | 13,919 | Office | 2,880,208 |
| Dec-07 | Conyers, Georgia | 6,400 | Office | 2,880,208 |
| | Total real estate, net | 5,558,278 | | \$ 324,761,772 |

The following table sets forth the components of the Company's investments in real estate:

| | December 31, 2007 | December 31, 2006 |
|--------------------------|----------------------|----------------------|
| Real estate: | | |
| Land | \$ 48,867,482 | \$ 33,764,113 |
| Building | 283,829,987 | 204,115,481 |
| Tenant improvements | 7,802,937 | 5,833,948 |
| Accumulated depreciation | (15,738,634) | (8,595,419) |
| Real estate, net | \$ 324,761,772 | \$ 235,118,123 |

On January 5, 2007, the Company acquired a 60,000 square foot office building in Mason, Ohio for approximately \$7.88 million, including transaction costs. At closing, the Company was assigned the previously existing triple net lease with the sole tenant, which had a remaining term of approximately six years. The tenant has two options to extend the lease for additional periods of five years each. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$0.68 million.

On February 16, 2007, the Company acquired an 115,500 square foot industrial building in Raleigh, North Carolina for approximately \$7.80 million, including transaction costs. At closing, the Company was assigned the previously existing triple net lease with the sole tenant, which had a remaining term of approximately three years. The tenant has one option to extend the lease for an additional period of five years. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$0.66 million.

On March 1, 2007, the Company acquired the leasehold interest in a 238,310 square foot office building in Tulsa, Oklahoma for \$15.81 million, including transaction costs. Under the terms of the leasehold interest, the Company has a ground lease on which the property is located that has a remaining term, including renewal options, of approximately 34.5 years. The annual amount of ground lease payments, reimbursable to us by the tenant, is approximately \$134,000. Upon acquisition of the leasehold interest in the building, the Company was assigned the previously existing triple net lease with the sole tenant, which had a remaining term of approximately 12.5 years at the time of assignment. The tenant also has two options to extend the lease for additional periods of five years each. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$1.57 million.

On March 9, 2007, the Company acquired a 132,337 square foot industrial building in Hialeah, Florida for approximately \$10.29 million, including transaction costs. At closing, the Company extended a 15 year triple net lease with the sole tenant, and the tenant has five options to extend the lease for additional periods of five years each. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$1.0 million.

On May 17, 2007, the Company acquired a 102,200 square foot industrial building in Tewksbury, Massachusetts for approximately \$11.25 million, including transaction costs. At closing, the Company extended a 10 year triple net lease with the sole tenant, and the tenant has three options to extend the lease for additional periods of five years each. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$0.92 million.

On July 13, 2007, the Company acquired a 21,264 square foot retail building in Mason, Ohio for approximately \$6.77 million, including transaction costs. At closing, the Company was assigned the previously existing triple net lease with the sole tenant, which had a remaining term of approximately 20 years. The tenant has five options to extend the lease for additional periods of five years each. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$0.58 million.

On September 6, 2007, the Company acquired a 71,880 square foot office building in Cicero, New York for approximately \$5.81 million, including transaction costs, which was funded by a combination of cash on hand, and the assumption of approximately \$4.5 million of financing on the property. The financing was recorded at fair value at the time of acquisition. At closing, the Company was assigned the previously existing triple net lease with the sole tenant, which had a remaining term of approximately 13 years. The tenant has two options to extend the lease for additional periods of five years each. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$0.53 million.

On September 28, 2007, the Company acquired a 63,235 square foot office building in Grand Rapids, Michigan for approximately \$12.38 million, including transaction costs. At closing, the Company was assigned the previously existing triple net lease with the sole tenant, which had a remaining term of approximately nine years. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$1.03 million.

On September 28, 2007, the Company acquired a 55,869 square foot industrial building in Bolingbrook, Illinois for approximately \$6.71 million, including transaction costs. At closing, the Company was assigned the previously existing triple net lease with the sole tenant, which had a remaining term of approximately seven years. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$0.62 million.

On December 13, 2007, the Company acquired six separate medical office properties from a single seller: a 26,600 square foot building located in Decatur, Georgia; a 12,412 square foot building located in Lawrenceville, Georgia; a 3,800 square foot building located in Snellville, Georgia; a 5,000 square foot building located in Covington, Georgia; a 13,919 square foot building located in Cumming, Georgia; and a 6,400 square foot building located in Conyers, Georgia. These six properties were acquired for an aggregate cost to the Company of approximately \$19.52 million, including transaction costs, and the purchase was funded using borrowings from the Company's line of credit. At closing, the Company was assigned the previously existing triple net lease with the sole tenant, which had a remaining term of approximately 19 years, with four options to extend the lease for additional periods of five years each. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$1.74 million.

In accordance with SFAS No. 141, Business Combinations, the Company allocated the purchase price of the properties acquired during the year ended December 31, 2007 as follows:

