Section 1: 10-K (10-K)

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

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2019

OR

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

For the transition period from to

Commission file number 000-55580

HIGHLANDS REIT, INC.

(Exact Name of Registrant as Specified in Its Charter)

Maryland	**81-0862795**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**
332 S Michigan Avenue, Ninth Floor Chicago, Illinois	**60604**
(Address of Principal Executive Offices)	**(Zip Code)**

(312) 583-7990
(Registrant’s telephone number, including area code)

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

Securities registered pursuant to Section 12(g) of the Act:
Common Stock, par value $0.01 per share
(Title of class)

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

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

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). ☑ Yes ☐ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

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

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

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

There is no established market for the registrant’s shares of common stock. The aggregate market value of the registrant’s common stock held by non-affiliates of the registrant as of June 28, 2019 (the last business day of the registrant’s most recently completed second quarter) was approximately $306.6 million, based on the estimated per share value of $0.35 as established by the registrant on December 31, 2018.

As of March 19, 2020 there were 879,553,830 shares of the registrant’s common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Part III of this Annual Report on Form 10-K incorporates by reference portions of the registrant’s Proxy Statement for its 2020 Annual Meeting of Stockholders expected to be held on June 4, 2020.

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Part I

Disclosure Regarding Forward-Looking Statements.

Certain statements in this Annual Report on Form 10-K, other than purely historical information, are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). These statements include statements about Highlands' plans, objectives, strategies, financial performance and outlook, trends, the amount and timing of future cash distributions, prospects or future events and involve known and unknown risks that are difficult to predict. As a result, our actual financial results, performance, achievements or prospects may differ materially from those expressed or implied by these forward-looking statements. In some cases, you can identify forward-looking statements by the use of words such as "may," "could," "expect," "intend," "plan," "seek," "anticipate," "believe," "estimate," "guidance," "predict," "potential," "continue," "likely," "will," "would," "illustrative" and variations of these terms and similar expressions, or the negative of these terms or similar expressions. Such forward-looking statements are necessarily based upon estimates and assumptions that, while considered reasonable by Highlands and its management based on their knowledge and understanding of the business and industry, are inherently uncertain. These statements are not guarantees of future performance, and stockholders should not place undue reliance on forward-looking statements. There are a number of risks, uncertainties and other important factors, many of which are beyond our control, that could cause our actual results to differ materially from the forward-looking statements contained in this Annual Report on Form 10-K. Such risks, uncertainties and other important factors include, among others: the risks, uncertainties and factors set forth under "Part I-Item IA. Risk Factors" and "Part II-Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations," and the risks and uncertainties related to the following: business, financial and operating risks inherent to real estate investments and the industry; our ability to renew leases, lease vacant space, or re-let space as leases expire; our ability to repay or refinance our debt as it comes due; the nature of our properties may make them more difficult to sell or re-lease due to their specific characteristics as described elsewhere in this report; the business, financial and operating risks inherent to real estate investments; contraction in the global economy or low levels of economic growth; our ability to sell our assets at a price and on a timeline consistent with our investment objectives, or at all; our ability to service our debt; changes in interest rates and operating costs; compliance with regulatory regimes and local laws; uninsured or underinsured losses, including those relating to natural disasters or terrorism; our status as an emerging growth company; the amount of debt that we currently have or may incur in the future; provisions in our debt agreements that may restrict the operation of our business; our organizational and governance structure; our status as a REIT; the cost of compliance with and liabilities under environmental, health and safety laws; adverse litigation judgments or settlements; the outcomes and projected length of any foreclosure proceedings relating to our assets; changes in real estate and zoning laws and increase in real property tax rates; changes in federal, state or local tax law, including legislative, administrative, regulatory or other actions affecting REITs; the impact of the changes in the tax code as a result of recent U.S. federal income tax reform and uncertainty as to how some of those changes may be applied; changes in governmental regulations or interpretations thereof; and estimates relating to our ability to make distributions to our stockholders in the future.

These factors are not necessarily all of the important factors that could cause our actual financial results, performance, achievements or prospects to differ materially from those expressed in or implied by any of our forward-looking statements. Other unknown or unpredictable factors also could harm our results. All forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements set forth above. Forward-looking statements speak only as of the date they are made, and we do not undertake or assume any obligation to update publicly any of these forward-looking statements to reflect actual results, new information or future events, changes in assumptions or changes in other factors affecting forward-looking statements, except to the extent required by applicable laws. If we update one or more forward-looking statements, no inference should be drawn that we will make additional updates with respect to those or other forward-looking statements.

Item 1. Business

Overview

References to "Highlands," "the Company," "we" or "us" are to Highlands REIT, Inc., as well as all of Highlands' wholly-owned and consolidated subsidiaries.

We are a self-advised and self-administered real estate investment trust ("REIT") created to own and manage substantially all of the "non-core" assets previously owned and managed by our former parent, InvenTrust Properties Corp., a Maryland corporation ("InvenTrust"). On April 28, 2016, we were spun-off from InvenTrust through a pro rata distribution (the "Distribution") by InvenTrust of 100% of the outstanding shares of our common stock to holders of InvenTrust's common stock. Prior to or concurrent with the separation, we and InvenTrust engaged in certain reorganization transactions that were designed to consolidate substantially all of InvenTrust's remaining "non-core" assets in Highlands. Highlands was incorporated in December 2015 as a Maryland corporation and operates in a manner that allows us to continue to qualify as a REIT for U.S. federal tax purposes.

This portfolio of "non-core" assets, which were acquired by InvenTrust between 2005 and 2008, included assets that are special use, single tenant or build to suit; face unresolved legal issues; are in undesirable locations or in weak markets or submarkets; are aging or functionally obsolete; and/or have sub-optimal leasing metrics. A number of our assets are retail properties located in tertiary markets, which are particularly susceptible to the negative trends affecting retail real estate. As a result of these characteristics, such assets are difficult to lease, finance and refinance and are relatively illiquid compared to other types of real estate assets. These factors also significantly limit our asset disposition options, impact the timing of such dispositions and restrict the viable options available to the Company for a future potential liquidity event.

Our strategy is focused on preserving, protecting and maximizing the total value of our portfolio with the long-term objective of providing stockholders with a return of their investment. We engage in rigorous asset management, and seek to sustain and enhance our portfolio, and improve the quality and income-producing ability of our portfolio, by engaging in selective dispositions, acquisitions, capital expenditures, financing, refinancing and enhanced leasing. We are also focused on cost containment efforts across our portfolio, improving our overall capital structure and making select investments in our existing "non-core" assets to maximize their disposition value. To the extent we are able to generate cash flows from operations or dispositions of assets, in addition to the cash uses outlined above, our board of directors has determined that it is in the best interests of the Company to seek to reinvest in assets that are more likely to generate more reliable and stable cash flows, such as multi-family assets, as part of the Company's overall strategy to optimize the value of the portfolio, enhance our options for a future potential liquidity event and maximize shareholder value. Given the nature and quality of the "non-core" assets in our portfolio as well as current market conditions, we expect this strategy will take multiple years to develop and execute.

As of December 31, 2019, our portfolio consisted of one office asset, two industrial assets, four retail assets, eleven multi-family assets, one correctional facility, one parcel of unimproved land and one bank branch, which are all located in the United States, with limited geographic concentration. We currently have four business segments, consisting of (i) net lease, (ii) retail, (iii) multi-tenant office and (iv) multi-family. Our unimproved land asset is presented in other assets (see Note 11 to the consolidated financial statements for additional information regarding segment reporting). We may have additional or fewer segments in the future to the extent we enter into additional real property sectors, dispose of property sectors, or change the character of assets.

2019 Highlights

- On January 8, 2019, we completed the acquisition of The Detroit and Detroit Terraces, two adjacent apartment buildings with 80 units, located in Denver, Colorado, for a purchase price of $19.1 million.

- On February 15, 2019, we entered into a credit agreement (as amended and supplemented, the "Credit Agreement") with Huntington National Bank ("HNB") and certain other lenders that provides for a revolving credit facility of up to $50.0 million and a term loan facility of up to $50.0 million with an accordion feature for an additional $100.0 million in potential financing.

- On April 5, 2019, we acquired The View, a 34-unit multi-family asset located in San Diego, California, for a purchase price of $16.4 million.

- On May 30, 2019, we sold a parcel of undeveloped land in Morrisville, North Carolina for a gross sale price of $0.6 million.

- On June 11, 2019, we acquired Tennyson44, a 47-unit multi-family asset located in San Diego, California for a purchase price of $19.2 million.

- On June 21, 2019, we sold our retail asset located in Lincoln, Rhode Island, commonly known as the "Lincoln Center", for a sale price of $55.8 million.

- Effective July 8, 2019, the Company hired Kimberly A. Karas to serve as the Company's Senior Vice President and Controller, and in such capacity to serve as our principal accounting officer.

- On August 16, 2019, we acquired The Locale (formerly Evolve at Allendale) through a joint venture, a 224-unit student housing asset located in Allendale, Michigan, for a purchase price of $27.7 million.

- On October 24, 2019, we acquired The Muse, a 120-unit student housing asset located in Denver, Colorado, for a purchase price of $48.8 million.

Business Strategy

Our investment objectives are to preserve, protect and maximize the total value of our portfolio. Given the quality and nature of the assets in our legacy “non-core” portfolio, which are generally disjointed, non-institutional grade, relatively illiquid, require substantial time and investment to bring to market and are not positioned to protect capital or deliver an acceptable risk-adjusted return, as well as current market conditions, we expect that this strategy will take multiple years to develop and execute. In order to meet our investment objectives, we intend to continue to engage in rigorous asset management, seek to sustain and enhance our portfolio, and improve the quality and income-producing ability of our portfolio, by engaging in selective dispositions, acquisitions, capital expenditures, financing, refinancing and enhanced leasing. We are also focused on cost containment efforts across our portfolio, improving its overall capital structure and making select investments in our existing “non-core” assets to maximize their value. To the extent we are able to generate cash flows from operations or dispositions of assets, in addition to the cash uses outlined above, our board of directors has determined that it is in the best interests of the Company to seek to reinvest in assets that are more likely to generate more reliable and stable cash flows, such as multi-family assets, as part of the Company's overall strategy to optimize the value of the portfolio, enhance our options for a future liquidity event and maximize shareholder value.

Disposition Policy

We evaluate each of our assets on a rigorous and ongoing basis in an effort to optimize and enhance the total value of our portfolio. In furtherance of this strategy, for the foreseeable future, we anticipate disposing of select “non-core” assets that are not generating income or have unfavorable risk-adjusted returns and generally, using the proceeds from such sales to prepare other “non-core” assets for sale or invest in assets that are more likely to generate more reliable and stable cash flows, such as multi-family assets.

The determination of when a particular asset should be sold or otherwise disposed of will be made after consideration of all of the relevant factors, including whether such disposition will better position the portfolio for a potential future liquidity event, prevailing and projected economic and market conditions, the cash flow being generated by a particular asset, tax implications of a disposition, investment opportunities for any cash proceeds, debt characteristics of the asset, and whether the value of the asset is anticipated to decline or increase. The timing of any disposition will depend upon then-prevailing economic and market conditions and the factors described above, which could result in differing holding periods among the assets. There can be no assurance that dispositions will occur as planned, on acceptable terms, or within our desired timing.

Financing Strategy

On February 15, 2019, we entered into the Credit Agreement which provides for a secured revolving credit facility of up to $50.0 million and a secured term loan facility of up to $50.0 million with an accordion feature for an additional $100.0 million in potential financing. In addition, certain of our existing assets are currently encumbered by debt, and debt financing may be used from time to time for property improvements, tenant improvements, acquisition financing, leasing commissions, general corporate purposes and other working capital needs. The form of our indebtedness may vary and could be long-term or short-term, secured or unsecured, or fixed-rate or floating rate. We will not enter into interest rate swaps or caps, or similar hedging transactions or derivative arrangements for speculative purposes, but may do so in order to manage or mitigate our interest rate risk on variable rate debt. For additional information regarding our existing debt, including our credit facility, please refer to “Management's Discussion and Analysis - Borrowings.”

As of December 31, 2019 and December 31, 2018, none of our mortgage debt was recourse to the Company, although we have provided certain customary, non-recourse carve-out guarantees in connection with obtaining mortgage loans on certain of our properties.

Tenants

As of December 31, 2019, approximately 26.7% of our revenues were derived from a net lease with The GEO Group, Inc. (“GEO”) on our Hudson correctional facility asset. The lease with GEO on this property expired in January of 2020 and GEO has vacated the facility. This vacancy will have a negative impact to our financial condition, cash flows and results of operations.

Conflict of Interest Policy

We maintain policies designed to reduce or eliminate potential conflicts of interest. Any transaction between us and any director, officer or 5% stockholder must be approved pursuant to our related party transaction policy. In addition, we have adopted a code of business conduct and ethics that seeks to identify and mitigate conflicts of interest between our employees, directors and officers and our company. However, we cannot assure you that these policies or provisions of law will always be successful in eliminating or minimizing the influence of such conflicts, and if they are not successful, decisions could be made that might fail to reflect fully the interests of stockholders.

Certain Other Policies

We intend to engage in future investment activities in a manner that is consistent with the requirements applicable to REITs for U.S. federal income tax purposes, unless the board of directors determines that it is no longer in our best interest to so qualify as a REIT.

We may issue senior securities, purchase and sell investments, offer securities in exchange for property and repurchase or reacquire shares or other securities in the future. To the extent we engage in these activities, we will comply with applicable law.

We do not currently have policies in place with respect to making loans to other persons (other than our conflict of interest policies described above) or investing in securities.

Competition

We are subject to significant competition in seeking tenants for the leasing of our assets, buyers for the sale of assets and sellers for the acquisition of assets. We compete with many third parties engaged in real estate investment activities, including other REITs, specialty finance companies, savings and loan associations, banks, mortgage bankers, insurance companies, mutual funds, institutional investors, investment banking firms, lenders, hedge funds, governmental bodies and other entities. Many of our competitors have substantially greater financial and other resources than we have and may have substantially more operating experience than us. We also face competition from other real estate investment programs for buyers, sellers and tenants that may be suitable for us. We perceive there to be a lower level of competition for certain assets in our portfolio based on, among other things, the characteristics of such assets, the number of willing buyers and the volume of transactions in their respective markets, which may make it challenging for us to sell these assets or attract tenants. Many of our retail tenants face intense competition from online retailers, which impacts demand for our brick-and-mortar retail real estate. A shift to e-commerce sales may adversely impact our retail tenants' sales thus causing those retailers to reduce the number of their retail locations in the future.

Regulations

Our assets are subject to various U.S. federal, state and local laws, ordinances and regulations, including, among other things, zoning regulations, land use controls, environmental controls relating to air and water quality, noise pollution and indirect environmental impacts such as increased motor vehicle activity. We believe that we have all permits and approvals necessary under current law to operate our assets.

Environmental

As an owner of real estate, we are subject to various environmental laws of U.S. federal, state and local governments. Compliance with existing laws has not had a material adverse effect on our financial condition or results of operations, and management does not believe it will have such an impact in the future. However, we cannot predict the impact of unforeseen environmental contingencies or new or changed laws or regulations on assets in which we hold an interest, or on assets that may be acquired directly or indirectly in the future.

Employees

At December 31, 2019, we had ten full-time employees, not including consultants and part-time workers. Due to the nature of our portfolio and our business strategy, we rely on consultants, professional firms and third parties, under our supervision, to perform many routine operations for us.

Insurance

We have insurance coverage for our properties which includes the type of coverage and limits we believe to be appropriate for each property and our business operations. Such coverage typically includes commercial general liability and property insurance which, includes property damage and loss of rental income resulting from such perils as fire, windstorm, flood and extended coverage. Our management believes our insurance coverage contains policy terms and conditions and insured limits that are customary for similar properties and operations.

Principal Executive Offices

Our principal executive offices are located at 332 S Michigan Avenue, Ninth Floor, Chicago, Illinois, 60604, and our telephone number is (312)-583-7990. We maintain a website at www.highlandsreit.com.

Available Information

Stockholders may obtain copies of our filings with the Securities and Exchange Commission ("SEC"), free of charge, from the website maintained by the SEC at www.sec.gov or from our website at www.highlandsreit.com. These include our annual report on Form 10-K, quarterly reports on form 10-Q, and our current reports on Form 8-K. Our filings will be available on our website as soon as reasonably practicable after we electronically file such materials with the SEC. However, the information from our website is not incorporated by reference into this report.

Item 1A. Risk Factors

You should carefully consider each of the following risks described below and all of the other information in this Annual Report on Form 10-K in evaluating us. Our business, financial condition, cash flows, results of operations and/or ability to pay distributions to our stockholders could be materially adversely affected by any of these risks. This Annual Report on Form 10-K also contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including the risks faced by us described below and elsewhere in this Annual Report on Form 10-K. See "Disclosure Regarding Forward-Looking Statements."

Risks Related to Our Business and Industry

Short-term multi-family community leases associated with any multi-family residential properties we acquire may expose us to the effects of declining market rent and could adversely impact our ability to make cash distributions to our stockholders.

We expect that, substantially all of our multi-family community leases will be for a term of one year or less. Because these leases generally permit the residents to leave at the end of the lease term without penalty, our rental revenues may be impacted by declines in market rents more quickly than if our leases were for longer terms.

The costs of compliance with laws and regulations relating to our residential properties may adversely affect our income and the cash available for any distributions.

Various laws, ordinances, and regulations affect multi-family residential properties, including regulations relating to recreational facilities, such as activity centers and other common areas. In addition, rent control laws may be applicable to any of our residential properties.

Some of these laws and regulations have been amended so as to require compliance with new or more stringent standards as of future dates. Compliance with new or more stringent laws or regulations, stricter interpretation of existing laws or the future discovery of environmental contamination may require material expenditures by us. Future laws, ordinances or regulations may impose material environmental liabilities, and the current environmental condition of our properties might be affected by the operations of the tenants, by the existing condition of the land, by operations in the vicinity of the properties, such as the presence of underground storage tanks, or by the activities of unrelated third parties.

These laws typically allow liens to be placed on the affected property. In addition, there are various local, state and federal fire, health, life-safety and similar regulations which we may be required to comply with, and which may subject us to liability in the form of fines or damages for noncompliance.

Any newly acquired or developed multi-family residential properties must comply with Title II of the Americans with Disabilities Act (the “ADA”) to the extent that such properties are “public accommodations” and/or “commercial facilities” as defined by the ADA. Compliance with the ADA requires removal of structural barriers to handicapped access in certain public areas of the properties where such removal is “readily achievable.” Our properties may not comply in all material respects with all present requirements under the ADA and applicable state laws. When acquiring properties, we may not succeed in placing the burden on the seller to ensure compliance with the ADA. Noncompliance with the ADA could result in the imposition of injunctive relief, monetary penalties or, in some cases, an award of damages to private litigants. The cost of defending against any claims of liability under the ADA or the payment of any fines or damages could adversely affect our financial condition and affect cash available to return capital and the amount of distributions to you.

Increased competition and increased affordability of residential housing could limit our ability to retain tenants, lease multi-family properties or increase or maintain rents.

The multi-family sector is highly competitive. This competition could reduce occupancy levels and revenues at our multi-family communities, which would adversely affect our operations. We face competition from many sources. We face competition from other multi-family communities both in the immediate vicinity and in the larger geographic market where our multi-family communities are located. These competitors may have greater experience and financial resources than us giving them an advantage in attracting tenants to their properties. For example, our competitors may be willing to offer multi-family housing at rental rates below our rates, causing us to lose existing or potential tenants and pressuring us to reduce our rental rates to retain existing tenants or convince new tenants to lease space at our property. Overbuilding of multi-family communities may also occur. If so, this will increase the number of multi-family housing available and may decrease occupancy and multi-family rental rates. In addition, increases in operating costs due to inflation may not be offset by increased multi-family rental rates. Furthermore, multi-family communities we acquire most likely compete, or will compete, with numerous housing alternatives in attracting tenants, including owner occupied single- and multi-family housing available to rent or purchase. Competitive housing in a particular area and the increasing affordability of owner occupied single and multi-family housing available to rent or buy caused by low mortgage interest rates and government programs to promote home ownership could adversely affect our ability to retain our tenants, lease multi-family housing and increase or maintain rental rates.

We could be negatively impacted by the condition of Fannie Mae or Freddie Mac and by changes in government support for multi-family housing.

Fannie Mae and Freddie Mac are a major source of financing for multi-family real estate in the United States. In the future, we may utilize loan programs sponsored by these entities as a source of capital to finance our growth and our operations. In September 2008, the U.S. government assumed control of Fannie Mae and Freddie Mac and placed both companies into a government conservatorship under the Federal Housing Finance Agency. In December 2009, the U.S. Treasury increased its financial support for these conservatorships. In February 2011, the Obama administration released its blueprint for winding down Fannie Mae and Freddie Mac and for reforming the system of housing finance. Since that time, members of Congress have introduced and Congressional committees have considered a substantial number of bills that include comprehensive or incremental approaches to winding down Fannie Mae and Freddie Mac or changing their purposes, businesses, or operations. A decision by the U.S. government to eliminate or downscale Fannie Mae or Freddie Mac or to reduce government support for multi-family housing more generally may adversely affect interest rates, capital availability, development of multi-family communities and the value of multi-family assets and, as a result, may adversely affect our future growth and operations.

We may be unable to renew our commercial leases, lease vacant space or re-let space as leases expire, thereby increasing or prolonging vacancies.

We cannot assure you that leases will be renewed or that our assets will be re-leased on terms equal to or better than the current terms, or at all. We also may not be able to lease space which is currently not occupied on acceptable terms and conditions, if at all. Certain of our assets are special use, single-tenant or build-to-suit; are in undesirable locations or weak markets or sub-markets; and/or are aging or functionally obsolete. As a result, these properties may be very difficult to lease. In addition, some of our tenants have leases that include early termination provisions that permit the lessee to terminate all or a portion of its lease with us after a specified date or upon the occurrence of certain events with little or no liability to us. We may be required to offer substantial rent abatements, tenant improvements, early termination rights or below-market renewal options to retain these tenants or attract new ones. It is possible that, in order to lease currently vacant space, or space that may become vacant, we will be required to make rent or other concessions to tenants, accommodate requests for renovations, make tenant improvements or other improvements or provide additional services to our tenants. Portions of our assets may remain vacant for extended periods of time. If the rental rates for our assets decrease, our existing tenants do not renew their leases or we do not re-lease a significant portion of our available space and space for which leases will expire, our financial condition, cash flows and results of operations could be adversely affected.

We may be unable to lease our correctional facility on acceptable terms or at all.

In 2019, approximately 26.7% of our current revenue derived from a lease with The GEO Group, Inc. on our Hudson correctional facility. The lease on this property expired in January of 2020 and The GEO Group, Inc. has vacated the facility. We cannot assure you that we will be able to lease the Hudson correctional facility on acceptable terms or at all. Correctional facilities are unique, specific purpose assets that have a limited market, and we face competition in this market from both government entities and private operators, many of which have a longer track record and more experience and greater financial resources than us. Additionally, the market for leasing correctional facilities is subject to a number of unique factors, including the level of government appropriations and acceptance of privatization of correctional facilities among the government and the general public. Further, if we are unable to lease our Hudson correctional facility on acceptable terms or at all, we may be required to make significant capital expenditures to reposition this asset or to finance the asset or sell this asset. If we are unable to lease our Hudson correctional facility on acceptable terms or at all, our financial condition, cash flows and results of operations may be adversely affected.

We depend on tenants for our revenue, and accordingly, lease terminations, vacancies, tenant defaults and bankruptcies could adversely affect the income produced by our assets.

Our business and financial condition depends on the financial stability of our tenants. Certain economic conditions may adversely affect one or more of our tenants. For example, business failures and downsizings can affect the tenants of our office and industrial assets. As a result, our tenants may delay lease commencements, decline to extend or renew their leases upon expiration, fail to make rental payments, or declare bankruptcy. Individual tenants may lease more than one asset or space at more than one asset. As a result, the financial failure of one tenant could increase vacancy at more than one asset or cause more than one lease to become non-performing. Any of these actions could result in the termination of the tenants' leases, the expiration of existing leases without renewal or the loss of rental income attributable to the terminated or expired leases, any of which could make our assets difficult to sell and could have a material adverse effect on our financial condition, cash flows and results of operations.

In the event of a tenant default or bankruptcy, we may experience delays in enforcing our rights as a landlord and may incur substantial costs in protecting our investment and re-leasing our asset. Specifically, a bankruptcy filing by, or relating to, one of our tenants or a lease guarantor would bar efforts by us to collect pre-bankruptcy debts from that tenant or lease guarantor, or its assets, unless we receive an order permitting us to do so from the bankruptcy court. In addition, we cannot evict a tenant solely because of bankruptcy. The bankruptcy of a tenant or lease guarantor could delay our efforts to collect past-due balances under the relevant leases, and could ultimately preclude collection of these sums. If a lease is rejected by a tenant in bankruptcy, we would have only a general, unsecured claim for damages. An unsecured claim would only be paid to the extent that funds are available and only in the same percentage as is paid to all other holders of general, unsecured claims. Restrictions under the bankruptcy laws further limit the amount of any other claims that we can make if a lease is rejected. As a result, it is likely that we would recover substantially less than the full value of the remaining rent during the term, and may not recover any balances at all.

Our legacy portfolio includes assets that are special use, single-tenant and/or build-to-suit; face unresolved legal issues; are aging or functionally obsolete; or have sub-optimal leasing metrics, which may make them difficult to lease, finance or sell.

Our legacy portfolio includes assets that are special use, single-tenant and/or build-to-suit; face unresolved legal issues; are aging or functionally obsolete; or have sub-optimal leasing metrics, which may make them relatively illiquid compared to other types of real estate assets. With these assets, if the current lease is terminated or not renewed, we may be required to make significant capital expenditures to reposition the asset or make rent concessions in order to lease the asset to another tenant, finance the asset or sell the asset.

Many of our properties are located in weak markets or submarkets, which may adversely affect our ability to rent such properties, increase rental rates and/or sell such properties.

Certain of our properties are located in weak markets or submarkets. These markets may be experiencing economic slowdowns, little or no job growth, and/or high numbers of vacancies. Also, with respect to our retail assets, a shift toward increased e-commerce sales could adversely impact the demand for our retail assets if retail tenants reduce the number of their brick-and-mortar locations. The weakness of an asset's market or submarket may adversely affect our ability to rent such properties, increase rental rates and/or sell such properties, which could have a material adverse effect on our financial condition, cash flows or results of operations.

Economic and market conditions could negatively impact our business, results of operations and financial condition.

Our business may be affected by market and economic challenges experienced by the United States or global economies or the real estate industry as a whole or by the local economic conditions in the markets in which our assets are located, including any dislocations in the credit markets. These conditions may materially affect our tenants, the value and performance of our assets and our ability to sell assets, as well as our ability to make principal and interest payments on, or refinance, any outstanding debt when due. Challenging economic conditions may also impact the ability of certain of our tenants to enter into new leasing transactions or satisfy rental payments under existing leases. Specifically, these conditions may have the following consequences:

- the financial condition of our tenants may be adversely affected, which may result in us having to increase concessions, reduce rental rates or make capital improvements in order to maintain occupancy levels or to negotiate for reduced space needs, which may result in a decrease in our occupancy levels;

- significant job loss may occur, which may decrease demand for space and result in lower occupancy levels, which will result in decreased revenues and which could diminish the value of assets, which depend, in part, upon the cash flow generated by our assets;

- an increase in the number of bankruptcies or insolvency proceedings of our tenants and lease guarantors, which could delay our efforts to collect rent and any past due balances under the relevant leases and ultimately could preclude collection of these sums;

- our ability to borrow on terms and conditions that we find acceptable may be limited;

- the amount of capital that is available to finance assets could diminish, which, in turn, could lead to a decline in asset values generally, slow asset transaction activity, and reduce the loan to value ratio upon which lenders are willing to lend; and

- the value of certain of our assets may decrease below the amounts we paid for them, which would limit our ability to dispose of assets at attractive prices or for potential buyers to obtain debt financing secured by these assets and could reduce our ability to finance our business.

An outbreak of disease or similar public health threat, such as the coronavirus, could adversely affect our and our tenants' financial condition and operations.

A local, regional, national or international outbreak of a contagious disease, including the COVID-19 coronavirus, Middle East Respiratory Syndrome, Severe Acute Respiratory Syndrome, H1N1 influenza virus, avian flu or any other similar illness, could decrease the willingness of customers to patronize our tenants' retail facilities, discourage residents from renting in our multi-family communities, cause shortages of employees to staff our tenants' operations, interrupt supplies from third parties upon which our tenants rely, cause us or our tenants to temporarily close one or more of our properties, result in governmental regulation adversely impacting our or our tenants' businesses and otherwise have a material adverse effect on our business, financial condition and results of operations. Such adverse effect could be rapid and unexpected.

Our ongoing business strategy involves the selling of assets; however, we may be unable to sell an asset at acceptable terms and conditions, if at all.

We intend to hold our assets until such time as we determine that a sale or other disposition appears to be advantageous to achieve our investment objectives. The determination of when a particular asset should be sold or otherwise disposed of will be made after consideration of all of the relevant factors, including whether such disposition will better position the portfolio for a potential future liquidity event, prevailing and projected economic and market conditions, the cash flow being generated by a particular asset, tax implications of a disposition, debt characteristics of the asset, and whether the value of the asset or other investment is anticipated to decline or increase investment opportunities for any proceeds. Even if we do determine to sell an asset, market conditions or individual asset characteristics may negatively affect the value of our assets and therefore reduce our return on the investment or prevent us from selling the asset on acceptable terms or at all. Some of our leases contain provisions giving the tenant a right to purchase the asset, such as a right of first offer or right of first refusal, which may lessen our ability to freely control the sale of the asset. Debt levels may exceed the value of our assets in the future, making it more difficult for us to rent, refinance or sell the assets. In addition, real estate investments are relatively illiquid and often cannot be sold quickly, limiting our ability to sell our assets when we decide to do so, or in response to such changing economic or asset-specific issues. Further, economic conditions may prevent potential purchasers from obtaining financing on acceptable terms, if at all, thereby delaying or preventing our ability to sell our assets.

We may not successfully implement our strategy, in which case you may have to hold your investment for an indefinite period.

We are under no obligation to complete our strategy within a specified time period, and market and economic conditions and other factors beyond our control could delay the execution of our strategy. Our investment objectives are to preserve, protect and maximize the total value of our portfolio with the long term objective of providing stockholders with a return of their investment. Given the nature of the assets in our portfolio, we expect that this strategy will take multiple years to develop and execute. We may not be able to control the timing of the sale of our assets, and there can be no assurance that we will be able to sell our assets so as to return any portion of our stockholders' invested capital, particularly our "non-core" assets, or fully satisfy our debt obligations. Our ability to sell our assets may also be limited by our need to avoid a 100% penalty tax that is imposed on gain recognized by a REIT from the sale of assets characterized as dealer property, which may cause us to forego or defer sales of assets that otherwise would be in our best interests.

If we are not successful in implementing our strategy in a timely manner, your shares may continue to be illiquid and you may, for an indefinite period of time, be unable to convert your investment into cash easily, if at all, and could suffer losses on your investment.

Real estate is a competitive business.

We compete with numerous developers, owners and operators of commercial real estate assets in the leasing market, many of which own assets similar to, and in the same market areas as, our assets. In addition, some of these competitors may be willing to accept lower returns on their investments than we are, and many have greater resources than we have and may enjoy significant competitive advantages that result from, among other things, a lower cost of capital and enhanced operating efficiencies. Principal factors of competition include rents charged, attractiveness of location, the quality of the asset and breadth and quality of services provided. Our success depends upon, among other factors, trends affecting national and local economies, the financial condition and operating results of current and prospective tenants and customers, availability and cost of capital, construction and renovation costs, taxes, governmental regulations, legislation, job creation and population trends.

We also face competition from other real estate investment programs for buyers. We perceive there to be a smaller universe of potential buyers for many of the types of assets that comprise our portfolio in comparison to assets in more core real estate sectors, which will likely make it challenging for us to sell our assets.

Any difficulties in obtaining capital necessary to make tenant improvements, pay leasing commissions and make capital improvements at our assets could materially and adversely affect our financial condition and results of operations.

Ownership of real estate is a capital intensive business that requires significant capital expenditures to operate, maintain and renovate assets. Access to the capital that we need to lease, maintain and renovate existing assets is critical to the success of our business. We may not be able to fund tenant improvements, pay leasing commissions or fund capital improvements at our existing assets solely from cash provided from our operating activities. As a result, our ability to fund tenant improvements, pay leasing commissions or fund capital improvements through retained earnings may be restricted. Consequently, we may have to rely upon the availability of debt, net proceeds from the dispositions of our assets or equity capital to fund tenant improvements, pay leasing commissions or fund capital improvements. Our ability to obtain debt on favorable terms or at all may be further limited by the fact that certain properties previously owned by the Company were foreclosed upon. The inability to access capital could impair our ability to compete effectively and harm our business.

There are inherent risks with investments in real estate, including the relative illiquidity of such investments.

Investments in real estate are subject to varying degrees of risk. For example, an investment in real estate cannot generally be quickly sold, and we cannot predict whether we will be able to sell any asset we desire to on the terms set by us or acceptable to us, or the length of time needed to find a willing purchaser and to close the sale of such asset. Moreover, the Internal Revenue Code of 1986, amended (the "Code") imposes restrictions on a REIT's ability to dispose of assets that are not applicable to other types of real estate companies. In particular, the tax laws applicable to REITs require that we hold our assets for investment, rather than primarily for sale in the ordinary course of business, which may cause us to forego or defer sales of assets that otherwise would be in our best interests. Therefore, we may not be able to vary our portfolio promptly in response to changing economic, financial, investment and market conditions and dispose of assets at opportune times, on favorable terms or at all, which may adversely affect our cash flows and our ability to make distributions to stockholders.

Investments in real estate are also subject to adverse changes in general economic conditions. Among the factors that could impact our assets and the value of an investment in us are:

- risks associated with the possibility that cost increases will outpace revenue increases and that in the event of an economic slowdown, the high proportion of fixed costs will make it difficult to reduce costs to the extent required to offset declining revenues;
- changes in tax laws and property taxes, or an increase in the assessed valuation of an asset for real estate tax purposes;
- adverse changes in the U.S. federal, state or local laws and regulations applicable to us, including those affecting zoning, fuel and energy consumption, water and environmental restrictions, and the related costs of compliance;
- changing market demographics;
- an inability to finance real estate assets on favorable terms, if at all;
- the ongoing need for owner-funded capital improvements and expenditures to maintain or upgrade assets;
- fluctuations in real estate values or potential impairments in the value of our assets;
- pandemics, natural disasters, such as earthquakes, floods or other insured or uninsured losses;
- war, political conditions or civil unrest, terrorist activities or threats heightened travel security measures instituted in response to these events; and
- changes in interest rates and availability, cost and terms of financing.

