UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

☑ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTER ENDED MARCH 31, 2005**

OR

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

COMMISSION FILE NUMBER: 0-50363

GLADSTONE COMMERCIAL CORPORATION

(Exact name of registrant as specified in its charter)

MARYLAND	**02-0681276**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1521 WESTBRANCH DRIVE, SUITE 200
MCLEAN, VIRGINIA 22102
(Address of principal executive office)
(703) 287-5800
(Registrant's telephone number, including area code)

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 is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes☑ No☐.

The number of shares of the issuer's Common Stock, $0.001 par value, outstanding as of April 29, 2005 was 7,667,000.

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GLADSTONE COMMERCIAL CORPORATION

CONSOLIDATED BALANCE SHEETS

	March 31, 2005 (Unaudited)	December 31, 2004
ASSETS		
Real estate, net	$ 71,226,016	$ 60,466,330
Mortgage note receivable	11,081,931	11,107,717
Cash and cash equivalents	18,059,875	29,153,987
Funds held in escrow	744,129	1,060,977
Interest receivable – mortgage note	71,109	64,795
Interest receivable – employees	4,685	4,792
Deferred rent receivable	697,210	210,846
Deferred financing costs	663,134	—
Prepaid expenses	203,026	170,685
Other assets	216,649	114,819
Lease intangibles, net of accumulated amortization of $308,159 and $194,047, respectively	4,023,315	3,230,146
TOTAL ASSETS	106,991,079	105,585,094
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Due to Adviser	142,598	129,231
Accounts payable and accrued expenses	417,464	168,389
Dividends payable	—	920,040
Mortgage note payable	3,150,000	—
Rent received in advance, security deposits and funds held in escrow	1,432,991	1,674,741
Total Liabilities	5,143,053	2,892,401
STOCKHOLDERS' EQUITY		
Common stock, $0.001 par value, 20,000,000 shares authorized and 7,667,000 shares issued and outstanding	7,667	7,667
Additional paid in capital	105,427,549	105,427,549
Notes receivable - employees	(374,792)	(375,000)
Distributions in excess of accumulated earnings	(3,212,398)	(2,367,523)
Total Stockholders' Equity	101,848,026	102,692,693
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 106,991,079	$ 105,585,094

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

GLADSTONE COMMERCIAL CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	For the three months ended March 31, 2005	For the three months ended March 31, 2004
OPERATING REVENUES		
Rental income	$ 1,847,007	$ 197,773
Interest income from mortgage note receivable	295,583	133,419
Tenant recovery revenue	2,043	—
Total operating revenues	2,144,633	331,192
OPERATING EXPENSES		
Depreciation and amortization	537,755	79,330
Management advisory fee	471,861	229,416
Professional fees	331,244	208,457
Taxes and licenses	128,273	10,320
Insurance	70,383	64,487
Interest	36,219	—
General and administrative	132,828	104,949
Total operating expenses	1,708,563	696,959
Income (loss) from operations	436,070	(365,767)
Interest income from temporary investments	94,521	172,462
Interest income - employee loans	4,685	—
Loss on foreign currency translation	(92)	—
Other income	99,114	172,462
NET INCOME (LOSS)	$ 535,184	$ (193,305)
Earnings (loss) per weighted average common share		
Basic	$ 0.07	$ (0.03)
Diluted	$ 0.07	$ (0.03)
Weighted average shares outstanding		
Basic	7,667,000	7,642,000
Diluted	7,733,335	7,642,000

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

GLADSTONE COMMERCIAL CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	For the three months ended March 31, 2005	For the three months ended March 31, 2004
Cash flows from operating activities:		
Net income (loss)	$ 535,184	$ (193,305)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	537,755	79,330
Changes in assets and liabilities:		
Amortization of deferred financing costs	16,246	—
Amortization of deferred rent asset	6,136	—
Increase in mortgage interest receivable	(6,314)	(68,261)
Decrease in employee interest receivable	107	—
(Increase) decrease in prepaid expenses	(32,341)	40,620
Decrease (increase) in other assets	48,170	(18,266)
Increase in deferred rent receivable	(97,499)	(13,764)
Increase in accounts payable and accrued expenses	249,075	102,266
Increase in due to Adviser	13,367	356,115
Increase in rent received in advance and security deposits	75,098	210,767
Net cash provided by operating activities	1,344,984	495,502
Cash flows from investing activities:		
Acquisition of real estate	(12,485,610)	(3,650,000)
Issuance of mortgage note receivable	—	(11,170,000)
Deposit on future acquisition	(200,000)	—
Principal repayments on mortgage note receivable	25,786	—
Net cash used in investing activities	(12,659,824)	(14,820,000)
Cash flows from financing activities:		
Offering costs	—	(7,730)
Proceeds from borrowings under mortgage note payable	3,150,000	—
Principal repayments on employee loans	208	—
Payments for deferred financing costs	(629,380)	—
Dividends paid	(2,300,100)	(76,420)
Net cash provided by (used in) financing activities	220,728	(84,150)
Net decrease in cash and cash equivalents	(11,094,112)	(14,408,648)
Cash and cash equivalents, beginning of period	29,153,987	99,075,765
Cash and cash equivalents, end of period	$ 18,059,875	$ 84,667,117

