SPIRIT FINANCE CORP
Form S-11/A
March 16, 2012
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As filed with the Securities and Exchange Commission on March 15, 2012

Registration No. 333-177904

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Amendment No. 3

to

Form S-11

REGISTRATION STATEMENT

UNDER

THE SECURITIES ACT OF 1933

Spirit Finance Corporation

(Exact Name of Registrant as Specified in Its Governing Instruments)

14631 North Scottsdale Road, Suite 200, Scottsdale, Arizona 85254

(480) 606-0820

(Address, Including Zip Code and Telephone Number, Including Area Code,

of Registrant s Principal Executive Offices)

Thomas H. Nolan, Jr., Chairman of the Board of Directors and Chief Executive Officer

Peter M. Mavoides, President and Chief Operating Officer

Spirit Finance Corporation 14631 North Scottsdale Road, Suite 200, Scottsdale, Arizona 85254

(480) 606-0820

(Name, Address, Including Zip Code and Telephone Number, Including Area Code, of Agent for Service)

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Approximate date of commencement of proposed sale to the public: As soon as practicable after this Registration Statement becomes effective.

If any of the Securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act, check the following box: ¨

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement of the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If delivery of the prospectus is expected to be made pursuant to Rule 434, check the following box. ¨

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

Large accelerated filer	¨	Accelerated filer	¨
Non-accelerated filer	x (Do not check if a smaller reporting company)	Smaller reporting company	¨

The registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment that specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, as amended, or until this registration statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

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The information in this preliminary prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This preliminary prospectus is not an offer to sell these securities and it is not soliciting an offer to buy these securities in any jurisdiction where the offer or sale is not permitted.

PROSPECTUS (Subject to Completion)

Issued , 2012

Shares

Spirit Finance Corporation

Common Stock

Spirit Finance Corporation is a self-administered and self-managed real estate company. We invest in single-tenant, operationally essential real estate throughout the United States that is leased on a long-term, triple-net basis primarily to tenants engaged in retail, service and distribution industries.

We are selling shares of our common stock. This is our initial public offering and no public market currently exists for our common stock. We currently expect the initial public offering price of our common stock to be between $ and $ per share.

We have applied to have our common stock listed on the New York Stock Exchange under the symbol .

As described herein, concurrently with the completion of this offering, we will issue additional shares of our common stock to certain of our existing lenders in exchange for the extinguishment of $330 million of our outstanding term loan debt. We will use a portion of the net proceeds from this offering to repay an additional $399 million of our outstanding term loan debt.

We have elected to be taxed as a real estate investment trust, or REIT, for federal income tax purposes commencing with our taxable year ended December 31, 2003. To assist us in complying with certain federal income tax requirements applicable to REITs, our charter contains certain restrictions relating to the ownership and transfer of our capital stock, including an ownership limit of 9.8% of our outstanding common stock. See Description of Our Capital Stock Restrictions on Ownership and Transfer for a detailed description of the ownership and transfer restrictions applicable to our common stock.

Investing in our common stock involves risks. See Risk Factors beginning on page 15.

PRICE $ PER SHARE

	Price to Public	Underwriting Discounts and Commissions	Proceeds, before Expenses, to Us
Per Share	$	$	$
Total	$	$	$

We have granted the underwriters an option to purchase up to additional shares of our common stock from us, at the initial public offering price, less underwriting discounts and commissions, within 30 days from the date of this prospectus to cover over-allotments, if any.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The underwriters expect to deliver the shares of our common stock to purchasers on , 2012.

Morgan Stanley

Macquarie Capital

UBS Investment Bank

Deutsche Bank Securities

RBC Capital Markets

, 2012

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Through and including , 2012 (the 25th day after the date of this prospectus), all dealers that buy, sell or trade the common stock may be required to deliver a prospectus, regardless of whether they are participating in this offering. This is in addition to a dealer s obligation to deliver a prospectus when acting as an underwriter and with respect to an unsold allotment or subscription.

You should rely only on the information contained in this prospectus, or in any free writing prospectus prepared by us. We have not, and the underwriters have not, authorized anyone to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. We are not, and the underwriters are not, making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. You should assume that the information appearing in this prospectus and any free writing prospectus prepared by us is accurate only as of their respective dates or on the date or dates which are specified in these documents. Our business, financial condition, liquidity, results of operations and prospects may have changed since those dates.

We use market data and industry forecasts and projections throughout this prospectus, and in particular in the sections entitled Prospectus Summary, Market Opportunity and Business and Properties. We have obtained substantially all of this information from a market study prepared for us in connection with this offering by Rosen Consulting Group, or RCG, a nationally recognized real estate consulting firm. We have paid RCG a fee of $45,000 for that market study. Such information is included in this prospectus in reliance on RCG s authority as an expert on such matters. Any forecasts prepared by RCG are based on data (including third party data), models and experience of various professionals, and are based on various assumptions, all of which are subject to change without notice. See Experts. In addition, we have obtained certain market and industry data from publicly available industry publications. These sources generally state that the information they provide has been obtained from sources believed to be reliable, but that the accuracy and completeness of the information are not guaranteed. The forecasts and projections are based on industry surveys and the preparers experience in the industry, and there is no assurance that any of the projected amounts will be achieved. We believe that the surveys and market research others have performed are reliable, but we have not independently verified this information.

Certain Terms Used in This Prospectus

Unless the context suggests otherwise, references in this prospectus to we, our, us and our company are to Spirit Finance Corporation, a Maryland corporation, together with its consolidated subsidiaries, including Spirit Realty Finance, L.P., which we refer to as our operating partnership.

In this prospectus, we refer to our lessees as tenants and our mortgage and equipment loan obligors as borrowers.

As used in this prospectus, annual rent equals rental revenue for the quarter ended December 31, 2011 multiplied by four.

The term original gross investment means our (and for periods prior to our July 31, 2007 privatization, our predecessor s) initial purchase price for investments, without giving effect to any adjustment to the book basis of our investments arising from our privatization or accumulated depreciation.

As used in this prospectus, the occupancy of our owned properties is calculated by dividing (1) the total number of our owned properties minus the number of our owned properties that are vacant and from which we are not receiving any rental payment, by (2) the total number of our owned properties.

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PROSPECTUS SUMMARY

The following summary highlights information contained elsewhere in this prospectus. This summary is not complete and does not contain all of the information that you should consider before investing in our common stock. You should read the entire prospectus carefully, including the section entitled Risk Factors, as well as the financial statements and related notes included elsewhere in this prospectus, before making an investment decision. Unless otherwise indicated, the information contained in this prospectus assumes (1) that the underwriters over-allotment option is not exercised, (2) that the common stock to be sold in this offering is sold at $ per share, which is the mid-point of the price range set forth on the front cover of this prospectus, and (3) the issuance of shares of our common stock to certain lenders in exchange for the extinguishment of $330 million of our outstanding term loan debt. The actual number of shares of our common stock issued to certain of our lenders will vary as described herein. See Pricing Sensitivity Analysis.

Spirit Finance Corporation

Overview

We invest in single-tenant, operationally essential real estate throughout the United States that is leased on a long-term, triple-net basis primarily to tenants engaged in retail, service and distribution industries. Single-tenant, operationally essential real estate consists of properties that are generally free-standing, commercial real estate facilities where our tenants conduct retail, service or distribution activities that are essential to the generation of their sales and profits. Under a triple-net lease, the tenant is typically responsible for all improvements and is contractually obligated to pay all property operating expenses, such as real estate taxes, insurance premiums and repair and maintenance costs. In support of our primary business of owning and leasing real estate, we have also strategically originated or acquired long-term, commercial mortgage and equipment loans.