Our assets may be subject to impairment charges that may materially affect our financial results.

Economic and other conditions may adversely impact the valuation of our assets, resulting in impairment charges that could have a material adverse effect on our results of operations and earnings. On a regular basis, we evaluate our assets for impairments based on various triggers, including changes in the projected cash flows of such assets and market conditions. If we determine that an impairment has occurred, then we would be required to make an adjustment to the net carrying value of the asset, which could have a material adverse effect on our results of operations in the accounting period in which the adjustment is made. During 2018, we determined that impairment with respect to two of our properties had occurred, resulting in reductions in net carrying value of those assets by an aggregate of $4.7 million. During 2019, no impaired assets were identified. Furthermore, changes in estimated future cash flows due to a change in our plans, policies, or views of market and economic conditions could result in the recognition of additional impairment losses for already impaired assets, which, under the applicable accounting guidance, could be substantial.

Many real estate costs and certain operating costs are fixed, even if revenue from our assets decreases.

Many real estate costs, such as real estate taxes, insurance premiums, maintenance costs and certain operating costs generally are more fixed than variable and, as a result, are not reduced even when an asset is not fully occupied, rents decrease or other circumstances cause a reduction in revenues. If we are unable to offset these fixed costs with sufficient revenues across our portfolio, it could materially and adversely affect our results of operations and profitability. This risk is particularly acute at our net lease assets.

Operating and other expenses may increase in the future, which may cause our cash flow and our operating results to decrease.

Certain operating expenses and certain general and administrative expenses are not fixed and may increase in the future. Any increases would cause our cash flow and our operating results to decrease. If we are unable to offset these decreases with sufficient revenues across our portfolio, our financial condition, cash flows and results of operations may be materially adversely affected.

Our revenue from our retail assets will be impacted by the success and economic viability of our anchor retail tenants. Our reliance on single or significant tenants in certain buildings may decrease our ability to lease vacated space and adversely affect our financial condition, cash flows and results of operations.

In the retail sector, a tenant occupying all or a large portion of the gross leasable area of a retail center, commonly referred to as an anchor tenant, may become insolvent, may suffer a downturn in business or may decide not to renew its lease. Any of these events would result in a reduction or cessation in rental payments to us and would adversely affect our financial condition. A lease termination by an anchor tenant also could result in lease terminations or reductions in rent by other tenants whose leases may permit cancellation or rent reduction if another tenant’s lease is terminated. Similarly, the leases of some anchor tenants may permit the anchor tenant to transfer its lease to another retailer. The transfer to a new anchor tenant could reduce customer traffic in the retail center and thereby reduce the income generated by that retail center. A transfer of a lease to a new anchor tenant could also allow other tenants to make reduced rental payments or to terminate their leases in accordance with lease terms. If we are unable to re-lease the vacated space to a new anchor tenant, we may incur additional expenses in order to remodel the space to be able to re-lease the space to more than one tenant.

Public resistance to privatization of correctional facilities could negatively impact our future tenants, if any, which could have an adverse impact on our business, financial condition or results of operations.

The management and operation of correctional facilities by private entities has not achieved complete acceptance by either government agencies or the public. Some governmental agencies have limitations on their ability to delegate their traditional management responsibilities for such facilities to private companies, and additional legislative changes or prohibitions could occur that further increase these limitations. In addition, the movement toward privatization of such facilities has encountered resistance from groups, and activists, that believe that correctional facilities should only be operated by governmental agencies. In addition, negative publicity about poor conditions, an escape, riot or other disturbance at a privately-managed facility may result in adverse publicity to the private corrections industry. Any of these occurrences or continued trends may make it more difficult for future tenants, if any, of our correctional facility asset to obtain new contracts. Changes in governing political parties could also result in significant changes to previously established views of privatization. Increased public resistance to the privatization of correctional facilities could have a material adverse effect on our future tenants, if any, who operate in this industry, which could adversely impact the value of our correctional facility asset, our ability to re-lease such asset and our results of operations.

The land underlying a portion of one of our assets is subject to a ground lease, which could limit our use of the asset, and a breach or termination of the ground lease could materially and adversely affect us.

We lease a portion of the land underlying one of our assets, Sherman Plaza, from a third party through a ground lease covering such land. As a lessee under a ground lease, we are exposed to the possibility of losing the right to use the portion of our asset covered by the ground lease upon termination, or an earlier breach by us, of the ground lease. The ground lease may also restrict our use of the asset, which may limit our flexibility in renting the asset and may impede our ability to sell the asset.

Uninsured and underinsured losses at our assets could materially and adversely affect our revenues and profitability.

We intend to maintain comprehensive insurance on each of our current assets, including liability, fire and extended coverage, of the type and amount we believe are customarily obtained for or by property owners. There are no assurances that coverage will be available at reasonable rates. Various types of catastrophic losses, like windstorms, earthquakes and floods, environmental events and losses from foreign terrorist activities may not be insurable or may not be economically insurable. Even when insurable, these policies may have high deductibles and/or high premiums. Lenders may require such insurance. Our failure to obtain such insurance could constitute a default under loan agreements, and/or our lenders may force us to obtain such insurance at unfavorable rates, which could materially and adversely affect our profitability and revenues.

In the event of a substantial loss, our insurance coverage may not be sufficient to cover the full current market value or replacement cost of our lost investment. Should an uninsured loss or a loss in excess of insured limits occur, we could lose all or a portion of the capital we have invested in an asset, as well as the anticipated future revenue from the asset. In that event, we might nevertheless remain obligated for any mortgage debt or other financial obligations related to the asset. Inflation, changes in building codes and ordinances, environmental considerations and other factors might also keep us from using insurance proceeds to replace or renovate an asset after it has been damaged or destroyed. Under those circumstances, the insurance proceeds we receive might be inadequate to restore our economic position on the damaged or destroyed property, which could materially and adversely affect our profitability.

In addition, insurance risks associated with potential terrorist acts could sharply increase the premiums we pay for coverage against property and casualty claims. With the enactment of the Terrorism Risk Insurance Program Reauthorization Act of 2007, United States insurers cannot exclude conventional, chemical, biological, nuclear and radiation terrorism losses. These insurers must make terrorism insurance available under their property and casualty insurance policies; however, this legislation does not regulate the pricing of such insurance. In many cases, mortgage lenders have begun to insist that commercial property owners purchase coverage against terrorism as a condition of providing mortgage loans. Such insurance policies may not be available at a reasonable cost, which could inhibit our ability to finance or refinance our assets. In such instances, we may be required to provide other financial support, either through financial assurances or self-insurance, to cover potential losses. We may not have adequate coverage for such losses, which could materially and adversely affect our revenues and profitability.

We could incur significant, material costs related to government regulation and litigation with respect to environmental matters, which could materially and adversely affect our revenues and profitability.

Our assets are subject to various U.S. federal, state and local environmental laws that impose liability for contamination. Under these laws, governmental entities have the authority to require us, as the current owner of an asset, to perform or pay for the clean-up of contamination (including hazardous substances, asbestos and asbestos-containing materials, waste or petroleum products) at, on, under or emanating from the asset and to pay for natural resource damages arising from such contamination. Such laws often impose liability without regard to whether the owner or operator or other responsible party knew of, or caused such contamination, and the liability may be joint and several. Because these laws also impose liability on persons who owned an asset at the time it became contaminated, it is possible we could incur cleanup costs or other environmental liabilities even after we sell assets. Contamination at, on, under or emanating from our assets also may expose us to liability to private parties for costs of remediation and/or personal injury or property damage. In addition, environmental laws may create liens on contaminated sites in favor of the government for damages and costs it incurs to address such contamination. If contamination is discovered on our assets, environmental laws also may impose restrictions on the manner in which the assets may be used or businesses may be operated, and these restrictions may require substantial expenditures. Moreover, environmental contamination can affect the value of an asset and, therefore, an owner’s ability to borrow funds using the asset as collateral or to sell the asset on favorable terms or at all. Furthermore, persons who sent waste to a waste disposal facility, such as a landfill or an incinerator, may be liable for costs associated with cleanup of that facility.

In addition, our assets are subject to various U.S. federal, state, and local environmental, health and safety laws and regulations that address a wide variety of issues, including, but not limited to, storage tanks, air emissions from emergency generators, storm water and wastewater discharges, lead-based paint, mold and mildew, and waste management. Some of our assets may handle and use hazardous or regulated substances and wastes as part of their operations, which substances and wastes are subject to regulation. Our assets incur costs to comply with these environmental, health and safety laws and regulations and could be subject to fines and penalties for non-compliance with applicable requirements.

Environmental laws in the U.S. also require that owners or operators of buildings containing asbestos properly manage and maintain the asbestos, adequately inform or train those who may come into contact with asbestos and undertake special precautions, including removal or other abatement, if that asbestos is disturbed during building renovation or demolition. These laws may impose fines and penalties on building owners or operators who fail to comply with these requirements and may allow third parties to seek recovery from owners or operators for personal injury associated with exposure to asbestos. Some of our assets may contain asbestos-containing building materials.

When excessive moisture accumulates in buildings or on building materials, mold growth may occur, particularly if the moisture problem remains undiscovered or is not addressed over a period of time. Some molds may produce airborne toxins or irritants. Indoor air quality issues can also stem from inadequate ventilation, chemical contamination from indoor or outdoor sources, and other biological contaminants such as pollen, viruses and bacteria. Indoor exposure to airborne toxins or irritants above certain levels can be alleged to cause a variety of adverse health effects and symptoms, including allergic or other reactions. As a result, the presence of significant mold or other airborne contaminants at any of our assets could require us to undertake a costly remediation program to contain or remove the mold or other airborne contaminants from the affected asset or increase indoor ventilation. In addition, the presence of significant mold or other airborne contaminants could expose us to liability to third parties if property damage or personal injury occurs.

Liabilities and costs associated with environmental contamination at, on, under or emanating from our assets, defending against claims related to alleged or actual environmental issues, or complying with environmental, health and safety laws could be material and could materially and adversely affect us. We can make no assurances that changes in current laws or regulations or future laws or regulations will not impose additional or new material environmental liabilities or that the current environmental condition of our assets will not be affected by our operations, the condition of the assets in the vicinity of our assets, or by third parties unrelated to us. The discovery of material environmental liabilities at our assets could subject us to unanticipated significant costs, which could significantly reduce or eliminate our profitability and the cash available for distribution to our stockholders.

The costs of compliance with laws and regulations relating to our properties may adversely affect our income and the cash available for any distributions.

Various laws, ordinances, and regulations affect our properties. Some of these laws and regulations have been amended so as to require compliance with new or more stringent standards as of future dates. Compliance with new or more stringent laws or regulations, stricter interpretation of existing laws or the future discovery of environmental contamination may require material expenditures by us. Future laws, ordinances or regulations may impose material environmental liabilities, and the current environmental condition of our properties might be affected by the operations of the tenants, by the existing condition of the land, by operations in the vicinity of the properties, such as the presence of underground storage tanks, or by the activities of unrelated third parties.

Any newly acquired or developed multi-family residential properties must comply with Title II of the Americans with Disabilities Act (the "ADA") to the extent that such properties are "public accommodations" and/or "commercial facilities" as defined by the ADA. Compliance with the ADA requires removal of structural barriers to handicapped access in certain public areas of the properties where such removal is "readily achievable." Our properties may not comply in all material respects with all present requirements under the ADA and applicable state laws. When acquiring properties, we may not succeed in placing the burden on the seller to ensure compliance with the ADA. Noncompliance with the ADA could result in the imposition of injunctive relief, monetary penalties or, in some cases, an award of damages to private litigants. The cost of defending against any claims of liability under the ADA or the payment of any fines or damages could adversely affect our financial condition and affect cash available to return capital and the amount of distributions to you.

Under the ADA and the Accessibility Guidelines promulgated thereunder; all public accommodations must meet various U.S. federal requirements related to access and use by disabled persons. Compliance with the ADA's requirements could require removal of access barriers, and non-compliance could result in the U.S. government imposing fines or in private litigants winning damages.

Our assets are also subject to various U.S. federal, state and local regulatory requirements, such as state and local fire and life safety requirements. If we fail to comply with these requirements, we could incur fines or private damage awards. We do not know whether existing requirements will change or whether compliance with future requirements would require significant unanticipated expenditures that would affect our cash flow and results of operations. If we incur substantial costs to comply with the ADA requirements or other safety regulations and requirements, it could materially and adversely affect our revenues and profitability.

Adverse judgments or settlements resulting from legal proceedings in which we may be involved in the normal course of our business could reduce our profits or limit our ability to operate our business.

In the normal course of our business, we are involved in various legal proceedings. The outcome of these proceedings cannot be predicted. If any of these proceedings were to be determined adversely to us or a settlement involving a payment of a material sum of money were to occur, it could materially and adversely affect our profits or ability to operate our business. Additionally, we could become the subject of future claims by third parties, including current or former tenants, our employees, our investors or regulators. Any significant adverse judgments or settlements would reduce our profits and could limit our ability to operate our business. Further, we may incur costs related to claims for which we have appropriate third-party indemnity, but such third parties fail to fulfill their contractual obligations.

If we fail to maintain an effective system of disclosure controls and procedures and internal control over financial reporting, our ability to produce timely and accurate financial statements or comply with applicable regulations could be impaired.

We are subject to the reporting requirements of the Exchange Act and the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act. We expect that the requirements of these rules and regulations will continue to increase our legal, accounting and financial compliance costs, make some activities more time-consuming and costly, and may place a strain on our personnel, systems and resources.

The Sarbanes-Oxley Act requires, among other things, that we maintain effective disclosure controls and procedures and internal control over financial reporting. We are also required to make a formal assessment and provide an annual management report on the effectiveness of our internal control over financial reporting. In order to maintain the effectiveness of our disclosure controls and procedures and internal control over financial reporting, we have expended, and anticipate that we will continue to expend, significant resources, including accounting-related costs and management oversight.

Current controls and any new controls that we develop may become inadequate due to changes in conditions of our business. Further, weaknesses in our disclosure controls and procedures and internal control over financial reporting may be discovered in the future. Any failure to maintain or develop effective controls or any difficulties encountered in their implementation or improvement could harm our operating results or cause us to fail to meet reporting obligations and may result in a restatement of our financial statements for prior periods. Any failure to maintain effective internal control over financial reporting also could adversely affect the results of periodic management evaluations.

As an "emerging growth company," we are permitted to rely on exemptions from certain reporting and disclosure requirements, which may make our future public filings different than that of other public reporting companies.

We are an "emerging growth company" as defined in the JOBS Act, and we are eligible to take advantage of certain exemptions from various reporting and disclosure requirements that are applicable to public reporting companies that are not emerging growth companies. We will remain an emerging growth company for up to five years, or until the earliest of: (1) the last date of the fiscal year during which we had total annual gross revenues of $1.07 billion or more; (2) the date on which we have, during the previous three-year period, issued more than $1 billion in non-convertible debt; or (3) the date on which we are deemed to be a "large accelerated filer" as defined under Rule 12b-2 under the Exchange Act. For so long as we remain an emerging growth company, we will not be required to:

- have an auditor attestation report on our internal control over financial reporting pursuant to Section 404(b) of the Sarbanes-Oxley Act;

- submit certain executive compensation matters to stockholder advisory votes pursuant to the "say on frequency" and "say on pay" provisions (requiring a non-binding stockholder vote to approve compensation of certain executive officers) and the "say on golden parachute" provisions (requiring a non-binding stockholder vote to approve golden parachute arrangements for certain executive officers in connection with mergers and certain other business combinations) of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010; or

- disclose certain executive compensation related items.

If we choose to take advantage of any or all of these exemptions, the information that we provide you in our future public filings may be different than that of other public reporting companies. The exact implications of the JOBS Act for us are still subject to interpretations and guidance by the Securities and Exchange Commission (the "SEC") and other regulatory agencies. In addition, if our business grows, we may no longer satisfy the conditions of an emerging growth company. We continue to evaluate and monitor developments with respect to these new rules and we cannot assure you that we will be able to take advantage of all of the benefits of the JOBS Act.

In addition, the JOBS Act provides that an emerging growth company may take advantage of an extended transition period for complying with new or revised accounting standards that have different effective dates for public reporting and private companies. This means that an emerging growth company can delay adopting certain accounting standards until such standards are otherwise applicable to private companies. We do not intend to take advantage of the extended transition period.

We are increasingly dependent on information technology, and potential cyber-attacks, security problems, or other disruption present risks.

A cyber incident is considered to be any adverse event that threatens the confidentiality, integrity or availability of our information resources. More specifically, a cyber incident is an intentional attack or an unintentional event that can include an intruder gaining unauthorized access to systems to disrupt operations, corrupt data or steal confidential information. As our reliance on technology has increased, so have the risks posed to our systems, both internal and those we have outsourced. Our three primary risks that could directly result from the occurrence of a cyber incident include operational interruption, damage to our relationships with our tenants and private data exposure. Our financial results and reputation may be negatively impacted by such an incident.

Risks Related to Debt Financing

If we are unable to repay or refinance our existing debt as it comes due, we may need to sell the underlying asset sooner than anticipated or the lender may foreclose, in which case our financial condition, cash flows and results of operations could be materially adversely affected.

Certain of our debt is secured by certain of our assets, and, if our subsidiaries are unable to repay or refinance the debt as it becomes due, we may need to sell the underlying asset sooner than anticipated or the lender may foreclose.

Although the mortgages on our properties do not mature in the near term, due to the near-term expiration of tenant leases at certain of these properties, we may be unable to make mortgage payments and may default under the applicable loan agreement. This may force us to dispose of those assets on disadvantageous terms, or the lender under such mortgages may foreclose, resulting in losses materially adversely affecting our cash flow, results of operations and financial condition. Generally, a borrower in foreclosure proceedings has limited or no control over the timing and speed of such proceedings, and the ultimate resolution of such proceedings may take years. The Company may provide customary, non-recourse carve-out guarantees in connection with obtaining mortgage loans.

Our special purpose property-owning subsidiaries may default under non-recourse mortgage loans.

All of our assets are held in special-purpose property-owning subsidiaries. In the future, such special purpose property-owning subsidiaries may default and/or send notices of imminent default on non-recourse mortgage loans where the relevant asset is or will be suffering from cash shortfalls on operating expenses, leasing costs and/or debt service obligations. If tenants at certain of our properties, fail to renew their leases and we are unable to find new tenants, we may be unable to make mortgage payments and may default under the loan agreement. Additionally, in connection with our separation from InvenTrust, certain lenders under such non-recourse mortgage loans may allege that a default has been deemed to occur under such loans.

Any default by our special purpose property-owning subsidiaries under non-recourse mortgage loans would give the special servicers the right to accelerate the payment on the loans and the right to foreclose on the asset underlying such loans. There are several potential outcomes on the default of a non-recourse mortgage loan, including foreclosure, a deed-in-lieu of foreclosure, a cooperative short sale, or a negotiated modification to the terms of the loan. There is no assurance that we will be able to achieve a favorable outcome on a cooperative or timely basis on any defaulted mortgage loan.

Our failure to comply with the covenants in our Credit Agreement and other debt agreements could materially and adversely affect us.

The Credit Agreement, which governs our new secured credit facility, contains various covenants with which we must comply and which limit the discretion of management with respect to certain business matters. These covenants place restrictions on, among other things, our ability to incur additional indebtedness, grant liens on our assets, make certain types of investments, engage in acquisitions, mergers or consolidations, sell assets, enter into hedging transactions, enter into certain transactions with affiliates and, during the continuance of an event of default, make distributions and prepay certain types of indebtedness. The Credit Agreement also contains financial covenants with which we must comply, including a maximum leverage ratio, a maximum variable rate leverage ratio, a maximum amount of recourse indebtedness, a minimum fixed charge coverage ratio, a prohibition on recourse debt, a maximum amount of cross-collateralized non-recourse debt, a minimum tangible net worth and a minimum number of unencumbered properties we must own and a minimum value for such unencumbered properties. Any other debt agreement that we enter into may place additional restrictions on us and may require us to meet certain financial ratios and tests. In addition, the Credit Agreement contains, and any future debt agreements may contain, cross-default provisions that trigger an event of default if we fail to make payments or otherwise fail to comply with our obligations with respect to certain of our other indebtedness. Our continued ability to borrow under the Credit Agreement and any other indebtedness that we have or may obtain will be subject to compliance with the covenants in the Credit Agreement or in the debt agreement governing such other indebtedness.

Our failure to comply with these covenants, as well as our inability to make required payments under the Credit Agreement or any future debt agreement, could cause an event of default under the Credit Agreement, which, if not waived, could result in the termination of the financing commitments under the Credit Agreement, the acceleration of the maturity of the outstanding indebtedness thereunder and the lenders under the Credit Agreement obtaining ownership of our subsidiaries whose equity interests were pledged as collateral for such indebtedness, or could cause an event of default under such future debt agreement, which could result in the acceleration of the debt and, in the case of secured debt, the lenders taking possession of the property or properties securing such debt. If repayment of any of our indebtedness is accelerated and/or we are unable to make additional borrowings under the Credit Agreement or any of our other debt agreements, we cannot provide assurance that we would be able to borrow sufficient funds to refinance such indebtedness or that we would be able to sell sufficient assets to repay such indebtedness. Even if we were able to obtain new financing, it may not be on commercially reasonable terms, or terms that are acceptable to us.

In addition, in connection with certain of our debt agreements we have entered, and in the future may enter, into lockbox and cash management agreements pursuant to which all or substantially all of the income generated by our assets will be deposited directly into lockbox accounts and then swept into cash management accounts for the benefit of our lenders and from which cash may not be distributed to us or will be distributed to us only after funding of certain items, which may include payment of principal and interest on our debt, insurance and tax reserves or escrows and other expenses. As a result, we may be forced to borrow additional funds in order to make distributions to our stockholders necessary to allow us to continue to qualify as a REIT.

If we are unable to repay or refinance our existing debt as it comes due, we may need to sell the underlying asset sooner than anticipated or the lender may foreclose, in which case our financial condition, cash flows and results of operations could be materially adversely affected.

Certain of our debt (including the Credit Agreement) is secured by certain of our assets, and, if we are unable to repay or refinance such debt as it becomes due, we may need to sell the underlying assets sooner than anticipated or the lender may foreclose.

Although the Credit Agreement and the mortgages on our properties do not mature in the near term, due to the near-term expiration of tenant leases at certain of our properties, we may be unable to make required debt payments and may default under the applicable debt agreement. This may force us to dispose of assets on disadvantageous terms, or cause the lender to exercise its remedies under the applicable debt agreement, which may include foreclosure of the underlying assets, resulting in losses materially adversely affecting our cash flow, results of operations and financial condition. Generally, a borrower in a foreclosure proceeding has limited or no control over the timing and speed of such proceedings, and the ultimate resolution of such proceedings may take years.

We may default under non-recourse mortgage loans.

All of our assets are held in special-purpose property-owning subsidiaries. In the future, such special purpose property-owning subsidiaries may default and/or send notices of imminent default on non-recourse mortgage loans where the relevant asset is or will be suffering from cash shortfalls on operating expenses, leasing costs and/or debt service obligations. If tenants at certain of our properties fail to renew their leases and we are unable to find new tenants, we may be unable to make mortgage payments and may default under the loan agreement. Additionally, in connection with our separation from InvenTrust, certain lenders under such non-recourse mortgage loans may allege that a default has been deemed to occur under such loans.

Any default by us under a non-recourse mortgage loan would give the lender the right to accelerate the payment on the loan and the right to foreclose on the asset underlying such loan. There are several potential outcomes on the default of a non-recourse mortgage loan, including foreclosure, a deed-in-lieu of foreclosure, a cooperative short sale, or a negotiated modification to the terms of the loan. There is no assurance that we will be able to achieve a favorable outcome on a cooperative or timely basis on any defaulted mortgage loan.

We are subject to obligations under certain "non-recourse carve-out" indemnity agreements and guarantees that may be deemed to be triggered in the future.

As of December 31, 2019, certain of our assets are encumbered by traditional non-recourse debt obligations. In connection with obtaining these loans, we entered into indemnity agreements and "non-recourse carve-out" guarantees, which provide for these otherwise non-recourse loans to become partially or fully recourse against us if certain triggering events occur. Although these events differ from loan to loan, some of the common events include:

- Our filing of a voluntary petition for bankruptcy or commencing similar insolvency proceedings;
- Subject to certain conditions, our failure to obtain the lender's written consent prior to any subordinate financing or other voluntary lien encumbering the associated asset; and
- Subject to certain conditions, our failure to obtain the lender's written consent prior to a transfer or conveyance of the associated asset.

In addition, other items that are customarily recourse to a non-recourse carve-out guarantor include, but are not limited to, the payment of real property taxes, the breach of representations related to environmental issues or hazardous substances, physical waste of the property, liens which are senior to the mortgage loan and outstanding security deposits.

In the event that any of these triggering events occur and such loans become partially or fully recourse against us, our business, financial condition, results of operations, and the value of our common stock would be materially adversely affected, and we may be forced to sell other assets and/or our insolvency could result. Additionally, in connection with our separation from InvenTrust, certain lenders under such non-recourse mortgage loans may allege that a default has been deemed to occur under such loans and may seek to recover from us and/or our subsidiaries the full extent of their losses with respect to such loans. Any allegations may create a distraction for our management, result in significant liability, or subject us to litigation that could be costly or otherwise materially adversely affect us.

We may be unable to satisfy our debt obligations upon a change of control.

Under the documents that govern our indebtedness, if we experience a change of control, we could be required to incur certain penalties, fees and other expenses, which may include repayment of the entire principal balance of some of our outstanding indebtedness plus additional fees and interest. We might not have sufficient funds to repay such amounts. Any of these events could have a material adverse impact on our liquidity, business, results of operations and financial condition.

Volatility in the financial markets and challenging economic conditions could adversely affect our ability to secure debt financing on attractive terms and our ability to service any future indebtedness that we may incur.

The domestic and international commercial real estate debt markets could become very volatile as a result of, among other things, the tightening of underwriting standards by lenders and credit rating agencies. This could result in less availability of credit and increasing costs for what is available. If the overall cost of borrowing increases, either by increases in the index rates or by increases in lender spreads, the increased costs may result in lower overall economic returns and potentially reducing future cash flow available for distribution. If these disruptions in the debt markets were to persist, our ability to borrow funds to finance activities related to real estate assets could be negatively impacted. In addition, we may find it difficult, costly or impossible to refinance indebtedness that is maturing.

Further, economic conditions could negatively impact commercial real estate fundamentals and result in declining values in our real estate portfolio and in the collateral securing any loan investments we may make, which could have various negative impacts. Specifically, the value of collateral securing any loan we hold could decrease below the outstanding principal amounts of such loans.

Borrowings may reduce the funds available for distribution and increase the risk of loss since defaults may cause us to lose the assets securing the loans.

We may from time to time borrow money for other purposes to, among other things, satisfy the requirement that we distribute at least 90% of our “REIT annual taxable income,” subject to certain adjustments, or as is otherwise necessary or advisable to assure that we qualify as a REIT for U.S. federal income tax purposes. Over the long term, however, payments required on any amounts we borrow reduce the funds available for, among other things, capital expenditures for existing assets or distributions to our stockholders because cash otherwise available for these purposes is used to pay principal and interest on this debt.

If there is a shortfall between the cash flow from an asset and the cash flow needed to service mortgage debt on an asset, then the amount of cash flow from operations available for distributions to stockholders may be reduced. In addition, incurring mortgage debt increases the risk of loss since defaults on indebtedness secured by an asset may result in lenders initiating foreclosure actions. In such a case, we could lose the asset securing the loan that is in default, thus reducing the value of your investment. For tax purposes, a foreclosure is treated as a sale of the asset or assets for a purchase price equal to the outstanding balance of the debt secured by the asset or assets. If the outstanding balance of the debt exceeds our tax basis in the asset or assets, we would recognize taxable gain on the foreclosure action and we would not receive any cash proceeds. We also may fully or partially guarantee any funds that subsidiaries borrow to operate assets. In these cases, we may be responsible to the lender for repaying the loans if the subsidiary is unable to do so.

Due to distressed assets within our portfolio and our relatively small size as compared with our former Parent’s size, it may be difficult for us to obtain debt financing or refinancing on favorable terms, or at all, which may adversely affect our business, financial condition and results of operations.

We may require debt financing from time to time for property improvements, tenant improvements, acquisition financing, leasing commissions, general corporate purposes and other working capital needs. There are currently, and are likely to continue to be, a number of distressed assets in our portfolio that are in danger of becoming subject to foreclosure proceedings. Lenders may consider the fact that such distressed assets exist within our portfolio when determining whether to advance credit to us in the future, even though each asset is owned by a separate subsidiary. Additionally, certain of our existing debt financing was entered into prior to our spin-off from InvenTrust. Due to our reduced size in comparison to InvenTrust, it may be difficult to refinance our existing debt on favorable terms. If we are unable to obtain debt financing on favorable terms, or at all, or if the ability to obtain financing is restricted by the terms of our credit facility or other indebtedness we may incur, our business, financial condition and results of operations may be adversely affected.

If we are unable to borrow at favorable rates, we may not be able to refinance existing loans at maturity.

If we are unable to borrow money at favorable rates, or at all, we may be unable to refinance existing loans at maturity. Further, we may enter into loan agreements or other credit arrangements that require us to pay interest on amounts we borrow at variable or "adjustable" rates. Increases in interest rates will increase our interest costs. If interest rates are higher when we refinance our loans, our expenses will increase. Any increases in our operating costs due to increases interest costs would reduce our cash flow, which could reduce the amount we are able to distribute to our stockholders. Further, during periods of rising interest rates, we may be forced to sell one or more of our assets earlier than anticipated in order to repay existing loans, which may not permit us to maximize the return on the particular assets being sold.

Interest-only indebtedness may increase our risk of default and ultimately may reduce our funds available for distribution to our stockholders.

We have obtained, and may continue to enter into mortgage indebtedness that does not require us to pay principal for all or a portion of the life of the debt instrument. During the period when no principal payments are required, the amount of each scheduled payment is less than that of a traditional amortizing mortgage loan. The principal balance of the mortgage loan is not reduced (except in the case of prepayments) because there are no scheduled monthly payments of principal required during this period. After the interest-only period, we may be required either to make scheduled payments of principal and interest or to make a lump-sum or "balloon" payment at or prior to maturity. These required principal or balloon payments will increase the amount of our scheduled payments and may increase our risk of default under the related mortgage loan if we do not have funds available or are unable to refinance the obligation.

Covenants applicable to current or future debt could restrict our ability to make distributions to our stockholders and, as a result, we may be unable to make distributions necessary to qualify as a REIT, which could materially and adversely affect us and the value of our common stock.

We intend to operate in a manner so as to maintain our qualification as a REIT for U.S. federal income tax purposes. In order to maintain our qualification as a REIT, we generally are required to distribute at least 90% of our REIT taxable income, determined without regard to the dividends paid deduction and excluding net capital gain, each year to our stockholders. To the extent that we satisfy this distribution requirement, but distribute less than 100% of our REIT taxable income, we will be subject to U.S. federal corporate income tax on our undistributed taxable income. In addition, we will be subject to a 4% nondeductible excise tax if the actual amount that we distribute to our stockholders in a calendar year is less than a minimum amount specified under the Code. If, as a result of covenants applicable to our current or future debt, including under the terms of our credit facility, we are restricted from making distributions to our stockholders, we may be unable to make distributions necessary for us to avoid U.S. federal corporate income and excise taxes and maintain our qualification as a REIT, which could materially and adversely affect us.

Our organizational documents have no limitation on the amount of indebtedness we may incur. As a result, we may become highly leveraged in the future, which could materially and adversely affect us.

Our organizational documents contain no limitations on the amount of debt that we may incur, and our board of directors may change our financing policy at any time without stockholder notice or approval. As a result, we may be able to incur substantial additional debt, including secured debt, in the future. Incurring debt could subject us to many risks, including the risks that:

- our cash flows from operations may be insufficient to make required payments of principal and interest;
- our debt and resulting maturities may increase our vulnerability to adverse economic and industry conditions;
- we may be required to dedicate a substantial portion of our cash flows from operations to payments on our debt, thereby reducing cash available for distribution to our stockholders, funds available for operations and capital expenditures, future business opportunities or other purposes;
- the terms of any refinancing may not be in the same amount or on terms as favorable as the terms of the existing debt being refinanced, or we may not be able to refinance our debt at all;
- we may be obligated to repay the debt pursuant to guarantee obligations; and
- the use of leverage could adversely affect our ability to raise capital from other sources or to make distributions to our stockholders and could adversely affect the value of our common stock.

Interest-only indebtedness may increase our risk of default and ultimately may reduce our funds available for distribution to our stockholders.

We have obtained, and may continue to enter into mortgage indebtedness that does not require us to pay principal for all or a portion of the life of the debt instrument. During the period when no principal payments are required, the amount of

each scheduled payment is less than that of a traditional amortizing mortgage loan. The principal balance of the mortgage loan is not reduced (except in the case of prepayments) because there are no scheduled monthly payments of principal required during this period. After the interest-only period, we may be required either to make scheduled payments of principal and interest or to make a lump-sum or "balloon" payment at or prior to maturity. These required principal or balloon payments will increase the amount of our scheduled payments and may increase our risk of default under the related mortgage loan if we do not have funds available or are unable to refinance the obligation.

Increases in interest rates could increase the amount of our debt payments and adversely affect our ability to make distributions to our stockholders.

We may in the future borrow money bearing interest at variable rates, which would expose us to increases in costs in a rising interest rate environment. Increases in future interest rates would increase our interest expense for any existing variable rate debt, as well as any debt that must be refinanced at higher interest rates at the time of maturity. Our future earnings and cash flows could be adversely affected due to the increased requirement to service our debt and could reduce the amount we are able to distribute to our stockholders.

Risks Related to Our Status as a REIT

Failure to remain qualified as a REIT would cause us to be taxed as a regular corporation, which would substantially reduce funds available for distributions to our stockholders.