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

1. Organization and Significant Accounting Policies

Gladstone Commercial Corporation, a Maryland corporation, (the "Company") was incorporated on February 14, 2003 under the General Corporation Law of Maryland for the purpose of engaging in the business of investing in property net leased to creditworthy entities and making mortgage loans to creditworthy entities. Subject to certain restrictions and limitations, the business of the Company is managed by Gladstone Management Corporation (the "Adviser").

Subsidiaries

On May 28, 2003, the Company completed the formation of a subsidiary, Gladstone Commercial Limited Partnership (the "Operating Partnership"). The Company conducts substantially all of its operations through the Operating Partnership. As the Company currently owns all of the general and limited partnership interests of the Operating Partnership, the financial position and results of operations of the Operating Partnership are consolidated with those of the Company.

On January 27, 2004, the Company completed the formation of a subsidiary, Gladstone Lending LLC ("Gladstone Lending"). Gladstone Lending was created to conduct all operations related to real estate mortgage loans of the Company. As the Operating Partnership currently owns all of the general and limited partnership interests of Gladstone Lending, the financial position and results of operations of Gladstone Lending are consolidated with those of the Operating Partnership.

On August 23, 2004, the Company completed the formation of a subsidiary, Gladstone Commercial Advisers, Inc. ("Commercial Advisers"). Commercial Advisers is a taxable REIT subsidiary, which was created to collect all non-qualifying income related to the Company's real estate portfolio. This income will predominately consist of fees received by the Company related to the leasing of real estate. Since the Company owns 100% of the voting securities of Commercial Advisers, the financial position and results of operations of Commercial Advisers are consolidated with those of the Company. There have been no such fees earned to date.

Interim financial information

Interim financial statements of the Company are prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information and pursuant to the requirements for reporting on Form 10-Q and Article 10 of Regulation S-X. Accordingly, certain disclosures accompanying annual financial statements prepared in accordance with GAAP are omitted. In the opinion of management, all adjustments, consisting solely of normal recurring accruals, necessary for the fair statement of financial statements for the interim period have been included.

Investments in real estate

The Company records investments in real estate at cost and capitalizes improvements and replacements when they extend the useful life or improve the efficiency of the asset. The Company expenses costs of repairs and maintenance as incurred. The Company computes depreciation using the straight-line method over the estimated useful life of 39 years for buildings and improvements, five to seven years for equipment and fixtures and the shorter of the useful life or the remaining lease term for tenant improvements and leasehold interests. Real estate depreciation expense was $423,643 and $65,743 for the three months ended March 31, 2005 and 2004, respectively.

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

The Company allocates purchase price to the fair value of the tangible assets of an acquired property (which includes the land, building, and tenant improvements) to be determined by valuing the property as if it were vacant. The "as-if-vacant" value is allocated to land, building, and tenant improvements based on management's determination of the relative fair values of these assets.

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

Above-market and below-market in-place lease values for owned properties are recorded based on the present value (using an interest rate which reflects the risks associated with the leases acquired) of the difference between (i) the contractual amounts to be paid pursuant to the in-place leases and (ii) management's estimate of fair market lease rates for the corresponding in-place leases, measured over a period equal to the remaining non-cancelable term of the lease. The capitalized above-market lease values will be amortized as a reduction of rental income over the remaining non-cancelable terms of the respective leases. The capitalized below-market lease values (presented in the accompanying balance sheet as value of assumed lease obligations) are amortized as an increase to rental income over the initial term and any fixed-rate renewal periods in the respective leases. Since the Company's strategy to a large degree involves sale-leaseback transactions with newly originated leases at market rates, the above-market and below-market in-place lease values have not been significant for any of the transactions that the Company has entered into.