We generate our revenue primarily by leasing our properties to our tenants. As of December 31, 2011, our undepreciated gross investment in real estate and loans totaled approximately $3.6 billion, representing investment in 1,153 properties, including properties securing our mortgage loans. Of this amount, 98.2% consisted of our gross investment in real estate, representing ownership of 1,064 properties, and the remaining 1.8% consisted of commercial mortgage and equipment loans receivable secured by 89 properties or related assets. As of December 31, 2011, our owned properties were approximately 98.4% occupied (based on number of properties), and our leases had a weighted-average non-cancelable remaining lease term (based on annual rent) of approximately 11.8 years. Our leases are generally long-term, with non-cancelable initial terms typically of 15 to 20 years and tenant renewal options for additional terms. As of December 31, 2011, approximately 96% of our leases (based on annual rent) provided for increases in future annual base rent.

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Our portfolio of 1,064 owned properties was leased to approximately 165 tenants as of December 31, 2011. Of our approximately 165 tenants, no tenant, other than Shopko Stores Operating Co., LLC, or Shopko, contributed more than 7% of our annual rent. Our tenants operate in 18 different industries, including: general, specialty and discount retail; restaurants; movie theaters; automotive dealers; educational and recreational facilities; and supermarkets. Our properties are geographically diversified across 46 states, with only 4 states contributing more than 5.0% of our annual rent.

The diversity of our portfolio has contributed to its stable occupancy. As of December 31, 2011, 2010, 2009, 2008 and 2007, our occupancy rate (based on number of properties) was 98.4%, 96.3%, 99.4%, 99.0% and 100%, respectively. We believe that the occupancy of our portfolio, particularly during the economic downturn of 2008 through 2010, reflects its strength. As illustrated in the chart below, since inception in 2003 our occupancy has never been below 96.1% (based on number of properties).

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As of December 31, 2011, one of our tenants, Shopko, contributed approximately 26.7% of our annual rent, with 112 properties leased pursuant to a master lease with an initial term that expires in June 2026 and two properties leased under individual leases. In February 2012, Shopko and Pamida Stores Operating Co., LLC, or Pamida, another one of our general merchandising tenants, completed a merger. The combined company would have contributed approximately 30.4% of our annual rent as of December 31, 2011. Based on financial information supplied to us by Shopko, the 112 properties that we lease to Shopko pursuant to a master lease had a property-level rent coverage ratio well in excess of our target underwriting standard of 2.0x for the fiscal year ended January 29, 2011. For a discussion of how we calculate property-level rent coverage, see Business and Properties Risk Management Tenant Financial Distress Risk Early Lease Termination Risk Measurement. Additionally, at the corporate level, Specialty Retail Shops Holding Corp., the guarantor of the Shopko leases, had corporate-level EBITDAR of $154.4 million for the fiscal year ended January 29, 2011 and a ratio of corporate-level EBITDAR to net interest and rent expense of 1.57x for that period. EBITDAR represents net income before net interest expense, depreciation and amortization, income tax expense (benefit) and rent. Shopko s operating performance has improved in recent years in a very competitive environment, and its shadow rating, as generated by a product licensed by us from Moody s Analytics, Inc., or Moody s Analytics, exceeds the targeted average for our portfolio. See Business and Properties Our Real Estate Investment Portfolio Investment Diversification Diversification by Tenant for a reconciliation of Specialty Retail Shops Holding Corp. s corporate-level EBITDAR to its net income.

As we look to selectively grow our portfolio, we will seek to leverage the experience of our senior management team and our existing underwriting, leasing, asset management and reporting infrastructure. We believe the acquisition of additional operationally essential retail, service and distribution properties, coupled with our $3.6 billion seasoned investment portfolio, will provide the opportunity to achieve superior risk-adjusted returns. We intend to continue to actively manage our existing portfolio and invest in real estate that produces stable rental revenue that increases over time pursuant to contractually specified rent increases.

Our History

We were formed in 2003 and became a public company in December 2004. We were subsequently taken private by a consortium of private investors in August 2007 in a transaction that was structured and led by an affiliate of Macquarie Capital (USA) Inc., one of the underwriters of this offering, which we refer to as our privatization. Following our privatization, we initially continued to execute our business plan and grow our portfolio. However, during 2008, in response to deteriorating economic conditions, we shifted our focus to reducing our indebtedness and managing our portfolio. From January 1, 2008 to December 31, 2011, we reduced our indebtedness by $629.5 million. The vast majority of the owned properties in our portfolio as of December 31, 2011 were acquired prior to our privatization. We have recently augmented our senior management team through the addition of executives with significant real estate, capital markets and net lease industry experience. Thomas H. Nolan, Jr., our Chief Executive Officer, has been active in the real estate industry for over 25 years, holding numerous leadership positions in private and public real estate companies. Peter M. Mavoides, our President and Chief Operating Officer, has been active in the single-tenant, net lease industry for over 13 years, holding leadership positions for the past 8 years. Under our new leadership, we have begun to pursue acquisition opportunities and have completed approximately $60 million of acquisitions since September 30, 2011.

We have elected to be taxed as a REIT for federal income tax purposes commencing with our taxable year ended December 31, 2003. We believe that we have been organized and have operated in a manner that has allowed us to qualify as a REIT for federal income tax purposes commencing with such taxable year, and we intend to continue operating in such a manner.

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Competitive Strengths

We believe the following competitive strengths contribute to the stability of our rental revenues and distinguish us from our competitors:

Large Scale and Diversified Portfolio. As of December 31, 2011, our portfolio consisted of 1,064 owned properties, with approximately 165 tenants operating in 46 states and diversified across 18 different industries, including: general, specialty and discount retail; restaurants; movie theaters; automotive dealers; educational and recreational facilities; and supermarkets. We believe it would be difficult for a new competitor to replicate such a diversified portfolio on a comparable scale. The diversity of our portfolio reduces the risks associated with adverse events affecting a particular tenant or an economic decline in any particular state or industry. Additionally, the scale of our portfolio allows us to make acquisitions without introducing additional concentration risks. In addition, our operating platform is scalable and will allow us to make new investments without the need for significant additional administrative or management costs.

Long-Term Triple-Net Leases. As of December 31, 2011, our owned properties were approximately 98.4% occupied (based on number of properties), with a weighted average non-cancelable remaining lease term (based on annual rent) of approximately 11.8 years. Due to the triple-net structure of over 95% of our leases (based on annual rent) as of December 31, 2011, we do not expect to incur significant capital expenditures, and the potential impact of inflation on our operating expenses is minimal. Additionally, as of December 31, 2011, approximately 96% of our leases (based on annual rent) provided for increases in future annual base rent.

Established Company with Proven Performance. Our company has been actively investing in triple-net leased real estate since 2003, is well-known within the industry and benefits from an established infrastructure supporting our underwriting, leasing, asset management and reporting functions. From our inception in 2003 through December 31, 2011, we have made gross investments in excess of $4.05 billion in properties and loans receivable. The vast majority of our owned properties as of December 31, 2011 were acquired prior to our privatization. Since our inception, our occupancy has never been below 96.1% (based on number of properties), despite the economic downturn of 2008 through 2010. We believe that our experience, in-depth knowledge of the triple-net lease market and extensive network of long-standing relationships in the real estate industry will contribute to the stability of our rental revenues and also provide us access to a pipeline of attractive investment opportunities to allow us to expand our revenue base.