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| | | | Tenant | | Customer | | Total |
|--------------------------|---------------|---------------|--------------|--------------|--------------|---------------|----------------|
| | Land | Building | Improvements | In-place | Leasing | relationships | Purchase |
| | | | | leases | Costs | | Price |
| Mason, Ohio | \$ 797,274 | \$ 5,962,067 | \$ 296,277 | \$ | \$ 144,703 | \$ 683,471 | \$ 7,883,792 |
| Raleigh, North Carolina | 1,605,551 | 5,464,586 | 48,767 | 142,209 | 64,110 | 478,083 | 7,803,306 |
| Tulsa, Oklahoma | | 13,858,489 | 198,738 | 437,117 | 587,605 | 723,168 | 15,805,117 |
| Hialeah, Florida | 3,562,455 | 6,619,258 | | | 817 | 104,508 | 10,287,038 |
| Tewksbury, Massachusetts | 1,394,902 | 8,637,010 | 256,233 | 421,446 | 865 | 535,416 | 11,245,872 |
| Mason, Ohio | 1,201,338 | 4,854,457 | 106,439 | | 416,142 | 189,699 | 6,768,075 |
| Cicero, New York | 299,066 | 5,018,628 | | 151,734 | 226,998 | 114,505 | 5,810,931 |
| Grand Rapids, Michigan | 1,629,270 | 10,196,137 | 303,929 | | 246,042 | | 12,375,378 |
| Bolingbrook, Illinois | 1,271,543 | 4,926,314 | 76,157 | 287,488 | 146,364 | | 6,707,866 |
| Decatur, Georgia | 1,300,963 | 4,836,034 | 250,341 | 190,506 | 357,834 | 287,054 | 7,222,732 |
| Lawrenceville, Georgia | 521,243 | 2,817,869 | 134,276 | 100,375 | 188,625 | 172,103 | 3,934,491 |
| Snellville, Georgia | 449,406 | 429,012 | 37,570 | 21,750 | 43,097 | 39,955 | 1,020,790 |
| Covington, Georgia | 199,451 | 944,807 | 49,863 | 31,460 | 60,858 | 57,743 | 1,344,182 |
| Cumming, Georgia | 670,284 | 2,984,821 | 146,609 | 97,781 | 202,017 | 177,026 | 4,278,538 |
| Conyers, Georgia | 226,526 | 1,237,558 | 63,790 | 40,547 | 78,203 | 74,029 | 1,720,653 |
| | \$ 15,129,272 | \$ 78,787,047 | \$ 1,968,989 | \$ 1,922,413 | \$ 2,764,280 | \$ 3,636,760 | \$ 104,208,761 |

The weighted average amortization period, for properties acquired during the year ended December 31, 2007, for in-place leases was approximately 13.1 years, for leasing costs was approximately 13.6 years, for customer relationships was approximately 25.9 years, and for all intangible assets was approximately 18.2 years. There were no above or below market lease intangibles allocated to the purchase price for the 10 acquisitions in 2007.

Future operating lease payments under non-cancelable leases, excluding customer reimbursement of expenses, in effect at December 31, 2007, were as follows:

| Year | Lease Payments |
|------------|----------------|
| 2008 | \$ 33,349,411 |
| 2009 | 32,781,897 |
| 2010 | 32,455,803 |
| 2011 | 31,969,623 |
| 2012 | 31,208,006 |
| Thereafter | 150,643,238 |

In accordance with the lease terms, substantially all tenant expenses are required to be paid by the tenant, however, the Company would be required to pay property taxes on the respective properties, and ground lease payments on the property located in Tulsa, Oklahoma, in the event the tenant fails to pay them. The total annualized property taxes for all properties outstanding as of December 31, 2007, was approximately \$5.1 million, and the total annual ground lease payments on the Tulsa, Oklahoma property were approximately \$134,000.

6. Discontinued Operations

On July 21, 2006, the Company sold its two Canadian properties for approximately \$6.9 million, for a gain on the sale of approximately \$1.4 million. The Company paid and expensed approximately \$315,000 in taxes related to the gain on the sale in 2006. The 2006 tax returns were subsequently filed in March of 2007, and the amount owed was approximately \$236,000. The Company received a refund in the amount of approximately \$79,000, which is reflected on the income statement in discontinued operations under taxes on sale of real estate. The operating expense during the year ended December 31, 2007 is legal fees related to the Canadian entities which are currently in the process of dissolution partially offset by interest income earned on letters of credit posted with the taxing agencies as part of the sale.

The Company classified its two Canadian properties as discontinued operations, in accordance with the provisions of SFAS 144. The table below summarizes the components of income from discontinued operations:

| | For the year ended December 31, | | |
|--|---------------------------------|--------------|------------|
| | 2007 | 2006 | 2005 |
| Operating revenue | \$ | \$ 342,629 | \$ 583,830 |
| Operating expense | (3,312) | (22,732) | (23,537) |
| Taxes & licenses | 78,667 | (11,736) | (6,448) |
| Interest expense | | (143,716) | (114,309) |
| Depreciation expense | | (52,300) | (129,991) |
| Gain on sale of real estate | | 1,106,590 | |
| Realized and unrealized gain (loss) on foreign currency transactions | 33,359 | (202,938) | (218,557) |
| Income from discontinued operations | \$ 108,714 | \$ 1,015,797 | \$ 90,988 |

7. Mortgage Note Receivable

On April 15, 2005, the Company originated a mortgage loan in the amount of \$10.0 million collateralized by an office building in McLean, Virginia, where the Company's Adviser and Administrator are subtenants in the building. The loan was funded using a portion of the net proceeds from the Company's initial public offering. This 12 year mortgage loan accrues interest at the greater of 7.5% per year or the one month London Interbank Offered Rate (LIBOR) rate plus 6.0% per year, with a ceiling of 10.0%. The interest rate as of December 31, 2007 was capped at 10.0%. The mortgage loan is interest only for the first nine years of the term, with payments of principal commencing after the initial period. The balance of the principal and all interest remaining is due at the end of the 12 year term.