Management's estimates of value are made using methods similar to those used by independent appraisers (e.g., discounted cash flow analysis). Factors considered by management in its analysis include an estimate of carrying costs during hypothetical expected lease-up periods considering current market conditions, and costs to execute similar leases. The Company also considers information obtained about each property as a result of its pre-acquisition due diligence, marketing and leasing activities in estimating the fair value of the tangible and intangible assets acquired. In estimating carrying costs, management also includes real estate taxes, insurance and other operating expenses and estimates of lost rentals at market rates during the expected lease-up periods, which primarily range from six to 18 months, depending on specific local market conditions. Management also estimates costs to execute similar leases including leasing commissions, legal and other related expenses to the extent that such costs are not already incurred in connection with a new lease origination as part of the transaction.

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

The value of in-place leases is amortized to expense over the initial term of the respective leases, which range from five to twenty years. The value of customer relationship intangibles are amortized to expense over the initial term and any renewal periods in the respective leases, but in no event does the amortization period for intangible assets exceed the remaining depreciable life of the building. Should a tenant terminate its lease, the unamortized portion of the in-place lease value and customer relationship intangibles will be charged to expense. Total amortization expense was $114,113 for the three months ended March 31, 2005, and $13,587 for three months ended March 31, 2004.

The following table summarizes the gross value of customer relationship intangibles:

	For the three months ended March 31, 2005	For the year ended December 31, 2004
In-place leases	$ 2,390,800	$ 1,929,800
Leasing costs	1,940,674	1,494,393
Accumulated amortization	(308,159)	(194,047)
	$ 4,023,315	$ 3,230,146

Impairment

Investments in Real Estate

The Company accounts for the impairment of real estate in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," which requires that the Company periodically review the carrying value of each property to determine if circumstances that indicate impairment in the carrying value of the investment exist or that depreciation periods should be modified. If circumstances support the possibility of impairment, the Company prepares a projection of the undiscounted future cash flows, without interest charges, of the specific property and determines if the investment in such property is recoverable. If impairment is indicated, the carrying value of the property is written down to its estimated fair value based on the Company's best estimate of the property's discounted future cash flows. There have been no impairments recognized on the Company's real estate assets at March 31, 2005.

Provision for Loan Losses

The Company's accounting policies require that it reflect in its financial statements an allowance for estimated credit losses with respect to mortgage loans it has made based upon its evaluation of known and inherent risks associated with its private lending assets. The Company has extended one mortgage loan and has not experienced any actual losses in connection with its lending investments. Management reflects provisions for loan losses on a portfolio basis based upon its assessment of general market conditions, its internal risk management policies and credit risk rating system, industry loss experience, its assessment of the likelihood of delinquencies or defaults, and the value of the collateral underlying its investments. Actual losses, if any, could ultimately differ from these estimates. There are no provisions for loan losses at March 31, 2005.

Cash and cash equivalents

The Company considers all short-term, highly liquid investments that are both readily convertible to cash and have a maturity of generally three months or less at the time of purchase to be cash equivalents; except that any such investments purchased with funds on deposit in escrow or similar accounts are classified as restricted deposits. Items classified as cash equivalents include commercial paper and money-market funds. All of the Company's cash and cash equivalents at March 31, 2005 were held in the custody of three financial institutions, and the Company's balance at times may exceed federally insurable limits. The Company mitigates this risk by depositing funds with major financial institutions.

Deferred financing costs

Deferred financing costs consist of costs incurred to obtain long-term financing. These costs consist of legal fees, origination fees, and administrative fees incurred in association with the long-term financing. The costs are deferred and amortized using the straight-line method, which approximates the effective interest method, over the term of the financing secured.

Revenue recognition

Rental revenues include rents that each tenant pays in accordance with the terms of its respective lease reported on a straight-line basis over the non-cancelable term of the lease. Certain of the Company's leases currently contain rental increases at specified intervals, and straight-line basis accounting requires the Company to record an asset, and include in revenues, deferred rent receivable that will be received if the tenant makes all rent payments required through the expiration of the initial term of the lease. Deferred rent receivable in the accompanying balance sheets represents the cumulative difference between rental revenue as recorded on a straight line basis and rents received from the tenants in accordance with the lease terms. Accordingly, the Company determines, in its judgment, to what extent the deferred rent receivable applicable to each specific tenant is collectible. The Company reviews deferred rent receivable on a quarterly basis and takes into consideration the tenant's payment history, the financial condition of the tenant, business conditions in the industry in which the tenant operates and economic conditions in the area in which the property is located. In the event that the collectability of deferred rent with respect to any given tenant is in doubt, the Company records an increase in the allowance for uncollectible accounts or records a direct write-off of the specific rent receivable, which would have an adverse effect on the net income for the year in which the reserve is increased or the direct write-off is recorded and would decrease total assets and stockholders' equity. No such reserves have been recorded as of March 31, 2005.