Disciplined Underwriting and Risk Management Expertise**.** Our developed underwriting and risk management expertise enhances our ability to identify and structure investments that provide superior risk-adjusted returns, due to specific investment risks that we believe can be identified and mitigated through intensive credit and real estate analysis, tailored lease structures (such as master leases) and ongoing tenant monitoring. When underwriting new acquisitions we generally target property-level rent coverage ratios in excess of 2.0x. Since our inception in 2003 through December 31, 2011, our estimated cumulative loss resulting from properties and loans receivable experiencing financial distress, which we define as tenant bankruptcy or tenant non-performance resulting in our possession of the properties, was $130.4 million (of which we have realized $110.3 million of losses), or 3.3% of our original gross investment since inception. Our recovery rate on properties and loans receivable experiencing financial distress (including an estimate for properties in distress that have not yet been resolved) during that period is 69.4%. We believe our developed underwriting and risk management expertise has contributed to identifying and mitigating risk and our recovery rate. For a discussion of how we calculated estimated cumulative loss and our recovery rate, see Business and Properties Risk Management Tenant Financial Distress Risk Historical Summary of Tenant Financial Distress Portfolio.

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Experienced Management Team. Our senior management has significant experience in the real estate industry and in managing public companies. Our Chairman and Chief Executive Officer, Thomas H. Nolan, Jr., has been active in the real estate industry for over 25 years, holding numerous leadership positions in private and public real estate companies. Our President and Chief Operating Officer, Peter M. Mavoides, has been active in the single-tenant, net lease industry for over 13 years, holding leadership positions for the past 8 years. Our Chief Financial Officer, Michael A. Bender, has held leadership positions for over 20 years in finance and real estate. Our Senior Vice President, Gregg A. Seibert, who has been with us since our inception, has over 20 years of experience in real estate finance, including over 15 years of leadership responsibilities in credit, acquisitions and portfolio management in the sale-leaseback sector. Excluding these individuals, our asset management and leasing management have worked at our company for an average of 5 years and have a high level of familiarity with our portfolio and tenants.

Attractive In-Place Long-Term Indebtedness. Upon the completion of this offering and the debt conversion described below, we expect to have approximately $2.0 billion principal balance of non-recourse mortgage indebtedness outstanding on a pro forma basis, which had a weighted average maturity of 6.8 years as of December 31, 2011 and an average annual interest rate of approximately 6.12% for the year ended December 31, 2011 (excluding non-cash interest expense attributable to the amortization of deferred financing costs and debt discounts). Prior to January 1, 2016, we only have $138.8 million of balloon payments due at maturity. Approximately $1.7 billion principal balance of our pro forma indebtedness is fully or partially amortizing, providing for an ongoing reduction in principal prior to maturity. In addition, we expect to have a $ million revolving credit facility in place upon the completion of this offering to help fund future acquisitions and for general corporate purposes.

Business and Growth Strategies

Our objective is to maximize stockholder value by seeking superior risk-adjusted returns, with an emphasis on stable rental revenue, by investing primarily in single-tenant, operationally essential real estate leased on a long-term, triple-net basis. Single-tenant, operationally essential real estate consists of properties that are generally free-standing, commercial real estate facilities where our tenants conduct retail, service or distribution activities that are essential to the generation of their sales and profits. As of December 31, 2011, we considered 99.5% of our occupied properties to be operationally essential. We intend to pursue our objective through the following business and growth strategies.

Focus on Small and Middle Market Companies. We primarily focus on investing in properties that we net lease to unrated small and middle market companies that we determine have attractive credit characteristics and stable operating histories. Properties leased to small and middle market companies may offer us the opportunity to achieve superior risk-adjusted returns, as a result of our intensive credit and real estate analysis, lease structuring and portfolio construction. Small and middle market companies are often willing to enter into leases with structures and terms that we consider attractive (such as master leases and leases that require ongoing tenant financial reporting) and that we believe increase the security of rental payments. For example, by acquiring multiple properties from a small or middle market company and leasing them back to the seller under a master lease, the leased properties may represent a meaningful percentage of the tenant s overall operations and increase the importance of the lease to the tenant s business. In addition to small and middle market companies, we selectively acquire properties leased to large companies where we believe that we can achieve superior risk-adjusted returns.

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The following chart highlights the tenants that we target based on company size and corporate credit equivalent:

Use Our Developed Underwriting and Risk Management Processes to Structure and Manage Our Portfolio. We seek to maintain the stability of our rental revenue and the long-term return on our investments by using our developed underwriting and risk management processes to structure and manage our portfolio. We believe the efficacy of our underwriting and risk management processes is illustrated by the historical performance of our portfolio. In particular, our underwriting and risk management processes emphasize the following:

- *Leases for Operationally Essential Real Estate with Relatively Long-Terms.* We seek to own properties that are operationally essential to our tenants, thereby reducing the risk that the tenant would choose not to renew an expiring lease or reject a lease in bankruptcy. In addition, we seek to enter into leases with relatively long-terms, typically with non-cancelable initial terms of 15 to 20 years and tenant renewal options for additional terms with attractive rent escalation provisions.

- *Use of the Master Lease Structure.* Where appropriate, we seek to enter into master leases, pursuant to which we lease multiple properties to a single tenant on an all or none basis. In a master lease structure, a tenant is responsible for a single lease payment relating to the entire portfolio of leased properties, as opposed to multiple lease payments relating to individually leased properties. The master lease structure prevents a tenant from cherry picking locations, where it unilaterally gives up underperforming properties while maintaining its leasehold interest in well-performing properties. As of December 31, 2011, we had 54 master leases that had an average non-cancellable remaining lease term (based on annual rent) of 13.2 years and contributed approximately 65.0% of our annual rent. Our largest master lease, consisting of 112 properties, contributed 26.6% of our annual rent, and our smallest master lease, consisting of two properties, contributed less than 1% of our annual rent. The average number of properties included under our master leases as of December 31, 2011 was 11.9.

- *Active Management and Monitoring of Risks Related to Our Investments.* When monitoring existing investments or evaluating new investments, we typically consider two broad categories of risk: (1) tenant financial distress risk; and (2) lease renewal risk. See Business and Properties Risk Management. We seek to measure these risks through various processes, including the use of a credit modeling product that we license from Moody s Analytics, estimates of the performance of the leased properties relative to rental payments due under the leases and review of current market data and our historical recovery rates on re-leased properties and property dispositions. Our underwriting and risk management processes are designed to structure new investments and manage existing investments to address and mitigate each of the above risks and preserve the long-term return on our invested capital.

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- *Portfolio Diversification.* We monitor and manage the diversification of our real estate investment portfolio in order reduce the risks associated with adverse developments affecting a particular tenant, property, industry or region. Our strategy emphasizes a portfolio that (1) derives no more than 10% of its annual rent from any single tenant or more than 2.5% of its annual rent from any single property, (2) is leased to tenants operating in various industries and (3) is located across the United States without significant geographic concentration. While we consider the foregoing when making investments, we have opportunistically made investments in the past that do not meet one or more of these criteria, and we may make additional investments that do not meet one or more of these criteria if we believe the opportunity is sufficiently attractive. As of December 31, 2011, one tenant, Shopko at 26.7%, contributed more than 10% of our annual rent (approximately 30.4%, assuming completion of Shopko s merger with another one of our tenants in February 2012), and no one property contributed more than 2.1% of our annual rent.