Our qualification as a REIT depends on our ability to meet requirements regarding our organization and ownership, distributions of our income, the nature and diversification of our income and assets as well as other tests imposed by the Code. We cannot assure you that our actual operations for any one taxable year will satisfy these requirements. Further, new legislation, regulations, administrative interpretations or court decisions could significantly affect our ability to qualify as a REIT or the consequences of our qualification as a REIT. If we fail to qualify as a REIT in any taxable year, we will face serious tax consequences that will substantially reduce the funds available for distributions to our stockholders because:

- we would not be allowed a deduction for dividends paid to stockholders in computing our taxable income and would be subject to U.S. federal income tax at regular corporate rates;
- we could be subject to increased state and local taxes; and
- unless we are entitled to relief under certain U.S. federal income tax laws, we could not re-elect REIT status for the four taxable years after the year in which we failed to qualify as a REIT.

In addition, if we fail to qualify as a REIT, we will no longer be required to make distributions. As a result of all these factors, our failure to qualify as a REIT could impair our ability to expand our business and raise capital, and it would adversely affect the value of our common stock.

If either InvenTrust or MB REIT failed to qualify as a REIT, we would be prevented from electing to qualify as a REIT.

We believe that prior to the separation from InvenTrust, we were a "qualified REIT subsidiary" of InvenTrust. Under applicable Treasury regulations, if either (i) InvenTrust failed to qualify as a REIT in its 2012 through 2016 taxable years or (ii) MB REIT failed to qualify as a REIT for its 2012 taxable year through its taxable year that ended on December 15, 2015 (when MB REIT became a "qualified REIT subsidiary" of InvenTrust), unless such failure was subject to relief under U.S. federal income tax laws, we would be prevented from electing to qualify as a REIT for the four taxable years following the year in which InvenTrust or MB REIT failed to qualify.

Even if we continue to qualify as a REIT for tax purposes, we may face other tax liabilities that reduce our cash flows.

Even if we continue to qualify as a REIT for tax purposes, we may be subject to certain U.S. federal, state and local taxes on our income and assets, including taxes on any undistributed income, tax on income from some activities conducted as a result of a foreclosure, and state or local income, property and transfer taxes. In addition, any taxable REIT subsidiary ("TRS") that we may form will be subject to regular corporate U.S. federal, state and local taxes. Any of these taxes would decrease cash available for distributions to stockholders.

Failure to make required distributions would subject us to U.S. federal corporate income tax.

We intend to operate in a manner so as to maintain our qualification as a REIT for U.S. federal income tax purposes. In order to maintain our qualification as a REIT, we generally are required to distribute at least 90% of our REIT taxable income, determined without regard to the dividends paid deduction and excluding any net capital gain, each year to our stockholders. To the extent that we satisfy this distribution requirement, but distribute less than 100% of our REIT taxable income, we will be subject to U.S. federal corporate income tax on our undistributed taxable income. In addition, we will be subject to a 4% nondeductible excise tax if the actual amount that we pay out to our stockholders in a calendar year is less than a minimum amount specified under the Code.

REIT distribution requirements could adversely affect our liquidity and may force us to borrow funds or sell assets during unfavorable market conditions.

To satisfy the REIT distribution requirements, we may need to borrow funds on a short-term basis or sell assets sooner than anticipated, even if the then-prevailing market conditions are not favorable for these borrowings or sales. Our cash flows from operations may be insufficient to fund required distributions as a result of differences in timing between the actual receipt of income and the recognition of income for U.S. federal income tax purposes, or the effect of non-deductible capital expenditures, the creation of reserves or required debt service or amortization payments. In addition, we may recognize significant cancellation of indebtedness income or gain from the workout of our debt or the disposition of our assets in foreclosure or deed-in-lieu transactions, which will result in the receipt of taxable income in excess of the cash received, if any, from those transactions. The insufficiency of our cash flows to cover our distribution requirements could have an adverse impact on our ability to raise short- and long-term debt or sell equity securities in order to fund distributions required to maintain our qualification as a REIT.

The prohibited transactions tax may limit our ability to dispose of our assets, and we could incur a material tax liability if the Internal Revenue Service successfully asserts that the 100% prohibited transaction tax applies to some of or all our dispositions.

A REIT’s net income from prohibited transactions is subject to a 100% tax. In general, prohibited transactions are sales or other dispositions of assets, other than foreclosure property, held primarily for sale to customers in the ordinary course of business. We may be subject to the prohibited transactions tax equal to 100% of net gain upon a disposition of an asset. As part of our plan to liquidate our portfolio, we intend to make dispositions of our assets in the future. Although a safe harbor to the characterization of the sale of property by a REIT as a prohibited transaction is available, some or all of our future dispositions may not qualify for that safe harbor. We intend to avoid disposing of property that may be characterized as held primarily for sale to customers in the ordinary course of business. To avoid the prohibited transaction tax, we may choose not to engage in certain sales of our assets or may conduct such sales through a TRS, which would be subject to U.S. federal, state and local income taxation. Moreover, no assurance can be provided that the Internal Revenue Service (“IRS”) will not assert that some or all of our future dispositions are subject to the 100% prohibited transactions tax. If the Internal Revenue Service (“IRS”) successfully imposes the 100% prohibited transactions tax on some or all of our dispositions, the resulting tax liability could be material.

The stock ownership limit imposed by the Code for REITs and our charter may restrict our business combination opportunities and you may be restricted from acquiring or transferring certain amounts of our common stock.

The stock ownership restrictions of the Code for REITs and the 9.8% stock ownership limit in our charter may restrict our business combination opportunities and restrict your ability to acquire or transfer certain amounts of our common stock.

In order to maintain our qualification as a REIT for each taxable year, five or fewer individuals, as defined in the Code, may not own, beneficially or constructively, more than 50% in value of our issued and outstanding capital stock at any time during the last half of a taxable year. Attribution rules in the Code determine if any individual or entity beneficially or constructively owns our capital stock under this requirement. Additionally, at least 100 persons must beneficially own our capital stock during at least 335 days of a taxable year for each taxable year. To help ensure that we meet these tests, our charter restricts the acquisition and ownership of shares of our capital stock. However, these ownership limits might delay or prevent a transaction or a change in our control or other business combination opportunities.

Our charter authorizes our directors to take such actions as are necessary and desirable to preserve our qualification as a REIT. Unless exempted by our board of directors (prospectively or retroactively), our charter prohibits any person from beneficially or constructively owning more than 9.8% in value or number of shares, whichever is more restrictive, of the outstanding shares of any class or series of our capital stock. Our board of directors may not grant an exemption from these restrictions to any proposed transferee whose ownership in excess of 9.8% of the value of our outstanding shares would result in our failing to qualify as a REIT. These restrictions on transferability and ownership will not apply, however, if our board of directors determines that it is no longer in our best interest to attempt to, or continue to, qualify as a REIT or that compliance is no longer required in order for us to maintain our qualification as a REIT.

Dividends payable by REITs do not qualify for the reduced tax rates available for some dividends.

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

Complying with REIT requirements may limit our ability to hedge effectively.

The REIT provisions of the Code may limit our ability to hedge the risks inherent to our operations. Under current law, any income that we generate from derivatives or other transactions intended to hedge our interest rate risk with respect to borrowings made, or to be made, to acquire or carry real estate assets generally will not constitute gross income for purposes of the 75% and 95% income tests applicable to REITs. In addition, any income from certain other qualified hedging transactions would generally not constitute gross income for purposes of both the 75% and 95% income tests. However, we may be required to limit the use of hedging techniques that might otherwise be advantageous, which could result in greater risks associated with interest rate or other changes than we would otherwise incur.

We may be subject to adverse legislative or regulatory tax changes that could reduce the value of our common stock.

At any time, the U.S. federal income tax laws governing REITs or the administrative interpretations of those laws may be amended. We cannot predict when or if any new U.S. federal income tax law, regulation, or administrative interpretation, or any amendment to any existing federal income tax law, regulation or administrative interpretation, will be adopted, promulgated or become effective and any such law, regulation, or interpretation may take effect retroactively. We and our stockholders could be adversely affected by any such change in, or any new, U.S. federal income tax law, regulation or administrative interpretation. In addition, the law relating to the tax treatment of other entities, or an investment in other entities, could change, making an investment in such other entities more attractive relative to an investment in a REIT.

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

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

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

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

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

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

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

- eliminating the corporate alternative minimum tax.

Many of these changes that are applicable to us were effective beginning with our 2018 taxable year, without any transition periods or grandfathering for existing transactions. The legislation is unclear in many respects and could be subject to potential amendments and technical corrections, as well as interpretations and implementing regulations by the IRS and the U.S. Department of the Treasury, any of which could lessen or increase the impact of the legislation. In addition, it is unclear how these U.S. federal income tax changes will affect state and local taxation, which often uses federal taxable income as a starting point for computing state and local tax liabilities. While some of the changes made by the tax legislation may adversely affect us in one or more reporting periods and prospectively, other changes may be beneficial on a going forward basis. We continue to work with our tax advisors and auditors to determine the full impact that the 2017 Tax Legislation as a whole will have on us.

The ability of our board of directors to revoke our REIT qualification without stockholder approval may cause adverse consequences to our stockholders.

Our charter provides that our board of directors may revoke or otherwise terminate our REIT election, without the approval of our stockholders, if it determines that it is no longer in our best interest to attempt to, or continue to qualify as a REIT. If we cease to be a REIT, we would become subject to U.S. federal income tax on our taxable income and would no longer be required to distribute most of our taxable income to our stockholders, which may have adverse consequences on our total return to our stockholders.

Changes to U.S. federal income tax laws could materially and adversely affect us and our stockholders.

The 2017 Tax Legislation makes substantial changes to the Code. Among those changes are a significant permanent reduction in the generally applicable corporate tax rate, changes in the taxation of individuals and other non-corporate taxpayers that generally but not universally reduce their taxes on a temporary basis subject to ‘‘sunset’’ provisions, the elimination or modification of various currently allowed deductions (including substantial limitations on the deductibility of interest and, in the case of individuals, the deduction for personal state and local taxes), and preferential rates of taxation on most ordinary REIT dividends and certain business income derived by non-corporate taxpayers in comparison to other ordinary income recognized by such taxpayers. The 2017 Tax Legislation also imposes certain additional limitations on the deduction of net operating losses, which may in the future cause us to be required to make distributions that will be taxable to our stockholders to the extent of our current or accumulated earnings and profits in order to comply with the annual REIT distribution requirements. The effect of these, and the many other, changes made in the 2017 Tax Legislation is highly uncertain, both in terms of their direct effect on the taxation of an investment in our common stock and their indirect effect on the value of our assets or market conditions generally. Furthermore, many of the provisions of the 2017 Tax Legislation will require guidance through the issuance of Treasury regulations in order to assess their effect. There may be a substantial delay before such regulations are promulgated, increasing the uncertainty as to the ultimate effect of the statutory amendments on us. It is also likely that there will be technical corrections legislation proposed with respect to the 2017 Tax Legislation this year, the effect of which cannot be predicted and may be adverse to us or our stockholders.

Additionally, the rules dealing with U.S. federal income taxation are continually under review by Congress, the IRS, and the U.S. Department of the Treasury. Any such changes could have an adverse effect on an investment in our shares or on the market value or the resale potential of our assets.

Risks Related to Ownership of Our Common Stock and Our Corporate Structure

There is no established public market for our shares and you may not be able to sell your shares.

Presently, we have no plans to list our shares of common stock on any securities exchange or other market, there is no established trading market for our shares, nor is there any assurance that one may develop. Our charter also prohibits the ownership of more than 9.8% (in value or number of shares, whichever is more restrictive) of the aggregate of the outstanding shares of any class or series of our capital stock by any person unless exempted prospectively or retroactively by our board. This may inhibit investors from purchasing a large portion of our shares. Our charter also does not require us to seek stockholder approval to liquidate our assets by a specified date, nor does our charter require us to list our shares for trading on a securities exchange or other market by a specified date or provide any other type of liquidity to our stockholders. Therefore, it will be difficult for you to sell your shares promptly or at all, including in the event of an emergency, and if you are able to sell your shares, you may have to sell them at a substantial discount from the estimated value per share.

The estimated value per share of our common stock is based on a number of assumptions and estimates that may not be accurate or complete and is also subject to a number of limitations.

On January 13, 2020, we announced an estimated value of our common stock equal to $0.36 per share. Our board of directors engaged Real Globe Advisors, LLC ("Real Globe"), an independent third-party real estate advisory firm, to estimate the per share value of our common stock on a fully diluted basis as of December 31, 2019. As with any methodology used to estimate value, the methodology employed by Real Globe and the recommendations made by us were based upon a number of estimates and assumptions that may not be accurate or complete. Further, different parties using different assumptions and estimates could derive a different estimated value per share, which could be significantly different from our estimated value per share. The estimated per share value does not represent (i) the amount at which our shares would trade at a national securities exchange, (ii) the amount a stockholder would obtain if he or she tried to sell his or her shares (iii) the amount per share that stockholders would receive in a sale of the entire Company in a single transaction or (iv) the amount stockholders would receive if we liquidated our assets and distributed the proceeds after paying all of our expenses and liabilities. Accordingly, with respect to the estimated value per share, we can give no assurance that:

- a stockholder would be able to resell his or her shares at this estimated value;
- a stockholder would ultimately realize distributions per share equal to our estimated value per share upon liquidation of our assets and settlement of our liabilities or a sale of the Company;
- our shares would trade at a price equal to or greater than the estimated value per share if we listed them on a national securities exchange;
- the certain estimated corporate-level transaction costs that we would expect to incur in connection with a future potential liquidity event reflected in our estimated value will be incurred at the level estimated by us; or
- the methodology used to estimate our value per share would be acceptable to FINRA or that the estimated value per share will satisfy the applicable annual valuation requirements under the Employee Retirement Income Security Act of 1974, as amended ("ERISA") and the Code, with respect to employee benefit plans subject to ERISA and other retirement plans or accounts subject to Section 4975 of the Code.

Our cash available for distribution to stockholders may not be sufficient to pay distributions at expected or required levels, and we may need external sources in order to make such distributions, or we may not be able to make such distributions at all.

We generally intend over time to make annual distributions in an amount at least equal to the amount that will allow us to qualify as a REIT and to avoid current entity-level U.S. federal income taxes, however, we may not have sufficient cash from operations to make a distribution required to maintain our qualification as a REIT. All distributions will be made at the discretion of our board of directors and will depend on our historical and projected results of operations, liquidity and financial condition, REIT qualification, debt service requirements, capital expenditures and operating expenses, prohibitions and other restrictions under financing arrangements and applicable law and other factors as our board of directors may deem relevant from time to time. No assurance can be given that our projections will prove accurate or that any level of distributions will be made or sustained or achieve a market yield.

We may pay distributions from sources other than cash flow from operations or funds from operations, including funding such distributions from external financing sources, which may be available only at commercially unattractive terms, if at all. To the extent that the aggregate amount of cash distributed in any given year exceeds the amount of our current and accumulated earnings and profits for the same period, the excess amount will be deemed a return of capital for U.S. federal income tax purposes, rather than a return on capital. Furthermore, in the event that we are unable to fund future distributions from our cash flows from operating activities, the value of your shares, the sale of our assets or any other liquidity event may be materially adversely affected.

At any time that we are not generating cash flow from operations sufficient to cover the current distribution rate, we may determine to pay lower distributions, or to fund all or a portion of our future distributions from other sources. If we utilize borrowings for the purpose of funding all or a portion of our distributions, we will incur additional interest expense. We have not established any limit on the extent to which we may use alternate sources of cash for distributions, except that, in accordance with the law of the State of Maryland and our organizational documents, generally, we may not make distributions that would: (i) cause us to be unable to pay our debts as they become due in the usual course of business, (ii) cause our total assets to be less than the sum of our total liabilities, or (iii) jeopardize our ability to maintain our qualification as a REIT for so long as the board of directors determines that it is in our best interests to continue to qualify as a REIT. Distributions that exceed cash flow from operations may not be sustainable at current levels, or at all.

Future issuances of debt securities, which would rank senior to our common stock upon our liquidation, and future issuances of equity securities, which would dilute the holdings of our existing common stockholders and may be senior to our common stock for the purposes of making distributions, periodically or upon liquidation, may negatively affect the value of our common stock.

In the future, we may issue debt or equity securities or incur other borrowings. Upon our liquidation, holders of our debt securities and other loans and preferred stock will receive a distribution of our available assets before common stockholders. If we incur debt in the future, our future interest costs could increase, and adversely affect our liquidity and results of operations. We are not required to offer any additional equity securities to existing common stockholders on a preemptive basis. Therefore, additional common stock issuances, directly or through convertible or exchangeable securities, warrants or options, will dilute the holdings of our existing common stockholders and such issuances, or the perception of such issuances, may reduce the value of our common stock. Our preferred stock, if issued, would likely have a preference on distribution payments, periodically or upon liquidation, which could eliminate or otherwise limit our ability to make distributions to common stockholders. Because our decision to issue debt or equity securities or incur other borrowings in the future will depend on market conditions and other factors beyond our control, we cannot predict or estimate the amount, timing, nature or success of our future capital raising efforts. Thus, common stockholders bear the risk that our future issuances of debt or equity securities or our incurrence of other borrowings will negatively affect the value of our common stock.

Your percentage ownership in us may be diluted in the future.

Your percentage ownership in us may be diluted in the future because of new equity issuances, capital market transactions or otherwise, including, without limitation, equity awards that may be granted to our directors, officers and employees.

Increases in market interest rates may reduce demand for our common stock and result in a decline in the value of our common stock.

The value of our common stock may be influenced by the dividend yield on our common stock (i.e., the amount of our annual distributions as a percentage of the fair market value of our common stock) relative to market interest rates. An increase in market interest rates, which are currently low compared to historical levels, may lead prospective purchasers of our common stock to expect a higher distribution yield, which we may not be able, or may choose not, to provide. Higher interest rates would also likely increase our borrowing costs and decrease our operating results and cash available for distribution. Thus, higher market interest rates could cause the value of our common stock to decline.

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

Under Maryland law generally, a director is required to perform his or her duties in good faith, in a manner he or she reasonably believes to be in our best interests and with the care that an ordinarily prudent person in a like position would use under similar circumstances. Under Maryland law, directors are presumed to have acted in accordance with this standard of conduct. In addition, our charter eliminates the liability of our directors and officers to us and our stockholders for money damages, except for liability resulting from:

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

Our charter authorizes us to obligate ourselves and our bylaws obligate us, to the maximum extent permitted by Maryland law in effect from time to time, to indemnify and to pay or reimburse reasonable expenses in advance of final disposition of a proceeding to any present or former director or officer who is made or threatened to be made a party to the proceeding by reason of his or her service to us in that capacity and certain other capacities. As a result, we and our stockholders may have more limited rights against our directors and officers than might otherwise exist absent the current provisions in our charter and bylaws.

Certain provisions of Maryland law could inhibit changes in control.

Certain provisions of the Maryland General Corporation Law ("MGCL"), may have the effect of deterring a third party from making a proposal to acquire us or of impeding a change in our control under circumstances that otherwise could provide the holders of our common stock with the opportunity to benefit from a sale of our common stock, including:

- "business combination" provisions that, subject to limitations, prohibit certain business combinations between us and an "interested stockholder" (defined generally as any person who beneficially owns, directly or indirectly, 10% or more of the voting power of our outstanding voting stock or an affiliate or associate of ours who was the beneficial owner, directly or indirectly, of 10% or more of the voting power of our then outstanding voting stock at any time within the two-year period immediately prior to the date in question) for five years after the most recent date on which the stockholder becomes an interested stockholder, and thereafter impose fair price and/or supermajority stockholder voting requirements on these combinations; and

- "control share" provisions that provide that "control shares" of our company (defined as voting shares that, when aggregated with other shares controlled by the stockholder, entitle the stockholder to exercise one of three increasing ranges of voting power in electing directors) acquired in a "control share acquisition" (defined as the direct or indirect acquisition of ownership or control of issued and outstanding control shares) have no voting rights except to the extent approved by our stockholders by the affirmative vote of at least two-thirds of all the votes entitled to be cast on the matter, excluding all interested shares.

As permitted by Maryland law, we have elected, by resolution of our board of directors, to opt out of the business combination provisions of the MGCL, with respect to business combinations that have been approved by our board of directors (including a majority of directors who are not affiliated with the interested stockholder), and, pursuant to a provision in our bylaws, to exempt any acquisition of our stock from the control share provisions of the MGCL. However, our board of directors may by resolution elect to repeal the exemption from the business combination provisions of the MGCL and may by amendment to our bylaws opt into the control share provisions of the MGCL at any time in the future.

If we have a class of equity securities registered under the Exchange Act and at least three independent directors, certain provisions of the MGCL permit our board of directors, without stockholder approval and regardless of what is currently provided in our charter or bylaws, to adopt certain governance provisions, some of which (for example, a classified board) we do not have. These provisions may have the effect of limiting or precluding a third party from making an acquisition proposal for us or of delaying, deferring or preventing a change in our control under circumstances that otherwise could provide the holders of our common stock with the opportunity to benefit from a sale of our common stock. Our charter contains a provision whereby we elect, at such time as we become eligible to do so, to be subject to the provisions of Title 3, Subtitle 8 of the MGCL relating to the filling of vacancies on our board of directors.

If our board of directors were to elect to be subject to the provision of Subtitle 8 providing for a classified board or the business combination provisions of the MGCL or if the provision of our bylaws opting out of the control share acquisition provisions of the MGCL were amended or rescinded, these provisions of the MGCL could have anti-takeover effects.

All of our assets are owned by subsidiaries. We depend on dividends and distributions from these subsidiaries. The creditors of these subsidiaries are entitled to amounts payable to them by the subsidiaries before the subsidiaries may pay any dividends or other distributions to us.

All of our assets are held through subsidiaries. We depend on cash distributions from our subsidiaries for substantially all of our cash flow. The creditors of each of our subsidiaries are entitled to payment of that subsidiary's obligations to them when due and payable before that subsidiary may make distributions or dividends to us. Thus, our ability to pay dividends, if any, to our stockholders depends on our subsidiaries' ability to first satisfy their obligations to their creditors and our ability to satisfy our obligations, if any, to our creditors.

In addition, our participation in any distribution of the assets of any of our subsidiaries upon the liquidation, reorganization or insolvency of the subsidiary, is only after the claims of the creditors, including trade creditors and preferred stockholders, if any, of the applicable direct or indirect subsidiaries are satisfied.

Our charter places limits on the amount of common stock that any person may own.

In order for us to maintain our qualification as a REIT under the Code, no more than 50% of the outstanding shares of our common stock may be beneficially owned, directly or indirectly, by five or fewer individuals at any time during the last half of each taxable year (other than the first taxable year for which an election to be a REIT has been made). Unless exempted by our board of directors, prospectively or retroactively, our charter prohibits any person or group from owning more than 9.8% in value or in number of shares, whichever is more restrictive, of the outstanding shares of any class or series of our capital stock. These provisions may have the effect of delaying, deferring or preventing a change in control of us, including an extraordinary transaction such as a merger, tender offer or sale of all or substantially all of our assets that might involve a premium price for holders of our common stock.

If anyone transfers shares in a way that would violate the ownership limit, or prevent us from maintaining our qualification as a REIT under the U.S. federal income tax laws, those shares instead will be transferred to a trust for the benefit of a charitable beneficiary and will be either purchased by us or sold to a person whose ownership of the shares will not violate the ownership limit. If this transfer to a trust fails to prevent such a violation or our continued qualification as a REIT, then the initial intended transfer shall be null and void from the outset. The intended transferee of those shares will be deemed never to have owned the shares. Anyone who acquires shares in violation of the ownership limit or the other restrictions on transfer in our charter bears the risk of suffering a financial loss when the shares are sold if the value of our shares falls between the date of purchase and the date of redemption or sale.

Our charter permits our board of directors to authorize the issuance of preferred stock on terms that may subordinate the rights of the holders of our current common stock or discourage a third party from acquiring us.

Our board may classify or reclassify any unissued shares of common or preferred stock into other classes or series of stock and establish the preferences, conversion or other rights, voting powers, restrictions, limitations as to dividends and other distributions, qualifications, and terms or conditions of redemption of the stock and may amend our charter from time to time to increase or decrease the aggregate number of shares or the number of shares of any class or series that we have authority to issue without stockholder approval. Thus, our board of directors could authorize us to issue shares of preferred stock with terms and conditions that could subordinate the rights of the holders of our common stock or shares of preferred stock or common stock that could have the effect of delaying, deferring or preventing a change in control of us, including an extraordinary transaction such as a merger, tender offer or sale of all or substantially all of our assets, that might provide a premium price for holders of our common stock.

Our conflict of interest policy may not be successful in eliminating the influence of future conflicts of interest that may arise between us and our directors, officers and employees.

We have adopted a policy that any transaction, agreement or relationship in which any of our directors, officers or employees has a material direct or indirect pecuniary interest must be approved by a majority of our disinterested directors. Other than this policy, however, we may not adopt additional formal procedures for the review and approval of conflict of interest transactions generally. As such, our policies and procedures may not be successful in eliminating the influence of conflicts of interest.

Our board of directors may change our investment strategy without stockholder approval, which could alter the nature of your investment.

Our investment strategy may change over time. The methods of implementing our investment strategy may also vary, as new investment techniques are developed. Our investment strategy, the methods for implementing them, and our other objectives, policies and procedures may be altered by a majority of the directors without the approval of our stockholders. As a result, the nature of your investment could change without your consent. A change in our investment strategy may, among other things, increase our exposure to interest rate risk, default risk and commercial real property market fluctuations, all of which could materially and adversely affect our ability to achieve our investment objectives.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

As of December 31, 2019, the Company owned 20 revenue-producing assets and one parcel of unimproved land.

General

The following is a list of the assets in the Highlands portfolio as of December 31, 2019.

Property Name	Location	Segment	Classification	Total Gross Leasable Area (GLA) (in square feet)	Percentage of Economic Occupancy (a)	Annualized Base Rent (b) (in thousands)	Annualized Base Rent per Leased Square Foot (c)	Significant Tenants (e)
Buerger Brothers Lofts	Denver, CO	Multi-Family	Multi-Family	39,961	97.79%	$ 664	$ 16.98	n/a
Chamber Lofts	Denver, CO	Multi-Family	Multi-Family	39,259	100.00%	801	20.41	n/a
The Lafayette	Denver, CO	Multi-Family	Multi-Family	25,575	97.46%	647	25.97	n/a
Kenilworth Court	Denver, CO	Multi-Family	Multi-Family	16,611	96.81%	422	26.21	n/a
1620 Central Street	Evanston, IL	Multi-Family	Multi-Family	51,808	98.57%	1,471	28.80	n/a
The Detroit and Detroit Terraces	Denver, CO	Multi-Family	Multi-Family	41,594	98.75%	1,235	30.06	n/a
The View	San Diego, CA	Multi-Family	Multi-Family	39,995	93.32%	1,103	29.55	n/a
Tennyson44	Denver, CO	Multi-Family	Multi-Family	34,680	94.77%	931	28.32	n/a
The Locale (formerly Evolve at Allendale)	Allendale, MI	Multi-Family	Multi-Family	239,379	98.16%	3,839	16.34	n/a
The Muse	Denver, CO	Multi-Family	Multi-Family	103,628	90.32%	2,654	28.35	n/a
Versacold USA - St. Paul	St. Paul, MN	Net Lease	Industrial	219,664	100.00%	1,225	5.58	Versacold USA, Inc.
Versacold USA - New Ulm	New Ulm, MN	Net Lease	Industrial	269,985	100.00%	903	3.35	Versacold USA, Inc.
Trimble	San Jose, CA	Multi-Tenant Office	Multi-Tenant Office	176,905	—%	—	—	n/a
Hudson Correctional Facility	Hudson, CO	Net Lease	Correctional Facility	301,029	100.00% (f)	10,166	33.77	The GEO Group, Inc.
Citizens - Providence	Providence, RI	Net Lease	Bank Branch	51,136	—%	—	—	n/a
Palazzo Land	Orlando, FL	Other	Unimproved Land	n/a	n/a	n/a	n/a	n/a
Shops at Sherman Plaza (d)	Evanston, IL	Retail	Retail	151,752	89.73%	3,122	22.93	Fitness International; Barnes & Noble; Target
Market at Hilliard	Hilliard, OH	Retail	Retail	115,221	94.51%	1,670	15.34	Aldi; Michaels; Office Max; Old Navy
State Street Market	Rockford, IL	Retail	Retail	193,657	100.00%	1,833	9.47	Burlington Coat Factory; Dick's Sporting Goods; PetsMart
Buckhorn Plaza	Bloomsburg, PA	Retail	Retail	86,835	93.90%	1,041	12.76	Marmaxx Operating; Dollar Tree
Total				2,198,674	87.38%	$ 33,727	$ 17.56	

(a) Economic occupancy is defined as the percentage of total gross leasable area for which a tenant is obligated to pay rent under the terms of its lease agreement, regardless of the actual use or occupation by that tenant of the area being leased.

(b) Annualized base rent per leased square foot is computed as revenue for the last month of the period multiplied by twelve months. Annualized rent includes the effect of rent abatements, lease inducements, and straight-line rent GAAP adjustments.

(c) Annualized base rent per leased square foot is computed as annualized base rent divided by the total occupied square footage at the end of the period.

(d) A portion of the land underlying this asset is subject to a ground lease. The term of the lease expires in October 2042, and the monthly payment as of December 31, 2019 is $1,749.

(e) Several of our assets have one or more tenants responsible for more than 10% of the asset's gross leasable area.

(f) The lease on this property expired in January of 2020 and the tenant has vacated the facility.

The following table sets forth our total gross leasable area ("GLA") in square feet, percentage of economic occupancy and average annual base rent per leased square foot for our portfolio as of December 31 for the last three years:

As of	Total GLA (Sq. Ft.)	Percentage of Economic Occupancy	Average Annual Base Rent per Leased Square Foot
December 31, 2019	2,198,674	87.4%	$17.56
December 31, 2018	2,197,614	91.5%	$15.77
December 31, 2017	2,663,508	83.7%	$15.48

Hudson Correctional Facility and Sherman Plaza accounted for 10% or more of our total revenues for the year ended December 31, 2019.

The Muse accounted for 10% or more of our total assets as of December 31, 2019.

Hudson Correctional Facility

As of December 31, 2019, 2018 and 2017, the total GLA for Hudson Correctional Facility was 301,029 square feet, the economic occupancy was 100% and the average annual base rent per leased square foot was $33.77.

As of December 31, 2019, Hudson Correctional Facility has one tenant, The Geo Group, Inc., a correctional facility operator, whose economic occupancy was 100% of the total gross leasable square feet. Its annualized base rent was $10.2 million. The GEO Group, Inc. vacated the building upon their lease expiration in January 2020.

Sherman Plaza

The following table sets forth the GLA in square feet, percentage of economic occupancy and average annual base rent per leased square foot for Sherman Plaza as of December 31 for the last three years:

As of	Total GLA (Sq. Ft.)	Percentage of Economic Occupancy	Average Annual Base Rent per Leased Square Foot
December 31, 2019	151,752	89.7%	$22.93
December 31, 2018	151,752	95.0%	$22.85
December 31, 2017	152,786	94.0%	$20.03

Significant tenants based on annualized base rent as of December 31, 2019 include Fitness International, Target and Barnes and Noble Booksellers.

The Muse

The following table sets forth the GLA in square feet, percentage of economic occupancy and average annual base rent as of December 31, 2019. The Muse, a newly developed property, was acquired by the Company on October 24, 2019.

As of	Total GLA (Sq. Ft.)	Percentage of Economic Occupancy	Average Annual Base Rent per Leased Square Foot
December 31, 2019	103,628	90.3%	$28.35

Lease Expirations

The following table sets forth lease expirations for all of our assets as of December 31, 2019, assuming none of the tenants exercise renewal options:

Lease Expiration Year	Number of Expiring Leases	GLA of Expiring Leases (Sq. Ft.)	Annualized Rent of Expiring Leases (in thousands)	Percent of Total Leased Area	Percent of Total Annualized Rent	Expiring Rent/Square Foot
2020	10	349,150	$ 10,727	26.3%	52.1%	$ 30.72
2021	5	116,633	1,714	8.8%	8.3%	14.70
2022	5	156,825	2,217	11.8%	10.8%	14.14
2023	4	11,155	181	0.8%	0.9%	16.22
2024	5	48,148	785	3.6%	3.8%	16.31
2025	8	48,647	671	3.7%	3.3%	13.80
2026	4	20,191	428	1.5%	2.1%	21.22
2027	4	499,036	2,449	37.7%	11.9%	4.91
2028	4	36,159	790	2.7%	3.8%	21.86
2029	3	30,842	444	2.3%	2.2%	14.38
Month to Month	2	11,125	167	0.8%	0.8%	15.04
Thereafter	—	—	—	—%	—%	—
	54	1,327,911	$ 20,573	100.0%	100.0%	$ 15.49

Mortgage Financing

The table below sets forth all material mortgages or other liens or encumbrances against any of our assets as of December 31, 2019. As of such date, none of this mortgage debt was recourse to the Company, although we have provided certain customary, non-recourse carve-out guarantees in connection with obtaining mortgage loans on certain of our properties.

Property	Current Principal amount (in thousands)	Interest and Amortization Provisions	Interest Rate	Prepayment Provisions	Maturity Date
Market at Hilliard	$15,511	Fixed Interest-Only for first 12 months	4.70%	If prior to 9/6/2026 must be in full, with penalty	12/6/2026
State Street Market	$9,166	Fixed Principal Plus Interest	5.24%	Only in full, and if prior to 1/6/22, with penalty	4/6/2022
Buckhorn Plaza	$10,142	Fixed Interest-Only for first 12 months	4.35%	If prior to 8/6/2026 must be in full, with penalty	11/6/2026
The Detroit and Detroit Terraces	$11,449	Interest-Only	3.99%	If prior to 9/1/2027 must be in full, with penalty	9/1/2027
The Locale (formerly Evolve at Allendale)	$18,658	Variable Interest	3.28%	If prior to 9/1/2023 must be in full, with penalty	9/1/2023

Item 3. Legal Proceedings

We are from time to time involved in legal actions arising in the ordinary course of business. We are not currently involved in any legal or administrative proceedings that we believe are likely to have a material adverse effect on our business, results of operations or financial condition.

Item 4. Mine Safety Disclosures

Not applicable.

Part II.

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

Market Information

Our shares of common stock are not listed on a national securities exchange and there is not otherwise an established public trading market for our shares. We publish an estimated per share value of our common stock to assist broker dealers to comply with the rules published by the Financial Industry Regulatory Authority (“FINRA”). On January 13, 2020, we announced an estimated value of our common stock as of December 31, 2019 equal to $0.36 per share on a fully diluted basis.