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

Stock based compensation

The Company currently accounts for the issuance of stock options under its 2003 Equity Incentive Plan (the "2003 Plan"), in accordance with APB Opinion No. 25, "Accounting for Stock Issued to Employees." In this regard, these options have been granted to individuals who are the Company's officers, and who would qualify as leased employees under FASB Interpretation No. 44 ("FIN 44"), "Accounting for Certain Transactions Involving Stock Compensation, an Interpretation of APB Opinion No. 25."

In December 2004, the Financial Accounting Standards Board ("FASB") approved the revision of SFAS No. 123, "Accounting for Stock-Based Compensation, and issued the revised SFAS No. 123(R), "Share-Based Payment." In April of 2005 the effective date of adoption was changed from interim periods ending after June 15, 2005 to annual periods beginning after June 15, 2005. SFAS No. 123(R) effectively replaces SFAS No. 123, and supersedes APB Opinion No. 25, "Accounting for Stock Issued to Employees." The new standard is effective for awards that are granted, modified, or settled in cash for

annual periods beginning after June 15, 2005. The adoption of SFAS No. 123(R) will require the Company to begin expensing the value of stock options granted as compensation cost beginning in January of 2006. The impact of the adoption of this amendment to current earnings is discussed below.

The following table summarizes the Company's operating results as if the Company elected to account for its stock-based compensation under the fair value provisions of SFAS No. 123(R), "Share-Based Payment," for the three months ended March 31, 2005 and 2004:

	For the three months ended March 31, 2005	For the three months ended March 31, 2004
Net income (loss), as reported	$ 535,184	$ (193,305)
Less: Stock-based compensation expense determined using the fair value based method	(95,792)	(65,392)
Net income (loss), pro-forma	$ 439,392	$ (258,697)
Basic, as reported	$ 0.07	$ (0.03)
Basic, pro-forma	$ 0.06	$ (0.03)
Diluted, as reported	$ 0.07	$ (0.03)
Diluted, pro-forma	$ 0.06	$ (0.03)

The stock-based compensation expense under the fair value method, as reported in the above table, was computed using an estimated weighted average fair value of $1.29 using the Black-Scholes option-pricing model, based on options issued from date of inception forward, and the following weighted-average assumptions: dividend yield of 4.99%, risk-free interest rate of 2.54%, expected volatility factor of 18.40%, and expected lives of 3 years.

Income taxes

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

Gladstone Commercial Advisers is a wholly-owned taxable REIT subsidiary, ("TRS"), that is subject to federal and state income taxes. The Company accounts for such income taxes in accordance with the provisions of SFAS No. 109. Under SFAS No. 109, the Company accounts for income taxes using the asset and liability method under which deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases.

Segment information

SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information" provides standards for public companies relating to the reporting of financial and descriptive information about their operating segments in financial statements. Operating segments are defined as components of an enterprise for which separate financial information is available and is evaluated regularly by the chief operating

decision maker or decision making group in determining how to allocate resources and in assessing performance. Company management is the chief decision making group. As discussed in Note 8, the Company's operations are derived from two operating segments.

Foreign Currency Transactions

The Company purchased two properties in Canada in October of 2004. Rental payments from these properties are received in Canadian Dollars. In accordance with SFAS No. 52 "Foreign Currency Translation," the rental revenue received is recorded using the exchange rate as of the transaction date, which is the first day of each month. Straight line rent and any deferred rent asset or liability are also recorded using the exchange rate as of the transaction date. If the rental payment is received on a date other than the transaction date, then a foreign currency gain or loss would be recorded on the financial statements. All deferred rent assets are re-valued at each balance sheet date to reflect the current exchange rate. For the quarter ended March 31, 2005, $92 was recorded as a foreign currency loss, resulting from rental payments being received on dates other than the transaction date and the valuation of deferred rent at the end of the quarter.