Enhance Our Portfolio through Contractual Growth. Approximately 96% of our leases (based on annual rent) contain contractual provisions that increase the rental revenue over the term of the lease. Of these leases, 25% contain fixed contractual rental increases, and the remaining 75% contain increases based on the lesser of a fixed contractual percentage increase or the increase in the consumer price index, or CPI. Assuming the same CPI growth experienced during the 12 months ended December 31, 2011, our contractual rent growth for the 12 months ending December 31, 2012 would be $4.3 million. Approximately $2.7 million of this amount is attributable to an increase in rent under our master lease with Shopko in June 2011. The rents under our master lease with Shopko adjust every three years.

Selectively Grow Our Portfolio through Acquisitions. We plan to selectively make acquisitions that contribute to our portfolio s tenant, industry and geographic diversification. According to Rosen Consulting Group, or RCG, a nationally recognized real estate consulting firm, through December 2011 the 12-month trailing investment volume in single-tenant properties was $23.6 billion. Given this volume of transactions in the single-tenant market, we believe there will be ample acquisition opportunities fitting our acquisition criteria.

Since September 30, 2011, we have completed approximately $60 million of acquisitions consistent with our underwriting criteria. We believe our experience, in-depth market knowledge and extensive network of long-standing relationships in the real estate industry will provide us access to an ongoing pipeline of attractive investment opportunities.

Continue to Deleverage Our Portfolio. Upon the completion of this offering and the debt conversion described below, we expect to have approximately $2.0 billion principal balance of non-recourse mortgage indebtedness outstanding on a pro forma basis (this represents a decrease of approximately $1.4 billion of indebtedness from January 1, 2008). Additionally, most of our remaining debt will be partially amortizing, and its principal amount will be reduced prior to the balloon payments due at maturity. Contractual amortization payments are scheduled to reduce our outstanding principal amount of indebtedness by $175.7 million prior to January 1, 2016. We also may use any cash from operations in excess of the distributions that we expect to pay to selectively reduce our indebtedness.

We believe contractual rent growth, selective growth through acquisitions and the ongoing deleveraging of our portfolio will contribute to our cash available for distributions.

Financing Strategy

Our long-term financing strategy is to maintain a leverage profile that creates operational flexibility and generates superior risk-adjusted returns for our stockholders. It is our intention to pursue a long-term capital strategy that brings our leverage profile in line with that of our peers over time. Although we are not required to maintain a particular leverage ratio, we intend to employ prudent amounts of debt financing as a means of providing additional funds for the acquisition of assets, to refinance existing debt or for general corporate purposes.

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We anticipate using a number of different sources to finance our acquisitions and operations going forward, including cash from operations, issuance of debt securities, private financings (such as bank credit facilities, which may or may not be secured by our assets), property-level mortgage debt, common or preferred equity issuances or any combination of these sources, to the extent available to us, or other sources that may become available from time to time. To the extent practicable, we expect to maintain a debt profile with manageable near-term maturities.

Market Opportunity

According to a market study prepared for us in connection with this offering by RCG, the current outlook for the net leased real estate market is positive for the following reasons:

- the net lease market has historically provided investors with attractive returns across various economic cycles when compared to other types of real estate investments;
- increased single-tenant transaction volume reflects investors growing interest in single-tenant investment opportunities;
- the market is well positioned to accommodate increased investment activity given the $1.5 trillion to more than $2.0 trillion of U.S. real estate estimated to be held by corporate owner-occupiers; and
- strict lending guidelines, a reduced appetite for risk from both debt and equity investors and upcoming mortgage and corporate debt maturities should yield attractive pricing for many single-tenant, net leased properties and increased opportunities for sale-leaseback transactions.

Summary Risk Factors

You should carefully consider the matters discussed in the Risk Factors section beginning on page 15 of this prospectus prior to deciding whether to invest in our common stock. Some of these risks include:

- We are subject to risks related to commercial real estate ownership that could reduce the value of our properties.
- Global market and economic conditions may materially and adversely affect us and our tenants.
- Our business is dependent upon our tenants successfully operating their businesses and their failure to do so could materially and adversely affect us.
- A substantial number of our properties are leased to one tenant, which may result in increased risk due to tenant and industry concentrations.
- One tenant, operating in the building materials industry, leases a substantial number of our properties that contribute 6.8% of our annual rent and has been adversely affected by the current economic environment, which may result in increased risk of tenant default.
- Loss of our key personnel with long-standing business relationships could materially impair our ability to operate successfully.

We expect to have approximately $2.0 billion principal balance of indebtedness outstanding following this offering and the debt conversion described below on a pro forma basis, which may expose us to the risk of default under our debt obligations.

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

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

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There can be no assurance that we will be able to make or maintain cash distributions, and certain agreements relating to our indebtedness may, under certain circumstances, limit or eliminate our ability to make distributions to our common stockholders.

Concurrent Debt Conversion

We currently have outstanding $729 million of term loan indebtedness, or the term loan, maturing in August 2013. The term loan is separated into two tranches: term loan B, or TLB, with an outstanding principal balance of $399 million and term loan C, or TLC, with an outstanding principal balance of $330 million. As described in further detail in Pricing Sensitivity Analysis, upon the completion of this offering, all $330 million of our currently outstanding TLC will be extinguished and converted into shares of our common stock. We refer to this transaction as the debt conversion. The number of shares of our common stock to be issued to TLC lenders in the debt conversion depends, in part, on the initial public offering price. See Pricing Sensitivity Analysis for a sensitivity analysis of the number of shares to be issued in the debt conversion. Assuming an initial public offering price of $ per share, which is the mid-point of the price range set forth on the front cover of this prospectus, we would issue shares of our common stock in the debt conversion.

Distribution Policy

We intend to pay cash distributions to our common stockholders out of assets legally available. We intend to make a pro rata distribution with respect to the period commencing upon the completion of this offering and ending on , 2012 based on a distribution rate of $ per share of our common stock for a full quarter. On an annualized basis, this would be $ per share of our common stock, or an annual distribution rate of approximately % based on the mid-point of the price range set forth on the front cover of this prospectus. We intend to maintain our initial distribution rate for the 12 months following the completion of this offering unless our results of operations, funds from operations, or FFO, liquidity, cash flows, financial condition, or prospects, economic conditions or other factors differ materially from the assumptions used in projecting our initial distribution rate. We intend to make distributions that will enable us to meet the distribution requirements applicable to REITs and to eliminate or minimize our obligation to pay corporate-level federal income and excise taxes. We do not intend to reduce the expected distribution per share if the underwriters over-allotment option is exercised.

Any distributions will be at the sole discretion of our board of directors, and their form, timing and amount, if any, will depend upon a number of factors, including our actual and projected results of operations, FFO, liquidity, cash flows and financial condition, the revenue we actually receive from our properties, our operating expenses, our debt service requirements, our capital expenditures, prohibitions and other limitations under our financing arrangements, our REIT taxable income, the annual REIT distribution requirements, applicable law and such other factors as our board of directors deems relevant.