Our board of directors (the “Board”) engaged Real Globe Advisors, LLC (“Real Globe”), an independent third-party real estate advisory firm, to estimate the per share value of our common stock on a fully diluted basis as of December 31, 2019. Real Globe has extensive experience estimating the fair values of commercial real estate. The report furnished to the Board and the audit committee of the Board (the “Audit Committee”) by Real Globe complies with the reporting requirements set forth under Standard Rule 2-2(a) of the Uniform Standards of Professional Appraisal Practice and is certified by a member of the Appraisal Institute with the MAI designation. The Real Globe report, dated as of January 6, 2020, reflects values as of December 31, 2019. Real Globe does not have any direct or indirect interests in any transaction with us or in any currently proposed transaction to which we are a party, and there are no conflicts of interest between Real Globe, on one hand, and the Company or any of our directors, on the other.

To estimate our per share value, Real Globe utilized the “net asset value” or “NAV” method which is based on the fair value of real estate, and all other assets, less the fair value of total liabilities, and also included certain estimated corporate-level transaction costs that we would expect to incur in connection with a future potential liquidity event, further described below. The fair value estimate of our real estate assets is equal to the sum of the individual real estate values.

Generally, Real Globe estimated the value of our real estate, using a discounted cash flow, or “DCF”, of projected net operating income, less capital expenditures, for the ten-year period ending December 31, 2029 and applying a market supported discount rate and capitalization rate. In the unique instances that a discounted cash flow methodology was not deemed to be the most appropriate valuation methodology, including, but not limited to, the valuation of land assets, a sales comparison approach was utilized. For all other assets, comprised of working capital (which includes cash and other current assets net of current liabilities), fair value was determined separately. Real Globe also estimated the fair value of our long-term debt obligations by comparing market interest rates to the contract rates on our long-term debt and discounting to present value the difference in future payments.

The estimate of certain corporate-level transaction costs was provided to Real Globe by the Company. Given that our strategy involves a future potential liquidity option for current stockholders, management and the Board determined that the deduction of certain estimated corporate-level transaction costs in connection therewith was appropriate in determining our new estimated per share value. However, there are no assurances that such costs will be incurred at the level estimated by us. We cannot predict the timing of any potential liquidity event. As a result, the actual fees and expenses incurred by us in connection with the execution of our strategy could differ materially from the amount provided to Real Globe.

Real Globe determined NAV in a manner consistent with the definition of fair value under U.S. generally accepted accounting principles (or “GAAP”) set forth in Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 820 Fair Measurements and Disclosures. Other than the deduction of certain estimated corporate-level transaction costs that we would expect to incur in connection with a future potential liquidity event, the net asset valuation performed by Real Globe complies with the Investment Program Association Practice Guideline 2013-01 “Valuation of Publicly Registered Non-Listed REITS”, dated April 29, 2013.

Generally, net asset value per share was estimated by subtracting the fair value of our total liabilities from the fair value of our total assets and dividing the result by the number of common shares outstanding on a fully diluted basis as of December 31, 2019. Real Globe then applied a discount rate and terminal capitalization rate sensitivity analysis by adding and subtracting 50 basis points to the terminal capitalization rate and discount rate for assets where the concluded value was solely derived based on the discounted cash flow methodology, resulting in a value range equal to $0.37 - $0.44 per share on a fully diluted basis. The mid-point in the final range was $0.40 per share. For reporting purposes, all per share numbers are rounded to the nearest cent.

On January 8, 2020, the Audit Committee met to review and discuss Real Globe's report. Following this review, and considering management's support of Real Globe's analysis, the Audit Committee unanimously adopted a resolution accepting the Real Globe analysis. The Audit Committee also unanimously adopted a resolution recommending an estimate of per share value as of December 31, 2019 equal to $0.36 per share on a fully diluted basis. At a full meeting of our Board held on January 8, 2020, the Audit Committee made a recommendation to the Board that the Board adopt and the Company publish an estimate of per share value as of December 31, 2019 equal to $0.36 per share on a fully diluted basis. The Board unanimously adopted this recommendation of estimated per share value, which falls within the range of per share net asset values for the Company's common stock that Real Globe provided in its report.

The following table shows a sensitivity range for estimated share price and terminal capitalization and discount rates:

	Range of Value and Rates		
	Not Including Certain Estimated Corporate-Level Transaction Costs		
	Low	**Midpoint**	**High**
Share Price	$0.37	$0.40	$0.44
Terminal Capitalization Rate	6.77%	6.27%	5.77%
Discount Rate	7.73%	7.23%	6.73%

In order to estimate the final range of value, Real Globe deducted $0.03 of certain estimated corporate-level transaction costs that were provided by the Company from the range of value above. The following chart presents the resulting final range of values, net of certain estimated corporate-level transaction costs that the Company would expect to incur in connection with a future potential liquidity event.

	Final Range of Value
	Share Price
Low	$0.34
Midpoint	$0.37
High	$0.41

As with any methodology used to estimate value, the methodology employed by Real Globe and the recommendations made by us were based upon a number of estimates and assumptions that may not be accurate or complete. Further, different parties using different assumptions and estimates could derive a different estimated value per share, which could be significantly different from our estimated value per share. The estimated per share value does not represent (i) the amount at which our shares would trade at a national securities exchange, (ii) the amount a stockholder would obtain if he or she tried to sell his or her shares (iii) the amount per share that stockholders would receive in a sale of the entire Company in a single transaction or (iv) the amount stockholders would receive if we liquidated our assets and distributed the proceeds after paying all of our expenses and liabilities. Accordingly, with respect to the estimated value per share, we can give no assurance that:

- a stockholder would be able to resell his or her shares at this estimated value;
- a stockholder would ultimately realize distributions per share equal to our estimated value per share upon liquidation of our assets and settlement of our liabilities or a sale of the Company;
- our shares would trade at a price equal to or greater than the estimated value per share if we listed them on a national securities exchange;
- the certain estimated corporate-level transaction costs that we would expect to incur in connection with a future potential liquidity event reflected in our estimated value will be incurred at the level estimated by us; or
- the methodology used to estimate our value per share would be acceptable to FINRA or that the estimated value per share will satisfy the applicable annual valuation requirements under the Employee Retirement Income Security Act of 1974, as amended ("ERISA") and the Code, with respect to employee benefit plans subject to ERISA and other retirement plans or accounts subject to Section 4975 of the Code.

The estimated value per share was approved by our Board on January 8, 2020 and reflects the fact that the estimate was calculated at a moment in time. The value of our shares has changed over time and will be influenced by changes to the value of our individual assets as well as changes and developments in the real estate and capital markets. We currently anticipate publishing a new estimated share value within one year. Nevertheless, stockholders should not rely on the estimated value per share in making a decision to buy or sell shares of our common stock.

Stockholders

As of January 7, 2020, we had 166,422 stockholders of record.

Distributions

For the twelve months ended December 31, 2019 and 2018, no cash distributions were paid by us.

We generally intend over time to make annual distributions in an amount at least equal to the amount that will allow us to qualify as a REIT and to avoid current entity-level U.S. federal income taxes. To qualify as a REIT, we must distribute to our stockholders an amount at least equal to:

i. 90% of our REIT taxable income, determined before the deduction for dividends paid and excluding any net capital gain (which does not necessarily equal net income as calculated in accordance with GAAP); plus

ii. 90% of the excess of our net income from foreclosure property over the tax imposed on such income by the Code; less

iii. any excess non-cash income (as determined under the Code).

Distributions made by us will be authorized and determined by our board of directors, in its sole discretion, out of legally available funds, and will be dependent upon a number of factors, including our actual and projected results of operations, financial condition, cash flows and liquidity, our qualification as a REIT and other tax considerations, capital expenditures and other obligations, debt covenants, contractual prohibitions or other limitations under applicable law and other such matters as our board of directors may deem relevant from time to time. We cannot assure you that our distribution policy will remain the same in the future, or that any estimated distributions will be made or sustained.

Our ability to make distributions to our stockholders will depend upon the performance of our portfolio and our ability to successfully execute on our disposition strategy. Distributions will be made in cash to the extent cash is available for distribution. We may not be able to generate sufficient cash flows to pay distributions to our stockholders. To the extent that our cash available for distribution is less than the amount required to be distributed under the REIT provisions of the Code, we may consider funding sources other than cash flow from operations or funds from operations, which may reduce the amount of capital available for operations, may have negative tax implications, and may have a negative effect on the value of your shares under certain conditions. In addition, our board of directors could change our distribution policy in the future. See “Risk Factors - Risks Related to Our Status as a REIT.”

Recent Sales of Unregistered Securities

None.

Item 6. Selected Financial Data

Not applicable.

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with “Part I-Item 1A. Risk Factors,” “Part I-Item 1. Business,” “Part I-Item 2. Properties” and the historical consolidated financial statements, and related notes included elsewhere in this Annual Report. The following discussion and analysis contains forward-looking statements based upon our current expectations, estimates and assumptions that involve risks and uncertainties. Our actual results could differ materially from those discussed in these forward-looking statements due to a variety of risks, uncertainties and other factors, including but not limited to, factors discussed in “Part I-Item 1A. Risk Factors” and “Disclosure Regarding Forward-Looking Statements.” The following discussion and analysis should be read in *conjunction with the Company's Consolidated Financial Statements and accompanying notes, which appear elsewhere in this Annual Report on Form 10-K.*

Overview

Highlands is a self-advised and self-administered real estate investment trust (“REIT”) created to own and manage substantially all of the “non-core” assets previously owned and managed by our former parent, InvenTrust Properties Corp., a Maryland corporation (“InvenTrust”). On April 28, 2016, Highlands was spun-off from InvenTrust through a pro rata distribution (the “Distribution”) by InvenTrust of 100% of the outstanding shares of our common stock to holders of InvenTrust’s common stock. Prior to or concurrent with the separation, we and InvenTrust engaged in certain reorganization transactions that were designed to consolidate substantially all of InvenTrust’s remaining “non-core” assets in Highlands.

This portfolio of “non-core” assets, which were acquired by InvenTrust between 2005 and 2008, included assets that are special use, single tenant or build to suit; face unresolved legal issues; are in undesirable locations or in weak markets or submarkets; are aging or functionally obsolete; and/or have sub-optimal leasing metrics. A number of our assets are retail properties located in tertiary markets, which are particularly susceptible to the negative trends affecting retail real estate. As a result of these characteristics, such assets are difficult to lease, finance and refinance and are relatively illiquid compared to other types of real estate assets. These factors also significantly limit our asset disposition options, impact the timing of such dispositions and restrict the viable options available to the Company for a future potential liquidity event.

Our strategy is focused on preserving, protecting and maximizing the total value of our portfolio with the long-term objective of providing stockholders with a return of their investment. We engage in rigorous asset management, and seek to sustain and enhance our portfolio, and improve the quality and income-producing ability of our portfolio, by engaging in selective dispositions, acquisitions, capital expenditures, financing, refinancing and enhanced leasing. We are also focused on cost containment efforts across our portfolio, and improving our overall capital structure and making select investments in our existing “non-core” assets to maximize their value. To the extent we are able to generate cash flows from operations or dispositions of assets, in addition to the cash uses outlined above, our board of directors has determined that it is in the best interests of the Company to seek to reinvest in assets that are more likely to generate more reliable and stable cash flows, such as multi-family assets, as part of the Company’s overall strategy to optimize the value of the portfolio, enhance our options for a future potential liquidity event and maximize shareholder value. Given the nature and quality of the “non-core” assets in our portfolio as well as current market conditions, we expect this strategy will take multiple years to develop and execute.

As of December 31, 2019, our portfolio of assets consisted of one office asset, two industrial assets, four retail assets, eleven multi-family assets, one correctional facility, one parcel of unimproved land and one bank branch. References to “Highlands,” “the Company,” “we” or “us” are to Highlands REIT, Inc., as well as all of Highlands' wholly-owned and consolidated subsidiaries.

We currently have four business segments, consisting of (i) net lease, (ii) retail, (iii) multi-tenant office and (iv) multi-family. Our unimproved land asset is presented in “other.” We may have additional or fewer segments in the future to the extent we enter into additional real property sectors, dispose of property sectors, or change the character of our assets. For the complete presentation of our reportable segments, see Note 11 to our consolidated financial statements for the years ended December 31, 2019 and 2018.

Basis of Presentation

The accompanying consolidated financial statements reflect the accounts of Highlands and its consolidated subsidiaries (collectively, the “Company”). Highlands consolidates its wholly-owned subsidiaries and any other entities which it controls (i) through voting rights or similar rights or (ii) by means other than voting rights if Highlands is the primary beneficiary of a variable interest entity (“VIE”). The portions of the equity and net income of consolidated subsidiaries that are not attributable to the Company are presented separately as amounts attributable to non-controlling interests in our consolidated financial statements. Entities which Highlands does not control and entities which are VIEs in which Highlands is not a primary beneficiary, if any, are accounted for under appropriate GAAP. Highlands' subsidiaries generally consist of limited liability companies (“LLCs”). The effects of all significant intercompany transactions have been eliminated.

Our Revenues and Expenses

Revenues

Our revenues are primarily derived from rental income and expense recoveries we receive from our tenants under leases with us, including monthly rent and other property income pursuant to tenant leases. Tenant recovery income primarily consists of reimbursements for real estate taxes, common area maintenance costs, management fees and insurance costs.

Expenses

Our expenses consist of property operating expenses, real estate taxes, depreciation and amortization expense, general and administrative expenses and provision for asset impairment. Property operating expenses primarily consist of repair and maintenance, management fees, utilities and insurance (in each case, some of which are recoverable from the tenant).

Key Indicators of Operating Performance

In evaluating our financial condition and operating performance, management focuses on the following financial and non-financial indicators, discussed in further detail herein:

- Cash flow from operations as determined in accordance with GAAP;
- Economic and physical occupancy and rental rates;
- Leasing activity and lease rollover;
- Management of operating expenses;
- Management of general and administrative expenses;
- Debt maturities and leverage ratios;
- Liquidity levels;
- Funds From Operations (“FFO”), a supplemental non-GAAP measure; and
- Adjusted Funds From Operations (“AFFO”), a supplemental non-GAAP measure.

Acquisition and Disposition Activity

During the year ended December 31, 2019, we continued to invest in multi-family assets with the following acquisitions of properties:

Property	Location	Acquisition Date		Acquisition Price
The Detroit and Detroit Terraces	Denver, Colorado	January 8, 2019	$	19,070
The View	San Diego, California	April 5, 2019		16,420
Tennyson44	Denver, Colorado	June 11, 2019		19,191
The Locale (formerly Evolve at Allendale) (1)	Allendale, MI	August 16, 2019		27,696
The Muse	Denver, Colorado	October 24, 2019		48,803
			$	131,180

(1) The purchase price of this acquisition was funded by the Corvue Venture with equity contributions from its members and with debt obtained by the Corvue Venture, as further discussed in Note 8. The portion of the aggregate equity contributions funded to the Corvue Venture that is not attributable to the Company is presented separately as amounts attributable to noncontrolling interests in our consolidated financial statements.

During the year ended December 31, 2019, we continued to execute on our strategy of disposing of legacy “non-core” assets by selling:

Property	Location	Disposition Date		Gross Disposition Price		Sale Proceeds, Net		Gain on Sale
RDU land	Raleigh, North Carolina	May 29, 2019	$	600	$	554	$	29
Lincoln Center	Lincoln, Rhode Island	June 21, 2019		55,750		52,609		8,812
			$	56,350	$	53,163	$	8,841

Results of Operations

Comparison of the years ended December 31, 2019 and 2018

Key performance indicators are as follows:

	As of December 31,	
	2019	2018
Economic occupancy (a)	87.4%	91.5%
Rent per square foot (b)	$ 17.56	$ 15.77

(a) Economic occupancy is defined as the percentage of total gross leasable area for which a tenant is obligated to pay rent under the terms of its lease agreement, regardless of the actual use or occupation by the tenant of the area being leased. Actual use may be less than economic square footage.

(b) Rent per square foot is computed as annualized base rent divided by the total occupied square footage at the end of the period. Annualized rent is computed as revenue for the last month of the period multiplied by twelve months. Annualized rent includes the effect of rent abatements, lease inducements and straight-line rent GAAP adjustments.

The decrease in occupancy in 2019 is due to a decrease in occupancy at one of our office assets. The increase in rent per square foot is due to the acquisition of multi-family assets.

Consolidated Results of Operations

	(in thousands) For the Year ended December 31,			
	2019	2018	Increase/(Decrease)	
Net income	$ 4,814	$ 24,928	$ (20,114)	(80.7)%

Net income decreased by $20.1 million to $4.8 million for the year ended December 31, 2019 from $24.9 million for the year ended December 31, 2018. The reduction can be primarily attributed to the gains recorded on the dispositions of one retail asset, one office asset and one detention facility during 2018, partially offset by gains recognized in 2019 for the sale of one retail asset and one parcel of land.

Operating Income and Expenses

	(in thousands) For the Year ended December 31,			
	2019	2018	Increase/(Decrease)	
Property income:				
Rental income	$ 36,626	$ 42,761	$ (6,135)	(14.3)%
Other property income	727	748	(21)	(2.8)%
	37,353	43,509	(6,156)	(14.1)%
Operating expenses:				
Property operating expenses	7,489	8,892	(1,403)	(15.8)%
Real estate taxes	5,691	5,028	663	13.2 %
Depreciation and amortization	13,014	12,178	836	6.9 %
General and administrative expenses	12,907	12,603	304	2.4 %
Provision for asset impairment	—	4,667	(4,667)	(100.0)%
Gain on sale of investment properties	8,841	27,863	(19,022)	(68.3)%

Property Income and Operating Expenses

Rental income consists of monthly rent, straight-line rent adjustments, tenant recovery income and amortization of acquired above and below market leases pursuant to tenant leases. Tenant recovery income consists of reimbursements for real estate taxes, common area maintenance costs, management fees, and insurance costs. Other property income consists of lease

termination fees and other miscellaneous property income. Property operating expenses consist of regular repair and maintenance, management fees, utilities, and insurance (in each case, some of which are recoverable from the tenant).

Total revenues decreased by $6.2 million in the year ended December 31, 2019 compared to the same period in 2018 as a result of the disposition of one office asset, one retail asset and one other asset during 2018 and one retail asset during 2019. Additionally, straight-line rental income related to a lease at one of our office assets was written off in December 2019. Partially offsetting these reductions were increases in rental income related to three multi-family asset acquisitions during 2018 and six multi-family asset acquisitions during 2019.

Property operating expenses decreased by $1.4 million in the year ended December 31, 2019 compared to the same period in 2018 as a result of the retail and office asset dispositions partially offset by the multi-family asset acquisitions discussed above.

Real Estate Taxes

Real estate taxes increased $0.7 million for the year ended December 31, 2019 compared to the same period in 2018 as a result of an adjustment of 2017 taxes for one of our previously disposed net lease assets, increases related to the multi-family asset acquisitions and an increase for one of the retail assets in 2019, partially offset by the disposition of assets during 2018 and 2019.

Depreciation and Amortization

Depreciation and amortization increased by $0.8 million for the year ended December 31, 2019 compared to the same period in 2018 primarily as a result of the asset acquisitions discussed above as well as a write-off of lease related assets at one of the office assets, partially offset by the dispositions discussed above.

General Administrative Expenses

General and administrative expenses increased by $0.3 million, or 2.4%, for the year ended December 31, 2019, consistent with the same period for the year ended December 31, 2018.

Provision for Asset Impairment

For the year ended December 31, 2018, we identified certain assets that may have a reduction in fair market value. We recorded an impairment of investment properties of $4.7 million on one net lease asset and one land parcel. No such impairments were recorded during the year ended December 31, 2019.

Gain on Sale of Investment Properties

During the year ended December 31, 2019, the gain on sale of investment properties was $8.8 million, which is primarily attributed to the sale of the Lincoln Center retail asset during 2019.

During the year ended December 31, 2018, the gain on sale of investment properties was $27.9 million, which is attributed to the sale of one retail asset, one multi-tenant office asset and one other asset during 2018.

Non-Operating Income and Expenses

	(in thousands) For the Year ended December 31,			
	2019	**2018**	**Increase/(Decrease)**	
Non-operating income and expenses:				
Interest income	$ 1,650	$ 497	$ 1,153	232.0 %
Loss on extinguishment of debt	—	(1,199)	(1,199)	(100.0)%
Other income	—	30	(30)	(100.0)%
Interest expense	(3,929)	(2,559)	1,370	53.5 %

Interest Income

Interest income increased by $1.2 million during the twelve months ended December 31, 2019 compared to the same periods in 2018 as a result of an increase in average cash balances during 2019 compared to 2018.

Loss on Extinguishment of Debt

During the year ended December 31, 2018, the loss on extinguishment of debt was $1.2 million, related to prepayment penalties on the payoff of mortgage debt for the Triangle retail asset sold in 2018. There were no debt extinguishments during the year ended December 31, 2019.

Interest Expense

Interest expense increased by $1.4 million to $3.9 million for the year ended December 31, 2019 from $2.6 million for the year ended December 31, 2018 primarily attributable to borrowings under the Term Loan Facility in the amount of $30.0 million in connection with entering into the credit facility. Additional factors contributing to the increase, is the Company's assumption of a mortgage loan of $11.4 million in connection with the acquisition of The Detroit and Detroit Terraces on January 8, 2019 and the mortgage loan in the amount of $18.8 million obtained in connection with the acquisition of The Locale (formerly Evolve at Allendale) on August 16, 2019.

Leasing Activity

Our primary source of funding for our property-level operating activities and debt payments is rent collected pursuant to our tenant leases. The following table represents lease expirations, excluding multi-family leases, as of December 31, 2019:

Lease Expiration Year	Number of Expiring Leases	Gross Leasable Area (GLA) of Expiring Leases (Sq. Ft.)	Annualized Rent of Expiring Leases (in thousands)	Percent of Total GLA	Percent of Total Annualized Rent	Expiring Rent/Square Foot
2020	10	349,150	$ 10,727	26.3%	52.1%	$ 30.72
2021	5	116,633	1,714	8.8%	8.3%	14.70
2022	5	156,825	2,217	11.8%	10.8%	14.14
2023	4	11,155	181	0.8%	0.9%	16.22
2024	5	48,148	785	3.6%	3.8%	16.31
2025	8	48,647	671	3.7%	3.3%	13.80
2026	4	20,191	428	1.5%	2.1%	21.22
2027	4	499,036	2,449	37.7%	11.9%	4.91
2028	4	36,159	790	2.7%	3.8%	21.86
2029	3	30,842	444	2.3%	2.2%	14.38
Month to Month	2	11,125	167	0.8%	0.8%	15.04
Thereafter	—	—	—	—%	—%	—
	54	1,327,911	$ 20,573	100.0%	100.0%	$ 15.49

The following table represents new and renewed leases that commenced (not including multi-family leases) in the year ended December 31, 2019.

	# of Leases	Gross Leasable Area	Rent per square foot	Weighted Average Lease Term
New	7	44,431	$ 16.46	7.44
Renewals	6	71,559	$ 14.08	4.19
Total	13	115,990	$ 14.99	5.44

During the year ended December 31, 2019, 13 new leases and renewals commenced with gross leasable area totaling 115,990 square feet. The weighted average lease term for new and renewal leases was 7.44 and 4.19 years, respectively.

As of December 31, 2018, 12 new leases and renewals commenced with gross leasable area totaling 164,551 square feet. The weighted average lease term for new and renewal leases was 9.91 and 4.31 years, respectively.

Critical Accounting Policies and Estimates

Revenue Recognition

The Company commences revenue recognition on our leases based on a number of factors. In most cases, revenue recognition under a lease begins when the lessee takes possession of, or controls, the physical use of the leased asset. Generally, this occurs on the lease commencement date. The determination of who is the owner, for accounting purposes, of the tenant improvements determines the nature of the leased asset and when revenue recognition under a lease begins. If we are the owner, for accounting purposes, of the tenant improvements, then the leased asset is the finished space and revenue recognition begins when the lessee takes possession of the finished space, typically when the improvements are substantially complete. If we conclude we are not the owner, for accounting purposes, of the tenant improvements (the lessee is the owner), then the leased asset is the unimproved space and any tenant improvement allowances funded under the lease are treated as lease incentives which reduces revenue recognized over the term of the lease. In these circumstances, we begin revenue recognition when the lessee takes possession of the unimproved space for the lessee to construct their own improvements. We consider a number of different factors to evaluate whether it or the lessee is the owner of the tenant improvements for accounting purposes. These factors include:

- whether the lease stipulates how and on what a tenant improvement allowance may be spent;
- whether the tenant or landlord retains legal title to the improvements;
- the uniqueness of the improvements;
- the expected economic life of the tenant improvements relative to the length of the lease; and
- who constructs or directs the construction of the improvements.

The determination of who owns the tenant improvements, for accounting purposes, is subject to significant judgment. In making that determination, we consider all of the above factors. No one factor, however, necessarily establishes its determination.

Rental income is recognized on a straight-line basis over the term of each lease. The difference between rental income earned on a straight-line basis and the cash rent due under the provisions of the lease agreements is recorded as deferred rent receivable and is included as a component of accounts and rents receivable in the accompanying consolidated balance sheets.

Rental income related receivables, which include contractual amounts accrued and unpaid from tenants and accrued straight-line rents receivable, are reduced for credit losses. Such amounts are recognized as a reduction to real estate rental revenues. The Financial Accounting Standards Board ("FASB") clarified in July 2019 that, under ASC 842, lessors can continue to recognize a reserve (i.e., allowance for uncollectible operating lease receivables) under the loss contingency guidance in ASC 450-20 after applying the collectibility guidance in ASC 842. We evaluate the collectability of lease receivables monthly using several factors including a lessee's creditworthiness. We recognize the credit loss on lease related receivables when, in the opinion of management, collection of substantially all lease payments is not probable. When collectability is determined not probable, any lease income subsequent to recognizing the credit loss is limited to the lesser of the lease income reflected on a straight-line basis or cash collected. The adoption of ASU 2016-02 resulted in an adjustment of $92 to rental income and property operating expenses, associated with lease related receivables where collection of substantially all operating lease payments is not probable during the year ended December 31, 2019.

The Company records lease termination income if there is a signed termination agreement, all of the conditions of the agreement have been met and amounts due are considered collectible.

Real Estate

We allocate the purchase price of real estate to land, building, other building improvements, tenant improvements, and intangible assets and liabilities (such as the value of above- and below-market leases, in-place leases and origination costs associated with in-place leases). The values of above- and below-market leases are recorded as intangible assets, net, and intangible liabilities, net, respectively, in the consolidated balance sheets, and are amortized as either a decrease (in the case of above-market leases) or an increase (in the case of below-market leases) to rental income over the remaining term of the associated tenant lease. The values associated with in-place leases are recorded in intangible assets, net in the consolidated balance sheets and are amortized to depreciation and amortization expense in the consolidated statements of operations and comprehensive income over the remaining lease term.

The difference between the contractual rental rates and our estimate of market rental rates is measured over a period equal to the remaining non-cancelable term of the leases, including below-market renewal options for which exercise of the renewal option appears to be reasonably assured. The remaining term of leases with renewal options at terms below market reflect the assumed exercise of such below-market renewal options and assume the amortization period would coincide with the extended lease term.

We perform, with the assistance of a third-party certified valuation specialist, the following procedures for properties we acquire:

- Determine the accounting of the transaction as either a business combination or an asset acquisition;
- Estimate the value of the property "as if vacant" as of the acquisition date;
- Allocate the value of the property among land, building, and other building improvements and determine the associated useful life for each;
- Calculate the value and associated life of above- and below-market leases on a tenant-by-tenant basis. The difference between the contractual rental rates and our estimate of market rental rates is measured over a period equal to the remaining term of the leases (using a discount rate which reflects the risks associated with the leases acquired, including geographical location, size of leased area, tenant profile and credit risk);
- Estimate the fair value of the tenant improvements, legal expenses and leasing commissions incurred to obtain the leases and calculate the associated useful life for each;
- Estimate the fair value of assumed debt, if any, and value the favorable or unfavorable debt position acquired; and
- Estimate the intangible value of the in-place leases based on lease execution costs of similar leases as well as lost rent payments during an assumed lease-up period and their associated useful lives on a tenant-by-tenant basis.

We recognize gains and losses from sales of investment properties and land in accordance with FASB ASC 610-20, "Gains and Losses From the Derecognition of Nonfinancial Assets." We recognize gains and losses from sales of investment properties and land when we transfer control of a property and when it is probable that we will collect substantially all of the related consideration.

Capitalization and Depreciation

Real estate is reflected at cost less accumulated depreciation. Ordinary repairs and maintenance are expensed as incurred. Depreciation expense is computed using the straight line method. Building and other improvements are depreciated based upon estimated useful lives of 30 years for building and improvements and 5-15 years for furniture, fixtures and equipment and site improvements. Tenant improvements are amortized on a straight line basis over the lesser of the life of the tenant improvement or the lease term as a component of depreciation and amortization expense. Leasing fees are amortized on a straight-line basis over the life of the related lease as a component of depreciation and amortization expense. Loan fees are amortized on a straight-line basis, which approximates the effective interest method, over the life of the related loan as a component of interest expense.

Direct and indirect costs that are clearly related to the construction and improvements of investment properties are capitalized. Costs incurred for property taxes and insurance are capitalized during periods in which activities necessary to get the asset ready for its intended use are in progress. Interest costs are also capitalized during such periods.

Assets Held for Sale

In determining whether to classify an investment property as held for sale, the Company considers whether: (i) management has committed to a plan to sell the investment property; (ii) the investment property is available for immediate sale, in its present condition; (iii) the Company has initiated a program to locate a buyer; (iv) the Company believes that the sale of the investment property is probable; (v) the Company has received a significant non-refundable deposit for the purchase of the property; (vi) the Company is actively marketing the investment property for sale at a price that is reasonable in relation to its fair value; and (vii) actions required for the Company to complete the plan indicate that it is unlikely that any significant changes will be made to the plan.

If all of the above criteria are met, the Company classifies the investment property as held for sale. On the day that these criteria are met, the Company suspends depreciation on the investment properties held for sale, including depreciation for tenant improvements and additions, as well as on the amortization of acquired in-place leases. The investment properties and liabilities associated with those investment properties that are held for sale are classified separately on the consolidated balance sheets for the most recent reporting period and recorded at the lesser of the carrying value or fair value less costs to sell.

There were no assets held for sale on the consolidated balance sheets as of December 31, 2019 and 2018.

Impairment

The Company assesses the carrying values of the respective long-lived assets, whenever events or changes in circumstances indicate that the carrying amounts of these assets may not be fully recoverable, such as a reduction in the expected holding period of the asset. If it is determined that the carrying value is not recoverable because the undiscounted cash flows do not exceed carrying value, the Company records an impairment loss to the extent that the carrying value exceeds fair value. The valuation and possible subsequent impairment of investment properties is a significant estimate that can and does change based on the Company’s continuous process of analyzing each asset and reviewing assumptions about uncertain inherent factors, as well as the economic condition of the asset at a particular point in time.

The use of projected future cash flows and related holding period is based on assumptions that are consistent with the estimates of future expectations and the strategic plan the Company uses to manage its underlying business. However, assumptions and estimates about future cash flows and capitalization rates are complex and subjective. Changes in economic and operating conditions and the Company’s ultimate investment intent that occur subsequent to the impairment analyses could impact these assumptions and result in future impairment charges of the real estate assets.

Liquidity and Capital Resources

As of December 31, 2019, we had $75.4 million of cash and cash equivalents, and $2.7 million of restricted escrows.

Our principal demands for funds have been or will be:

- to pay the operating expenses of our assets;
- to pay our general and administrative expenses;
- to pay for acquisitions;
- to pay for capital commitments;
- to pay for short-term obligations;
- to service or pay-down our debt; and
- to fund capital expenditures and leasing related costs.

Generally, our cash needs have been and will be funded from:

- cash flows from our investment assets;
- proceeds from sales of assets; and
- proceeds from debt.

Our assets have lease maturities within the next two years that we expect to reduce our cash flows from operations. In particular, 26.7% of our revenue for the year ended December 31, 2019 was derived from a net lease with The GEO Group, Inc. on our Hudson correctional facility asset. This lease expired in January of 2020. The GEO Group, Inc. has vacated the facility.

We may, from time to time, repurchase our outstanding equity and/or debt securities, if any, through cash purchases or via other transactions. Such repurchases or transactions, if any, will depend on our liquidity requirements, contractual restrictions, and other factors. The amounts involved may be material.

Borrowings

The table below presents, on a consolidated basis, the principal amount, weighted average interest rates and maturity date (by year) on our mortgage debt and debt from our credit facility, as of December 31, 2019 (dollar amounts are stated in thousands).

Fixed and variable rate debt maturing during the year ended December 31,	As of December 31, 2019	Weighted average interest rate
2020	$ —	—%
2021	—	—%
2022	9,166	5.24%
2023	18,658	3.28% [1]
2024	30,000	3.60%
Thereafter	37,102	4.38%
Total	$ 94,926	4.00%

[1] See Note 9 in the accompanying consolidated financial statements for discussion of the swap agreement entered into with the mortgage loan obtained in connection with the acquisition of The Locale (formerly Evolve at Allendale). The weighted average interest rate reflected is the strike rate.

As of December 31, 2019 and 2018, none of our mortgage debt was recourse to the Company, although we have provided certain customary, non-recourse carve-out guarantees in connection with obtaining mortgage loans on certain of our properties.

Our ability to pay off our mortgages when they become due is, in part, dependent upon our ability either to refinance the related mortgage debt or to sell the related asset. With respect to each loan, if we are unable to refinance or sell the related asset, or in the event that the estimated asset value is less than the mortgage balance, we may, if appropriate, satisfy a mortgage obligation by transferring title of the asset to the lender or permitting a lender to foreclose.

Volatility in the capital markets could expose us to the risk of not being able to borrow on terms and conditions acceptable to us for refinancing.

Total debt outstanding as of December 31, 2019 and 2018 was $94.9 million and $35.4 million, respectively, and had a weighted average interest rate of 4.00% and 4.74% per annum, respectively.

We assumed a mortgage loan in the principal amount of $11.4 million in connection with the acquisition of The Detroit and Detroit Terraces on January 8, 2019. According to the terms of the note agreement, the contractual fixed interest rate is 3.99% and payments are interest only through September 30, 2022. The maturity date of the mortgage loan is on August 31, 2027.