8. Mortgage Notes Payable

As of December 31, 2007 the Company had 14 fixed-rate mortgage notes payable collateralized by a total of 33 properties. Each of these notes is in a separate borrowing entity which holds the real estate collateral. The Company is not a co-borrower but has limited recourse liabilities that could result from: a borrower voluntarily filing for bankruptcy, improper conveyance of a property, fraud or material misrepresentation, misapplication or misappropriation of rents, security deposits, insurance proceeds or condemnation proceeds, and physical waste or damage to the property resulting from a borrower's gross negligence or willful misconduct. The Company also indemnifies lenders against claims resulting from the presence of hazardous substances or activity involving hazardous substances in violation of environmental laws on a property. The weighted-average interest rate on the mortgage notes payable as of December 31, 2007 was approximately 5.8%. A summary of the mortgage notes payable is below:

| Date of Issuance of Note | Principal Maturity Date | Interest Rate | Principal Balance Outstanding | |
|-----------------------------|----------------------------|---------------|-------------------------------|-------------------|
| | | | December 31, 2007 | December 31, 2006 |
| 3/16/2005 | 4/1/2030 | 6.33% | \$ 3,003,582 | \$ 3,060,093 |
| 8/25/2005 | 9/1/2015 | 5.33% | 21,664,476 | 21,757,000 |
| 9/12/2005 | 9/1/2015 | 5.21% | 12,588,000 | 12,588,000 |
| 12/21/2005 | 12/8/2015 | 5.71% | 19,456,000 | 19,456,000 |
| 2/21/2006 | 12/1/2013 | 5.91% | 9,480,063 | 9,620,050 |
| 2/21/2006 | 6/30/2014 | 5.20% | 19,782,270 | 20,104,716 |
| 3/29/2006 | 4/1/2016 | 5.92% | 17,000,000 | 17,000,000 |
| 4/27/2006 | 5/5/2016 | 6.58% | 14,514,214 | 14,753,579 |
| 11/22/2006 | 12/1/2016 | 5.76% | 14,309,000 | 14,309,000 |
| 12/22/2006 | 1/1/2017 | 5.79% | 21,846,000 | 21,846,000 |
| 2/8/2007 | 3/1/2017 | 6.00% | 13,775,000 | |
| 6/5/2007 | 6/8/2017 | 6.11% | 14,240,000 | |
| 9/6/2007 | 12/11/2015 | 5.81% | 4,487,205 | |
| 10/15/2007 | 11/8/2017 | 6.63% | 15,974,661 | |
| | | | \$ 202,120,471 | \$ 154,494,438 |

The fair market value of all fixed-rate debt outstanding as of December 31, 2007 was approximately \$192.6 million, as compared to the carrying value stated above of approximately \$202.1 million.

Scheduled principal payments of mortgage notes payable are as follows:

| Year | Scheduled principal payments |
|------------|------------------------------------|
| 2008 | \$ 1,594,392 |
| 2009 | 2,254,470 |
| 2010 | 2,389,806 |
| 2011 | 2,676,907 |
| 2012 | 2,953,229 |
| Thereafter | 190,251,667 |
| | \$ 202,120,471 |

On February 8, 2007, through wholly-owned subsidiaries, the Company borrowed approximately \$13.8 million pursuant to a long-term note payable from KeyBank, which is collateralized by security interests in its Austin, Texas property, its Richmond, Virginia property and its Baytown, Texas property in the amounts of approximately \$6.5 million, \$5.3 million and \$2.0 million, respectively. The note accrues interest at a rate of 6.0% per year and the Company may not repay this note prior to maturity, or the Company would be subject to a substantial prepayment penalty. The note has a maturity date of March 1, 2017. The Company used the proceeds from the note for acquisitions of properties.

On June 5, 2007, through wholly-owned subsidiaries, the Company borrowed approximately \$14.2 million pursuant to a long-term note payable from Countrywide Commercial Real Estate Finance, which is collateralized by security interests in its Menomonee Falls, Wisconsin property, its Hazelton, Missouri property and its Raleigh, North Carolina property in the amounts of approximately \$6.9 million, \$2.4 million and \$4.9 million, respectively. The note accrues interest at a rate of 6.11% per year and the Company may not repay this note prior to the last three months of the term,

or the Company would be subject to a substantial prepayment penalty. The note has a maturity date of June 8, 2017. The Company used the proceeds from the note to pay down the outstanding balance on the line of credit.

On September 6, 2007, the Company assumed approximately \$4.5 million of indebtedness pursuant to a long-term note payable from Citigroup Global Markets Realty Corporation, in connection with the Company's acquisition, on the same date, of a property located in Cicero, New York. The note accrues interest at a rate of 5.81% per year, and the Company may not repay this note prior to the last two months of the term, or the Company would be subject to a substantial prepayment penalty. The note matures on December 11, 2015.

On October 15, 2007, through wholly-owned subsidiaries, the Company borrowed \$16.0 million pursuant to a long-term note payable from Countrywide Commercial Real Estate Finance, which is collateralized by security interests in its Mt. Pocono, Pennsylvania property, its Raleigh, North Carolina property and its Mason, Ohio property in the amounts of approximately \$5.4 million, \$5.6 million and \$5.0 million, respectively. The note accrues interest at a rate of 6.63% per year and the Company may not repay this note prior to the last three months of the term, or the Company would be subject to a substantial prepayment penalty. The note has a maturity date of November 8, 2017. The Company used the proceeds from the note to pay down the outstanding balance on the line of credit.

9. Stockholders' Equity

The 7.75% Series A Cumulative Redeemable Preferred Stock (the "Series A Preferred Stock"), has a par value of \$0.001 per share, and there are currently 1,000,000 shares issued and outstanding. The Series A Preferred Stock may be redeemed at a liquidation preference in the amount of \$25.00 per share plus any unpaid dividends at the election of the Company on or after January 30, 2011. These securities have no stated maturity, sinking fund or mandatory redemption and are not convertible into any other securities of the Company. The Series A Preferred Stock is traded on the NASDAQ Global Market under the trading symbol GOODP.

The 7.5% Series B Cumulative Redeemable Preferred Stock (the "Series B Preferred Stock"), has a par value \$0.001 per share, and there are currently 1,150,000 shares issued and outstanding. The Series B Preferred Stock may be redeemed at a liquidation preference in the amount of \$25.00 per share plus any unpaid dividends at the election of the Company on or after October 31, 2011. These securities have no stated maturity, sinking fund or mandatory redemption and are not convertible into any other securities of the Company. The Series B Preferred Stock is traded on the NASDAQ Global Market under the trading symbol GOODO.