Restrictions on Ownership and Transfer of Our Common Stock

Our charter, subject to certain exceptions, authorizes our directors to take such actions as are necessary or advisable to preserve our qualification as a REIT. Furthermore, our charter prohibits any person from actually or constructively owning more than 9.8% in value or in number, whichever is more restrictive, of the outstanding shares of our common stock or 9.8% in value of the aggregate of the outstanding shares of all classes and series of our stock. Our board of directors, in its sole discretion, may exempt a proposed transferee from the ownership limits if certain conditions are satisfied. However, our board of directors may not grant an exemption from the ownership limits to any proposed transferee whose ownership, direct or indirect, in excess of 9.8% of the value or number of outstanding shares of our common stock or 9.8% in value of the aggregate of the outstanding shares of all classes or series of our stock, could jeopardize our status as a REIT. These restrictions on transferability and ownership will

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not apply if our board of directors determines that it is no longer in our best interests to continue to qualify as a REIT. The ownership limits may delay or impede a transaction or a change of control that might be in your best interest. See Description of Our Capital Stock Restrictions on Ownership and Transfer.

As permitted by our charter, our board of directors will, upon completion of this offering, grant to exemptions from the ownership limits, subject to various conditions and limitations, as described under Description of Our Capital Stock Restrictions on Ownership and Transfer.

Our Tax Status

We have elected to be taxed as a REIT for federal income tax purposes commencing with our taxable year ended December 31, 2003. We believe that we have been organized and have operated in a manner that has allowed us to qualify as a REIT for federal income tax purposes commencing with such taxable year, and we intend to continue operating in such a manner. To maintain REIT status, we must meet a number of organizational and operational requirements, including a requirement that we annually distribute to our stockholders at least 90% of our REIT taxable income, determined without regard to the dividends paid deduction and excluding any net capital gains. See Federal Income Tax Considerations.

Corporate Information

We were formed in 2003 and became a public company in December 2004. We were subsequently taken private in August 2007. Our principal executive office is located at 14631 North Scottsdale Road, Suite 200, Scottsdale, Arizona 85254. Our telephone number is (480) 606-0820.

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The Offering

Common stock offered by us	shares (plus up to an additional shares of our common stock that we may issue and sell upon the exercise of the underwriters over-allotment option in full).
Common stock to be outstanding after this offering	shares[(1)]
Use of proceeds	We estimate that the net proceeds to us from this offering, after deducting underwriting discounts and commissions and other estimated expenses payable by us, will be approximately $ million, based on an assumed initial public offering price of $ per share, which is the mid-point of the price range set forth on the front cover of this prospectus ($ million if the underwriters exercise their over-allotment option in full). We intend to use $399 million of the net proceeds from this offering to repay our outstanding TLB, $ million to pay expenses associated with securing lenders consents to this offering and related transactions and the remainder for general business and working capital purposes, including potential future acquisitions. See Use of Proceeds.
Risk Factors	Investing in our common stock involves risks. You should carefully read and consider the information set forth under the heading Risk Factors beginning on page 15 and other information included in this prospectus before investing in our common stock.
Proposed New York Stock Exchange symbol	

(1) Includes (1) shares of our common stock held by continuing investors, (2) shares of our common stock that we will issue to TLC lenders in the concurrent debt conversion, assuming an initial public offering price of $ per share, which is the mid-point of the price range set forth on the front cover of this prospectus, and (3) restricted shares of our common stock to be granted to our directors, executive officers and other employees pursuant to our equity incentive plan, or the Incentive Award Plan. See Pricing Sensitivity Analysis for a sensitivity analysis of the number of shares to be issued in the debt conversion. Excludes (1) shares of our common stock issuable upon the exercise of the underwriters over-allotment option in full and (2) shares of our common stock reserved for further issuance under the Incentive Award Plan, as more fully described in Executive Compensation Incentive Award Plan.

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Summary Selected Financial Data

Our historical consolidated balance sheet data as of December 31, 2011 and 2010 and consolidated operating data for the years ended December 31, 2011, 2010 and 2009 have been derived from our audited historical consolidated financial statements included elsewhere in this prospectus. Our historical consolidated balance sheet data as of December 31, 2009 has been derived from historical consolidated financial statements not included in this prospectus. Our historical consolidated financial data included below and set forth elsewhere in this prospectus are not necessarily indicative of our future performance.

Our unaudited summary selected pro forma consolidated financial and operating data as of and for the year ended December 31, 2011 assumes the completion of this offering, the debt conversion and related transactions as of the beginning of the periods presented for the operating data and as of the stated date for the balance sheet data. Our pro forma financial information is not necessarily indicative of what our actual financial position and results of operations would have been as of the date and for the period indicated, nor does it purport to represent our future financial position or results of operations.

You should read the following summary selected financial and other data together with Management s Discussion and Analysis of Financial Condition and Results of Operations, Business and Properties and our consolidated financial statements and related notes appearing elsewhere in this prospectus.

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	Year Ended December 31, (in thousands, except per share data)			
	Pro forma 2011 (unaudited)	**Historical 2011**	**Historical 2010**	**Historical 2009**
Operating Data:				
Revenues:				
Rentals	$ 268,616	$ 268,616	$ 268,588	$ 265,047
Interest income on loans receivable	6,772	6,772	9,572	10,098
Interest income and other	820	820	14,481	6,477
Total revenues	276,208	276,208	292,641	281,622
Expenses:				
General and administrative	19,218	28,371	19,622	19,853
Litigation	151	151	22,282	
Property costs	5,279	5,279	2,884	2,964
Interest	130,355	169,888	173,054	208,538
Depreciation and amortization	110,809	110,809	111,220	111,983
Impairments	14,042	14,042	23,879	7,584
Total expenses	279,854	328,540	352,941	350,922
Loss from continuing operations before other income (expense) and income tax (benefit) expense	(3,646)	(52,332)	(60,300)	(69,300)
Total other income (expense)			(3,110)	6,810
Loss from continuing operations before income tax (benefit) expense	(3,646)	(52,332)	(63,410)	(62,490)
Income tax (benefit) expense	(60)	(60)	239	3,346
Loss from continuing operations	$ (3,586)	(52,272)	(63,649)	(65,836)
Loss from discontinued operations[1]		(11,591)	(22,888)	(56,847)
Net loss		$ (63,863)	$ (86,537)	$ (122,683)
Loss per share of common stock from continuing operations:				
Basic	$			
Diluted	$			
Weighted average outstanding shares of common stock:				
Basic				
Diluted				

(1) Gains and losses from property dispositions during a period or expected losses from properties classified as held for sale at the end of the period, as well as all operations from those properties, are reclassified to and reported as part of discontinued operations.

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	Year Ended December 31, (dollars in thousands)			
	Pro forma 2011 (unaudited)	**Historical 2011**	**Historical 2010**	**Historical 2009 (unaudited)**
Balance Sheet Data (end of period):				
Gross investments including related lease intangibles	$ 3,582,870	$ 3,582,870	$ 3,610,834	$ 3,740,261
Real estate, net	2,867,302	2,867,302	2,979,496	3,116,070
Cash and cash equivalents	90,312	49,536	88,341	65,072
Total assets	3,263,437	3,231,561	3,396,842	3,618,507
Debt obligations, net	1,901,411	2,627,146	2,730,994	2,866,923
Total liabilities	1,977,104	2,705,201	2,806,741	2,948,828
Stockholders equity	1,286,333	526,360	590,101	669,679
Other Data (unaudited):				
Cash NOI from continuing operations before lease termination fees[(1)]	$ 268,596	$ 268,596	$ 273,540	$ 270,537
FFO[(1)]		$ 69,782	$ 70,563	$ 58,112
FFO from continuing operations, as adjusted[(1)]	$ 118,223	$ 69,537	$ 95,151	$ 40,243
EBITDA from continuing operations[(1)]	$ 237,518	$ 228,365	$ 220,864	$ 258,031
EBITDA from continuing operations, as adjusted[(1)]	$ 251,711	$ 242,558	$ 270,135	$ 258,805
Number of properties in investment portfolio	1,153	1,153	1,161	1,157
Owned properties occupancy at period end (based on number of properties)	98%	98%	96%	99%

(1) For definitions and reconciliations of Cash NOI from continuing operations before lease termination fees, FFO, FFO from continuing operations, as adjusted, EBITDA from continuing operations and EBITDA from continuing operations, as adjusted, see Selected Financial Data.