On February 15, 2019, we entered into a Credit Agreement with Huntington National Bank. The Credit Agreement provides for (i) a secured revolving credit facility (the “Revolving Credit Facility”) with revolving commitments in an aggregate principal amount of $50.0 million, including a letter of credit subfacility for 10% of the then available revolving commitments, and (ii) a secured term loan credit facility (the “Term Loan Facility” and together with the Revolving Credit Facility, the “Credit Facility”) with term loan commitments in an aggregate principal amount of $50.0 million. The Revolving Credit Facility has a maturity date of February 15, 2022, but can be extended at the Company’s option for two additional one-year periods conditioned on, among other things, payment of a 15-basis points extension fee upon each such extension. The Term Loan Facility has a maturity date of February 15, 2024. The Company currently expects to use borrowings under the Credit Facility for working capital purposes, which may include repayment of indebtedness, capital expenditures, lease up costs, redevelopment costs, property acquisitions and other general corporate purposes. As of December 31, 2019, we had borrowed $30.0 million under the Term Loan Facility and had no outstanding borrowings under the Revolving Credit Facility.

The Company obtained a mortgage loan in the principal amount of $18.8 million in connection with the acquisition of The Locale (formerly Evolve at Allendale) on August 16, 2019. We entered into a swap agreement with respect to the loan, effective through August 31, 2023, to swap the variable interest rate to a fixed rate of approximately 3.27% per annum. The interest rate is based on the London Interbank Offered Rate ("LIBOR") plus the applicable spread. The effective interest rate as of December 31, 2019, is approximately 3.46%.

Capital Expenditures and Reserve Funds

During the twelve months ended December 31, 2019, we made total capital expenditures of $1.0 million. Our total capital expenditures in 2018 was $4.3 million.

Summary of Cash Flows

Comparison of the years ended December 31, 2019 and ***December 31, 2018***

	(in thousands) For the Year ended December 31,	
	2019	**2018**
Cash provided by operating activities	$ 16,809	$ 15,765
Cash (used in) provided by investing activities	(68,351)	34,446
Cash provided by (used in) financing activities	45,856	(22,477)
Increase (decrease) in cash and cash equivalents	(5,686)	27,734
Cash, cash equivalents and restricted cash, at beginning of year	83,741	56,007
Cash, cash equivalents and restricted cash, at end of year	$ 78,055	$ 83,741

Cash provided by operating activities was $16.8 million and $15.8 million for the years ended December 31, 2019, and 2018, respectively, and was generated primarily from operating income from property operations. Cash provided by operating activities increased by $1.0 million when comparing the year ended December 31, 2019 to the same period in 2018 primarily as a result of proceeds from a letter of credit received pursuant to a lease amendment.

Cash used in investing activities was $68.4 million for the year ended December 31, 2019 compared to cash provided in the amount of $34.4 million for the year ended December 31, 2018. Cash used in investing activities increased $102.8 million when comparing the year ended December 31, 2019 to the same period in 2018. During the year ended December 31, 2019, cash was used to purchase investment properties for $119.7 million, payments for capital expenditures of $1.0 million and payments for leasing fees of $0.8 million. Partially offsetting cash used during the year ended December 31, 2019 was cash provided by proceeds from the sale of investment properties, net in the amount of $53.2 million. In the year ended December 31, 2018, net cash provided by proceeds from the sale of investment properties was $76.5 million offset by cash used to purchase properties for $36.0 million, payments for capital expenditures of $4.3 million and payments for leasing fees of $1.8 million.

Cash provided by financing activities was $45.9 million for the year ended December 31, 2019. Cash provided by financing activities for the twelve months ended December 31, 2019 was primarily related to borrowings in the amount of $30.0 million related to the Credit Facility and borrowings related to the acquisition of multi-family assets in the amount of $18.7 million. See also Note 8 to the consolidated financial statements for a summary of the Credit Agreement and mortgage debt. Cash used in financing activities for the year ended December 31, 2018 of $22.5 million was primarily due to payoff of mortgage debt of $19.5 million and principal payments of mortgage debt of $1.0 million.

We consider all demand deposits, money market accounts and investments in certificates of deposit and repurchase agreements with a maturity of three months or less, at the date of purchase, to be cash equivalents. We maintain our cash and cash equivalents at financial institutions. The combined account balances at one or more institutions exceed the Federal Depository Insurance Corporation ("FDIC") insurance coverage and, as a result, there is a concentration of credit risk related to amounts on deposit in excess of FDIC insurance coverage.

Funds From Operations and Adjusted Funds From Operations

The National Association of Real Estate Investment Trusts ("NAREIT"), an industry trade group, has promulgated a non-GAAP financial measure known as Funds From Operations, or FFO. As defined by NAREIT, FFO is net income (loss) in accordance with GAAP excluding gains (or losses) resulting from dispositions of properties, plus depreciation and amortization and impairment charges on depreciable property. We have adopted the NAREIT definition in our calculation of FFO as management considers FFO a widely accepted and appropriate measure of performance for REITs. FFO is not equivalent to our net income or loss as determined under GAAP.

Since the definition of FFO was promulgated by NAREIT, management and many investors and analysts have considered the presentation of FFO alone to be insufficient. Accordingly, in addition to FFO, we also use Adjusted Funds From Operations, or AFFO as a measure of our operating performance. We define AFFO, a non-GAAP financial measure, to exclude from FFO adjustments for gains or losses related to early extinguishment of debt instruments as these items are not related to our continuing operations. By excluding these items, management believes that AFFO provides supplemental information related to sustainable operations that will be more comparable between other reporting periods and to other public, non-traded REITs. AFFO is not equivalent to our net income or loss as determined under GAAP.

In calculating FFO and AFFO, impairment charges of depreciable real estate assets are added back even though the impairment charge may represent a permanent decline in value due to decreased operating performance of the applicable property. Further, because gains and losses from sales of property are excluded from FFO and AFFO, it is consistent and appropriate that impairments, which are often early recognition of losses on prospective sales of property, also be excluded.

We believe that FFO and AFFO are useful measures of our properties' operating performance because they exclude noncash items from GAAP net income. Neither FFO nor AFFO is intended to be an alternative to "net income" nor to "cash flows from operating activities" as determined by GAAP as a measure of our capacity to pay distributions. Other REITs may use alternative methodologies for calculating similarly titled measures, which may not be comparable to our calculation of FFO and AFFO.

The following section presents our calculation of FFO and AFFO to net income (in thousands):

	Year Ended December 31,	
	2019	**2018**
Net income attributable to Highlands REIT, Inc. common stockholders	$ 4,849	$ 24,928
Depreciation and amortization related to investment assets (a)	12,907	12,178
Impairment of investment properties	—	4,667
Gain on sale of investment properties, net	(8,841)	(27,863)
Funds From Operations	$ 8,915	$ 13,910
Loss on extinguishment of debt	—	1,199
Adjusted Funds From Operations	$ 8,915	$ 15,109

(a) The depreciation and amortization addback excludes the portion of expense attributable to the non-controlling interest.

The table below reflects additional information related to certain items that significantly impact the comparability of our FFO and AFFO and net income or significant non-cash items from the periods presented (in thousands).We have included this table because these items are not included in NAREIT's definition of FFO, but we believe these items provide useful supplemental information that may facilitate comparisons of our ongoing operating performance between periods, as well as between REITs that include similar disclosure.

	Year Ended December 31,	
	2019	**2018**
Amortization of mark to market debt discounts and financing costs	$ 290	$ 80

Distributions

For the years ended December 31, 2019 and 2018, no cash distributions were paid by Highlands.

Inflation

A number of our leases contain provisions designed to partially mitigate any adverse impact of inflation. With respect to current economic conditions and governmental fiscal policy, inflation may become a greater risk. Our commercial leases typically require the tenant to pay its share of operating expenses, including common area maintenance, real estate taxes and insurance. By sharing these costs with our tenants, we may reduce our exposure to increases in costs and operating expenses resulting from inflation. A portion of our leases also include clauses enabling us to receive percentage rents based on a tenant’s gross sales above predetermined levels or escalation clauses which are typically related to increases in the Consumer Price Index or similar inflation indices.

Off-Balance Sheet Arrangements

As of December 31, 2019 and 2018, we had no off-balance sheet arrangements.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

We are subject to market risk associated with changes in interest rates both in terms of variable-rate debt and the price of new fixed-rate debt upon maturity of existing debt and for acquisitions.

Interest Rate Risk

Our interest rate risk management objectives are to limit the impact of interest rate changes on earnings and cash flows and to lower our overall borrowing costs. As of December 31, 2019, our debt included an outstanding variable-rate term loan of $30.0 million and a variable rate mortgage loan of $18.8 million, which has been swapped to a fixed rate. If market rates of interest on all variable-rate debt as of December 31, 2019, that is not under a swap agreement, permanently increased or decreased by 1%, the annual increase or decrease in interest expense on the variable-rate debt and future earnings and cash flows would be approximately $0.3 million.

With regard to our variable-rate financing, we assess interest rate cash flow risk by identifying and monitoring changes in interest rate exposures that may adversely impact expected future cash flows and by evaluating hedging opportunities. We maintain risk management control systems to monitor interest rate cash flow risk attributable to both outstanding or forecasted debt obligations.

We may use financial instruments to hedge exposures to changes in interest rates on loans. To the extent we do, we are exposed to credit risk and market risk. Credit risk is the risk of failure of the counterparty to perform under the terms of the derivative contract. When the fair value of a derivative contract is positive, the counterparty owes us, which creates a credit risk for us. When the fair value of a derivative contract is negative, we owe the counterparty and, therefore, it does not pose credit risk. We seek to minimize the credit risk in derivative instruments by entering into transactions with what we believe are high-quality counterparties. Market risk is the adverse effect on the value of a financial instrument resulting from a change in interest rates.

In the event that LIBOR is discontinued, the interest rate for certain of our debt instruments, including our unsecured Revolving Credit Facility due 2022, unsecured Term Loan Facility due 2024 and interest rate swap agreements that are indexed to LIBOR, will be based on a replacement rate or an alternate base rate as specified in the applicable documentation governing such debt or swaps or as otherwise agreed upon. Such an event would not affect our ability to borrow or maintain already outstanding borrowings or swaps, but the replacement rate or alternate base rate could be higher or more volatile than LIBOR prior to its discontinuance. We understand that LIBOR is expected to remain available through the end of 2021, but may be discontinued or otherwise become unavailable thereafter.

Our credit facilities and interest rate swaps are indexed to USD-LIBOR. However, as our Credit Facility and interest rate swap agreements have provisions that allow for a transition to a new alternative rate, we believe that the transition from USD-LIBOR to the alternative rate will not have a material impact on our condensed consolidated financial statements.

As of December 31, 2019, we had one derivative financial instrument designated as a cash flow hedge, with a notional amount of $18.8 million and a maturity date of September 1, 2023. The fair value of the derivative was $0.02 million as of December 31, 2019 and is included in other assets in the accompanying consolidated balance sheets. The gains or losses resulting from marking-to-market our derivative financial instruments during the periods presented are recognized as an increase or decrease in comprehensive income on our consolidated statements of operations and comprehensive income.

Item 8. Consolidated Financial Statements and Supplementary Data

HIGHLANDS REIT, INC.

Index

All schedules other than those listed in the Index have been omitted, as the required disclosure is inapplicable or the information is presented in the financial statements or related notes.

See accompanying notes to consolidated financial statements.

Report of Independent Registered Public Accounting Firm

To the Stockholders and Board of Directors

Highlands REIT, Inc.:

Opinion on the Consolidated Financial Statements

We have audited the accompanying consolidated balance sheets of Highlands REIT, Inc. and subsidiaries (the Company) as of December 31, 2019 and 2018, the related consolidated statements of operations and comprehensive income, equity, and cash flow for each of the years in the two-year period ended December 31, 2019, and the related notes and financial statement schedule III (collectively, the consolidated financial statements). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2019 and 2018, and the results of its operations and its cash flows for each of the years in the two-year period ended December 31, 2019, in conformity with U.S. generally accepted accounting principles.

Change in Accounting Principle

As discussed in Note 2 to the consolidated financial statements, the Company has changed its method of accounting for leases as of January 1, 2019 due to the adoption of Accounting Standards Codification Topic 842, *Leases*.

Basis for Opinion

These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits, we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ KPMG LLP

We have served as the Company's auditor since 2015.

Chicago, Illinois
March 20, 2020

HIGHLANDS REIT, INC.

Consolidated Balance Sheets

(Amounts in thousands, except share and per share amounts)

	As of December 31,	
	2019	**2018**
Assets		
Investment properties		
Land	$ 82,877	$ 72,630
Building and other improvements	289,351	241,897
Construction in progress	—	32
Total	372,228	314,559
Less accumulated depreciation	(56,431)	(72,822)
Net investment properties	315,797	241,737
Cash and cash equivalents	75,404	80,512
Restricted cash and escrows	2,651	3,229
Accounts and rents receivable (net of allowance of $1,178 and $1,161, respectively)	3,105	5,861
Intangible assets, net	1,339	408
Deferred costs and other assets	1,936	4,233
Total assets	$ 400,232	$ 335,980
Liabilities		
Debt, net	$ 93,203	$ 34,953
Accounts payable and accrued expenses	11,535	11,653
Intangible liabilities, net	842	3,004
Other liabilities	4,055	2,270
Total liabilities	109,635	51,880
Commitments and contingencies		
Stockholders' Equity		
Common stock, $0.01 par value, 1,000,000,000 shares authorized, 876,074,038 and 871,688,704 shares issued and outstanding as of December 31, 2019 and 2018, respectively	8,761	8,717
Additional paid-in capital	1,408,993	1,407,502
Accumulated distributions in excess of net income	(1,127,270)	(1,132,119)
Accumulated other comprehensive income	18	—
Total Highlands REIT, Inc. stockholders' equity	290,502	284,100
Non-controlling interests	95	—
Total equity	290,597	284,100
Total liabilities and equity	$ 400,232	$ 335,980

See accompanying notes to consolidated financial statements.

HIGHLANDS REIT, INC.

Consolidated Statements of Operations and Comprehensive Income
(Amounts in thousands, except share and per share amounts)

	Year Ended December 31,	
	2019	**2018**
Revenues		
Rental income	$ 36,626	$ 42,761
Other property income	727	748
Total revenues	37,353	43,509
Expenses		
Property operating expenses	7,489	8,892
Real estate taxes	5,691	5,028
Depreciation and amortization	13,014	12,178
General and administrative expenses	12,907	12,603
Provision for asset impairment	—	4,667
Total expenses	39,101	43,368
Gain on sale of investment properties	8,841	27,863
Loss on extinguishment of debt	—	(1,199)
Income from operations	7,093	26,805
Interest income	1,650	497
Other income	—	30
Interest expense	(3,929)	(2,559)
Income before income taxes	4,814	24,773
Income tax benefit	—	155
Net income	4,814	24,928
Net loss attributable to non-controlling interests	35	—
Net income attributable to Highlands REIT, Inc. common stockholders	$ 4,849	$ 24,928
Net income per common share, basic and diluted	$ 0.01	$ 0.03
Weighted average number of common shares outstanding, basic and diluted	875,313,817	871,177,934
Comprehensive income		
Net income	$ 4,814	$ 24,928
Unrealized gain on derivatives	21	—
Total other comprehensive income	21	—
Comprehensive income	4,835	24,928
Comprehensive loss attributable to non-controlling interests	32	—
Comprehensive income attributable to Highlands REIT, Inc. common stockholders	$ 4,867	$ 24,928

See accompanying notes to consolidated financial statements.

HIGHLANDS REIT, INC.

Consolidated Statements of Equity
(Amounts in thousands, except share amounts)

For the years ended December 31, 2019 and 2018

	Common Stock		Additional Paid-in Capital	Accumulated Other Comprehensive Income	Accumulated Distributions in Excess of Net Income	Total Company's Stockholders Equity	Non-controlling interests	Total
	Shares	Amount						
Balance at January 1, 2018	868,423,581	$ 8,684	$ 1,406,460	$ —	$ (1,157,047)	$ 258,097	$ —	$ 258,097
Net income	—	—	—	—	24,928	24,928	—	24,928
Share-based compensation	3,265,123	33	1,042	—	—	1,075	—	1,075
Balance at December 31, 2018	871,688,704	8,717	1,407,502	—	(1,132,119)	284,100	—	284,100
Net income (loss)	—	—	—	—	4,849	4,849	(35)	4,814
Other comprehensive income	—	—	—	18	—	18	3	21
Non-controlling interest equity contributions	—	—	—	—	—	—	127	127
Share-based compensation	4,385,334	44	1,491	—	—	1,535	—	1,535
Balance at December 31, 2019	876,074,038	$ 8,761	$ 1,408,993	$ 18	$ (1,127,270)	$ 290,502	$ 95	$ 290,597

See accompanying notes to consolidated financial statements.

HIGHLANDS REIT, INC.
Consolidated Statements of Cash Flow
(Dollar amounts in thousands)

	Year ended December 31, 2019	Year ended December 31, 2018
Cash flows from operating activities:		
Net income	$ 4,814	$ 24,928
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	13,014	12,178
Amortization of above and below market leases, net	(266)	(407)
Amortization of debt discounts and financing costs	290	80
Straight-line rental income	(186)	(828)
Write-off of lease related assets	2,745	—
Loss on extinguishment of debt	—	1,199
Gain on sale of investment properties, net	(8,841)	(27,863)
Provision for asset impairment	—	4,667
Non-cash stock-based compensation expense	2,242	2,497
Changes in assets and liabilities:		
Accounts and rents receivable, net	205	(432)
Deferred costs and other assets	146	(1,457)
Accounts payable and accrued expenses	839	658
Other liabilities	1,807	545
Net cash flows provided by operating activities	$ 16,809	$ 15,765
Cash flows from investing activities:		
Capital expenditures and tenant improvements	(1,011)	(4,251)
Proceeds from sale of investment properties, net	53,163	76,526
Acquisition of investment properties	(119,725)	(36,014)
Payment of leasing fees	(778)	(1,815)
Net cash flows (used in) provided by investing activities	$ (68,351)	$ 34,446
Cash flows from financing activities:		
Payment of debt issuance costs	(437)	—
Proceeds from credit agreement	29,375	—
Proceeds from debt	18,684	—
Payoff of debt	—	(19,479)
Principal payments of debt	(716)	(964)
Prepayment penalties on the payoff of debt	—	(1,158)
Payment for tax withholding for share-based compensation	(1,177)	(876)
Contributions from non-controlling interests	127	—
Net cash flows provided by (used in) financing activities	$ 45,856	$ (22,477)
Net (decrease) increase in cash and cash equivalents	(5,686)	27,734
Cash, cash equivalents and restricted cash, at beginning of year	83,741	56,007
Cash, cash equivalents and restricted cash, at end of year	$ 78,055	$ 83,741

See accompanying notes to consolidated financial statements.

HIGHLANDS REIT, INC.
Consolidated Statements of Cash Flow
(Dollar amounts in thousands)

	Year Ended December 31,	
	2019	2018
Supplemental disclosure of cash flow information:		
Cash paid for interest	$ 3,493	$ 2,565
Cash paid for taxes	92	185
Supplemental schedule of non-cash investing and financing activities:		
Disposal of lease related assets	$ 2,745	$ —
Other assets arising from unrealized gain on derivative instruments	$ 21	$ —
Lease assets and liabilities arising from the recognition of right-of-use assets	$ 300	$ —
Assumption of mortgage debt on acquired properties	$ 11,449	$ —

See accompanying notes to consolidated financial statements.

HIGHLANDS REIT, INC.

Notes to Consolidated Financial Statements
(Amounts in thousands, except share and per share amounts)
December 31, 2019

1. Organization

Highlands REIT, Inc. (“Highlands”), which was formed in December 2015, is a Maryland corporation with a portfolio of multi-family assets, retail assets, office assets, industrial assets, a correctional facility, unimproved land and a bank branch. Prior to April 28, 2016, Highlands was a wholly-owned subsidiary of InvenTrust Properties Corp. (“InvenTrust” and formerly known as Inland American Real Estate Trust, Inc.), its former parent. Unless stated otherwise or the context otherwise requires, the terms “we,” “our” and “us” and references to the “Company” refer to Highlands and its consolidated subsidiaries.

On April 28, 2016, Highlands spun-off from InvenTrust through a pro rata distribution by InvenTrust of 100% of the outstanding shares of common stock, $0.01 par value per share (the “Common Stock”), of Highlands to holders of record of InvenTrust's common stock as of the close of business on April 25, 2016 (the “Record Date”). Each holder of record of InvenTrust's common stock received one share of Common Stock for every one share of InvenTrust's common stock held at the close of business on the Record Date (the “Distribution”). As a result, Highlands became an independent, self-advised, non-traded public company. Highlands has elected to be taxed, and currently qualifies, as a real estate investment trust ("REIT") under the Internal Revenue Code of 1986, as amended (the "Code") for U.S. federal income tax purposes commencing with Highlands' short taxable year ending December 31, 2016.

Each asset is owned by a separate legal entity, which maintains its own books and financial records, and each entity’s assets are not available to satisfy the liabilities of other affiliated entities, except as otherwise disclosed in Note 8.

As of December 31, 2019, the Company owned 20 assets and one parcel of unimproved land. As of December 31, 2018, the Company owned 15 assets and two parcels of unimproved land.

2. Summary of Significant Accounting Policies

The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) and require 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 consolidated financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

Principles of Consolidation and Basis of Presentation

The accompanying consolidated financial statements include the accounts of Highlands, as well as all of Highlands' consolidated subsidiaries (collectively, “the Company”). Highlands consolidates its wholly-owned subsidiaries and any other entities which it controls (i) through voting rights or similar rights or (ii) by means other than voting rights if Highlands is the primary beneficiary of a variable interest entity (“VIE”). The portions of the equity and net income of consolidated subsidiaries that are not attributable to the Company are presented separately as amounts attributable to non-controlling interests in our consolidated financial statements. Entities which Highlands does not control and entities which are VIEs in which Highlands is not a primary beneficiary, if any, are accounted for under appropriate GAAP. Highlands' subsidiaries generally consist of limited liability companies (“LLCs”). The effects of all significant intercompany transactions have been eliminated.

Variable Interest Entities

A VIE is an entity that either (i) has insufficient equity to permit the entity to finance its activities without additional subordinated financial support, or (ii) has equity investors who lack the characteristics of a controlling financial interest. Under Accounting Standards Codification (“ASC”) 810 - Consolidation, an entity that holds a variable interest in a VIE and meets certain requirements would be considered to be the primary beneficiary of the VIE and is required to consolidate the VIE in its consolidated financial statements. In order to be considered the primary beneficiary of a VIE, an entity must hold a variable interest in the VIE and have both the power to direct the activities that most significantly impact the economic performance of the VIE, and the right to receive benefits from, or the obligation to absorb losses of, the VIE that could be potentially significant to the VIE. See Note 3 for additional discussion of the Company's consolidated variable interest entity.

Revenue Recognition

The Company commences revenue recognition on our leases based on a number of factors. In most cases, revenue recognition under a lease begins when the lessee takes possession of, or controls, the physical use of the leased asset. Generally, this occurs on the lease commencement date. The determination of who is the owner, for accounting purposes, of the tenant improvements determines the nature of the leased asset and when revenue recognition under a lease begins. If we are the owner, for accounting purposes, of the tenant improvements, then the leased asset is the finished space and revenue recognition begins when the lessee takes possession of the finished space, typically when the improvements are substantially complete. If we conclude we are not the owner, for accounting purposes, of the tenant improvements (the lessee is the owner), then the leased asset is the unimproved space and any tenant improvement allowances funded under the lease are treated as lease incentives which reduces revenue recognized over the term of the lease. In these circumstances, we begin revenue recognition when the lessee takes possession of the unimproved space for the lessee to construct their own improvements. We consider a number of different factors to evaluate whether it or the lessee is the owner of the tenant improvements for accounting purposes. These factors include:

- whether the lease stipulates how and on what a tenant improvement allowance may be spent;
- whether the tenant or landlord retains legal title to the improvements;
- the uniqueness of the improvements;
- the expected economic life of the tenant improvements relative to the length of the lease; and
- who constructs or directs the construction of the improvements.

The determination of who owns the tenant improvements, for accounting purposes, is subject to significant judgment. In making that determination, we consider all of the above factors. No one factor, however, necessarily establishes its determination.

Rental income is recognized on a straight-line basis over the term of each lease. The difference between rental income earned on a straight-line basis and the cash rent due under the provisions of the lease agreements is recorded as deferred rent receivable and is included as a component of accounts and rents receivable in the accompanying consolidated balance sheets.

Rental income related receivables, which include contractual amounts accrued and unpaid from tenants and accrued straight-line rents receivable, are reduced for credit losses. Such amounts are recognized as a reduction to real estate rental revenues. The Financial Accounting Standards Board ("FASB") clarified in July 2019 that, under ASC 842, lessors can continue to recognize a reserve (i.e., allowance for uncollectible operating lease receivables) under the loss contingency guidance in ASC 450-20 after applying the collectibility guidance in ASC 842. We evaluate the collectability of lease receivables monthly using several factors including a lessee's creditworthiness. We recognize the credit loss on lease related receivables when, in the opinion of management, collection of substantially all lease payments is not probable. When collectability is determined not probable, any lease income subsequent to recognizing the credit loss is limited to the lesser of the lease income reflected on a straight-line basis or cash collected. The adoption of ASU 2016-02 resulted in an adjustment of $92 to rental income and property operating expenses, associated with lease related receivables where collection of substantially all operating lease payments is not probable during the year ended December 31, 2019.

The Company records lease termination income if there is a signed termination agreement, all of the conditions of the agreement have been met and amounts due are considered collectible.

Real Estate

We allocate the purchase price of real estate to land, building, other building improvements, tenant improvements, and intangible assets and liabilities (such as the value of above- and below-market leases, in-place leases and origination costs associated with in-place leases). The values of above- and below-market leases are recorded as intangible assets, net, and intangible liabilities, net, respectively, in the consolidated balance sheets, and are amortized as either a decrease (in the case of above-market leases) or an increase (in the case of below-market leases) to rental income over the remaining term of the associated tenant lease. The values associated with in-place leases are recorded in intangible assets, net in the consolidated balance sheets and are amortized to depreciation and amortization expense in the consolidated statements of operations and comprehensive income over the remaining lease term.

The difference between the contractual rental rates and our estimate of market rental rates is measured over a period equal to the remaining non-cancelable term of the leases, including below-market renewal options for which exercise of the renewal option appears to be reasonably assured. The remaining term of leases with renewal options at terms below market reflect the assumed exercise of such below-market renewal options and assume the amortization period would coincide with the extended lease term.

We perform, with the assistance of a third-party certified valuation specialist, the following procedures for properties we acquire:

- Estimate the value of the property “as if vacant” as of the acquisition date;
- Allocate the value of the property among land, building, and other building improvements and determine the associated useful life for each;
- Calculate the value and associated life of above- and below-market leases on a tenant-by-tenant basis. The difference between the contractual rental rates and our estimate of market rental rates is measured over a period equal to the remaining term of the leases (using a discount rate which reflects the risks associated with the leases acquired, including geographical location, size of leased area, tenant profile and credit risk);
- Estimate the fair value of the tenant improvements, legal expenses and leasing commissions incurred to obtain the leases and calculate the associated useful life for each;
- Estimate the fair value of assumed debt, if any, and value the favorable or unfavorable debt position acquired; and
- Estimate the intangible value of the in-place leases based on lease execution costs of similar leases as well as lost rent payments during an assumed lease-up period and their associated useful lives on a tenant-by-tenant basis.

We recognize gains and losses from sales of investment properties and land in accordance with FASB ASC 610-20, “Gains and Losses From the Derecognition of Nonfinancial Assets”. We recognize gains and losses from sales of investment properties and land when we transfer control of a property and when it is probable that we will collect substantially all of the related consideration.

Capitalization and Depreciation

Real estate is reflected at cost less accumulated depreciation. Ordinary repairs and maintenance are expensed as incurred. Depreciation expense is computed using the straight line method. Building and other improvements are depreciated based upon estimated useful lives of 30 years for building and improvements and 5-15 years for furniture, fixtures and equipment and site improvements. Tenant improvements are amortized on a straight line basis over the lesser of the life of the tenant improvement or the lease term as a component of depreciation and amortization expense. Leasing fees are amortized on a straight-line basis over the life of the related lease as a component of depreciation and amortization expense. Loan fees are amortized on a straight-line basis, which approximates the effective interest method, over the life of the related loan as a component of interest expense.

Direct and indirect costs that are clearly related to the construction and improvements of investment properties are capitalized. Costs incurred for property taxes and insurance are capitalized during periods in which activities necessary to get the asset ready for its intended use are in progress. Interest costs are also capitalized during such periods.

Assets Held for Sale

In determining whether to classify an investment property as held for sale, the Company considers whether: (i) management has committed to a plan to sell the investment property; (ii) the investment property is available for immediate sale, in its present condition; (iii) the Company has initiated a program to locate a buyer; (iv) the Company believes that the sale of the investment property is probable; (v) the Company has received a significant non-refundable deposit for the purchase of the property; (vi) the Company is actively marketing the investment property for sale at a price that is reasonable in relation to its fair value; and (vii) actions required for the Company to complete the plan indicate that it is unlikely that any significant changes will be made to the plan.

If all of the above criteria are met, the Company classifies the investment property as held for sale. On the day that these criteria are met, the Company suspends depreciation on the investment properties held for sale, including depreciation for tenant improvements and additions, as well as on the amortization of acquired in-place leases. The investment properties and liabilities associated with those investment properties that are held for sale are classified separately on the consolidated balance sheets for the most recent reporting period and recorded at the lesser of the carrying value or fair value less costs to sell.

There were no assets held for sale on the consolidated balance sheets as of December 31, 2019 and 2018.

If the sale represents a strategic shift that has (or will have) a major effect on the Company's results of operations, the income and expenses for the period are classified as discontinued operations on the consolidated statement of operations and comprehensive income for all periods presented.

Impairment

The Company assesses the carrying values of the respective long-lived assets, whenever events or changes in circumstances indicate that the carrying amounts of these assets may not be fully recoverable, such as a reduction in the expected holding period of the asset. If it is determined that the carrying value is not recoverable while undiscounted cash flows from the anticipated use and disposal of the association long-lived asset, the Company records an impairment loss to the extent that the carrying value exceeds the property's fair value. The valuation and possible subsequent impairment of investment properties is a significant estimate that can and does change based on the Company’s continuous process of analyzing each asset and reviewing assumptions about uncertain inherent factors, as well as the economic condition of the asset at a particular point in time.

The use of projected future cash flows and related holding period is based on assumptions that are consistent with the estimates of future expectations and the strategic plan the Company uses to manage its underlying business. However, assumptions and estimates about future cash flows and capitalization rates are complex and subjective. Changes in economic and operating conditions and the Company’s ultimate investment intent that occur subsequent to the impairment analyses could impact these assumptions and result in future impairment charges of the real estate assets.

The Company recorded $4,667 of impairments during the year ended December 31, 2018. There were no such impairments during the year ended December 31, 2019. See Note 9 to the consolidated financial statements for additional information.

Recently Issued Accounting Pronouncements

In August 2018, the FASB issued ASU No. 2018-13, Fair Value Measurement (Topic 820): Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement. This ASU modifies the disclosure requirements on fair value measurements. The ASU removes the requirement to disclose: the amount of and reasons for transfers between Level 1 and Level 2 of the fair value hierarchy; the policy for timing of transfers between levels; and the valuation processes for Level 3 fair value measurements. Our effective date for adoption of this guidance is our fiscal year beginning January 1, 2020 with early adoption permitted. We are currently evaluating the effect that this guidance will have on our consolidated financial statements. The adoption of ASU No. 2018-13 is not expected to have a material impact on the consolidated financial statements.

(Amounts in thousands, except share and per share amounts)

Recently Adopted Accounting Pronouncements

In February 2016, the FASB issued ASU No. 2016-02, Leases ("ASU 2016-02"), which established ASC 842, *Leases*, which introduces a lessee model that brings most leases on the balance sheet and, among other changes, eliminates the requirement in current GAAP for an entity to use bright-line tests in determining lease classification. ASC 842 allows for several practical expedients which permit the following: no reassessment of lease classification or initial direct costs; use of the standard's effective date as the date of initial application; and no separation of non-lease components from the related lease components and, instead, to account for those components as a single lease component if certain criteria are met. We have elected these practical expedients and adopted ASC 842 on January 1, 2019 using the effective date as our date of initial application and no transition adjustment was recorded. Therefore, financial information and disclosures under ASC 842 will not be provided for periods prior to January 1, 2019. The Company has elected the practical expedient, among others, to not separate lease and non-lease components for all qualifying leases. Due to the new standard's narrowed definition of initial direct costs, beginning January 1, 2019, the Company recognizes expense as incurred on certain lease origination costs previously capitalized and amortized to expense over the lease term. Any costs no longer qualifying as initial direct costs are an increase to property operating expenses in the consolidated statements of operations and comprehensive income in the period of adoption and prospectively. As a lessee, beginning January 1, 2019, the Company recognized a right-of-use asset and lease liability on the consolidated balance sheet, included in deferred costs and other assets and other liabilities, with a balance as of December 31, 2019 of approximately $298, which was estimated by utilizing an average discount rate of approximately 4.5%, reflecting the Company's incremental borrowing rate. These estimates are based on the Company's ground lease arrangement as of the adoption date. As a lessor, the Company believes that substantially all of the Company's leases will continue to be classified as operating leases under the new standard and will continue to record revenues from rental properties on a straight-line basis. However, certain ground, anchor, and other long-term leases entered into or acquired have an increased likelihood of being classified as either sales-type or finance-type leases.

In November 2016, the FASB issued ASU No. 2016-18, Classification and Presentation of Restricted Cash in the Statement of Cash Flows. ASU No. 2016-18 requires an explanation in the cash flow statement of a change in the total of (1) total cash, (2) cash equivalents, and (3) restricted cash or restricted cash equivalents. The Company adopted ASU No. 2016-18 effective January 1, 2018, the effects of which include presenting restricted cash and escrows with cash and cash equivalents in the consolidated statements of cash flow. The Company is required to escrow cash balances for specific uses stipulated by certain of its lenders and other various agreements. As of December 31, 2019 and 2018, the Company's cash balances restricted for these uses were $2,651 and $3,229, respectively.

	December 31, 2019	December 31, 2018
Cash and cash equivalents	$ 75,404	$ 80,512
Restricted cash	2,651	3,229
Total cash, cash equivalents and restricted cash	$ 78,055	$ 83,741

In February 2017, the FASB issued ASU No. 2017-05, Other Income—Gains and Losses from the Derecognition of Nonfinancial Assets. As it relates to gains on sale of real estate, we will apply the provisions of ASC 610-20, Gain or Loss From Derecognition of Non-financial Assets (ASC 610-20), and we expect to recognize any gains when we transfer control of a property and when it is probable that we will collect substantially all of the related consideration. The adoption of ASC 610-20 on January 1, 2018 did not have a material impact on our consolidated financial statements.