Dividends paid per common share for the year ended December 31, 2007, 2006 and 2005 were \$1.44, \$1.44 and \$0.96 per share, respectively. Dividends paid per share of Series A Preferred Stock for the year ended December 31, 2007 and 2006 were approximately \$1.94 and \$1.79 per share, respectively. Dividends paid per share of Series B Preferred Stock for the year ended December 31, 2007 and 2006 were approximately \$1.88 and \$0.34, respectively. The tax status of the distributions is reflected in the table below:

| | Ordinary Income | Return of Capital | Long-Term Capital Gains |
|--------------------------------------|--------------------|----------------------|----------------------------|
| Common Stock | | | |
| For the year ended December 31, 2004 | 68.97050% | 31.02945% | 0.00000% |
| For the year ended December 31, 2005 | 50.44580% | 49.55420% | 0.00000% |
| For the year ended December 31, 2006 | 2.06500% | 95.60560% | 2.32940% |
| For the year ended December 31, 2007 | 25.86040% | 74.13960% | 0.00000% |
| Series A Preferred Stock | | | |
| For the year ended December 31, 2006 | 46.99260% | 0.00000% | 53.00740% |
| For the year ended December 31, 2007 | 100.00000% | 0.00000% | 0.00000% |
| Series B Preferred Stock | | | |
| For the year ended December 31, 2006 | 46.99260% | 0.00000% | 53.00740% |
| For the year ended December 31, 2007 | 100.00000% | 0.00000% | 0.00000% |

10. Segment Information

As of December 31, 2007, the Company's operations were derived from two operating segments. One segment purchases real estate (land, buildings and other improvements), which is simultaneously leased to existing users and the other segment extends mortgage loans and collects principal and interest payments. The following table summarizes the Company's consolidated operating results and total assets by segment as of and for the years ended December 31, 2007, 2006 and 2005:

As of and for the year ended December 31, 2007

| | Real Estate Leasing | Real Estate Lending | Other | Total |
|-------------------------|------------------------|------------------------|----------------|----------------|
| Operating revenues | \$ 31,779,650 | \$ 1,013,889 | \$ | \$ 32,793,539 |
| Operating expenses | (23,031,267) | | (4,354,904) | (27,386,171) |
| Other income | | | 624,147 | 624,147 |
| Discontinued operations | 108,714 | | | 108,714 |
| Net income (loss) | \$ 8,857,097 | \$ 1,013,889 | \$ (3,730,757) | \$ 6,140,229 |
| Total Assets | \$ 360,844,356 | \$ 10,000,000 | \$ 8,058,333 | \$ 378,902,689 |

As of and for the year ended December 31, 2006

| | Real Estate Leasing | Real Estate Lending | Other | Total |
|-------------------------|------------------------|------------------------|----------------|----------------|
| Operating revenues | \$ 24,100,315 | \$ 1,845,231 | \$ | \$ 25,945,546 |
| Operating expenses | (18,177,002) | | (4,994,988) | (23,171,990) |
| Other income | | | 583,475 | 583,475 |
| Discontinued operations | 1,015,797 | | | 1,015,797 |
| Net income (loss) | \$ 6,939,110 | \$ 1,845,231 | \$ (4,411,513) | \$ 4,372,828 |
| Total Assets | \$ 264,511,627 | \$ 10,000,000 | \$ 41,254,395 | \$ 315,766,022 |

As of and for the year ended December 31, 2005

| | Real Estate Leasing | Real Estate Lending | Other | Total |
|-------------------------|------------------------|------------------------|----------------|----------------|
| Operating revenues | \$ 10,965,711 | \$ 1,915,795 | \$ | \$ 12,881,506 |
| Operating expenses | (6,260,781) | | (3,257,635) | (9,518,416) |
| Other income | | | 147,867 | 147,867 |
| Discontinued operations | 90,988 | | | 90,988 |
| Net income (loss) | \$ 4,795,918 | \$ 1,915,795 | \$ (3,109,768) | \$ 3,601,945 |
| Total Assets | \$ 179,848,595 | \$ 21,096,564 | \$ 6,101,795 | \$ 207,046,954 |

The amounts included under the other column in the tables above include other income, which consists of interest income and any other miscellaneous income earned, and operating expenses that were not specifically derived from either operating segment

11. Line of Credit and Short-Term Loan

On December 29, 2006, the Company entered into a \$75 million senior revolving credit agreement with a syndicate of banks led by KeyBank National Association, which matures on December 29, 2009 with an option to extend for an additional year. The Company subsequently increased the availability under the line of credit to \$95 million in November 2007. The credit facility replaced a previous facility led by BB&T, which was terminated upon the closing of the new line. The interest rate charged on the advances under the facility is based on the LIBOR, the prime rate or the federal funds rate, depending on market conditions, and adjusts periodically. The unused portion of the line of credit is subject to a fee of 0.15% per year. The Company's ability to access this funding source is subject to the Company continuing to meet customary lending requirements such as compliance with financial and operating covenants and meeting certain lending limits. One such covenant requires the Company to limit its distributions to stockholders to 95% of its funds from operations, beginning with the quarter ended December 31, 2007. In addition, the maximum amount the Company may draw under this agreement is based on a percentage of the value of properties pledged as collateral to the banks, which must meet agreed upon eligibility standards. As the Company arranges for long-term mortgages for these pledged properties, the banks will release the properties from the line of credit and reduce the availability under the line of credit by the advanced amount of the removed property. Conversely, as the Company purchases new properties meeting the eligibility standards, the Company may pledge these new properties to obtain additional advances under this agreement. The Company may use the advances under the line of credit for both general corporate purposes and the acquisition of new investments. As of December 31, 2007, there was \$4.4 million outstanding under the line of credit at an interest rate of approximately 6.95%. At December 31, 2007, the remaining borrowing capacity available under the line of credit was \$90.6 million.