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RISK FACTORS

Investing in our common stock involves risks. Before you invest in our common stock, you should carefully consider the risk factors below together with all of the other information included in this prospectus. The occurrence of any of the following risks could materially and adversely affect our business, prospects, financial condition, liquidity, results of operations and our ability to service our debt and make or sustain distributions to our stockholders, which could result in a partial or complete loss of your investment in our common stock. Some statements in this prospectus, including statements in the following risk factors, constitute forward-looking statements. Please refer to the section in this prospectus entitled Special Note Regarding Forward-Looking Statements.

Risks Related to Our Business and Properties

We are subject to risks related to commercial real estate ownership that could reduce the value of our properties.

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

- inability to collect rents from tenants due to financial hardship, including bankruptcy;
- changes in local real estate conditions in the markets in which we operate, including the availability and demand for single-tenant retail space;
- changes in consumer trends and preferences that affect the demand for products and services offered by our tenants;
- inability to lease or sell properties upon expiration or termination of existing leases;
- environmental risks related to the presence of hazardous or toxic substances or materials on our properties;
- the subjectivity of real estate valuations and changes in such valuations over time;
- the illiquid nature of real estate compared to most other financial assets;
- changes in laws and governmental regulations, including those governing real estate usage and zoning;
- changes in interest rates and the availability of financing; and
- changes in the general economic and business climate.

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

Global market and economic conditions may materially and adversely affect us and our tenants.

In the United States, market and economic conditions continue to be challenging as a result of the recent economic crisis, which resulted in increased unemployment, large-scale business failures and tight credit markets. Our results of operations are sensitive to changes in the overall economic conditions that impact our tenants financial condition and leasing practices. Adverse economic conditions such as high unemployment levels, interest rates, tax rates and fuel and energy costs may have an impact on the results of operations and financial conditions of our tenants. During periods of economic slowdown, rising interest rates and declining demand for real estate may result in a general decline in rents or an increased incidence of defaults under existing leases. Rental rates and valuations for retail space, which have decreased over the past few years, have not fully recovered to pre-recession levels and we are unable to predict when they may do so. Continued volatility in the

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United States and global markets makes it difficult to determine the breadth and duration of the impact of the recent economic and financial market crises and the ways in which our tenants and our business may be affected. A continuation of the recent lack of demand for rental space could adversely affect our ability to maintain our current tenants and gain new tenants, which may affect our growth and profitability. Accordingly, the prolonged continuation or further worsening of recent financial conditions could materially and adversely affect us.

Our business is dependent upon our tenants successfully operating their businesses and their failure to do so could materially and adversely affect us.

Generally, each of our properties is operated and occupied by a single tenant. Therefore, the success of our investments is materially dependent on the financial stability of our tenants. The success of any one of our tenants is dependent on its individual business and its industry, which could be adversely affected by economic conditions in general, changes in consumer trends and preferences and other factors over which neither they nor we have control. Our portfolio consists primarily of properties leased to single tenants that operate in multiple locations, which means we own numerous properties operated by the same tenant. To the extent we finance numerous properties operated by one company, the general failure of that single tenant or a loss or significant decline in its business could materially and adversely affect us.

At any given time, any tenant may experience a downturn in its business that may weaken its operating results or the overall financial condition of individual properties or its business as whole. As a result, a tenant may delay lease commencement, fail to make rental payments when due, decline to extend a lease upon its expiration, become insolvent or declare bankruptcy. We depend on our tenants to operate the properties we own in a manner which generates revenues sufficient to allow them to meet their obligations to us, including their obligations to pay rent, maintain certain insurance coverage, pay real estate taxes and maintain the properties in a manner so as not to jeopardize their operating licenses or regulatory status. The ability of our tenants to fulfill their obligations under our leases may depend, in part, upon the overall profitability of their operations. Cash flow generated by certain tenant businesses may not be sufficient for a tenant to meet its obligations to us. Although we consider 99.5% of our occupied properties to be operationally essential to our tenants, meaning the property is essential to the tenant s generation of sales and profits, this does not guarantee that a tenant s operations at a particular property will be successful or that the tenant will meet all of its obligations to us. We could be materially and adversely affected if a number of our tenants were unable to meet their obligations to us.

Single-tenant leases involve significant risks of tenant default.

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

A substantial number of our properties are leased to one tenant, which may result in increased risk due to tenant and industry concentrations.

Approximately 26.7% of our annual rent was generated by properties leased to Shopko, which operates general merchandise retail locations under the Shopko name. In February 2012, Shopko and Pamida, another one of our general merchandising tenants, completed a merger. The combined company would have contributed approximately 30.4% of our annual rent as of December 31, 2011. Currently, 114 properties are leased to Shopko

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pursuant to the terms of one master lease and two individual leases. As a result of the completion of the Shopko-Pamida merger, we lease an

additional 67 stores to the combined company, pursuant to our master lease with Pamida. Because a significant portion of our revenues are derived from rental revenues received from Shopko, defaults, breaches or delay in payment of rent by Shopko may materially and adversely affect us. Effective January 2009, we began deferring collection and recognition of a portion of Shopko s rent for a two-year period totaling $3.0 million in the aggregate and postponed scheduled contingent rent increases during this time. In September 2010, Shopko repaid, and we recognized, the total accumulated deferred amount ($2.6 million) plus interest before its contractual due dates. As agreed, the scheduled contingent rent increase from Shopko was postponed from its originally scheduled date of June 2009 to June 2011, at which time Shopko began to pay and we began to recognize the increased rent amount.

As a result of the significant number of properties leased to Shopko, our results of operations and financial condition will be closely tied to the performance of the Shopko stores and the retail industry in which they operate. Shopko operates as a multi-department general merchandise retailer and retail health services provider primarily in mid-size and larger communities in the Midwest, Pacific Northwest and Western Mountain states. Shopko is subject to the following risks, as well as other risks that we are not currently aware of, that could adversely affect its ability to pay rent to us:

- The retail industry in which Shopko operates is highly competitive, which could limit growth opportunities and reduce profitability for Shopko. Shopko competes with other discount retail merchants as well as mass merchants, catalog merchants, internet retailers and other general merchandise, apparel and household merchandise retailers. Shopko faces strong competition from large national discount retailers, such as Walmart, Kmart and Target, and mid-tier merchants such as Kohl s and JCPenney.

- Shopko stores are geographically located in a limited number of regions, particularly in the Midwest, Pacific Northwest and Western Mountain states. Adverse economic conditions in these regions may materially and adversely affect Shopko s results of operations, retail sales and ability to make payments to us under its leases.