In June 2018, the FASB issued ASU No. 2018-07, Compensation – Stock Compensation (Topic 718), Improvements to Nonemployee Share-Based Payment Accounting. This ASU is intended to simplify aspects of share-based compensation issued to non-employees by making the guidance consistent with the accounting for employee share-based compensation. It is effective for annual reporting periods, and interim periods within those years, beginning after December 15, 2018. The adoption of ASU No. 2018-07 on January 1, 2019 did not have a material impact on our consolidated financial statements.

(Amounts in thousands, except share and per share amounts)

3. Acquired Assets

The Company records identifiable assets and liabilities acquired at fair value. During the year ended December 31, 2019, the Company acquired six multi-family assets for a gross acquisition price of $131,180. Under ASU No. 2017-01, the Company determined these transactions should be accounted for as asset acquisitions. Accordingly, the Company capitalized transaction costs of approximately $480.

The following table reflects the properties acquired during the year ended December 31, 2019.

Property	Location	Acquisition Date	Acquisition Price
The Detroit and Detroit Terraces	Denver, Colorado	January 8, 2019	$ 19,070
The View	San Diego, California	April 5, 2019	16,420
Tennyson44	Denver, Colorado	June 11, 2019	19,191
The Locale (formerly Evolve at Allendale) [1]	Allendale, MI	August 16, 2019	27,696
The Muse	Denver, Colorado	October 24, 2019	48,803
			$ 131,180

[1] The purchase price of this acquisition was funded by the Corvue Venture with equity contributions from its members and with debt obtained by the Corvue Venture, as further discussed in Note 8. The portion of the aggregate equity contributions funded to the Corvue Venture that is not attributable to the Company is presented separately as amounts attributable to noncontrolling interests in our consolidated financial statements.

The purchase price allocation has been recorded as follows:

	The Detroit and Detroit Terraces	The View	Tennyson44	The Locale	The Muse	Total
Land	$ 3,370	$ 7,272	$ 1,533	$ 4,295	$ 5,303	$ 21,773
Buildings and other improvements	15,006	8,862	17,410	22,460	42,809	106,547
Intangible assets, net	301	286	248	941	691	2,467
Total assets	$ 18,677	$ 16,420	$ 19,191	$ 27,696	$ 48,803	$ 130,787
						—
Debt discount on mortgage assumption	393	—	—	—	—	393
Total liabilities	$ 393	$ —	$ —	$ —	$ —	$ 393
Total acquisition price	$ 19,070	$ 16,420	$ 19,191	$ 27,696	$ 48,803	$ 131,180

Consolidated VIE

As of December 31, 2019, we have determined we are the primary beneficiary of one VIE - the Corvue Venture and have consolidated the operations of this entity in the accompanying consolidated financial statements.

We reviewed the operating agreement of the Corvue Venture in order to determine our rights and the rights of our third-party partner, including whether those rights are protective or participating. We have determined we are the primary beneficiary of the Corvue Venture because we have (a) the power to direct the activities that most significantly impact the economic performance of the Corvue Venture, (b) the obligation to absorb the losses that could be significant to the Corvue Venture and (c) the right to receive the benefits that could be significant to the Corvue Venture.

(Amounts in thousands, except share and per share amounts)

Included in total assets on the Company's consolidated balance sheets as of December 31, 2019 is $28,073 related to the Corvue Venture. Included in total liabilities on the Company's consolidated balance sheets as of December 31, 2019 is $19,074 related to the Corvue Venture. The assets of the Corvue Venture may only be used to settle obligations of the Corvue Venture and the creditors of the Corvue Venture have no recourse to the general credit of the Company.

During the twelve months ended December 31, 2018, the Company acquired three multi-family assets for an acquisition price of $36.0 million. Under ASU No. 2017-01, the Company determined these transactions should be accounted for as asset acquisitions. Accordingly, the Company capitalized transaction costs of approximately $240.

The following table reflects the properties acquired during the year ended December 31, 2018.

Property	Location	Acquisition Date		Acquisition Price
The Lafayette	Denver, Colorado	May 15, 2018	$	9,679
1620 Central Street	Evanston, Illinois	August 22, 2018		20,552
Kenilworth Court	Denver, Colorado	September 12, 2018		5,784
			$	36,015

The purchase price allocation has been recorded as follows:

		The Lafayette		1620 Central Street		Kenilworth Court		Total
Land	$	2,457	$	3,075	$	2,496	$	8,028
Buildings and other improvements		7,067		17,133		3,203		27,403
Intangible assets, net		155		344		85		584
Total acquisition price	$	9,679	$	20,552	$	5,784	$	36,015

4. Disposed Assets

The following table reflects the property dispositions during the year ended December 31, 2019.

Property	Location	Date		Gross Disposition Price		Sale Proceeds, Net		Gain on Sale
RDU land	Raleigh, North Carolina	May 29, 2019	$	600	$	554	$	29
Lincoln Center	Lincoln, Rhode Island	June 21, 2019		55,750		52,609		8,812
			$	56,350	$	53,163	$	8,841

(Amounts in thousands, except share and per share amounts)

The following table reflects the property dispositions during the year ended December 31, 2018.

Property	Location	Date	Gross Disposition Price	Sale Proceeds, Net	Gain on Sale
Buckhorn Plaza (partial lot sale)	Bloomsburg, PA	8-Feb-18	$ 60	$ 60	$ 25
Rolling Plains (correctional facility)	Haskell, TX	7-Aug-18	3,600	3,237	3,368
Triangle Center [(1)]	Longview, WA	24-Sep-18	38,340	37,425	8,908
Bridgeside Point	Pittsburgh, PA	28-Dec-18	38,500	35,804	15,562
			$ 80,500	$ 76,526	$ 27,863

[(1)] Mortgage debt in the amount of $19,479 was paid off with the proceeds from the sale.

5. Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses consist of the following:

	Year ended December 31,	
	2019	2018
Accrued real estate taxes	$ 6,372	$ 5,669
Accrued compensation	3,606	3,232
Accrued interest payable	369	119
Other accrued expenses	1,188	2,633
Total accounts payable and accrued expenses	$ 11,535	$ 11,653

6. Leases

Leasing as a lessor

Revenue Recognition

We lease multi-family properties under operating leases with terms of generally one year or less. We lease commercial properties (our net lease, office and retail segments) under operating leases with remaining lease terms that range from less than one year to ten years as of December 31, 2019 and terms that range from less than one year to twenty years as of December 31, 2018.

We recognize rental income and rental abatements from our multi-family and commercial leases when earned on a straight-line basis over the lease term. Recognition of rental income commences when control of the leased space has been transferred to the tenant.

We recognize cost reimbursement income from pass-through expenses on an accrual basis over the periods in which the expenses were incurred. Pass-through expenses are comprised of real estate taxes, operating expenses and common area maintenance costs which are reimbursed by tenants in accordance with specific allowable costs per tenant lease agreements.

Parking revenues are derived from leases and monthly parking agreements. We recognize parking revenues from leases on a straight-line basis over the lease term and other parking revenues as earned.

Upon adoption of ASU 2016-02, we elected not to bifurcate lease contracts into lease and non-lease components, since the timing and pattern of revenue is not materially different and the non-lease components are not the primary component of the lease. Accordingly, both lease and non-lease components are presented in rental income in our consolidated financial statements. The adoption of ASU 2016-02 did not result in a material change to our recognition of real estate rental revenue.

Notes to Consolidated Financial Statements
(Amounts in thousands, except share and per share amounts)
December 31, 2019

Lease related receivables, which include contractual amounts accrued and unpaid from tenants and accrued straight-line rents receivable, are reduced for credit losses. Such amounts are recognized as a reduction to real estate rental revenues. The FASB clarified in July 2019 that, under ASC 842, lessors can continue to recognize a reserve (i.e., allowance for uncollectible operating lease receivables) under the loss contingency guidance in ASC 450-20 after applying the collectibility guidance in ASC 842. We evaluate the collectability of lease receivables monthly using several factors including a lessee's creditworthiness. We recognize the credit loss on lease related receivables when, in the opinion of management, collection of substantially all lease payments is not probable. When collectability is determined not probable, any lease income subsequent to recognizing the credit loss is limited to the lesser of the lease income reflected on a straight-line basis or cash collected.

In December 2019, the Company executed an amendment to its lease with Alta Devices, Inc. for one building of our office asset located in San Jose, California. The amendment with Alta Devices acknowledged Alta Devices was in payment default of its lease, and we collected on a letter of credit, in the amount of $1,701, that secured Alta Devices obligations under the lease. The letter of credit proceeds have been and will continue to be applied to rental income and other fees, if applicable, pursuant to the terms of the lease. We have written off all lease related assets related to the premises in the original lease with Alta Devices, Inc. including a lease inducement $1,249, lease commissions $1,169 and straight-line rent $1,649.

On August 2, 2019, we received a notice of non-renewal from The GEO Group, Inc. indicating that it would not be seeking an extension of its lease on our Hudson correctional facility asset. The lease on this asset expired in January, 2020 and The GEO Group, Inc. has vacated the facility. For the year ended December 31, 2019, 26.7% of our revenue was derived from The GEO Group, Inc.'s net lease on our Hudson correctional facility asset. A non-renewal by The GEO Group Inc. was contemplated when we recorded an impairment of the asset of $3,765 during the fourth quarter of 2018. While we will seek to re-lease or find alternative users for this asset, given the nature of the property, its location and its extended period of vacancy, we expect it will be very difficult to re-lease or find alternative users for this property. Even if we are successful in finding alternative users, we expect it will take an extended period of time to do so, if at all. Further, we believe it is unlikely that we will be able to find alternative users on similar terms. As we do not expect to find alternative users, re-lease the property, or re-lease on similar terms in the foreseeable future, we expect the expiration of this lease to have a material adverse effect on our financial condition, cash flows and results of operations. Notwithstanding the expiration of this lease, we believe we have sufficient liquidity and capital resources to fund our operations for the foreseeable future.

Lease income related to the Company's operating leases is comprised of the following:

	Year ended December 31, 2019	Year ended December 31, 2018
Lease income related to fixed lease payments	$ 30,391	$ 34,966
Lease income related to variable lease payments	6,235	7,795
Other [(1)]	727	748
Lease income	$ 37,353	$ 43,509

(1) For the year ended December 31, 2019 and 2018, respectively, other is primarily comprised of parking revenues and termination fees related to early lease expirations.

Future Minimum Rental Income

As of December 31, 2019, commercial operating leases provide for future minimum rental income, assuming no expiring leases are renewed, as follows. Apartment leases are not included as the terms are generally for one year or less.

(Amounts in thousands, except share and per share amounts)

2020	$	10,282
2021		8,597
2022		6,133
2023		5,533
2024		5,059
Thereafter		12,338
Total	$	47,942

As of December 31, 2018, commercial operating leases provide for future minimum rental income assuming no expiring leases are renewed, as follows:

2019	$	29,214
2020		17,418
2021		14,014
2022		11,423
2023		10,358
Thereafter		36,357
Total	$	118,784

The remaining lease terms range from one year to fifteen years. The majority of the revenue from the Company's assets consists of rents received under long-term operating leases. Some leases provide for the payment of fixed base rent paid monthly in advance, and for the reimbursement by tenants to the Company for the tenant's pro rata share of certain operating expenses including real estate taxes, special assessments, insurance, utilities, common area maintenance, management fees, and certain building repairs paid by the landlord and recoverable under the terms of the lease. Under these leases, the landlord pays all expenses and is reimbursed by the tenant for the tenant's pro rata share of recoverable expenses paid. Certain other tenants are subject to net leases which provide that the tenant is responsible for fixed base rent as well as all costs and expenses associated with occupancy. Under net leases where all expenses are paid directly by the tenant rather than the landlord, such expenses are not included in the consolidated statements of operations and comprehensive income. Under leases where all expenses are paid by the landlord, subject to reimbursement by the tenant, the expenses are included within property operating expenses and reimbursements are included in tenant recovery income on the consolidated statements of operations and comprehensive income.

Leasing as a Lessee

We lease a portion of the land underlying one of our retail assets, Sherman Plaza, from a third party through a ground lease covering such land with a lease term expiring in October 2042.

Upon adoption of ASU 2016-02, we recognized a right of use asset (included in deferred costs and other assets) and lease liability (included in other liabilities). At December 31, 2019, the balances were $298 and were recorded in the consolidated balance sheets. We used a discount rate of approximately 4.5%, reflecting the Company's incremental borrowing rate.

The following table sets forth the undiscounted cash flows of our scheduled obligations for future minimum payments on our operating ground lease at December 31, 2019 and a reconciliation of those cash flows to the operating lease liability at December 31, 2019.

(Amounts in thousands, except share and per share amounts)

2020	$	21
2021		21
2022		21
2023		21
2024		21
Thereafter		373
		478
Imputed interest		(180)
Lease liability	$	298

7. Intangible Assets

The following table summarizes the Company's identified intangible assets and intangible liabilities as of December 31, 2019 and 2018.

	Balance as of December 31,			
	2019		2018	
Intangible Assets:				
Acquired in-place lease	$	22,165	$	19,884
Acquired above market lease		—		127
Accumulated amortization		(20,826)		(19,603)
Intangible assets, net	$	1,339	$	408
Intangible liabilities:				
Acquired below market leases	$	2,629	$	8,106
Accumulated amortization		(1,787)		(5,102)
Intangible Liabilities, net	$	842	$	3,004

The portion of the purchase price allocated to acquired above market lease costs and acquired below market lease costs are amortized on a straight-line basis over the life of the related lease, including the respective renewal period for below market lease costs with fixed rate renewals, as an adjustment to rental income. Amortization pertaining to the above market lease costs was applied as a reduction to rental income. Amortization pertaining to the below market lease costs was applied as an increase to other property income. The portion of the purchase price allocated to acquired in-place lease intangibles is amortized on a straight line basis over the life of the related lease and is recorded as amortization expense.

The following table summarizes the amortization related to acquired above and below market lease costs and acquired in-place lease intangibles for the years ended December 31, 2019 and 2018.

	Year ended December 31,			
	2019		2018	
Amortization of:				
Acquired above market lease	$	(1)	$	(2)
Acquired below market lease		267		409
Net revenues increase	$	266	$	407
Acquired in-place lease intangibles	$	1,529	$	735

(Amounts in thousands, except share and per share amounts)

The following table presents the amortization during the next five years and thereafter related to intangible assets and liabilities as of December 31, 2019.

	2020	2021	2022	2023	2024	Thereafter	Total
Amortization of:							
Acquired below market lease	$ 99	$ 85	$ 85	$ 85	$ 85	$ 403	$ 842
Net revenues increase	$ 99	$ 85	$ 85	$ 85	$ 85	$ 403	$ 842
Acquired in-place lease intangibles	$ 1,339	$ —	$ —	$ —	$ —	$ —	$ 1,339

8. Debt

During the years ended December 31, 2019 and 2018, the following principal debt transactions occurred:

Balance at December 31, 2017		$ 55,886
Paydown of debt		(20,443)
Balance at December 31, 2018		35,443
Assumption of mortgage debt on acquired properties	—	11,449
Proceeds from credit agreement		30,000
Proceeds from mortgage debt		18,750
Paydown of debt		(716)
Balance at December 31, 2019		$ 94,926

Total debt outstanding as of December 31, 2019 and December 31, 2018, net of unamortized deferred financing costs and debt discounts, were $93,203 and $34,953, respectively, and had a weighted average interest rate of 4.00% and 4.74% per annum, respectively. Deferred financing costs, net, as of December 31, 2019 and December 31, 2018 were $1,374 and $490, respectively. Debt discounts, as of December 31, 2019 and December 31, 2018 were $349 and $0, respectively. As of December 31, 2019, scheduled maturities for the Company's outstanding mortgage indebtedness and the credit facility had various due dates through August 2027, as follows:

For the year ended December 31,	As of December 31, 2019	Weighted average interest rate
2020	$ —	—%
2021	—	—%
2022	9,166	5.24%
2023	18,658	3.28% (1)
2024	30,000	3.60%
Thereafter	37,102	4.38%
Total	$ 94,926	4.00%

(1) See below for discussion of the swap agreement entered into with the mortgage loan obtained in connection with the acquisition of the The Locale (formerly Evolve at Allendale) asset. The weighted average interest rate reflected is the strike rate.

The Company's ability to pay off mortgages when they become due is dependent upon the Company's ability either to refinance the related mortgage debt or to sell the related asset. With respect to each loan, if the applicable subsidiary is unable to refinance or sell the related asset, or in the event that the estimated asset value is less than the mortgage balance, we may, if appropriate, satisfy a mortgage obligation by transferring title of the asset to the lender or permitting a lender to foreclose. As of December 31, 2019 and December 31, 2018, none of our mortgage debt was recourse to the Company, although Highlands or its subsidiaries may act as guarantor under customary, non-recourse carve-out guarantees in connection with obtaining mortgage loans on certain of our properties.

Some of the mortgage loans require compliance with certain covenants, such as debt service ratios, investment restrictions and distribution limitations. As of December 31, 2019 and 2018, the Company is in compliance with such covenants in all material respects.

On January 8, 2019, the Company assumed a mortgage loan in the principal amount of $11,089, net of a debt discount of $360 in connection with the acquisition of The Detroit and Detroit Terraces. The contractual rate and terms of the assumed debt was marked to market as of the acquisition date. According to the terms of the note agreement, the contractual fixed interest rate is 3.99% and payments are interest only through September 30, 2022. The maturity date of the mortgage loan is on August 31, 2027.

We obtained a mortgage loan in the principal amount of $18,750 in connection with the acquisition of Locale (formerly Evolve at Allendale) on August 16, 2019. We entered into a swap agreement with respect to the loan, effective through its September 1, 2023 maturity date, to swap the variable interest rate to a fixed rate of approximately 3.27% per annum. The interest rate is based on the LIBOR plus the applicable spread. The effective interest rate as of December 31, 2019, is approximately 3.46%.

Credit Agreement

On February 15, 2019, the Company entered into a Credit Agreement (the "Credit Agreement") by and among the Company, as borrower, The Huntington National Bank ("HNB"), individually and as administrative agent, issuing lender, lead arranger, book manager and syndication agent, and certain other lenders thereunder. The Credit Agreement provides for (i) a secured revolving credit facility (the "Revolving Credit Facility") with revolving commitments in an aggregate principal amount of $50,000, including a letter of credit subfacility for 10% of the then available revolving commitments, and (ii) a secured term loan credit facility (the "Term Loan Facility" and together with the Revolving Credit Facility, the "Credit Facility") with term loan commitments in an aggregate principal amount of $50,000.

The Credit Agreement provides that, subject to customary conditions, we may seek to increase the aggregate lending commitments by up to $100,000, with such increase in total lending commitments to be allocated to increasing the revolving commitments and/or establishing one or more new tranches of term loans at our request.

The Revolving Credit Facility has a maturity date of February 15, 2022, but can be extended at the Company's option for two additional one-year periods conditioned on, among other things, payment of a 15-basis points extension fee upon each such extension. The Term Loan Facility has a maturity date of February 15, 2024. The Company is permitted to prepay all or any portion of the loans under the Credit Facility prior to maturity without premium or penalty, subject to reimbursement of any London Interbank Offered Rate ("LIBOR") breakage costs of the lenders.

The interest rates applicable to loans under the Revolving Credit Facility are, at the Company's option, equal to either a base rate plus a margin ranging from 1.0% to 1.3% per annum or LIBOR plus a margin ranging from 2.0% to 2.3% per annum based on the debt to assets ratio of the Company. The interest rates applicable to loans under the Term Loan Facility are, at the Company's option, equal to either a base rate plus a margin ranging from 0.9% to 1.2% per annum or LIBOR plus a margin ranging from 1.9% to 2.2% per annum based on the debt to assets ratio of the Company and its consolidated subsidiaries. The Company has chosen the second option for the interest rate applicable to the current loan under the term loan facility during the year ended December 31, 2019. In addition, the Company will pay (a) an unused facility fee on the revolving commitments under the Revolving Credit Facility ranging from 0.15% to 0.25% per annum, calculated daily based on the average unused commitments under the Revolving Credit Facility, and (b) with respect to any amount of the Term Loan Facility that remains undrawn during the period beginning thirty (30) days after the execution of the Credit Agreement and ending one year after execution of the Credit Agreement, an unused facility fee of 0.25% per annum, calculated daily based on the undrawn portion of the Term Loan Facility.

9. Fair Value Measurements

In accordance with ASC 820, Fair Value Measurement and Disclosures, the Company defines fair value based on the price that would be received upon sale of an asset or the exit price that would be paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Company uses a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value. The fair value hierarchy consists of three broad levels, which are described below:

- Level 1 - Quoted prices in active markets for identical assets or liabilities that the entity has the ability to access.
- Level 2 - Observable inputs, other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.
- Level 3 - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets and liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

The Company has estimated fair value using available market information and valuation methodologies the Company believes to be appropriate for these purposes. Considerable judgment and a high degree of subjectivity are involved in developing these estimates and, accordingly, they are not necessarily indicative of amounts that would be realized upon disposition.

Financial Assets and Liabilities Measured at Fair Value on a Recurring Basis

Risk Management Objective of Using Derivatives

The Company is exposed to certain risks arising from both its business operations and economic conditions. The Company principally manages its exposures to a wide variety of business and operational risks through management of its core business activities. The Company manages economic risks, including interest rate, liquidity, and credit risk primarily by managing the amount, sources, and duration of debt funding and, to a limited extent, the use of derivative financial instruments. Specifically, the Company may enter into derivative financial instruments to manage exposures that arise from business activities that result in the receipt or payment of future known and uncertain cash amounts, the value of which are determined by interest rates. The Company's derivative financial instruments, described below, are used to manage differences in the amount, timing, and duration of the Company's known or expected cash receipts and its known or expected cash payments principally related to the Company's borrowings.

Cash Flow Hedges of Interest Rate Risk

The Company's objectives in using interest rate derivatives are to add stability to interest expense and to manage its exposure to interest rate movements. To accomplish this objective, the Company may use interest rate swaps as part of its interest rate risk management strategy. Interest rate swaps designated as cash flow hedges involve the receipt of variable-rate amounts from a counterparty in exchange for the Company making fixed-rate payments over the life of the agreements without exchange of the underlying notional amount. We do not enter into derivative financial instruments for speculative purposes. As of December 31, 2019, we had one derivative financial instrument designated as a cash flow hedge, with a notional amount of $18,750 and a maturity date of September 1, 2023. This derivative is an interest rate swap that is measured at fair value on a recurring basis.

For derivatives designated and that qualify as cash flow hedges of interest rate risk, the gain or loss on the derivative is recorded in accumulated other comprehensive income on the consolidated balance sheets and is subsequently reclassified into interest expense in the same period during which the hedged transaction affects earnings. The amount recorded as other comprehensive income related to the unrealized gain on our derivative financial instrument was $21 for the year ended December 31, 2019. The Company had no derivative instruments during the year ended December 31, 2018. Realized gains and losses will be recognized as they accrue in interest expense.

(Amounts in thousands, except share and per share amounts)

Amounts reported in accumulated other comprehensive income related to derivatives will be reclassified to interest expense as interest payments are made on our variable rate debt. The Company estimates that $16 will be reclassified as a decrease to interest expense over the next twelve months.

The table below presents the fair value of the Company’s derivative financial instrument as well as its classification on the consolidated balance sheets as of December 31, 2019. The Company did not have any derivative instruments as of December 31, 2018.

	December 31, 2019			
	Level 1	**Level 2**	**Level 3**	**Total**
Derivative financial instruments designated as cash flow hedges:				
Classified as assets in “Deferred costs and other assets”	$ —	$ 21	$ —	$ 21

The fair value of our derivative financial instrument was determined using widely accepted valuation techniques, including discounted cash flow analysis on the expected cash flows of the derivative financial instrument. This analysis reflected the contractual terms of the derivative, including the period to maturity, and used observable market-based inputs, including interest rate market data and implied volatilities in such interest rates. While it was determined that the majority of the inputs used to value the derivative fall within Level 2 of the fair value hierarchy under authoritative accounting guidance, the credit valuation adjustments associated with the derivative also utilized Level 3 inputs, such as estimates of current credit spreads to evaluate the likelihood of default. However, as of December 31, 2019, the significance of the impact of the credit valuation adjustments on the overall valuation of the derivative financial instrument was assessed, and it was determined that these adjustments were not significant to the overall valuation of the derivative financial instrument. As a result, it was determined that the derivative financial instrument in its entirety should be classified in Level 2 of the fair value hierarchy.

Non-Recurring Measurements

During the year ended December 31, 2018, the Company identified certain assets which may have a reduction in the expected holding period, a reduction in occupancy or a reduction in fair market value which represented an impairment trigger, and recorded an impairment of investment properties of $4,667 on one net lease asset and one land parcel. No such impairments were recorded during the year ended December 31, 2019. The following table presents these assets measured at fair value on a nonrecurring basis as of December 31, 2018 aggregated by the level within the fair value hierarchy in which those measurements fall. Methods and assumptions used to estimate the fair value of these assets are described after the table.

	Fair Value				
	Level 1	**Level 2**	**Level 3**	**Total**	**Provision for impairment**
December 31, 2018					
Investment Properties	—	—	$ 19,225 (a)	$ 19,225	$ 4,667

(a) The estimate of fair value of the land parcel was based on recent negotiations for the sale of similar assets to third parties. The estimate of fair value relating to the correctional facility's impairment analysis was based on a 10-year discounted cash flow model. The cash flows consist of observable inputs such as contractual revenues and unobservable inputs such as forecasted revenues and expenses. These unobservable inputs are based on market conditions and the Company’s expected growth rates. Capitalization rates ranging from 4.00% to 10.50% and discount rates ranging from 5.30% to 11.00% were utilized in the models and are based upon observable rates that the Company believes to be within a reasonable range of current market rates.

Financial Instruments Not Measured at Fair Value

(Amounts in thousands, except share and per share amounts)

The table below represents the fair value of financial instruments presented at carrying values in the consolidated financial statements as of December 31, 2019 and 2018.

	December 31, 2019		December 31, 2018	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Mortgages payable and term loan	$ 94,926	$ 94,934	$ 35,443	$ 35,222

The Company estimates the fair value of its debt instruments using a weighted average market effective interest rate of 3.93% and 4.70% per annum as of December 31, 2019 and 2018, respectively. The Company estimates the fair value of its mortgage loans and term loan facility by discounting the anticipated future cash flows of each instrument at rates currently offered to the Company by its lenders for similar debt instruments of comparable maturities. The rates used are based on credit spreads observed in the marketplace during the quarter for similar debt instruments, and a floor rate that the Company has derived using its subjective judgment for each asset segment. Based on this, the Company determines the appropriate rate for each of its individual mortgage loans and term loan facility based upon the specific terms of the agreement, including the term to maturity, the quality and nature of the underlying property and its leverage ratio. The weighted average market effective interest rates used range from 3.42% to 4.93% and 4.18% to 5.03% as of December 31, 2019 and 2018, respectively. The fair value estimate of the unsecured credit facility approximated the carrying value due to limited market volatility in pricing. The assumptions reflect the terms currently available on similar borrowing terms to borrowers with credit profiles similar to the Company’s. The Company has determined that its debt instrument valuations are classified in Level 2 of the fair value hierarchy.

10. Income Taxes

The Company is taxed and operates in a manner that will allow the Company continue to qualify as a REIT for U.S. federal income tax purposes. So long as it maintains its qualification as a REIT, the Company generally will not be subject to U.S. federal income tax on taxable income that is distributed to stockholders. A REIT is subject to a number of organizational and operational requirements, including a requirement that it distribute at least 90% of its REIT taxable income (subject to certain adjustments) to its stockholders each year. If the Company fails to continue to qualify as a REIT in any taxable year, without the benefit of certain relief provisions, the Company will be subject to U.S. federal and state income tax on its taxable income at regular corporate tax rates and would not be able to re-elect REIT status during the four years following the year of the failure. Even if the Company qualifies for taxation as a REIT, the Company may be subject to certain state and local taxes on its income and U.S. federal income and excise taxes on its undistributed income.

MB REIT is currently disregarded as a separate entity from the Company for U.S. federal income tax purposes and is a QRS of the Company. All assets, liabilities and items of income, deduction and credit of MB REIT are treated for U.S. federal income tax purposes as those of the Company.

During the year ended December 31, 2019, no income tax benefit or expense was included in the consolidated statements of operations and comprehensive income. During the year ended December 31, 2018, an income tax benefit of $155, was included on the consolidated statements of operations and comprehensive income.

Uncertain Tax Positions

The Company had no unrecognized tax benefits as of or during the two year period ended December 31, 2019. The Company expects no significant increases or decreases in unrecognized tax benefits due to changes in tax positions within one year of December 31, 2019. The Company has no material interest or penalties relating to income taxes recognized in the consolidated statements of operations and comprehensive income for the years ended December 31, 2019 and 2018 or in the consolidated balance sheets as of December 31, 2019 and 2018. As of December 31, 2019, the Company's, including its predecessors, 2018, 2017 and 2016 tax years remain subject to examination by U.S. and various state tax jurisdictions.

11. Segment Reporting

(Amounts in thousands, except share and per share amounts)

GAAP has established guidance for reporting information about a company's operating segments. The Company monitors and reviews its segment reporting structure in accordance with guidance under FASB ASC Topic 280, Segment Reporting ("ASC 280") to determine whether any changes have occurred that would impact its reportable segments. The Company currently has four business segments, consisting of (i) net lease, (ii) retail, (iii) multi-tenant office and (iv) multi-family. The net lease segment consists of single-tenant office and industrial assets, as well as the Company's correctional facility. The Company's unimproved land asset is presented below in Other.

The following table summarizes net operating income (loss) by segment for the year ended December 31, 2019.

	Total	Net Lease	Retail	Multi-Tenant Office	Multi-family	Other
Rental income	$ 36,626	$ 12,450	$ 15,638	$ 79	$ 8,459	$ —
Other property income	727	—	149	38	534	6
Total income	37,353	12,450	15,787	117	8,993	6
Operating expenses	13,180	618	7,245	760	3,963	594
Net operating income (loss)	$ 24,173	$ 11,832	$ 8,542	$ (643)	$ 5,030	$ (588)
Non-allocated expenses (a)	(25,921)					
Other income and expenses (b)	(2,279)					
Gain on sale of investment properties (c)	8,841					
Net income	$ 4,814					
Balance Sheet Data						
Real estate assets, net (d)	$ 317,136	$ 34,755	$ 66,276	$ 26,400	$ 180,753	$ 8,952
Non-segmented assets (e)	83,096					
Total assets	400,232					
Capital expenditures	$ 1,011	$ —	$ 468	$ —	$ 543	$ —

(a) Non-allocated expenses consists of general and administrative expenses and depreciation and amortization.

(b) Other income and expenses consists of interest income and interest expense.

(c) Gain on the sale of investment properties is related to one retail asset and one other asset.

(d) Real estate assets include intangible assets, net of amortization.

(e) Non-segmented assets include cash and cash equivalents, restricted cash and escrows, accounts and rents receivable and deferred costs and other assets.

(Amounts in thousands, except share and per share amounts)

The following table summarizes net operating income (loss) by segment for the year ended December 31, 2018.

	Total	Net Lease	Retail	Multi-Tenant Office	Multi-family	Other
Rental income	$ 42,761	$ 12,725	$ 23,126	$ 4,526	$ 2,384	$ —
Other property income	748	—	39	523	186	—
Total income	43,509	12,725	23,165	5,049	2,570	—
Operating expenses and real estate taxes	13,920	577	9,461	2,702	1,063	117
Net operating income (loss)	$ 29,589	$ 12,148	$ 13,704	$ 2,347	$ 1,507	$ (117)
Non-allocated expenses (a)	(24,781)					
Other income and expenses (b)	(1,877)					
Provision for asset impairment (c)	(4,667)					
Gain on sale of investment properties (d)	27,863					
Loss on extinguishment of debt (e)	(1,199)					
Net income	$ 24,928					
Balance Sheet Data						
Real estate assets, net (f)	$ 242,145	$ 36,318	$ 113,853	$ 28,337	$ 54,159	$ 9,478
Non-segmented assets (g)	$ 93,835					
Total assets	$ 335,980					
Capital expenditures	$ 4,251	$ —	$ 676	$ 3,547	$ 35	$ (7)

(a) Non-allocated expenses consists of general and administrative expenses and depreciation and amortization.

(b) Other income and expenses consists of interest income, other income, interest expense, and income tax benefit.

(c) Provision for asset impairment includes $4,667 related to one net lease asset and one land parcel.

(d) Gain on sale of investment properties is related to the disposition of one multi-tenant office asset, one other asset and one retail asset.

(e) Loss on extinguishment of debt is related to prepayment penalties on the payoff of mortgage debt

(f) Real estate assets include intangible assets, net of amortization.

(g) Non-segmented assets include cash and cash equivalents, restricted cash and escrows, accounts and rents receivable, and deferred costs and other assets.

12. Earnings Per Share

Basic earnings per common share is calculated by dividing net income attributable to Highlands REIT, Inc. common stockholders by the weighted-average number of common shares outstanding during the period. Diluted earnings per common share is calculated by dividing net income attributable to Highlands REIT, Inc. common stockholders by the weighted-average number of common shares outstanding during the period, plus any additional common shares that would have been outstanding if the dilutive potential common shares had been issued.

The following table reconciles net income attributable to the Company to basic and diluted EPS (in thousands, except share and per share data):

	Year Ended December 31, 2019	Year Ended December 31, 2018
Numerator:		
Net income attributable to Highlands REIT, Inc. common stockholders	$ 4,849	$ 24,928
Denominator:		
Weighted average shares outstanding - basic and diluted	875,313,817	871,177,934
Basic and diluted income per share:		
Net income per common share	$ 0.01	$ 0.03

13. Share Based Compensation

Incentive Award Plan

On April 28, 2016, the board of directors adopted, ratified and approved the Highlands REIT, Inc. 2016 Incentive Award Plan (the “Incentive Award Plan”), under which the Company may grant cash and equity-based incentive awards to eligible employees, directors, and consultants. Prior to the Company’s spin-off from InvenTrust, the board of directors of the Company (then a wholly-owned subsidiary of InvenTrust) adopted, and InvenTrust, as the sole stockholder of Highlands, approved, the Incentive Awards Plan.

For the year ended December 31, 2019, the Company granted 6,100,002 of fully vested shares of common stock with an aggregate value of $2,135 based on an estimated fair value per share of $0.35. Additionally, under ASC 718, pursuant to an employment agreement with one of its executive officers, the Company granted shares with an aggregate value of $125 that will fully vest in August 2020, subject to the applicable executive's continued employment with the Company through the vesting date.