On December 21, 2007, the Company entered into a \$20 million unsecured term loan with KeyBank National Association, which matures on December 21, 2008 with an option to extend for an additional six months. The Company can exercise the option to extend the term as long as it is in compliance with all covenants under the loan at the time it exercises its option. The interest rate charged on the loan is based on the LIBOR, the prime rate or the federal funds rate, depending on market conditions, and adjusts periodically. The Company's ability to maintain this funding source is subject to it continuing to meet customary lending requirements such as compliance with financial and operating covenants and meeting certain lending limits. One such covenant requires the Company to limit distributions to its stockholders to 95% of its funds from operations, or FFO, beginning with the quarter ended December 31, 2007. As of December 31 2007, the interest rate on the short-term loan was approximately 7.44%.

12. Pro Forma Financial Information (unaudited)

The Company acquired 14 properties and one leasehold interest during the year ended December 31, 2007. The following table reflects pro-forma condensed consolidated income statements as if the 14 properties and one leasehold interest were acquired as of the beginning of the periods presented:

| | For the year ended December 31, | |
|---|---------------------------------|---------------|
| | 2007 | 2006 |
| Operating Data: | | |
| Total operating revenue | \$ 37,261,725 | \$ 30,413,732 |
| Total operating expenses | (17,176,935) | (15,422,401) |
| Other expense | (13,898,935) | (11,530,105) |
| Income from continuing operations | 6,185,855 | 3,461,226 |
| Dividends attributable to preferred stock | (4,093,750) | (2,186,890) |
| Net income available to common stockholders | \$ 2,092,105 | \$ 1,274,336 |
| Share and Per Share Data: | | |
| Basic net income | \$ 0.24 | \$ 0.16 |
| Diluted net income | \$ 0.24 | \$ 0.16 |
| Weighted average shares outstanding-basic | 8,565,264 | 7,827,781 |
| Weighted average shares outstanding-diluted | 8,565,264 | 7,986,690 |

These pro-forma consolidated income statements are not necessarily indicative of what actual results would have been had the Company acquired the specified properties and leasehold interest as of the beginning of the periods presented.

13. Quarterly Financial Information (unaudited)

The following table reflects the quarterly results of operations for the years ended December 31, 2007 and 2006, certain amounts from prior quarters' financial statements have been reclassified to conform to the current quarter's presentation. These reclassifications had no effect on previously reported net income or stockholders' equity.

| | Year ended December 31, 2007 | | | |
|---|------------------------------|-----------------------------|----------------------------------|---------------------------------|
| | Quarter ended March 31, 2007 | Quarter ended June 30, 2007 | Quarter ended September 30, 2007 | Quarter ended December 31, 2007 |
| Operating revenues | \$ 7,383,771 | \$ 8,079,568 | \$ 8,360,508 | \$ 8,969,692 |
| Operating expenses | 3,711,491 | 3,948,741 | 3,984,969 | 4,176,429 |
| Other expense | (2,216,609) | (2,573,068) | (2,824,541) | (3,326,176) |
| Income from continuing operations | 1,455,671 | 1,557,759 | 1,550,998 | 1,467,087 |
| Discontinued operations | 74,673 | (1,447) | 39,462 | (3,974) |
| Net income | 1,530,344 | 1,556,312 | 1,590,460 | 1,463,113 |
| Dividends attributable to preferred stock | (1,023,437) | (1,023,437) | (1,023,438) | (1,023,438) |
| Net income available to common stockholders | 506,907 | 532,875 | 567,022 | 439,675 |
| Net income available to common stockholders - basic | \$ 0.06 | \$ 0.06 | \$ 0.07 | \$ 0.05 |
| Net income available to common stockholders - diluted | 0.06 | 0.06 | 0.07 | 0.05 |
| Weighted average shares outstanding - basic | 8,565,264 | 8,565,264 | 8,565,264 | 8,565,264 |
| Weighted average shares outstanding - diluted | 8,565,264 | 8,565,264 | 8,565,264 | 8,565,264 |
| | Year ended December 31, 2006 | | | |
| | Quarter ended March 31, 2006 | Quarter ended June 30, 2006 | Quarter ended September 30, 2006 | Quarter ended December 31, 2006 |
| Operating revenues | \$ 5,425,611 | \$ 6,630,062 | \$ 6,735,976 | \$ 7,153,897 |
| Operating expenses | 3,022,998 | 3,523,818 | 3,620,149 | 3,900,131 |
| Other income (expense) | (1,605,650) | (2,112,922) | (2,450,869) | (2,351,978) |
| Income from continuing operations | 796,963 | 993,322 | 664,958 | 901,788 |
| Discontinued operations | 49,837 | (140,557) | 1,112,461 | (5,944) |
| Net income | 846,800 | 852,765 | 1,777,419 | 895,844 |
| | (344,444) | (484,375) | (484,375) | (873,696) |

| | | | | |
|---|-----------|-----------|-----------|-----------|
| Dividends attributable to preferred stock | | | | |
| Net income available to common stockholders | 502,356 | 368,390 | 1,293,044 | 22,148 |
| Net income available to common stockholders - basic | \$ 0.07 | \$ 0.05 | \$ 0.16 | \$ 0.00 |
| Net income available to common stockholders - diluted | 0.06 | 0.05 | 0.16 | 0.00 |
| Weighted average shares outstanding - basic | 7,672,000 | 7,762,503 | 7,820,376 | 8,052,148 |
| Weighted average shares outstanding - diluted | 7,821,658 | 7,911,871 | 7,981,071 | 8,196,605 |

14. Subsequent Events

On January 8, 2008, the Company's Board of Directors declared cash dividends of \$0.125 per common share, \$0.1614583 per share of the Series A Preferred Stock, and \$0.15625 per share of the Series B Preferred Stock for each of the months of January, February and March of 2008. Monthly dividends will be payable on January 31, 2008, February 29, 2008 and March 31, 2008, to those stockholders of record for the dates of January 23, 2008, February 21, 2008 and March 21, 2008, respectively.