- Fluctuations in quarterly performance and seasonality in retail operations may cause Shopko s results of operations to vary considerably from quarter to quarter and could adversely affect Shopko s cash flows.

- Shopko stores are dependent on the efficient functioning of their distribution networks. Problems that cause delays or interruptions in the distribution networks could materially and adversely affect Shopko s results of operations.

- Shopko stores depend on attracting and retaining quality employees. Many employees are entry level or part-time employees with historically high rates of turnover.

If Shopko experiences declines in its business, financial condition or result of operations, it may request discounts or deferrals on the rents it pays to us, seek to terminate its master lease with us or close certain of its stores, all of which could decrease the amount of revenue we receive from Shopko. Decreases in the amount of revenue received from Shopko could materially and adversely affect us.

One tenant, operating in the building materials industry, leases a substantial number of our properties that contribute 6.8% of our annual rent and has been adversely affected by the current economic environment, which may result in increased risk of tenant default.

Approximately $6.9 million of net annual cash flow, representing $18.4 million (6.8% of our annual rent) less non-cash revenue and non-recourse commercial mortgage-backed security, or CMBS, debt service, was generated by 101 properties that we master lease to 84 Properties, LLC and its affiliates. 84 Properties, LLC and

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its affiliates, which we collectively refer to as 84 Lumber, are privately held building materials and services suppliers to professional contractors and build-it-yourselfers that operate more than 280 stores, component plants, door shops, installation centers and engineered wood product shops in 33 states. Because a significant portion of our revenues is derived from rental revenues received from 84 Lumber, defaults, breaches or delay in payment of rent by 84 Lumber may materially and adversely affect us.

84 Lumber is currently meeting its rent payment obligations to us and based upon financial information supplied to us (which we cannot independently verify), the properties subject to the master lease generate sufficient EBITDAR to cover the rental payments due to us. However, 84 Lumber generated operating losses for the past three years and has historically used cash generated from the sale of surplus properties and loans from shareholders to fund these operating deficits. There can be no assurance that 84 Lumber will have the ability to continue to do this or that shareholders will continue to provide loans.

84 Lumber s operating losses resulted in a triggering event under the loan agreement relating to our CMBS loan secured by the properties leased to 84 Lumber, as 84 Lumber s 12-month EBITDAR ratio (based on the information given to us by 84 Lumber, which we cannot independently verify) fell below 1.25:1.00 as of the end of one quarter in 2011. Accordingly, 84 Lumber is required to remit monthly tax and insurance deposits along with its monthly rent directly to an account controlled by the lender, whereupon amounts in excess of monthly tax and insurance costs are disbursed to us. As of January 1, 2012, 84 Lumber s 12-month EBITDAR ratio was 1.35:1.00. 84 Lumber must maintain its 12-month EBITDAR ratio above 1.25:1.00 for 4 consecutive quarters in order to terminate the triggering event. If a monetary event of default were to occur under the 84 Lumber master lease or an event of default under the loan relating to the CMBS debt, then all funds, including those in excess of monthly tax and insurance costs, would be withheld by the lender. This would limit the amount of cash available for us to use in our business and could limit or eliminate our ability to make distributions to our common stockholders. See Management s Discussion and Analysis of Financial Condition and Results of Operation Liquidity and Capital Resources Description of Certain Debt CMBS Loan Secured by 84 Lumber Properties.

As a result of the significant number of properties leased to 84 Lumber, our results of operations and financial condition will be impacted by the performance of the 84 Lumber stores and the building materials supply industry in which they operate. 84 Lumber is subject to the following risks, as well as other risks that we are not currently aware of, that could adversely affect its ability to pay rent to us:

- 84 Lumber s financial performance depends significantly on the stability of the housing, residential construction and home improvement markets, as well as general economic conditions, including changes in gross domestic product. Adverse conditions in or sustained uncertainty about these markets or the economy could adversely impact consumer confidence, causing 84 Lumber s customers to delay purchasing or determine not to purchase home improvement products and services. Other factors (e.g., high levels of unemployment and foreclosures, interest rate fluctuations, fuel and other energy costs, labor and healthcare costs, the availability of financing, the state of the credit markets, including mortgages, home equity loans and consumer credit, weather, natural disasters and other conditions beyond our control) could further adversely affect demand for 84 Lumber s products and services, its costs of doing business and its ability to pay rent to us.

- 84 Lumber operates in markets that are highly competitive. In each market it serves, there are a number of other home improvement stores, electrical, plumbing and building materials supply houses and lumber yards. With respect to some products and services, 84 Lumber also competes with specialty design stores, showrooms, discount stores, local, regional and national hardware stores, mail order firms, warehouse clubs, independent building supply stores and other retailers, as well as with installers of home improvement products. Intense competitive pressures from one or more competitors could affect prices or demand for 84 Lumber s products and services and could adversely affect 84 Lumber and its ability to pay rent to us.

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The vast majority of our properties are leased to unrated tenants, and the tools we use to measure credit quality may not be accurate.

The vast majority of our properties are leased to unrated tenants whom we determine, through our internal underwriting and credit analysis, to be creditworthy. Substantially all of our tenants are required to provide corporate-level financial information, which includes balance sheet, income statement and cash flow statement data on an annual basis, and approximately 80.4% of our leases require the tenant to provide property-level performance information, which includes income statement data on an annual basis. To assist in our determination of a tenant s credit quality, we license a product from Moody s Analytics that provides an estimated default frequency, or EDF, and a shadow rating, and we evaluate a lease s property-level rent coverage ratio. An EDF is only an estimate of default probability based, in part, on assumptions incorporated into the product. A shadow rating does not constitute a published credit rating and lacks the extensive company participation that is typically involved when a rating agency publishes a rating; accordingly, a shadow rating may not be as indicative of creditworthiness as a rating published by Moody s Investment Services, Inc., or Moody s, Standard & Poor s, or S&P, or another nationally recognized statistical rating organization. Our calculations of EDFs, shadow ratings and rent coverage ratios are based on financial information provided to us by our tenants and prospective tenants without independent verification on our part, and we must assume the appropriateness of estimates and judgments that were made by the party preparing the financial information. If our assessment of credit quality proves to be inaccurate, we may be subject to defaults, and investors may view our cash flows as less stable. The ability of an unrated tenant to meet its obligations to us may not be considered as well assured as that of rated tenant.

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

As of December 31, 2011, leases representing approximately 38.6% and 18.5% of our annual rent were with tenants in the retail and restaurant industries, respectively. In the future we may acquire additional retail and restaurant properties. Accordingly, decreases in the demand for retail and/or restaurant spaces may have a greater adverse effect on us than if we had fewer investments in these industries. The market for retail and restaurant space has been, and could continue to be, adversely affected by weakness in the national, regional and local economies, the adverse financial condition of some large retail and restaurant companies, the ongoing consolidation in the retail and restaurant industries, the excess amount of retail and restaurant space in a number of markets and, in the case of the retail industry, increasing consumer purchases through catalogues or the internet. To the extent that these conditions continue, they are likely to negatively affect market rents for retail and restaurant space and could materially and adversely affect us.