Under the Incentive Award Plan, the Company is authorized to grant up to 43,000,000 shares of the Company's common stock pursuant to awards under the plan. At December 31, 2019, 17,465,437 shares were available for future issuance under the Incentive Award Plan. A summary of the Company's stock awards activity as of December 31, 2019 is as follows:

(Amounts in thousands, except share and per share amounts)

Non-Vested stock awards	Stock Awards	Weighted Average Grant Date Fair Value
Balance at January 1, 2019	2,121,212	$ 0.33
Granted	6,100,002	0.35
Vested	(7,742,859)	0.35
Other [(1)]	(121,212)	—
Balance at December 31, 2019	357,143	$ 0.35

[(1)] Represents the change in the number of shares granted in 2018 based on an estimated net asset value per share of $0.33 and the actual shares vested in 2019 based on an estimated net asset value per share of $0.35.

The Company recognized stock-based compensation expense for the years ended December 31, 2019 and 2018 of $2,242 and $2,497, respectively, related to the Incentive Award Plan. At December 31, 2019, there was approximately $49 of estimated unrecognized compensation expense related to these awards. For the years ended December 31, 2019 and 2018, the Company paid $1,177 and $876, respectively, related to tax withholding for share-based compensation.

The Company repurchased and retired 116,334 of fully vested shares previously awarded to an employee pursuant to a separation agreement during the first quarter of 2018. The shares were repurchased for $0.33 per share, which was based on the Company's estimated share value as of December 31, 2017.

14. Commitments and Contingencies

The Company is subject, from time to time, to various legal proceedings and claims that arise in the ordinary course of business. While the resolution of these matters cannot be predicted with certainty, management believes, based on currently available information, that the final outcome of such matters will not have a material adverse effect on the financial statements of the Company.

Highlands has also agreed to indemnify InvenTrust against all taxes related to the Company and its assets, including taxes attributable to periods prior to the separation and distribution. InvenTrust has agreed to indemnify the Company for any taxes attributable to InvenTrust’s or MB REIT’s failure to maintain its qualification as a REIT for any taxable year ending on or before December 31, 2016.

(Amounts in thousands, except share and per share amounts)

15. Quarterly Supplemental Financial Information (unaudited)

The following represents the results of operations, for each quarterly period, during 2019 and 2018.

	For the Quarter Ended			
	March 31, 2019	June 30, 2019	September 30, 2019	December 31, 2019
Total revenues	$ 10,257	$ 10,401	$ 9,198	$ 7,497
Property operating expenses	1,904	1,985	1,565	2,035
Real estate taxes	1,306	1,317	1,156	1,912
Depreciation and amortization	2,730	2,729	3,109	4,446
General and administrative expenses	4,383	3,082	2,373	3,069
Total expenses	10,323	9,113	8,203	11,462
Gain on sale of investment properties	—	8,841	—	—
(Loss) income from operations	(66)	10,129	995	(3,965)
Interest income	369	398	581	302
Interest expense	(758)	(1,006)	(1,058)	(1,107)
Net (loss) income	(455)	9,521	518	(4,770)
Net loss (income) attributable to non-controlling interests	$ —	$ —	$ (10)	$ 45
Net (loss) income attributable to Highlands REIT, Inc. common stockholders	$ (455)	$ 9,521	$ 508	$ (4,725)
Net (loss) income per common share, basic and diluted	$ 0.00	$ 0.01	$ 0.00	$ (0.01)
Weighted average number of common shares outstanding, basic and diluted (a)	873,379,003	875,755,799	876,007,008	876,074,038

Notes to Consolidated Financial Statements
(Amounts in thousands, except share and per share amounts)
December 31, 2019

	For the Quarter Ended			
	March 31, 2018	June 30, 2018	September 30, 2018	December 31, 2018
Total revenues	$ 10,645	$ 10,823	$ 11,649	$ 10,392
Property operating expenses	2,304	1,991	2,353	2,244
Real estate taxes	1,474	766	1,388	1,400
Depreciation and amortization	3,131	3,216	3,406	2,425
General and administrative expenses	4,179	3,004	2,594	2,826
Provision for asset impairment	—	—	—	4,667
Total expenses	11,088	8,977	9,741	13,562
Gain on sale of investment properties	25	—	12,276	15,562
(Loss) income from operations	(418)	1,846	14,184	12,392
Interest income	133	157	81	126
Loss on extinguishment of debt	—	—	(1,199)	—
Other income	—	—	23	7
Interest expense	(706)	(708)	(700)	(445)
(Loss) income before income taxes	(991)	1,295	12,389	12,080
Income tax benefit	155	—	—	—
Net (loss) income	(836)	1,295	12,389	12,080
Net (loss) income per common share, basic and diluted	$ 0.00	$ 0.00	$ 0.01	$ 0.01
Weighted average number of common shares outstanding, basic and diluted (a)	870,102,100	871,427,298	871,537,188	871,624,475

(a) Quarterly income per common share amounts may not total the annual amounts due to rounding and the changes in number of weighted common shares outstanding.

HIGHLANDS REIT, INC.
Schedule III
Real Estate and Accumulated Depreciation
(Amounts in thousands)

		Initial Cost (A)				Gross amount at which carried at end of period				
	Encumbrance	Land	Buildings and Improvements	Adjustments to Land Basis (B)	Adjustments to Building Basis (B)	Land	Buildings and Improvements	Total (C)	Accumulated Depreciation (D,E)	Date of Completion of Construction or Acquisition
Retail										
BUCKHORN PLAZA Bloomsburg, PA	10,142	1,651	11,770	(35)	2,221	1,616	13,991	15,607	6,763	2006
SHERMAN PLAZA Evanston, IL		9,655	30,982		9,360	9,655	40,341	49,996	17,988	2006
STATE STREET MARKET Rockford, IL	9,166	3,950	14,184		1,821	3,950	16,006	19,956	7,930	2006
THE MARKET AT HILLIARD Hilliard, OH	15,511	4,432	13,308		3,483	4,432	16,791	21,223	7,824	2005
Net Lease										
CITIZENS (CFG) RHODE ISLAND Providence, RI		1,278	3,817	(702)	(2,947)	576	870	1,446	233	1970
ATLAS - ST PAUL St. Paul, MN		3,890	10,093			3,890	10,093	13,983	4,327	2007
ATLAS-NEW ULM New Ulm, MN		900	9,359			900	9,359	10,259	4,019	2007
HUDSON CORRECTIONAL FACILITY Hudson, CO		1,382		(908)	18,017	474	18,017	18,491	845	2009

HIGHLANDS REIT, INC.
Schedule III
Real Estate and Accumulated Depreciation
(Amounts in thousands)

		Initial Cost (A)				Gross amount at which carried at end of period				
	Encumbrance	Land	Buildings and Improvements	Adjustments to Land Basis (B)	Adjustments to Building Basis (B)	Land	Buildings and Improvements	Total (C)	Accumulated Depreciation (D,E)	Date of Completion of Construction or Acquisition
Multi-tenant office										
TRIMBLE I San Jose, CA		12,732	10,045		5,784	12,732	15,829	28,561	2,161	2013
Multi-family										
BUERGER BROTHER LOFTS Denver, CO		3,117	7,114		183	3,117	7,297	10,414	607	2017
CHAMBER LOFTS Denver, CO		2,797	6,388		83	2,797	6,471	9,268	538	2017
THE LAFAYETTE Denver, CO		2,457	7,067		149	2,457	7,216	9,673	406	2018
KENILWORTH COURT Denver, CO		2,496	3,203		7	2,496	3,210	5,706	149	2018
1620 CENTRAL STREET Evanston, IL		3,075	17,140		93	3,075	17,233	20,308	864	2018
THE DETROIT AND DETROIT TERRACES Denver, CO	11,449	3,370	15,006		—	3,370	15,006	18,376	531	2019
TENNYSON Denver, CO		1,533	17,410		—	1,533	17,410	18,943	349	2019
THE MUSE Denver, CO		5,303	42,809		7	5,303	42,816	48,119	281	2019
THE VIEW San Diego, CA		7,272	8,862		10	7,272	8,869	16,141	254	2019
THE LOCALE (FORMERLY EVOLVE AT ALLENDALE) Allendale, MI	18,658	4,294	22,461		46	4,294	22,507	26,801	357	2019
Other										
PALAZZO DEL LAGO Orlando, FL		8,938			19	8,938	19	8,957	5	2010
Totals	$ 64,926	$84,522	$ 251,018	$ (1,645)	$ 38,336	$82,877	$ 289,351	$372,228	$ 56,431	

(Amounts in thousands)

Notes to Schedule III:

The aggregate cost of real estate owned at December 31, 2019 for U.S. federal income tax purposes was approximately $445,244 (unaudited).

(A) The initial cost to the Company represents the original purchase price of the asset, including amounts incurred subsequent to acquisition which were contemplated at the time the asset was acquired.

(B) Adjustments to basis include provisions for asset impairments, partial dispositions and costs capitalized subsequent to acquisitions.

(C)Reconciliation of real estate owned:

	2019	2018
Balance at January 1	$ 314,527	$ 375,367
Acquisitions and capital improvements	129,407	38,303
Dispositions and write-offs	(71,706)	(73,105)
Asset impairments	—	(26,038)
Balance at December 31,	$ 372,228	$ 314,527

(D)Reconciliation of accumulated depreciation:

	2019	2018
Balance at January 1	$ 72,822	$ 109,928
Depreciation expense	9,637	10,984
Dispositions and write-offs	(26,028)	(26,720)
Asset impairments	—	(21,370)
Balance at December 31,	$ 56,431	$ 72,822

(E)Depreciation is computed based upon the following estimated lives:

Buildings and improvements	30 years
Tenant improvements	Life of the lease
Furniture, fixtures, & equipment	5-15 years

Item 9. Changes in or Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

Disclosure Controls and Procedures

As required by Rule 13a-15(b) and Rule 15d-15(b) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), our management, including our principal executive officer and our principal financial officer evaluated, as of December 31, 2019, the effectiveness of our disclosure controls and procedures as defined in Rules 13a-15(e) and Rule 15d-15(e) of the Exchange Act. Based on that evaluation, our principal executive officer and our principal financial officer concluded that our disclosure controls and procedures, as of December 31, 2019, were effective at a reasonable assurance level for the purpose of ensuring that information required to be disclosed by us in this report is recorded, processed, summarized and reported within the time periods specified by the rules and forms of the Exchange Act and is accumulated and communicated to management, including our principal executive officer and our principal financial officer, as appropriate, to allow timely decisions regarding required disclosures.

Management's Annual Report on Internal Control Over Financial Reporting.

Our management is responsible for establishing and maintaining adequate internal controls over financial reporting pursuant to Exchange Act Rules 13a-15(f) and 15d-15(f) as of December 31, 2019. Our management, including our principal executive officer and principal financial officer evaluated the effectiveness of our internal controls over financial reporting based on the framework in "Internal Control-Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013). Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Therefore, even those systems determined to be effective can only provide reasonable assurance with respect to financial statement preparation and presentation. Based on its evaluation, our management has concluded that we maintained effective internal control over financial reporting as of December 31, 2019.

Changes in Internal Control Over Financial Reporting

There has been no change in the Company’s internal control over financial reporting during the quarter ended December 31, 2019 that has materially affected, or is reasonably likely to materially affect, the Company’s internal control over financial reporting.

Item 9B. Other Information

2020 Annual Meeting of Stockholders Record Date

On February 7, 2020, the Board established the close of business on March 20, 2020 as the record date for determining stockholders entitled to vote at our 2020 Annual meeting of stockholders, expected to be held on June 4, 2020.

Part III

Item 10. Directors, Executive Officers and Corporate Governance.

Except as set forth below, the information called for by this Item is contained in our definitive Proxy Statement for our 2020 Annual Meeting of Stockholders, and is incorporated herein by reference.

Executive Officers of the Registrant

Richard Vance, age 56, has served as a director and our President and Chief Executive Officer since our formation in December 2015. Prior to our spin-off from InvenTrust Properties Corp. (“*InvenTrust*”), Mr. Vance served as Senior Vice President - Portfolio Management & Corporate Strategy for InvenTrust, where he was responsible for managing InvenTrust’s “non-core” portfolio with regard to asset management, property operations and leasing. Beginning in 2013 and until InvenTrust’s self-management in 2014, Mr. Vance served as Vice President for InvenTrust’s former business manager, and, following InvenTrust’s self-management, Mr. Vance continued to serve as Vice President for InvenTrust until 2015. In this role, Mr. Vance had various responsibilities, including spearheading InvenTrust’s self-management and various asset management responsibilities. Beginning in 2010, Mr. Vance began working with InvenTrust’s former business manager and former property manager as an independent consultant, and was primarily responsible for managing a diverse portfolio of InvenTrust’s office, industrial and retail assets. Mr. Vance has more than 20 years of experience in commercial real estate and commercial real estate finance, including various positions prior to 2010 with GMAC Commercial Mortgage, Equity Residential, Deutsche Bank, Ernst & Young or their affiliates. Mr. Vance received a Master of Business Administration degree from the University of Michigan-Ann Arbor, a Juris Doctor from Loyola University of Chicago, and a Bachelor of Arts from the University of Michigan-Flint.

Robert J. Lange, age 37, has served as Executive Vice President, General Counsel and Secretary of Highlands since June 2016. Prior to joining the Company, Mr. Lange served as Vice President, Head Corporate Counsel and Assistant Secretary at InvenTrust, Highlands’ former parent company. In that capacity, he oversaw all aspects of InvenTrust’s corporate legal affairs, including material transactions, governance, public company reporting and compliance, employee matters and executive compensation and benefits. Prior to joining InvenTrust in 2014, Mr. Lange practiced law at Skadden Arps Slate Meagher & Flom LLP, where he represented companies in mergers and acquisitions and advised clients on a broad variety of general corporate matters. Mr. Lange received a Bachelor of Business Administration degree, with distinction, from the University of Wisconsin - Madison and a Juris Doctor degree, with honors, from the University of Chicago.

Paul A. Melkus, age 55, has served as Executive Vice President and Chief Financial Officer of Highlands since 2018. Prior to this appointment, Mr. Melkus served from April 2016 to April 2018 as a director of Highlands, chair of the board’s audit committee, and a member of the board’s compensation committee. Mr. Melkus served as Global Head of Capital Markets - Real Estate and Infrastructure Department for the Abu Dhabi Investment Authority, one of the world’s largest sovereign wealth funds, and as a member of its Executive Committee from 2012 to 2016. In this role, he was responsible for the development of financing strategy and management of lending relationships for Abu Dhabi Investment Authority’s global real estate investment portfolio. Mr. Melkus served as Senior Vice President - Capital Markets at General Growth Properties, Inc., a publicly traded REIT, from 2010 to 2011, as Director - Capital Markets at Deutsche Bank Asset Management from 2004 to 2009 and as Director - Capital Markets Investments at General Electric Capital Corporation from 1998 to 2004. Mr. Melkus has also consulted at Ernst & Young on a variety of capital markets and real estate related transactions and served as a securities analyst and asset manager at Northern Trust Company. Mr. Melkus is a graduate of DePauw University where he earned his Bachelor of Arts majoring in Economics and Management. He earned his Master of Science degree from the University of Wisconsin’s Real Estate Investment and Urban Economics program.

Kimberly A. Karas, age 44, has served as Senior Vice President and Controller of Highlands since July 8, 2019. Prior to this appointment, Ms. Karas previously served as Vice President of Finance for Link Industrial Properties (formerly Gateway Industrial Properties), a Blackstone platform company, from 2018 to 2019. Blackstone is one of the largest real estate private equity firms in the world. In this role, Ms. Karas was responsible for the budget and forecast of the industrial platform, financial integration of new acquisitions and the creation of operating tools and reports. Ms. Karas previously worked at IRC Retail Centers (formerly Inland Real Estate Corporation) from 2000 to 2018, most recently serving as Vice President and Controller and as a member of its Management Committee. In this role, she oversaw the corporate accounting function, with responsibilities over Securities and Exchange Commission reporting, preparation of consolidated financial statements, maintenance of accounting policies and procedures, compliance with the Sarbanes-Oxley Act of 2002 and coordination of annual audits and tax return filings. Ms. Karas earned her Bachelor of Science in Accounting from the University of Illinois at Chicago.

Code of Ethics

Our board has adopted a code of ethics and business conduct (the “Code of Ethics and Business Conduct”) applicable to our directors, officers and employees, which is available on our website at www.highlandsreit.com through the “Investor Relations - Governance Documents” tab. In the event that the Company amends or waives any of the provisions of the Code of Ethics that applies to the Company's Chief Executive Officer, Chief Financial Officer or Principal Accounting Officer, and other senior financial officers performing similar functions, the Company intends to disclose the subsequent information on its website. In addition, printed copies of the Code of Ethics and Business Conduct are available to any stockholder, without charge, by writing us at Highlands REIT, Inc., attn Corporate Secretary, 332 S. Michigan Avenue, 9th Floor, Chicago, Illinois 60604.

Item 11. Executive Compensation.

The information called for by this Item is contained in our definitive Proxy Statement for our 2020 Annual Meeting of Stockholders, and is incorporated herein by reference.

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

Except as set forth below, the information called for by this Item is contained in our definitive Proxy Statement for our 2020 Annual Meeting of the Stockholders, and is incorporated herein by reference.

Securities Authorized for Issuance Under Equity Compensation Plans

The following table sets forth information regarding securities authorized for issuance under our equity compensation plans, as of December 31, 2019.

	(a)	(b)	(c)
Plan category	Number of securities to be issued upon exercise of outstanding rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity compensation plans approved by security holders			
Highlands REIT, Inc. 2016 Incentive Award Plan	—	—	17,465,437
Equity compensation plans not approved by security holders	—	—	—
Total	—	—	17,465,437

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

The information called for by this Item is contained in our definitive Proxy Statement for our 2020 Annual Meeting of Stockholders, and is incorporated herein by reference.

Item 14. Principal Accountant Fees and Services.

The information called for by this Item is contained in our definitive Proxy Statement for our 2020 Annual Meeting of Stockholders, and is incorporated herein by reference.

Part IV.

Item 15. Exhibits and Financial Statement Schedules

(a) List of documents filed:

- a. Financial Statements:
  - i. Report of Independent Registered Public Accounting Firm
  - ii. The consolidated financial statements of the Company are set forth in the report in Item 8.
- b. Financial Statement Schedules:
  - i. Real Estate and Accumulated Depreciation (Schedule III)
  - ii. All schedules other than those indicated in the index have been omitted as the required information is inapplicable or the information is presented in the consolidated financial statements or related notes.
- c. Exhibits:
  - i. The list of exhibits filed as part of this Annual Report is set forth on the Exhibit Index attached hereto.

(b) Exhibits:

- a. The exhibits filed in response to Item 601 of Regulation S-K are listed on the Exhibit Index attached hereto.

(c) Financial Statement Schedules

All schedules other than those indicated in the index have been omitted as the required information is inapplicable or the information is presented in the consolidated financial statements or related notes.

Item 16. Form 10-K Summary

Omitted at registrant's option.

EXHIBIT NO.	DESCRIPTION
2.1	Separation and Distribution Agreement between Highlands REIT, Inc. and InvenTrust Properties Corp., dated as of April 15, 2016 (incorporated by reference to Exhibit 2.1 to the Company’s Current Report on Form 8-K filed on April 14, 2016)
3.1	Articles of Amendment and Restatement of Highlands REIT, Inc. (incorporated by reference to Exhibit 4.1 to the Company's Registration Statement on Form S-8, filed with the Securities and Exchange Commission on April 27, 2016)
3.2	Amended and Restated Bylaws of Highlands REIT, Inc. (incorporated by reference to Exhibit 3.2 to the Company's Current Report on Form 8-K, filed with the Securities and Exchange Commission on April 28, 2016)
4.1	Description of Securities Registered Pursuant to Section 12 of the Securities Exchange Act of 1934
10.1	Transition Services Agreement between Highlands REIT, Inc. and InvenTrust Properties Corp., dated as of April 28, 2016 (incorporated by reference to Exhibit 2.1 to the Company’s Current Report on Form 8-K filed on April 14, 2016)
10.2	Employee Matters Agreement between Highlands REIT, Inc. and InvenTrust Properties Corp., dated as of April 28, 2016 (incorporated by reference to Exhibit 2.1 to the Company’s Current Report on Form 8-K filed on April 14, 2016)
10.3#	Highlands REIT, Inc. 2016 Incentive Award Plan (incorporated by reference to Exhibit 99.1 to the Company’s Registration Statement on Form S-8, filed with the Securities and Exchange Commission on April 27, 2016)
10.4#	Form of Indemnification Agreement entered into between Highlands REIT, Inc. and each of its directors and executive officers (incorporated by reference to Exhibit 10.5 of Company’s Registration Statement on Form 10, filed with the Securities and Exchange Commission on March 18, 2016)
10.5#	First Amendment to Highlands REIT, Inc. 2016 Incentive Award Plan (incorporated by reference to Exhibit 10.5 to the Company’s Quarterly Report on Form 10-Q, filed with the Securities and Exchange Commission on May 10, 2016)
10.6#	Form of Highlands REIT, Inc. 2016 Incentive Award Plan Stock Payment Award Grant Notice (incorporated by reference to Exhibit 10.8 to the Company’s Quarterly Report on Form 10-Q, filed with the Securities and Exchange Commission on May 10, 2016)
10.7#	Amended and Restated Employment Agreement, dated November 7, 2018, by and between Highlands REIT, Inc. and Richard Vance (incorporated by reference to Exhibit 10.1 to the Company’s Current Report on Form 8-K, filed with the Securities and Exchange Commission on November 8, 2018)
10.8#	Amended and Restated Employment Agreement, dated November 7, 2018, by and between Highlands REIT, Inc. and Robert J. Lange (incorporated by reference to Exhibit 10.2 to the Company’s Current Report on Form 8-K, filed with the Securities and Exchange Commission on November 8, 2018)
10.9#	Highlands REIT, Inc. Director Compensation Program (incorporated by reference to Exhibit 10.9 of Amendment No. 1 to the Company’s Registration Statement on Form 10, filed with the Securities and Exchange Commission on April 8, 2016)
10.10#	Highlands REIT, Inc. Retention Bonus Plan (incorporated by reference to Exhibit 10.10 to the Company's Quarterly Report on Form 10-Q, filed with the Securities Exchange Commission on August 12, 2016)
10.11#	Amended and Restated Employment Agreement, dated November 7, 2018, by and between Highlands REIT, Inc. and Paul Melkus (incorporated by reference to Exhibit 10.3 to the Company’s Current Report on Form 8-K, filed with the Securities and Exchange Commission on November 8, 2018)
10.12#	Offer Letter, dated June 6, 2019, by and between Highlands REIT, Inc. and Kimberly A. Karas (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K, filed with the Securities and Exchange Commission on July 12, 2019)
10.13#	Change in Control and Severance Agreement, dated as of July 8, 2019, by and between Highlands REIT, Inc. and Kimberly A. Karas (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K, filed with the Securities and Exchange Commission on July 12, 2019)
10.14	Credit Agreement, dated February 15, 2019, by and among Highlands REIT, Inc., a Maryland corporation, as borrower, and certain of its subsidiaries, as guarantors, The Huntington National Bank, certain other lending institutions party thereto, as lenders, and The Huntington National Bank, as administrative agent and as issuing lender, lead arranger, book manager and syndication agent (incorporated by reference to Exhibit 10.1 to the Company’s Current Report on Form 8-K, filed with the Securities and Exchange Commission on February 21, 2019)

EXHIBIT NO.	DESCRIPTION
10.15*	First Amendment to Credit Agreement, dated November 12, 2019, by and among Highlands REIT, Inc., a Maryland corporation, as borrower, and certain of its subsidiaries, as guarantors, The Huntington National Bank, certain other lending institutions party thereto, as lenders, and The Huntington National Bank, as administrative agent and as issuing lender, lead arranger, book manager and syndication agent
10.16*	Second Amendment to Credit Agreement, dated February 20, 2020, by and among Highlands REIT, Inc., a Maryland corporation, as borrower, and certain of its subsidiaries, as guarantors, The Huntington National Bank, certain other lending institutions party thereto, as lenders, and The Huntington National Bank, as administrative agent and as issuing lender, lead arranger, book manager and syndication agent
10.17	Purchase and Sale Agreement, dated as of September 26, 2019, by and between Hill University Partners Owner, LLC and The Muse Owner, LLC (incorporated by reference to Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q, filed with the Securities and Exchange Commission on November 12, 2019)
10.18	Agreement of Purchase and Sale, dated February 13, 2019, by and among MB Lincoln Mall, LLC, as seller, and Lincoln Mall Owner, LLC, as purchaser (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q, filed with the Securities and Exchange Commission on May 10, 2019)
21.1*	List of Subsidiaries
23.1*	Consent of KPMG LLP
31.1*	Certification of Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2*	Certification of Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1*	Certification of Principal Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2*	Certification of Principal Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema Document
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document
101.PRE*	XBRL Taxonomy Extension Presentation Link Document

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* Filed as part of this Annual Report on Form 10-K.

\# Management contract or compensatory plan or arrangement.

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.

HIGHLANDS REIT, INC.
By: /s/ Richard Vance
Name: Richard Vance
Title: President and Chief Executive Officer
(Principal Executive Officer)
Date: March 20, 2020

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

Signature	Title	Date
/s/ Richard Vance Richard Vance	President and Chief Executive Officer (Principal Executive Officer) and Director	March 20, 2020
/s/ Paul Melkus Paul Melkus	Executive Vice President and Chief Financial Officer (Principal Financial Officer)	March 20, 2020
/s/ Kimberly A. Karas Kimberly A. Karas	Senior Vice President and Controller (Principal Accounting Officer)	March 20, 2020
/s/ R. David Turner R. David Turner	Director and Chairman	March 20, 2020
/s/ Jeffrey L. Shekell Jeffrey L. Shekell	Director	March 20, 2020

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Section 2: EX-4.1 (EXHIBIT 4.1)

Exhibit 4.1

DESCRIPTION OF SECURITIES
REGISTERED PURSUANT TO SECTION 12 OF THE
SECURITIES EXCHANGE ACT OF 1934

Highlands REIT, Inc. (“our company,” “we,” “our” or “us”) has one class of securities registered under Section 12 of the Securities Exchange Act of 1934, as amended: our common stock, par value $0.01 per share (“common stock”). The following summary of the common stock does not purport to be complete and is subject to and qualified in its entirety by reference to Maryland law and to our charter and bylaws, copies of which are incorporated by reference as exhibits to our Annual Report on Form 10-K.

General

Our charter provides that we may issue up to 1,000,000,000 shares of common stock, $0.01 par value per share, and up to 50,000,000 shares of preferred stock, $0.01 par value per share ("preferred stock"). Our board of directors has the power, without stockholder approval, to amend our charter from time to time to increase or decrease the aggregate number of shares of stock or the number of shares of stock of any class or series we are authorized to issue. Under Maryland law, stockholders generally are not personally liable for our debts or obligations solely as a result of their status as stockholders.

Common Stock

All outstanding shares of our common stock will be duly authorized, fully paid and nonassessable. Our common stockholders are entitled to receive dividends when authorized by our board of directors and declared by us out of assets legally available for the payment of dividends. Our common stockholders are also entitled to share ratably in our assets legally available for distribution to our stockholders in the event of our liquidation, dissolution or winding up, after payment of, or adequate provision for, all of our known debts and liabilities. These rights are subject to the preferential rights of any other class or series of our stock and to the provisions of our charter regarding restrictions on ownership and transfer of our stock.

Subject to our charter restrictions on ownership and transfer of our stock and except as may otherwise be provided in our charter, each outstanding share of our common stock entitles the holder thereof to one vote on all matters submitted to a vote of stockholders, including the election of directors. Except as provided with respect to any other class or series of stock, our common stockholders will possess exclusive voting power. Cumulative voting in the election of directors is not permitted. Directors will be elected by a plurality of all of the votes cast in the election of directors at a duly called meeting at which a quorum is present. A majority of the votes cast at a meeting of stockholders duly called and at which a quorum is present shall be sufficient to approve any other matter which may properly come before the meeting, unless more than a majority of the votes cast is required by statute or by the charter.

Our common stockholders have no preference, conversion, exchange, sinking fund or redemption rights and have no preemptive rights to subscribe for any of our capital stock. Subject to our charter restrictions on ownership and transfer of our stock, holders of shares of our common stock will initially have equal dividend, liquidation and other rights. Our common stockholders will not have appraisal rights unless our board of directors determines that appraisal rights apply, with respect to all or any classes or series of stock, to one or more transactions occurring after the date of such determination in connection with which stockholders would otherwise be entitled to exercise appraisal rights.

Our charter authorizes our board of directors to reclassify any unissued shares of our common stock into other classes or series of stock, to establish the designation and number of shares of each such class or series and to set or change, subject to the provisions of our charter regarding the restrictions on ownership and transfer of our stock, the preferences, conversion or other rights, voting powers, restrictions, limitations as to dividends or other distributions, qualifications or terms or conditions of redemption of each such class or series.

Preferred Stock

Under the terms of our charter, our board of directors is authorized to classify any unissued shares of our preferred stock and to reclassify any previously classified but unissued shares of preferred stock into other classes or series of stock. Before the issuance of shares of each class or series, our board of directors is required by Maryland law and our charter to set, subject to our charter restrictions on ownership and transfer of stock, the terms, preferences, conversion or other rights, voting powers, restrictions, limitations as to dividends or other distributions, qualifications or terms or conditions of redemption for each class or series. As a result, our board of directors could authorize the issuance of shares of preferred stock that have priority over shares of our common stock with respect to dividends or other distributions or rights upon liquidation, exclusive or class voting rights or with other terms and conditions that could have the effect of delaying, deferring or preventing a transaction or a change of control of our company that might involve a premium price for holders of our common stock or that our common stockholders otherwise believe to be in their best interest. As of the date hereof, we have no outstanding shares of preferred stock.

Power to Issue Additional Shares of Common Stock and Preferred Stock

Our board has the power to authorize the issuance of additional shares of our common stock or preferred stock and to classify or reclassify unissued shares of our common stock or preferred stock and to authorize the issuance of such classified or reclassified shares. These actions can be taken without action by our stockholders, unless stockholder approval is required by applicable law or the rules of any stock exchange or automated quotation system on which our stock may be listed or traded. Although we have no present intention of doing so, we could issue a class or series of stock that could delay, defer or prevent a transaction or a change in control of our company that might involve a premium price for our common stock or that our common stockholders otherwise believe to be in their best interest.

Restrictions on Ownership and Transfer

In order to qualify as a REIT under the Code, our shares of stock must be beneficially owned by 100 or more persons during at least 335 days of a taxable year of 12 months (other than the first year for which an election to be a REIT has been made) or during a proportionate part of a shorter taxable year. Also, not more than 50% of the value of our outstanding shares of capital stock may be owned, directly or indirectly, by five or fewer individuals (as defined in the Code to include certain entities) during the last half of a taxable year (other than the first year for which an election to be a REIT has been made).

Our charter, subject to certain exceptions, contains restrictions on the number of shares of our stock that a person may own. Our charter provides that no person may beneficially or constructively own more than 9.8% in value or in number of shares, whichever is more restrictive, of the outstanding shares of any class or series of our capital stock. We refer to the foregoing restrictions as the “Ownership Limit.”

Our charter also prohibits any person from:

- beneficially owning shares of our capital stock to the extent that such beneficial ownership would result in our being “closely held” within the meaning of Section 856(h) of the Code (without regard to whether the ownership interest is held during the last half of the taxable year);
- transferring shares of our capital stock to the extent that such transfer would result in our shares of capital stock being beneficially owned by fewer than 100 persons (determined under the principles of Section 856(a)(5) of the Code);
- beneficially or constructively owning shares of our capital stock to the extent such beneficial or constructive ownership would cause us to constructively own ten percent or more of the ownership interests in a tenant (other than a TRS) of our real property within the meaning of Section 856(d)(2)(B) of the Code; or
- beneficially or constructively owning or transferring shares of our capital stock if such beneficial or constructive ownership or transfer would otherwise cause us to fail to qualify as a REIT under the Code.

Our board of directors, in its sole discretion, may prospectively or retroactively exempt a person from certain of the limits described in the paragraph above and may establish or increase an excepted holder percentage limit for that person. The person seeking an exemption must provide to our board of directors any representations, covenants and undertakings that our board of directors may deem appropriate in order to conclude that granting the exemption will not cause us to lose our status as a REIT. Our board of directors may not grant an exemption to any person if that exemption would result in our failing to qualify as a REIT. Our board of directors may require a ruling from the IRS or an opinion of counsel, in either case in form and substance satisfactory to our board of directors, in its sole discretion, in order to determine or ensure our status as a REIT.

Any attempted transfer of shares of our capital stock which, if effective, would violate any of the restrictions described above will result in the number of shares of our capital stock causing the violation (rounded up to the nearest whole share) to be automatically transferred to a trust for the exclusive benefit of one or more charitable beneficiaries, except that any transfer that results in the violation of the restriction relating to shares of our capital stock being beneficially owned by fewer than 100 persons will be void ab initio. In either case, the proposed transferee will not acquire any rights in those shares. The automatic transfer will be deemed to be effective as of the close of business on the business day prior to the date of the purported transfer or other event that results in the transfer to the trust. Shares held in the trust will be issued and outstanding shares. The proposed transferee will not benefit economically from ownership of any shares held in the trust, will have no rights to dividends or other distributions and will have no rights to vote or other rights attributable to the shares held in the trust. The trustee of the trust will have all voting rights and rights to dividends or other distributions with respect to shares held in the trust. These rights will be exercised for the exclusive benefit of the charitable beneficiary. Any dividend or other distribution paid prior to our discovery that shares have been transferred to the trust will be paid by the recipient to the trustee upon demand. Any dividend or other distribution authorized but unpaid will be paid when due to the trustee. Any dividend or other distribution paid to the trustee will be held in trust for the charitable beneficiary. Subject to Maryland law, the trustee will have the authority (i) to rescind as void any vote cast by the proposed transferee prior to our discovery that the shares have been transferred to the trust and (ii) to recast the vote in accordance with the desires of the trustee acting for the benefit of the charitable beneficiary. However, if we have already taken irreversible corporate action, then the trustee will not have the authority to rescind and recast the vote.