Use of estimates

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

Reclassifications

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

2. Management Advisory Fee

The Company has no employees, and all of the Company's operations are managed by the Company's Adviser pursuant to an advisory agreement. Pursuant to the advisory agreement, the Adviser is responsible for managing the Company on a day-to-day basis and for identifying, evaluating, negotiating and consummating investment transactions consistent with the Company's criteria. In exchange for such services, the Company pays the Adviser a management advisory fee, which consists of the reimbursement of certain expenses of the Adviser. The Company reimburses the Adviser for its pro-rata share of the payroll and related benefit expenses on an employee-by-employee basis, based on the percentage of each employee's time devoted to Company matters. The Company also reimburses the Adviser for general overhead expenses multiplied by the ratio of hours worked by Adviser employees on Company matters to the total hours worked by the Adviser's employees.

Under the terms of the advisory agreement, the Company will only be required to reimburse the Adviser for its portion of the Adviser's general overhead expenses if the amount of payroll and benefits reimbursed to the Adviser is less than 2.0% of the Company's average invested assets for the year. Additionally, the Company will only be required to reimburse the Adviser for overhead expenses up to the point that reimbursed overhead expenses and payroll and benefits expenses, on a combined basis, equal 2.0% of the Company's average invested assets for the year. However, to the extent that payroll and benefits reimbursements exceed the annual management fee cap of 2.0%, these payroll amounts will be reimbursed by the Company. The Adviser will bill the Company on a monthly basis for these amounts. The Adviser must reimburse the Company annually for the amount by which amounts billed to and paid by the Company exceed this 2.0% limit during a given year. To the extent that overhead expenses payable or reimbursable by the Company exceed this limit and the Company's independent directors determine that the excess expenses were justified based on unusual and nonrecurring factors which they deem sufficient,

the Company may reimburse the Adviser in future years for the full amount of the excess expenses, or any portion thereof, but only to the extent that the reimbursement would not cause the Company's overhead expense reimbursements to exceed the 2.0% limitation in any year. To date, the advisory fee has not exceeded the annual cap.

For the three months ended March 31, 2005, the Company incurred approximately $472,000 in management advisory fees. For the three months ended March 31, 2004, the Company incurred approximately $229,000 in management advisory fees. Approximately $143,000 and $129,000 was unpaid at March 31, 2005 and December 31, 2004, respectively.

The following table shows the breakdown of the management advisory fee for the three months ended March 31, 2005 and 2004:

	For the three months ended March 31, 2005	For the three months ended March 31, 2004
Allocated payroll and benefits	$ 347,314	$ 165,839
Allocated overhead expenses	$ 124,547	$ 63,577
Total management advisory fee	$ 471,861	$ 229,416

3. Stock Options

At March 31, 2005, 865,000 options were outstanding with exercise prices ranging from $15 to $16.85 with terms of ten years.

In 2004, an employee of the Company exercised 25,000 options at $15.00 per share for a like number of shares of common stock in consideration for a promissory note in the principal amount of $375,000. This note has full recourse back to the employee, has a term of nine years and bears interest at 5% per year. This note was recorded as a loan to employee in the equity section of the accompanying consolidated balance sheets. No compensation expense was recorded related to this transaction. As of March 31, 2005, approximately $375,000 of indebtedness was owed by current employees to the Company, and no current or former directors or executive officers had any loans outstanding.

4. Earnings Per Common Share

The following tables set forth the computation of basic and diluted earnings (loss) per share for the three months ended March 31, 2005 and 2004:

	For the three months ended March 31, 2005	For the three months ended March 31, 2004
Net income (loss)	$ 535,184	$ (193,305)
Denominator for basic weighted average shares	7,667,000	7,642,000
Dilutive effect of stock options [a]	66,335	—
Denominator for diluted weighted average shares	7,733,335	7,642,000
Basic earnings (loss) per common share	$ 0.07	$ (0.03)
Diluted earnings (loss) per common share	$ 0.07	$ (0.03)

[a] The dilutive effect of options outstanding as of March 31, 2004 are not included in the calculation as they are anti-dilutive.