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

Our results of operations depend on our ability to continue to strategically lease space in our properties, including renewing expiring leases, leasing vacant space and re-leasing space in properties where leases are expiring, optimizing our tenant mix or leasing properties on more economically favorable terms. As of December 31, 2011, leases representing approximately 1.1% of our annual rent will expire during 2012. As of December 31, 2011, 17 of our properties, representing approximately 1.6% of our total number of owned properties, were vacant. Current tenants may decline, or may not have the financial resources available, to renew current leases and we cannot assure you that leases that are renewed will have terms that are as economically favorable to us as the expiring lease terms. If tenants do not renew the leases as they expire, we will have to find new tenants to lease our properties and there is no guarantee that we will be able to find new tenants or that our properties will be re-leased at rental rates equal to or above the current average rental rates or that substantial rent abatements, tenant improvement allowances, early termination rights or below-market renewal options will not be offered to attract new tenants. We may experience significant costs in connection with re-leasing a significant number of our properties, which could materially and adversely affect us.

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

Most of our leases contain rent escalators, or provisions that periodically increase the base rent payable by the tenant under the lease. Although some of our rent escalators increase rent at a fixed amount on fixed dates, most of our rent escalators increase rent by the lesser of (1) 1 to 1.25 times any increase in the CPI over a specified period or (2) a fixed percentage. If the product of any increase in the CPI multiplied by the applicable factor is less than the fixed percentage, the increased rent we are entitled to receive will be less than what we otherwise would have been entitled to receive if the rent escalator was based solely on a fixed percentage. Therefore, during periods of low inflation or deflation, small increases or decreases in the CPI will subject us to the risk of receiving lower rental revenue than we otherwise would have been entitled to receive if our rent escalators were based solely on fixed percentages or amounts. Conversely, if the product of any increase in the CPI multiplied by the applicable factor is more than the fixed percentage, the increased rent we are entitled to receive will be less than what we otherwise would have been entitled to receive if the rent escalator was based solely on an increase in CPI. Therefore, periods of high inflation will subject us to the risk of receiving lower rental revenue than we otherwise would have been entitled to receive if our rent escalators were based solely on CPI increases.

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

The occurrence of a tenant bankruptcy or insolvency could diminish the income we receive from that tenant s lease or leases. If a tenant becomes bankrupt or insolvent, federal law may prohibit us from evicting such tenant based solely upon such bankruptcy or insolvency. In addition, a bankrupt or insolvent tenant may be authorized to reject and terminate its lease or leases with us. Any claims against such bankrupt tenant for unpaid future rent would be subject to statutory limitations that would likely result in our receipt of rental revenues that are substantially less than the contractually specified rent we are owed under the lease or leases. In addition, any claim we have for unpaid past rent, if any, may not be paid in full. We may also be unable to re-lease a terminated or rejected space or to re-lease it on comparable or more favorable terms. As a result, tenant bankruptcies may materially and adversely affect us.

Tenants who are considering filing for bankruptcy protection may request that we agree to amendments of their master leases to remove certain of the properties they lease from us from such master leases. In 2010, two of the tenants with whom we have master leases filed for protection under federal bankruptcy law. During such bankruptcy filings, we entered into amendments to the master leases with both tenants, pursuant to which one tenant was permitted to remove from its master lease 15 of the 22 properties it leased from us in exchange for $6.25 million in termination fees and the other tenant was permitted to remove from its master lease three of the nine properties it leased from us for $6.0 million in termination fees. Although, as of December 31, 2011, we have sold or re-leased 15 of the 18 properties that were vacated in connection with these amendments, we cannot guarantee that we will be able to sell or re-lease the remaining properties on terms that are favorable to us, or at all. As of December 31, 2011, four of our properties with an original gross investment of $5.7 million are master leased to a tenant that has filed for bankruptcy protection. This proceeding is ongoing and we cannot predict its outcome with certainty. We cannot guarantee that we will be able to sell or re-lease properties that we agree to release from tenants leases in the future or that lease termination fees, if any, will be sufficient to make up for the rental revenues lost as a result of lease amendments.

There can be no assurance that future recoveries relating to properties leased to tenants experiencing financial distress will meet our historical recovery rate or that a larger percentage of our tenants will not experience financial distress.

Since our inception in 2003 through December 31, 2011, we have experienced or expect to experience $130.4 million of aggregate losses (of which $20.1 million are estimated losses as of December 31, 2011) due to tenant financial distress, or 3.3% of our gross investment of approximately $4.05 billion in properties and loans receivable. Included in our historical losses are estimated losses relating to 18 properties. See Business and

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Properties Risk Management Tenant Financial Distress Risk Historical Summary of Tenant Financial Distress Portfolio for a discussion of how we estimate losses based on our historical experience. Our actual losses on these properties could exceed our estimate by a material amount. It is also possible that a larger percentage of our tenants could experience financial distress in the future and cause us to incur significant additional losses. Furthermore, no assurance can be given that future recoveries relating to properties leased to tenants experiencing financial distress will match our historical recovery rate.

Property vacancies could result in significant capital expenditures.

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

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

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

- we face competition from other real estate investors with significant capital, including REITs and institutional investment funds, which may be able to accept more risk than we can prudently manage, including risks associated with paying higher acquisition prices;

- we face competition from other potential acquirers which may significantly increase the purchase price for a property we acquire, which could reduce our growth prospects;

- we may incur significant costs and divert management attention in connection with evaluating and negotiating potential acquisitions, including ones that we are subsequently unable to complete;

- we may acquire properties that are not accretive to our results upon acquisition, and we may be unsuccessful in managing and leasing such properties in accordance with our expectations;

- our cash flow from an acquired property may be insufficient to meet our required principal and interest payments with respect to debt used to finance the acquisition of such property;

- we may discover unexpected items, such as unknown liabilities, during our due diligence investigation of a potential acquisition or other customary closing conditions may not be satisfied, causing us to abandon an acquisition opportunity after incurring expenses related thereto;

- we may fail to obtain financing for an acquisition on favorable terms or at all;

we may spend more than budgeted amounts to make necessary improvements or renovations to acquired properties;

market conditions may result in higher than expected vacancy rates and lower than expected rental rates; or

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- we may acquire properties subject to liabilities and without any recourse, or with only limited recourse, with respect to unknown liabilities such as liabilities for clean-up of undisclosed environmental contamination, claims by tenants, vendors or other persons dealing with the former owners of the properties, liabilities incurred in the ordinary course of business and claims for indemnification by general partners, directors, officers and others indemnified by the former owners of the properties.

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

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

The real estate investments made, and expected to be made, by us are relatively difficult to sell quickly. As a result, our ability to promptly sell one or more properties in our portfolio in response to changing economic, financial or investment conditions is limited. Return of capital and realization of gains, if any, from an investment generally will occur upon disposition or refinancing of the underlying property. We may be unable to realize our investment objective by sale, other disposition or refinancing at attractive prices within any given period of time or may otherwise be unable to complete any exit strategy. In particular, these risks could arise from weakness in or even the lack of an established market for a property, changes in the financial condition or prospects of prospective purchasers, changes in national or international economic conditions, such as the economic downturn of 2008 through 2010, and changes in laws, regulations or fiscal policies of the jurisdiction in which the property is located.

In addition, the Internal Revenue Code of 1986, as amended, or the Code, imposes restrictions on a REIT s ability to dispose of properties that are not applicable to other types of real estate companies. In particular, the tax laws applicable to REITs effectively require that we hold our properties for investment, rather than primarily for sale in the ordinary course of business, which may cause us to forgo or defer sales of properties that otherwise would be in our best interest. Therefore, we may not be able to vary our portfolio in response to economic or other conditions promptly or on favorable terms, which may materially and adversely affect us.

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

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

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

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