On January 29, 2008, the Company acquired a 42,900 square foot industrial building in Reading, Pennsylvania for approximately \$7.2 million, including transaction costs. At closing, the Company extended a 20 year triple net lease with the sole tenant, and the tenant has four options to extend the lease for additional periods of five years each. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$0.72 million.

On February 26, 2008, the Company acquired a 74,160 square foot office building in Fridley, Minnesota for approximately \$10.6 million, including transaction costs. At closing, the Company was assigned the previously existing triple net lease with the sole tenant, which had a remaining term of approximately five years. The tenant has two options to extend the lease for additional periods of five years each. The lease provides for prescribed rent escalations over the life of the lease, with annualized straight line rents of approximately \$0.95 million. The Company was also assigned a ground lease on the parking lot at the time of closing, which has a remaining term of approximately six years. At the end of the term, the Company has the option to purchase the land. The rent due under the ground lease has been prepaid by the current tenant through the end of the term.

GLADSTONE COMMERCIAL CORPORATION
SCHEDULE III - REAL ESTATE AND ACCUMULATED DEPRECIATION
DECEMBER 31, 2007

| Property | Encumbrances | Initial Cost | | Costs | Total Cost | | Accumulated | Net Real | |
|----------------------------------|--------------|--------------|--------------|--|------------|--------------|--------------|------------|-----------------------------|
| | | Land | Improvements | Capitalized Subsequent to Acquisition | Land | Improvements | | | Depreciation ⁽¹⁾ |
| h ice | \$ 4,940,000 | \$ 960,000 | \$ 4,480,772 | \$ | \$ 960,000 | \$ 4,480,772 | \$ 5,440,772 | \$ 812,435 | \$ 4,628,337 |
| , Office | | | | | | | | | |
| | 2,950,000 | 186,739 | 3,082,007 | | 186,739 | 3,082,007 | 3,268,746 | 344,783 | 2,923,963 |
| Office & uilding | 7,560,000 | 1,974,000 | 6,769,565 | 19,782 | 1,974,000 | 6,789,347 | 8,763,347 | 657,311 | 8,106,036 |
| rth ice | | | | | | | | | |
| | 7,094,700 | 741,296 | 8,423,389 | 59,190 | 741,296 | 8,482,579 | 9,223,875 | 772,530 | 8,451,345 |
| n mmercial ring | | | | | | | | | |
| | 3,003,582 | 150,000 | 5,050,000 | | 150,000 | 5,050,000 | 5,200,000 | 450,421 | 4,749,579 |
| ship, | | | | | | | | | |
| & uilding orth mmercial | 5,760,000 | 100,000 | 6,573,902 | 6,907 | 100,000 | 6,580,809 | 6,680,809 | 578,471 | 6,102,338 |
| | | | | | | | | | |
| | 2,881,000 | 850,000 | 2,106,845 | 6,637 | 850,000 | 2,113,482 | 2,963,482 | 185,102 | 2,778,380 |
| , Office | 6,500,000 | 1,000,000 | 6,295,794 | 46,095 | 1,000,000 | 6,341,889 | 7,341,889 | 538,049 | 6,803,840 |
| inia, & g | | | | | | | | | |
| | | 190,000 | 739,521 | 18,190 | 190,000 | 757,711 | 947,711 | 62,269 | 885,442 |
| , & g | | | | | | | | | |
| | 5,346,519 | 350,000 | 5,818,703 | 18,430 | 350,000 | 5,837,133 | 6,187,133 | 487,282 | 5,699,851 |
| Texas, ce | | | | | | | | | |
| | 7,260,000 | 843,000 | 7,513,750 | 22,673 | 843,000 | 7,536,423 | 8,379,423 | 740,984 | 7,638,439 |
| hio, ilding | 2,800,000 | 410,000 | 2,385,108 | | 410,000 | 2,385,108 | 2,795,108 | 179,391 | 2,615,717 |

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| | | | | | | | | | |
|---------------------------------|------------|-----------|------------|-----------|-----------|------------|------------|---------|------------|
| New York, Building | 5,630,000 | 275,000 | 6,459,318 | 33,666 | 275,000 | 6,492,984 | 6,767,984 | 457,838 | 6,310,146 |
| Texas, Bakery | 8,798,419 | 1,525,000 | 9,702,731 | 51,453 | 1,525,000 | 9,754,184 | 11,279,184 | 701,816 | 10,577,368 |
| Office | 4,168,000 | 635,964 | 3,431,307 | 37,604 | 635,964 | 3,468,911 | 4,104,875 | 247,742 | 3,857,133 |
| ew | 2,078,000 | 525,000 | 1,876,992 | 119,736 | 525,000 | 1,996,728 | 2,521,728 | 181,748 | 2,339,980 |
| wnship, Office & Building | 4,580,000 | 1,350,630 | 3,520,062 | 6,681 | 1,350,630 | 3,526,743 | 4,877,373 | 270,626 | 4,606,747 |
| h ice & g | 6,790,000 | 1,631,534 | 6,199,849 | | 1,631,534 | 6,199,849 | 7,831,383 | 391,443 | 7,439,940 |
| Missouri, Warehouse | 14,569,776 | 977,898 | 13,472,678 | 1,902,582 | 977,898 | 15,375,260 | 16,353,158 | 937,994 | 15,415,164 |
| | 2,360,000 | 763,178 | 2,309,058 | 29,962 | 763,178 | 2,339,020 | 3,102,198 | 151,444 | 2,950,754 |