Within 20 days of receiving notice from us that shares of our stock have been transferred to the trust, the trustee will sell the shares to a person, designated by the trustee, whose ownership of the shares will not violate the above ownership and transfer limitations. Upon the sale, the interest of the charitable beneficiary in the shares sold will terminate and the trustee will distribute the net proceeds of the sale to the proposed transferee and to the charitable beneficiary as follows. The proposed transferee will receive the lesser of (i) the price paid by the proposed transferee for the shares or, if the proposed transferee did not give value for the shares in connection with the event causing the shares to be held in the trust (e.g., a gift, devise or other similar transaction), the market price (as defined in our charter) of the shares on the day of the event causing the shares to be held in the trust and (ii) the price per share received by the trustee (net of any commission and other expenses of sale) from the sale or other disposition of the shares. The trustee may reduce the amount payable to the proposed transferee by the amount of dividends or other distributions paid to the proposed transferee and owed by the proposed transferee to the trustee. Any net sale proceeds in excess of the amount payable to the proposed transferee will be paid immediately to the charitable beneficiary. If, prior to our discovery that shares of our stock have been transferred to the trust, the shares are sold by the proposed transferee, then (i) the shares shall be deemed to have been sold on behalf of the trust and (ii) to the extent that the proposed transferee received an amount for the shares that exceeds the amount he or she was entitled to receive, the excess shall be paid to the trustee upon demand.

In addition, shares of our stock held in the trust will be deemed to have been offered for sale to us, or our designee, at a price per share equal to the lesser of (i) the price per share in the transaction that resulted in the transfer to the trust (or, in the case of a devise or gift, the market price at the time of the devise or gift) and (ii) the market price on the date we, or our designee, accept the offer, which we will reduce by the amount of dividends and other distributions paid to the proposed transferee and owed by the proposed transferee to the trustee. We will have the right to accept the offer until the trustee has sold the shares. Upon a sale to us, the interest of the charitable beneficiary in the shares sold will terminate and the trustee will distribute the net proceeds of the sale to the proposed transferee. If a transfer to a charitable trust, as described above, would be ineffective for any reason to prevent a violation of a restriction, the transfer that would have resulted in a violation will be void ab initio, and the proposed transferee shall acquire no rights in those shares.

Any certificate representing shares of our capital stock, and any notices delivered in lieu of certificates with respect to the issuance or transfer of uncertificated shares, will bear a legend referring to the restrictions described above.

Any person who acquires or attempts or intends to acquire beneficial or constructive ownership of shares of our capital stock that will or may violate any of the foregoing restrictions on transferability and ownership, or any person who would have owned shares of our capital stock that resulted in a transfer of shares to a charitable trust, is required to give written notice immediately to us, or in the case of a proposed or attempted transaction, to give at least 15 days' prior written notice, and provide us with such other information as we may request in order to determine the effect of the transfer on our status as a REIT. The foregoing restrictions on transferability and ownership will not apply if our board of directors determines that it is no longer in our best interests to attempt to qualify, or to continue to qualify, as a REIT or that compliance is no longer required in order for us to qualify as a REIT.

Every owner of 5% or more (or any lower percentage as required by the Code or the regulations promulgated thereunder) in number or value of the outstanding shares of our capital stock, within 30 days after the end of each taxable year, is required to give us written notice, stating his or her name and address, the number of shares of each class and series of shares of our capital stock that he or she beneficially owns and a description of the manner in which the shares are held. Each of these owners must provide us with additional information that we may request in order to determine the effect, if any, of his or her beneficial ownership on our status as a REIT and to ensure compliance with the ownership limits. In addition, each stockholder will upon demand be required to provide us with information that we may request in order to determine our status as a REIT and to comply with the requirements of any taxing authority or governmental authority or to determine such compliance and to ensure compliance with our Ownership Limit.

These ownership limitations could delay, defer or prevent a transaction or a change in control that might involve a premium price for our shares of common stock or otherwise be in the best interest of our stockholders.

Certain Provisions of Maryland Law and Our Charter and Bylaws

The following summary of certain provisions of Maryland law and our charter and bylaws does not purport to be complete and is subject to and qualified in its entirety by reference to Maryland law and to our amended and restated charter and bylaws, copies of which are incorporated by reference as exhibits to our Annual Report on Form 10-K.

Our Board of Directors

According to our charter and bylaws, the number of directors of our company may be established, increased or decreased only by a majority of our entire board of directors but may not be fewer than the minimum number required under the MGCL (which is currently one) nor, unless our bylaws are amended, more than 15. We currently have 3 directors. Our charter provides that, at such time as we have a class of securities registered under the Exchange Act and at least three independent directors, we will elect to be subject to a provision of Maryland law requiring that vacancies on our board of directors may be filled only by an affirmative vote of a majority of the remaining directors and that any individual elected to fill a vacancy will serve for the remainder of the full term of the directorship in which the vacancy occurred and until his or her successor is duly elected and qualifies.

Removal of Directors

Our charter provides that, subject to the rights of holders of one or more classes or series of preferred stock to elect or remove one or more directors, a director may be removed only for cause (as defined in our charter) and only by the affirmative vote of stockholders entitled to cast at least two-thirds of the votes entitled to be cast generally in the election of directors.

Business Combinations

Under the Maryland General Corporation Law ("MGCL"), certain "business combinations" (including a merger, consolidation, statutory share exchange or, in certain circumstances specified under the statute, an asset transfer or issuance or reclassification of equity securities) between a Maryland corporation and any interested stockholder, or an affiliate of such an interested stockholder, are prohibited for five years after the most recent date on which the interested stockholder becomes an interested stockholder. Maryland law defines an interested stockholder as:

- any person who beneficially owns, directly or indirectly, 10% or more of the voting power of the corporation's outstanding voting stock; or
- an affiliate or associate of the corporation who, at any time within the two-year period prior to the date in question, was the beneficial owner of 10% or more of the voting power of the then-outstanding stock of the corporation.

A person is not an interested stockholder under the MGCL if the board of directors approved in advance the transaction by which the person otherwise would have become an interested stockholder. In approving a transaction, the board of directors may provide that its approval is subject to compliance, at or after the time of the approval, with any terms and conditions determined by it.

After such five-year period, any such business combination must be recommended by the board of directors of the corporation and approved by the affirmative vote of at least:

- 80% of the votes entitled to be cast by holders of outstanding shares of voting stock of the corporation; and
- two-thirds of the votes entitled to be cast by holders of voting stock of the corporation other than shares held by the interested stockholder with whom (or with whose affiliate) the business combination is to be effected or held by an affiliate or associate of the interested stockholder.

These supermajority approval requirements do not apply if, among other conditions, the corporation's common stockholders receive a minimum price (as defined in the MGCL) for their shares and the consideration is received in cash or in the same form as previously paid by the interested stockholder for its shares.

These provisions of the MGCL do not apply, however, to business combinations that are approved or exempted by a corporation's board of directors prior to the time that the interested stockholder becomes an interested stockholder. Our board of directors has, by board resolution, exempted business combinations between us and any other person, provided that such business combination is first approved by our board, including a majority of our directors who are not affiliated with the interested stockholder. Consequently, the five-year prohibition and the supermajority vote requirements will not apply to business combinations between us and any such person.

We cannot assure you that our board of directors will not amend or repeal this resolution in the future.

Control Share Acquisitions

The MGCL provides that a holder of "control shares" of a Maryland corporation acquired in a "control share acquisition" has no voting rights with respect to those shares except to the extent approved by the affirmative vote of at least two-thirds of the votes entitled to be cast by stockholders entitled to exercise or direct the exercise of the voting power in the election of directors generally but excluding: (1) the person who has made or proposes to make the control share acquisition; (2) any officer of the corporation; or (3) any employee of the corporation who is also a director of the corporation. "Control shares" are voting shares of stock that, if aggregated with all other such shares of stock previously acquired by the acquirer or in respect of which the acquirer is able to exercise or direct the exercise of voting power (except solely by virtue of a revocable proxy), would entitle the acquirer to exercise voting power in electing directors within one of the following ranges of:

- one-tenth or more but less than one-third;
- one-third or more but less than a majority; or
- a majority or more of all voting power.

Control shares do not include shares that the acquiring person is then entitled to vote as a result of having previously obtained stockholder approval or shares acquired directly from the corporation. A "control share acquisition" means the acquisition, directly or indirectly, of ownership of, or the power to direct the exercise of voting power with respect to, issued and outstanding control shares, subject to certain exceptions.

A person who has made or proposes to make a control share acquisition, upon satisfaction of certain conditions (including an undertaking to pay expenses and making an "acquiring person statement" as described in the MGCL), may compel the board of directors of the company to call a special meeting of stockholders to be held within 50 days of demand to consider the voting rights of the control shares. If no request for a special meeting is made, the corporation may itself present the question at any stockholders meeting.

If voting rights of control shares are not approved at the meeting or if the acquiring person does not deliver an "acquiring person statement" as required by the statute, then, subject to certain conditions and limitations, the corporation may redeem any or all of the control shares (except those for which voting rights have previously been approved) for fair value determined, without regard to the absence of voting rights for the control shares, as of the date of any meeting of stockholders at which the voting rights of such shares are considered and not approved or, if no such meeting is held, as of the date of the last control share acquisition by the acquiror. If voting rights for control shares are approved at a stockholders meeting and the acquirer becomes entitled to vote a majority of the shares entitled to vote, all other stockholders may exercise appraisal rights. The fair value of the shares as determined for purposes of such appraisal rights may not be less than the highest price per share paid by the acquirer in the control share acquisition.

The control share acquisition statute does not apply (1) to shares acquired in a merger, consolidation or statutory share exchange if the corporation is a party to the transaction or (2) to acquisitions approved or exempted by the charter or bylaws of the corporation.

Our bylaws contain a provision exempting from the control share acquisition statute any and all acquisitions by any person of shares of our stock. Our board of directors may amend or eliminate this provision at any time in the future, whether before or after the acquisition of control shares.

Subtitle 8

Subtitle 8 of Title 3 of the MGCL permits a Maryland corporation with a class of equity securities registered under the Exchange Act and at least three independent directors to elect to be subject, by provision in its charter or bylaws or a resolution of its board of directors and notwithstanding any contrary provision in the charter or bylaws, to any or all of the following five provisions:

- a classified board;
- a two-thirds vote requirement for removing a director;
- a requirement that the number of directors be fixed only by vote of the directors;
- a requirement that a vacancy on the board be filled only by the remaining directors and for the remainder of the full term of the class of directors in which the vacancy occurred; or
- a majority requirement for the calling of a special meeting of stockholders.

Our charter provides that, at such time as we have a class of equity securities registered under the Exchange Act and at least three independent directors, we will elect to be subject to the provisions of Subtitle 8 relating to the filling of vacancies on our board of directors. Through provisions in our charter and bylaws unrelated to Subtitle 8, we already (1) require a two-thirds vote for the removal of any director from our board of directors, which removal must be for cause, (2) vest in our board of directors the exclusive power to fix the number of directorships and (3) require, unless called by the chairman of our board of directors, our president, our chief executive officer or our board of directors, the written request of stockholders entitled to cast not less than a majority of all votes entitled to be cast on any matter that may properly be considered at a meeting of stockholders to call a special meeting to act on such matter. We have not elected to create a classified board. In the future, our board of directors may elect, without stockholder approval, to create a classified board or adopt one or more of the other provisions of Subtitle 8.

Extraordinary Actions / Amendments to Our Charter and Bylaws

Generally, our charter may be amended only if such amendment is declared advisable by our board of directors and approved by the affirmative vote of stockholders entitled to cast a majority of the votes entitled to be cast on the matter.

Under Maryland law, a Maryland corporation generally cannot dissolve, amend its charter, merge, convert into another entity, sell all or substantially all of its assets, engage in a statutory share exchange or engage in similar transactions unless declared advisable by the board of directors and approved by the affirmative vote of stockholders entitled to cast at least two-thirds of all of the votes entitled to be cast on the matter unless a lesser percentage (but not less than a majority of the votes entitled to be cast on the matter) is set forth in the corporation’s charter. Our charter provides for approval of these matters by the affirmative vote of stockholders entitled to cast a majority of the votes entitled to be cast on such matters, except that the affirmative vote of stockholders entitled to cast at least two-thirds of the votes entitled to be cast generally in the election of directors is required to amend provisions of our charter relating to director removal, amendments to our bylaws or the vote required for certain amendments. Maryland law also permits a corporation to transfer all or substantially all of its assets without the approval of its stockholders to an entity all of the equity interests of which are owned, directly or indirectly, by the corporation. Our operating assets may be held by our wholly owned subsidiaries and these subsidiaries may be able to merge or transfer all or substantially all of their assets without the approval of our stockholders.

Our board of directors has the exclusive power to adopt, alter or repeal any provision of our bylaws or to make new bylaws.

Exclusive Forum

Our bylaws provide that, unless we consent in writing to the selection of an alternative forum, the sole and exclusive forum for (a) any derivative action or proceeding brought on our behalf, (b) any action asserting a claim of breach of any duty owed by us or by any director or officer or other employee to us or to our stockholders, (c) any action asserting a claim against us or any director or officer or other employee arising pursuant to any provision of the MGCL or our charter or bylaws or (d) any action asserting a claim against us or any director or officer or other employee that is governed by the internal affairs doctrine shall be the Circuit Court for Baltimore City, Maryland, or, if that Court does not have jurisdiction, the United States District Court for the District of Maryland, Baltimore Division.

Meetings of Stockholders

Under our bylaws, annual meetings of stockholders will be held each year at a date and time determined by our board of directors. Special meetings of stockholders may be called by our board of directors, the chairman of our board of directors, our president or our chief executive officer. Additionally, subject to the provisions of our bylaws, special meetings of the stockholders must be called by our secretary to act on any matter that may properly be considered at a meeting of stockholders upon the written request of stockholders entitled to cast not less than a majority of the votes entitled to be cast on such matter at such meeting who have requested the special meeting in accordance with the procedures set forth in, and provided the information and certifications required by, our bylaws. Only matters set forth in the notice of the special meeting may be considered and acted upon at such a meeting.

Advance Notice of Director Nominations and New Business

Our bylaws provide that:

- with respect to an annual meeting of stockholders, nominations of individuals for election to our board of directors and the proposal of business to be considered by stockholders at the annual meeting may be made only:
    - pursuant to our notice of the meeting;
    - by or at the direction of our board of directors; or
    - by a stockholder who was a stockholder of record at the record date set by our board of directors for the purpose of determining stockholders entitled to vote at the annual meeting, at the time of giving of the

notice required by our bylaws and at the time of the annual meeting (and any postponement or adjournment thereof), who is entitled to vote at the meeting in the election of each individual nominated or on such other business, and who has complied with the advance notice procedures set forth in, and provided the information and certifications required by, our bylaws; and

- with respect to special meetings of stockholders, only the business specified in our company's notice of meeting may be brought before the special meeting of stockholders, and nominations of individuals for election to our board of directors may be made only;
    - by or at the direction of our board of directors; or
    - provided that the meeting has been called in accordance with our bylaws for the purpose of electing directors, by a stockholder who is a stockholder of record at the record date set by our board of directors for the purpose of determining stockholders entitled to vote at the special meeting, at the time of giving of the notice required by our bylaws and at the time of the special meeting (and any postponement or adjournment thereof), who is entitled to vote at the meeting in the election of each individual so nominated and who has complied with the advance notice provisions set forth in, and provided the information and certifications required by, our bylaws.

The purpose of requiring stockholders to give advance notice of nominations and other proposals is to afford our board of directors and our stockholders the opportunity to consider the qualifications of the proposed nominees or the advisability of the other proposals and, to the extent considered necessary by our board of directors, to inform stockholders and make recommendations regarding the nominations or other proposals.

Limitation of Liability and Indemnification of Directors and Officers

Maryland law permits a Maryland corporation to include in its charter a provision limiting the liability of its directors and officers to the corporation and its stockholders for money damages except for liability resulting from actual receipt of an improper benefit or profit in money, property or services or active and deliberate dishonesty that is established by a final judgment and is material to the cause of action. Our charter contains such a provision that eliminates such liability to the maximum extent permitted by Maryland law.

The MGCL requires a Maryland corporation (unless its charter provides otherwise, which our charter does not) to indemnify a director or officer who has been successful, on the merits or otherwise, in the defense of any proceeding to which he or she is made or threatened to be made a party by reason of his or her service in that capacity. The MGCL permits a Maryland corporation to indemnify its present and former directors and officers, among others, against judgments, penalties, fines, settlements and reasonable expenses actually incurred by them in connection with any proceeding to which they may be made or are threatened to be made a party to by reason of their service in those or other capacities unless it is established that:

- the act or omission of the director or officer was material to the matter giving rise to the proceeding and:
    - was committed in bad faith; or
    - was the result of active and deliberate dishonesty;
- the director or officer actually received an improper personal benefit in money, property or services; or
- in the case of any criminal proceeding, the director or officer had reasonable cause to believe that the act or omission was unlawful.

However, under the MGCL, a Maryland corporation may not indemnify a director or officer for an adverse judgment in a suit by or in the right of the corporation or if the director or officer was adjudged liable on the basis that personal benefit was improperly received, unless in either case a court orders indemnification and then only for expenses. A court may order indemnification if it determines that the director or officer is fairly and reasonably entitled to indemnification, even though the director or officer did not meet the prescribed standard of conduct or was adjudged liable on the basis that personal benefit was improperly received.

In addition, the MGCL permits a Maryland corporation to advance reasonable expenses to a director or officer upon the corporation's receipt of:

- a written affirmation by the director or officer of his or her good faith belief that he or she has met the standard of conduct necessary for indemnification by the corporation; and

- a written undertaking, which may be unsecured, by the director or officer or on the director's or officer's behalf to repay the amount paid if it shall ultimately be determined that the standard of conduct has not been met.

Our charter authorizes us, and our bylaws obligate us, to the maximum extent permitted by Maryland law in effect from time to time, to indemnify and to pay or reimburse reasonable expenses in advance of final disposition of a proceeding without requiring a preliminary determination of the director's or officer's ultimate entitlement to indemnification to:

- any present or former director or officer who is made or threatened to be made a party to, or witness in, the proceeding by reason of his or her service in that capacity; or
- any individual who, while a director or officer of our company and at our request, serves or has served as a director, officer, partner, member, manager or trustee of another corporation, real estate investment trust, partnership, limited liability company, joint venture, trust, employee benefit plan or any other enterprise and who is made or threatened to be made a party to, or witness in, the proceeding by reason of his or her service in that capacity.

Our charter and bylaws also permit us, with the approval of our board of directors, to indemnify and advance expenses to any person who served as a predecessor of ours in any of the capacities described above and to any employee or agent of our company or a predecessor of our company.

REIT Qualification

Our charter provides that our board of directors may revoke or otherwise terminate our REIT election, without approval of our stockholders, if it determines that it is no longer in our best interest to attempt to, or to continue to, be qualified as a REIT. Our charter also provides that our board of directors may determine that compliance with the restrictions on ownership and transfer of our stock is no longer required for us to qualify as a REIT.

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Section 3: EX-10.15 (EXHIBIT 10.15)

EXHIBIT 10.15

FIRST AMENDMENT TO CREDIT AGREEMENT

This First Amendment to Credit Agreement (the "Amendment") is made as of November 12, 2019 (the "Effective Date"), by and among HIGHLANDS REIT, INC., a Maryland corporation (the "Borrower"), and THE HUNTINGTON NATIONAL BANK, as "Agent" and as an existing "Lender".

R E C I T A L S

A. Borrower, Agent and certain other Lenders have entered into a Credit Agreement dated as of February 15, 2019 (the "Original Credit Agreement"). All capitalized terms used herein and not otherwise defined shall have the meanings given to them in the Original Credit Agreement.

B. Borrower and Lenders wish to amend the Original Credit Agreement to modify certain of the terms, covenants and provisions in the Original Credit Agreement, all as set forth herein.

NOW, THEREFORE, in consideration of the foregoing Recitals and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

AGREEMENTS

1. The foregoing Recitals to this Amendment hereby are incorporated into and made part of this Amendment.

2. Section 1.1 of the Original Credit Agreement is hereby modified by adding the following defined terms:

Multi-Family Availability NOI. The aggregate of (a) Underwritten NOI for Multi-Family Assets owned less than twelve (12) months and (b) Adjusted NOI for Multi- Family Assets owned twelve (12) months or longer.

Underwritten NOI. The reasonably calculated pro forma annual projection of net operating income for any Real Estate based on actual historic metrics, such as a rent roll, with other reasonable assumptions, as underwritten by Borrower and/or its Subsidiaries when acquiring such Real Estate, in accordance with Borrower's and its Subsidiaries' ordinary course of business and past practice.

3. Section 1.1 of the Original Credit Agreement is hereby modified by deleting the defined term "Pool Property Availability" in its entirety and replacing it with the following:

Pool Property Availability. The Pool Property Availability shall be bifurcated based on Multi-Family Assets (resulting in the "Multi-Family Pool Property Availability") and Legacy Assets (resulting in the "Legacy Pool Property Availability") as set forth below. Pool Property Availability shall equal the sum of Multi-Family Pool Property Availability and Legacy Pool Property Availability.

(a) Multi-Family Pool Property Availability shall at no time exceed the lesser of the following:

(i) Sixty-five percent (65%) multiplied by the Multi-Family Pool Value; and
(ii) As of any date of determination, the quotient obtained by dividing (A) the Multi-Family Availability NOI by (B) (x) the product of 1.25 and (y) the Multi-Family Mortgage Constant.

(b) Legacy Pool Property Availability shall at no time exceed the lesser of the following:

(i) Sixty percent (60%) multiplied by the Legacy Pool Value; and

(ii) As of any date of determination, the quotient obtained by dividing (A) the aggregate Adjusted NOI attributable to the Legacy Assets by (B) (x) the product of 1.65 and (y) the Legacy Mortgage Constant.

4. Borrower hereby represents and warrants that, as of the Effective Date, there is no Default or Event of Default, the representations and warranties contained in Article 6 of the Original Credit Agreement are true and correct in all material respects, Borrower has no offsets or claims against Lender and Borrower has full power and authority to execute this Amendment.

5. As expressly modified as provided herein, the Original Credit Agreement shall continue in full force and effect.

6. All references in the Loan Documents to the Original Credit Agreement henceforth shall be deemed to refer to the Original Credit Agreement as amended by this Amendment. In the event of a conflict or inconsistency between the provisions of the Loan Documents and the provisions of this Amendment, the provisions of this Amendment shall govern.

7. This Amendment may be executed in any number of counterparts, all of which taken together shall constitute one agreement, and any of the parties hereto may execute this Amendment by signing any such counterpart.

8. The undersigned Guarantors, having executed and joined in this Amendment as shown below, jointly and severally, hereby (i) approve and ratify this Amendment, (ii) confirm that they have previously joined in, or hereby join in, that certain Guaranty dated as of February 15, 2019 and Environmental Indemnity dated as of February 15, 2019 (as each may be amended, restated, extended, supplemented or otherwise modified in writing from time to time, collectively, the “Guaranty”), that they are Guarantors or Indemnitors, as applicable, under the Guaranty and that their obligations under the Guaranty will continue in full force and effect and (iii) agree to fully and timely perform each and every obligation of a Guarantor or Indemnitor, as applicable, under and in accordance with such Guaranty.

[Remainder of page intentionally blank;
Signature page follows]

AGENT, ISSUING LENDER, AND LENDER:

THE HUNTINGTON NATIONAL BANK

By: /s/ Rebecca Stirnkoro
Name: Rebecca Stirnkoro
Title: Assistant Vice President

LENDERS:

CHEMICAL BANK,
a division of TCF National Bank

By: /s/ Ronald Konstantinovsky
Name: Ronald Konstantinovsky
Title: Vice President

MIDFIRST BANK

By: /s/ Todd Wright
Name: Todd Wright
Title: Senior Vice President

FIRST NATIONAL BANK

By: /s/ John E Wilgus II
Name: John E Wilgus II
Title: Senior Vice President

IN WINESS HEREOF, the parties have executed and delivered this Amendment as of the date first written above.

BORROWER:

HIGHLANDS REIT, INC., a Maryland corporation

By: /s/ Paul Melkus
Name: Paul Melkus
Title: Authorized Officer

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Section 4: EX-10.16 (EXHIBIT 10.16)

EXHIBIT 10.16

SECOND AMENDMENT TO CREDIT AGREEMENT

This Second Amendment to Credit Agreement (the "Amendment") is made as of February 14, 2020 (the "Effective Date"), by and among HIGHLANDS REIT, INC., a Maryland corporation (the "Borrower"), and THE HUNTINGTON NATIONAL BANK, as "Agent" and as an existing "Lender".

R E C I T A L S

A. Borrower, Agent and certain other Lenders have entered into a Credit Agreement dated as of February 15, 2019, as amended by that certain First Amendment to Credit Agreement dated as of November 12, 2019 (collectively, the "Original Credit Agreement"). All capitalized terms used herein and not otherwise defined shall have the meanings given to them in the Original Credit Agreement.

B. Borrower and Lenders wish to amend the Original Credit Agreement to modify certain of the terms, covenants and provisions in the Original Credit Agreement, all as set forth herein.

NOW, THEREFORE, in consideration of the foregoing Recitals and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

AGREEMENTS

1. The foregoing Recitals to this Amendment hereby are incorporated into and made part of this Amendment.

2. Section 2.1(b) of the Original Credit Agreement is hereby deleted in its entirety and replaced with the following:

(b) Term Facility. Subject to the terms and conditions set forth herein, on the Closing Date, each Term Lender severally agrees to make a Term Loan to the Borrower in the aggregate principal amount equal to such Term Lender's Term Loan Commitment. The Term Loans shall mature on the Term Loan Maturity Date. The initial Advance of the Term Loan shall be $30,000,000 and the remaining Term Loan Commitments of $20,000,000 may be drawn in increments of $10,000,000, in up to two Advances (in addition to the initial Advance) by Borrower's (x) delivery of a Request for Loan, in the form attached hereto as Exhibit C, to Agent and (y) satisfaction of each of the conditions to an Advance set forth in §11; provided that the Loan Exposure, after giving effect to Borrower's requested Advance of a Term Loan, shall not exceed the lesser of the Total Commitment and Pool Property Availability. Any amount of the Term Loan that remains undrawn during the period commencing on March 18, 2019 and ending on December 31, 2020 (the "*Undrawn Term Loan Commitments*") shall be subject to an unused fee payable in arrears to the Agent for the account of each Term Lender, computed on a daily basis by multiplying (i) twenty five (25) basis points (0.25%) per annum, expressed as a per diem rate, times (ii) the undrawn portion of the Term Loan Commitments on such day (the "*Term Loan Unused Fee*"). Borrower shall make the first payment of the Term Loan Unused Fee to Administrative Agent on or prior to February 14, 2020 for all amounts accrued up to and on December 31, 2019. Thereafter, Borrower shall make payments of the Term Loan Unused Fee quarterly in arrears on the last Business Day of each March, June, September and December of 2020 for all amounts accrued up to and on such date. Any portion of the Undrawn Term Loan Commitments that remains undrawn as of December 31, 2020, shall thereafter be unavailable for Borrower to draw, and (i) the Term Loan Commitments shall be reduced accordingly, pro rata among the Term Lenders, and (ii) the Term Loan Unused Fee shall no longer accrue on the Undrawn Term Loan Commitments. Following its receipt of any such Term Loan Unused Fee, Agent shall promptly pay to each Term Lender an amount equal to such Term Lender's Term Loan Commitment Percentage of the daily amount of such Term Loan Unused Fee based on such Term Lender's Term Loan Commitment on such day. The Borrower may not reborrow any portion of any Term Loan once repaid. Term Loans may be Base Rate Loans or LIBOR Rate Loans, as further provided herein.

3. Borrower hereby represents and warrants that, as of the Effective Date, there is no Default or Event of Default, the representations and warranties contained in Article 6 of the Original Credit Agreement are true and correct in all material respects, Borrower has no offsets or claims against Lender and Borrower has full power and authority to execute this Amendment.

4. As expressly modified as provided herein, the Original Credit Agreement shall continue in full force and effect.

5. All references in the Loan Documents to the Original Credit Agreement henceforth shall be deemed to refer to the Original Credit Agreement as amended by this Amendment. In the event of a conflict or inconsistency between the provisions of the Loan Documents and the provisions of this Amendment, the provisions of this Amendment shall govern.

6. This Amendment may be executed in any number of counterparts, all of which taken together shall constitute one agreement, and any of the parties hereto may execute this Amendment by signing any such counterpart.

7. The undersigned Guarantors, having executed and joined in this Amendment as shown below, jointly and severally, hereby (i) approve and ratify this Amendment, (ii) confirm that they have previously joined in, or hereby join in, that certain Guaranty dated as of February 15, 2019 and Environmental Indemnity dated as of February 15, 2019 (as each may be amended, restated, extended, supplemented or otherwise modified in writing from time to time, collectively, the "Guaranty"), that they are Guarantors or Indemnitors, as applicable, under the Guaranty and that their obligations under the Guaranty will continue in full force and effect and (iii) agree to fully and timely perform each and every obligation of a Guarantor or Indemnitor, as applicable, under and in accordance with such Guaranty.

[Remainder of page intentionally blank;
Signature page follows]

IN WITNESS HEREOF, the parties have executed and delivered this Amendment as of the date first written above.

BORROWER:

HIGHLANDS REIT, INC., a Maryland corporation

By: /s/ Paul Melkus
Name: Paul Melkus
Title: Authorized Officer

AGENT, ISSUING LENDER, AND LENDER:

THE HUNTINGTON NATIONAL BANK

By: /s/ Joshua Arundel
Name: Joshua Arundel
Title: Vice President

LENDERS:

CHEMICAL BANK,
a division of TCF National Bank

By: /s/ Ronald Konstantinovsky
Name: Ronald Konstantinovsky
Title: Vice President

MIDFIRST BANK

By: /s/ Todd Wright
Name: Todd Wright
Title: Senior Vice President

FIRST NATIONAL BANK

By: /s/ John E Wilgus II
Name: John E Wilgus II
Title: Senior Vice President

GUARANTOR:

1560 DOWNING LLC,
1620 CENTRAL LLC,
CHAMPA STREET LOFTS, LLC
IA ST. PAUL ATLAS LLC
IA NEW ULM ATLAS, LLC
MB EVANSTON SHERMAN LLC
THE LAFAYETTE DENVER, LLC
TRIMBLE JUNCTION VENTURES, LLC,
THE VIEW ONWER, LLC
each a Delaware limited liability company

By: Highlands REIT, Inc.,
a Maryland corporation
Its Sole Member

By: /s/ Paul Melkus
Name: Paul Melkus
Title: Authorized Officer

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Section 5: EX-21.1 (EXHIBIT 21.1)

Exhibit 21.1

List of Subsidiaries

Entity Name	***Jurisdiction of Incorporation or Formation***
Tennyson 44 Owner LLC	Delaware
The Muse Owner LLC	Delaware
The View Owner LLC	Delaware
Detroit Street Denver LLC	Delaware
1560 Downing LLC	Delaware
1620 Central LLC	Delaware
HRI Vue Venture LLC	Delaware
Champa Street Lofts, LLC	Delaware
Highlands Property Management, LLC	Delaware
IA CFG Portfolio, L.L.C.	Delaware
IA New Ulm Atlas, L.L.C.	Delaware
IA Orlando Palazzo, L.L.C.	Delaware
IA St. Paul Atlas, L.L.C.	Delaware
IVT PPD Hudson Associates, L.L.C.	Delaware
MB Bloomsburg Buckhorn LLC	Delaware

MB Columbus Hilliard, L.L.C.	Delaware
MB Evanston Sherman, L.L.C.	Delaware
MB Lincoln Mall, L.L.C.	Delaware
MB REIT (Florida), Inc. Florida	Florida
MB Rockford State, L.L.C.	Delaware
The Lafayette Denver, LLC	Delaware
Trimble-Junction Ventures, LLC	Delaware

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Section 6: EX-23.1 (EXHIBIT 23.1)

Exhibit 23.1

Consent of Independent Registered Public Accounting Firm

The Board of Directors

Highlands REIT, Inc.:

We consent to the use of our report incorporated by reference in the registration statement on Form S-8 (No. 333-210952) of Highlands REIT, Inc. of our report dated March 20, 2020, with respect to the consolidated balance sheets of Highlands REIT, Inc. as of December 31, 2019 and 2018, and the consolidated statements of operations and comprehensive income, equity, and cash flow for each of the years in the two-year period ended December 31, 2019 and the related financial statement schedule III, which report appears in the December 31, 2019 annual report on Form 10-K of Highlands, REIT, Inc. herein and to the reference to our firm under the heading “Experts” in the prospectus.

Our report on the consolidated financial statements refers to a change in the method of accounting for leases.

/s/ KPMG, LLP

Chicago, Illinois
March 20, 2020

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Section 7: EX-31.1 (EXHIBIT 31.1)

Exhibit 31.1

Certification of Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Richard Vance, certify that:

1. I have reviewed this Annual Report on Form 10-K of Highlands REIT, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 20, 2020

/s/ Richard Vance

Name: Richard Vance

Title: President and Chief Executive Officer (Principal Executive Officer)

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Section 8: EX-31.2 (EXHIBIT 31.2)

Exhibit 31.2

Certification of Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Paul Melkus, certify that:

1. I have reviewed this Annual Report on Form 10-K of Highlands REIT, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 20, 2020

/s/ Paul Melkus
Name: Paul Melkus
Title: Executive Vice President and Chief Financial Officer (Principal Financial Officer)

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Section 9: EX-32.1 (EXHIBIT 32.1)

Exhibit 32.1

Certification of Principal Executive Officer
Pursuant To 18 U.S.C. Section 1350,
as Adopted Pursuant to
Section 906 of The Sarbanes-Oxley Act of 2002

In connection with the Annual Report on Form 10-K of Highlands REIT, Inc. (the "Company") for the period ended December 31, 2019 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned officer of the Company certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to such officer's knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date:	March 20, 2020	/s/ Richard Vance
		Name: Richard Vance
		Title: President and Chief Executive Officer (Principal Executive Officer)

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

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as a part of the Report or on a separate disclosure document.

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Section 10: EX-32.2 (EXHIBIT 32.2)

Exhibit 32.2

Certification of Principal Financial Officer
Pursuant To 18 U.S.C. Section 1350,
as Adopted Pursuant to
Section 906 of The Sarbanes-Oxley Act of 2002

In connection with the Annual Report on Form 10-K of Highlands REIT, Inc. (the “Company”) for the period ended December 31, 2019 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), the undersigned officer of the Company certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to such officer’s knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date:	March 20, 2020	/s/ Paul Melkus
		Name: Paul Melkus
		Title: Executive Vice President and Chief Financial Officer (Principal Financial Officer)

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

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as a part of the Report or on a separate disclosure document.

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