5. Real Estate

A summary of all properties held by the Company as of March 31, 2005 is as follows:

Date Acquired	Location	Square Footage (unaudited)	Property Description	Net Real Estate
Dec-03	Raleigh, North Carolina	58,926	Office	$ 5,176,352
Jan-04	Canton, Ohio	54,018	Office and Warehouse	3,553,526
Apr-04	Akron, Ohio	83,891	Office and Laboratory	8,505,450
Jun-04	Charlotte, North Carolina	64,500	Office	9,169,689
Jul-04	Canton, North Carolina	228,000	Commercial and Manufacturing	5,105,669
Aug-04	Snyder Township, Pennsylvania	290,000	Commercial and Warehouse	6,556,148
Aug-04	Lexington, North Carolina	154,000	Commercial and Warehouse	2,927,408
Sep-04	Austin, Texas	51,993	Flexible Office	7,243,781
Oct-04	Norfolk, Virginia	25,797	Commercial and Manufacturing	918,236
Oct-04	Mt. Pocono, Pennsylvania	223,275	Commercial and Manufacturing	6,117,554
Oct-04	Granby, Quebec	99,981	Commercial and Manufacturing	3,012,465
Oct-04	Montreal, Quebec	42,490	Commercial and Manufacturing	1,840,387
Feb-05	San Antonio, Texas	60,245	Flexible Office	8,314,494
Feb-05	Columbus, Ohio	39,000	Industrial	2,784,857
				$ 71,226,016

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

	March 31, 2005	December 31, 2004
Real estate:		
Land	$ 8,922,000	$ 7,669,000
Building	61,848,662	52,641,933
Tenant improvements	1,664,122	940,522
Accumulated depreciation	(1,208,768)	(785,125)
Real estate, net	$ 71,226,016	$ 60,466,330

On February 10, 2005, the Company acquired a 60,245 square foot flexible office building in San Antonio, Texas for $9.0 million, including transaction costs, and the purchase was funded using a portion of the net proceeds from the Company's initial public offering. Upon acquisition of the property, the Company was assigned the previously existing triple net lease with the sole tenant, which had a remaining term of approximately nine years at the time of assignment. The lease provides for annual rents of approximately $753,000 through 2008, with prescribed escalations thereafter.

On February 10, 2005, the Company acquired a 39,000 square foot industrial building in Columbus, Ohio for $3.4 million, including transaction costs, and the purchase was funded using a portion of the net proceeds from the Company's initial public offering. Upon acquisition of the property, the Company was assigned the previously existing triple net lease with the sole tenant, which had a remaining term of approximately ten years at the time of assignment. The lease provides for annual rents of approximately $318,000 through 2006, with prescribed escalations thereafter.

In accordance with SFAS No. 141, "Business Combinations," the Company allocated the purchase price of the properties acquired during the three months ended March 31, 2005 as follows:

Three months ended March 31, 2005

	San Antonio, Texas	Columbus, Ohio	Total
Land	$ 843,000	$ 410,000	$ 1,253,000
Building	6,795,312	2,379,947	9,175,259
Tenant Improvments	718,439	5,161	723,600
Lease Intangibles	664,218	638,063	1,302,281
Total Purchase Price	$ 9,020,969	$ 3,433,171	$ 12,454,140

Future operating lease payments under non-cancelable leases, excluding customer reimbursement of expenses, in effect at March 31, 2005 are as follows:

Year	Rental Payments
2005	$ 5,659,644
2006	7,587,011
2007	7,677,824
2008	7,780,656
2009	6,730,158
Thereafter	49,384,169

Lease payments for certain properties, where payments are denominated in Canadian dollars, have been translated to US dollars using the exchange rate as of March 31, 2005 for the purposes of the table above.

In accordance with the lease terms, substantially all tenant expenses are required to be paid by the tenant, however the Company would be required to pay property taxes on the respective property in the event the tenant fails to pay them, which would amount to a total of $1.1 million on an annual basis for all properties and loans outstanding as of March 31, 2005.

6. Mortgage Note Receivable

On February 18, 2004, the Company extended a promissory mortgage note in the amount of $11,170,000 collateralized by property in Sterling Heights, Michigan. The note was issued from a portion of the net proceeds of the Company's initial public offering. The note accrues interest at the greater of 11% per year or the one month LIBOR rate plus 5% per year, and is for a period of 10 years maturing on February 18, 2014. At March 31, 2005, the outstanding balance of the note was $11,081,931.