GLADSTONE COMMERCIAL CORPORATION
SCHEDULE III - REAL ESTATE AND ACCUMULATED DEPRECIATION (Continued)
DECEMBER 31, 2007

| Description of Property | Encumbrances | Initial Cost | | Costs | Total Cost | | Accumulated Depreciation ⁽¹⁾ | Net Real Estate | A | |
|---------------------------------------|--------------|--------------|--------------|------------------------------------|------------|--------------|---|-----------------|------------|----------------------|
| | | Land | Improvements | Capitalized Subsequent Acquisition | Land | Improvements | | | | Total ⁽²⁾ |
| Indiana, Building | 727,922 | 65,780 | 1,074,758 | | 65,780 | 1,074,758 | 1,140,538 | 66,496 | 1,116,968 | |
| Indiana, Building | 727,922 | 131,559 | 1,129,874 | | 131,559 | 1,129,874 | 1,261,433 | 66,496 | 1,116,968 | |
| s, Illinois, Building | 727,922 | 35,082 | 1,113,340 | | 35,082 | 1,113,340 | 1,148,422 | 66,495 | 1,116,969 | |
| port, setts, Building | 6,846,000 | 628,690 | 6,504,056 | 42,895 | 628,690 | 6,546,951 | 7,175,641 | 377,373 | 6,798,268 | 10 |
| le, a, Industrial uring | 3,532,029 | 54,674 | 4,717,090 | | 54,674 | 4,717,090 | 4,771,764 | 269,724 | 4,502,040 | 10 |
| ights, Ohio, Building | 10,896,000 | 1,608,976 | 10,065,475 | 37,869 | 1,608,976 | 10,103,344 | 11,712,320 | 612,594 | 11,099,726 | 12 |
| l, Virginia Building | 5,275,000 | 735,820 | 5,335,863 | 36,437 | 735,820 | 5,372,300 | 6,108,120 | 299,021 | 5,809,099 | 12 |
| ho Industrial Building | 3,000,000 | 263,068 | 2,811,801 | 39,916 | 263,068 | 2,851,717 | 3,114,785 | 175,759 | 2,939,026 | 12 |
| lley, setts Building | | 470,636 | 2,765,376 | 10,000 | 470,636 | 2,775,376 | 3,246,012 | 132,961 | 3,113,051 | 2 |
| n, Illinois ilding | 9,480,063 | 3,645,770 | 10,803,824 | 10,546 | 3,645,770 | 10,814,370 | 14,460,140 | 582,108 | 13,878,032 | 2 |
| Minnesota ilding | 19,782,270 | 2,587,757 | 25,290,127 | | 2,587,757 | 25,290,127 | 27,877,884 | 1,469,477 | 26,408,409 | 2 |
| e, Minnesota ilding | 12,000,000 | 3,510,711 | 8,746,407 | | 3,510,711 | 8,746,407 | 12,257,118 | 488,738 | 11,768,380 | 5 |
| ee Falls, n Industrial Building | 6,940,000 | 624,700 | 6,910,616 | | 624,700 | 6,910,616 | 7,535,316 | 270,211 | 7,265,105 | 6 |
| Texas ilding | 2,000,000 | 221,314 | 2,443,469 | | 221,314 | 2,443,469 | 2,664,783 | 106,239 | 2,558,544 | 7 |
| ights, Industrial Building | | 2,734,887 | 8,606,190 | 12,676 | 2,734,887 | 8,618,866 | 11,353,753 | 281,561 | 11,072,192 | 9 |
| am, Alabama Building | | 326,516 | 1,241,666 | | 326,516 | 1,241,666 | 1,568,182 | 40,963 | 1,527,220 | 9 |
| | | 326,517 | 1,241,667 | | 326,517 | 1,241,667 | 1,568,184 | 40,963 | 1,527,220 | 9 |

ery,
Industrial

, Missouri
Building

| | | | | | | | |
|---------|-----------|---------|-----------|-----------|--------|-----------|---|
| 326,517 | 1,241,667 | 326,517 | 1,241,667 | 1,568,184 | 40,963 | 1,527,220 | 9 |
| | | 31 | | | | | |

GLADSTONE COMMERCIAL CORPORATION
SCHEDULE III - REAL ESTATE AND ACCUMULATED DEPRECIATION (Continued)
DECEMBER 31, 2007

| | Initial Cost | | Costs Capitalized Subsequent to Acquisition | Total Cost | | Total ⁽²⁾ | Accumulated Depreciation ⁽¹⁾ | Net Re Estate | |
|-----------------------|----------------|-----------------------------|---|--------------|-----------------------------|----------------------|--|------------------|------------|
| | Land | Buildings & Improvements | | Land | Buildings & Improvements | | | | |
| Property Encumbrances | 797,274 | 6,258,344 | | 797,274 | 6,258,344 | 7,055,618 | 198,831 | 6,856 | |
| | 5,647,043 | 1,605,551 | 5,513,353 | 1,605,551 | 5,513,353 | 7,118,904 | 125,353 | 6,993 | |
| | | | 14,057,227 | | 14,057,227 | 14,057,227 | 350,674 | 13,706 | |
| | | 3,562,452 | 6,671,600 | 3,562,452 | 6,671,600 | 10,234,052 | 139,614 | 10,094 | |
| | | 1,394,902 | 8,893,243 | 1,394,902 | 8,893,243 | 10,288,145 | 153,732 | 10,134 | |
| | 4,981,099 | 1,201,338 | 4,960,896 | 1,201,338 | 4,960,896 | 6,162,234 | 60,569 | 6,101 | |
| | 4,487,205 | 299,066 | 5,018,628 | 299,066 | 5,018,628 | 5,317,694 | 41,106 | 5,276 | |
| | | 1,629,270 | 10,500,066 | 1,629,270 | 10,500,066 | 12,129,336 | 76,413 | 12,052 | |
| | | 1,271,543 | 5,002,471 | 1,271,543 | 5,002,471 | 6,274,014 | 35,340 | 6,238 | |
| | | 561,312 | 2,322,092 | 561,312 | 2,322,092 | 2,883,404 | 3,196 | 2,880 | |
| | | 561,312 | 2,322,092 | 561,312 | 2,322,092 | 2,883,404 | 3,197 | 2,880 | |
| | | 561,312 | 2,322,092 | 561,312 | 2,322,092 | 2,883,404 | 3,197 | 2,880 | |
| | | 561,312 | 2,322,092 | 561,312 | 2,322,092 | 2,883,404 | 3,197 | 2,880 | |
| | | 561,312 | 2,322,092 | 561,312 | 2,322,092 | 2,883,404 | 3,197 | 2,880 | |
| | | 561,313 | 2,322,092 | 561,313 | 2,322,092 | 2,883,405 | 3,197 | 2,880 | |
| | \$ 202,120,471 | \$ 48,867,482 | \$ 289,062,997 | \$ 2,569,927 | \$ 48,867,482 | \$ 291,632,924 | \$ 340,500,406 | \$ 15,738,634 | \$ 324,761 |