7. Dividends Declared per Share

During the three months ended March 31, 2005, the Company commenced paying a monthly dividend. The following table summarizes the dividends paid during the three months ended March 31, 2005:

Record Date	Payment Date	Dividend per Share
January 17, 2005	January 31, 2005	$0.06
February 14, 2005	February 25, 2005	$0.06
March 16, 2005	March 30, 2005	$0.06

8. Segment Information

As of March 31, 2005, the Company's operations are derived from two operating segments. One segment purchases real estate (land, buildings and other improvements), which is simultaneously leased to existing users and the other segment extends mortgage loans and collects principal and interest payments. The following table summarizes the Company's consolidated operating results and total assets by segment as of and for the three months ended March 31, 2005 and 2004:

	As of and for the Three Months Ended March 31, 2005			
	Real Estate Leasing	Real Estate Lending	Other	Total
Revenue	$ 1,849,050	$ 295,583	$ —	$ 2,144,633
Expenses	666,028	—	1,042,535	1,708,563
Income (loss) from operations	1,183,022	295,583	(1,042,535)	436,070
Other income (loss)	(92)	—	99,206	99,114
Net income (loss)	$ 1,182,930	$ 295,583	$ (943,329)	$ 535,184
Total Assets	$ 76,146,541	$ 11,153,040	$ 19,691,498	$ 106,991,079

	As of and for the Three Months Ended March 31, 2004			
	Real Estate Leasing	Real Estate Lending	Other	Total
Revenue	$ 197,773	$ 133,419	$ —	$ 331,192
Expenses	79,330	—	617,629	696,959
Income (loss) from operations	118,443	133,419	(617,629)	(365,767)
Other income	—	—	172,462	172,462
Net income (loss)	$ 118,443	$ 133,419	$ (445,167)	$ (193,305)
Total Assets	$ 9,378,607	$ 11,443,769	$ 84,836,195	$ 105,658,571

9. Line of Credit

On February 28, 2005 the Company entered into a line of credit agreement with a syndicate of banks led by Branch Banking & Trust Company, which provides the Company with up to $50 million of financing. The line of credit matures on February 28, 2008. The Company has the option of increasing the line of credit up to an additional $25 million, for a total of $75 million, upon agreement of the syndicate of banks. The interest rate charged on the advances under the facility is based on LIBOR, the Prime Rate or the Federal Funds Rate, depending on market conditions, and adjusts periodically. The unused portion of the line of credit is subject to a fee of 0.25% per year. The Company's ability to access this funding source is subject to the Company continuing to meet customary lending requirements such as compliance with financial and operating covenants and meeting certain lending limits. For example, as is customary with such line of credit facilities, the maximum amount the Company may draw under this agreement is based on the percentage of the value of its properties meeting agreed-upon eligibility standards that the Company has pledged as collateral to the banks. As the Company arranges for long-term mortgages for these properties, the banks will release the properties from the line of credit and reduce the availability under the line of credit by the advanced amount of the removed property. Conversely, as the Company purchases new properties meeting the eligibility standards, the Company may pledge these new properties to obtain additional advances under this agreement. As of May 4, 2005, the Company may draw up to $38.2 million under this agreement. As of March 31, 2005, there were no borrowings under the line of credit.

10. Mortgage Note Payable

On March 16, 2005 the Company borrowed $3,150,000 pursuant to a long-term note payable from Key Bank National Association, which is collateralized by a security interest in its Canton, North Carolina property. The note accrues interest at an initial interest rate of 6.33% per year until the anticipated repayment date of April 1, 2010. Monthly payments on the note are based upon a twenty-five year term, with both principal and interest being paid each month. If the note is not repaid before the anticipated repayment date, interest will accrue on the remaining outstanding principal balance from and after the anticipated repayment date at the greater of the initial interest rate plus 2%, or the treasury rate for the week ending prior to the anticipated repayment date plus 2%. The Company may repay this note at any time after June 23, 2009 and not be subject to a prepayment penalty. The note matures on April 1, 2030, however the Company expects to repay the note in full prior to the anticipated repayment date. The Company intends to use the proceeds from the note to acquire additional investments for its portfolio.

11. Subsequent Events

On April 15, 2005, the Company acquired a 120,000 square foot industrial building in Big Flats, New York for $7.1 million, including transaction costs, and the purchase was funded using a portion of the net proceeds from the Company's initial public offering. Upon acquisition of the property, the Company was assigned the previously existing triple net lease with the sole tenant, which had a remaining term of approximately eight years at the time of assignment. The lease provides for annual rents of approximately $616,000 through 2006, with prescribed escalations thereafter.