- (1) Depreciable life of all buildings is 39 years. Depreciable life of all improvements is the life of the respective leases on each building, which range from 5-20 years.
- (2) The aggregate cost for federal income tax purposes is the same as the total gross cost.

The following table reconciles the change in the balance of real estate during the years ended December 31, 2007, 2006, and 2005, respectively:

| | 2007 | 2006 | 2005 |
|---------------------------------|----------------|----------------|----------------|
| Balance at beginning of period | \$ 243,713,542 | \$ 165,043,640 | \$ 61,251,455 |
| Acquisitions during period | 95,396,039 | 83,466,860 | 103,792,185 |
| Improvements or other additions | 1,390,825 | 183,000 | |
| Dispositions during period | | (4,979,958) | |
| Balance at end of period | \$ 340,500,406 | \$ 243,713,542 | \$ 165,043,640 |

The following table reconciles the change in the balance of accumulated depreciation during the years ended December 31, 2007, 2006, and 2005, respectively:

| | 2007 | 2006 | 2005 |
|--------------------------------|---------------|--------------|--------------|
| Balance at beginning of period | \$ 8,595,419 | \$ 3,408,879 | \$ 785,125 |
| Additions during period | 7,143,215 | 5,351,414 | 2,623,754 |
| Dispositions during period | | (164,874) | |
| Balance at end of period | \$ 15,738,634 | \$ 8,595,419 | \$ 3,408,879 |

GLADSTONE COMMERCIAL CORPORATION
SCHEDULE IV MORTGAGE LOANS ON REAL ESTATE
DECEMBER 31, 2007

| Location and Type of Real Estate | Type of Loan | Interest Rate | Final Maturity Date | Periodic Payment Term | Prior Lien | Face Amount of Mortgage | Carrying Amount of Mortgage | Principal Amount of Mortgage |
|-----------------------------------|----------------|--|---------------------|--|------------|-------------------------|-----------------------------|------------------------------|
| McLean, Virginia; Office Property | First Mortgage | 1 month LIBOR +6%; Floor of 7.5%, Ceiling of 10% | 5/30/2017 | Monthly payment based upon a 24 year amortization term, which changes based on LIBOR, with a floor of 7.5% and a ceiling of 10%. Balloon payment at maturity is \$8,488,578. | | \$ 10,000,000 | \$ 10,000,000 | \$ 10,000,000 |
| | | | | | | \$ 10,000,000 | \$ 10,000,000 | \$ 10,000,000 |

(1) The aggregate cost for federal income tax purposes is the same as the total gross cost.

The following table reconciles the change in the balance of mortgage loans on real estate during the years ended December 31, 2007, 2006, and 2005, respectively:

| | 2007 | 2006 | 2005 |
|--|---------------|---------------|---------------|
| Balance at beginning of period | \$ 10,000,000 | \$ 21,025,815 | \$ 11,107,717 |
| New mortgage loans | | | 10,000,000 |
| Collections of principal | | (44,742) | (81,902) |
| Satisfaction of mortgage loan receivable | | (10,981,073) | |
| Balance at end of period | \$ 10,000,000 | \$ 10,000,000 | \$ 21,025,815 |

PART IV

Item 15. Exhibits and Financial Statement Schedules

Exhibit Description of Document

- | | |
|-------|---|
| 31.1 | Certification of Chief Executive Officer pursuant to Section 302 of The Sarbanes-Oxley Act of 2002. |
| 31 .2 | Certification of Chief Financial Officer pursuant to Section 302 of The Sarbanes-Oxley Act of 2002. |
| 32 .1 | Certification of Chief Executive Officer pursuant to Section 906 of The Sarbanes-Oxley Act of 2002. |
| 32 .2 | Certification of Chief Financial Officer pursuant to Section 906 of The Sarbanes-Oxley Act of 2002. |

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Gladstone Commercial Corporation

Date: May 15, 2008

By: /s/ Harry Brill

Harry Brill
Chief Financial Officer

Exhibit Index

Exhibit Description of Document

- | | |
|------|---|
| 31.1 | Certification of Chief Executive Officer pursuant to Section 302 of The Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of Chief Financial Officer pursuant to Section 302 of The Sarbanes-Oxley Act of 2002. |
| 32.1 | Certification of Chief Executive Officer pursuant to Section 906 of The Sarbanes-Oxley Act of 2002. |
| 32.2 | Certification of Chief Financial Officer pursuant to Section 906 of The Sarbanes-Oxley Act of 2002. |

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