On April 15, 2005, the Company extended a mortgage loan in the amount of $10.0 million on an office building in McLean, Virginia, where the Company's Adviser is a subtenant in the building. The loan was funded using a portion of the net proceeds from the Company's initial public offering. This 12 year mortgage loan, collateralized by the McLean property, accrues interest at the greater of 7.5% per year or the one month LIBOR rate plus six percent per year, with a ceiling of 10.0%.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following analysis of our financial condition and results of operations should be read in conjunction with our financial statements and the notes thereto contained elsewhere in this Form 10-Q.

Forward-Looking Statements

Some of the statements in this Quarterly Report onForm 10-Q constitute forward-looking statements under Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, including statements made with respect to possible or assumed future results of our business, financial condition, liquidity, results of operations, plans and objectives. When we use the words "believe," "expect," "anticipate," "estimate" or similar expressions, we intend to identify forward-looking statements. You should not place undue reliance on these forward-looking statements. Statements regarding the following subjects are forward-looking by their nature:

- *our business strategy;*
- *pending transactions;*
- *our projected operating results;*
- *our ability to obtain future financing arrangements;*
- *estimates relating to our future distributions;*
- *our understanding of our competition;*
- *market trends;*
- *projected capital expenditures; and*
- *use of the proceeds of our initial public offering and credit facilities.*

These statements involve known and unknown risks, uncertainties and other factors that may cause results, levels of activity, growth, performance, tax consequences or achievements to be materially different from any future results, levels of activity, growth, performance, tax consequences or achievements expressed or implied by such forward-looking statements.

The forward-looking statements are based on our beliefs, assumptions and expectations of our future performance, taking into account all information currently available to us. Although we believe that these beliefs, assumptions and expectations are reasonable, we cannot guarantee future results, levels of activity, performance, growth or achievements. These beliefs, assumptions and expectations can change as a result of many possible events or factors, not all of which are known to us. If a change occurs, our business, financial condition, liquidity and results of operations may vary materially from those expressed in or implied by our forward-looking statements. You should carefully consider these risks before you make an investment decision with respect to our common stock, along with the following factors that could cause actual results to vary from our forward-looking statements:

- *the loss of any of our key employees, such as Mr. David Gladstone, our chairman and chief executive officer, Mr. Terry Lee Brubaker, our president and chief operating officer, or Mr. George Stelljes III, our executive vice president and chief investment officer;*
- *general volatility of the capital markets and the market price of our common stock;*
- *risks associated with negotiation and consummation of pending and future transactions;*
- *changes in our business strategy;*
- *availability, terms and deployment of capital, including the ability to maintain and borrow under our existing credit facility and secure one or more additional long-term credit facilities;*
- *availability of qualified personnel;*
- *changes in our industry, interest rates or the general economy; and*
- *the degree and nature of our competition.*

We are under no duty to update any of the forward-looking statements after the date of this report to conform such statements to actual results.

Overview

We were incorporated under the General Corporation Law of the State of Maryland on February 14, 2003 primarily for the purpose of investing in and owning net leased industrial and commercial rental property and selectively making long-term mortgage loans collateralized by industrial and commercial property. We expect that a large portion of our tenants and borrowers will be small and medium-sized businesses that have significant buyout fund ownership and will be well capitalized, with equity constituting between 20% and 40% of their permanent capital. We expect that other tenants and borrowers will be family-owned businesses that have built significant equity from paying down the mortgage loans securing their real estate or through the appreciation in the value of their real estate. We seek to enter into purchase agreements for real estate that have triple net leases with terms of approximately 15 years, with rent increases built into the leases. Under a triple net lease, the tenant is required to pay all operating, maintenance and insurance costs and real estate taxes with respect to the leased property. At March 31, 2005, we owned fourteen properties and had one mortgage loan. We have also acquired one property and extended one mortgage loan subsequent to March 31, 2005. We are actively communicating with buyout funds, real estate brokers and other third parties to locate properties for potential acquisition or mortgage financing in an effort to build our portfolio.

We conduct substantially all of our activities through, and all of our properties are held directly or indirectly by, Gladstone Commercial Limited Partnership, a Delaware limited partnership formed on May 28, 2003, which we refer to as our "Operating Partnership." We control our Operating Partnership through our wholly owned subsidiary Gladstone Commercial Partners, LLC, which serves as the Operating Partnership's sole general partner, and we also own all limited partnership units of our Operating Partnership. We expect our Operating Partnership to issue limited partnership units from time to time in exchange for industrial and commercial real property. By structuring our acquisitions in this manner, the sellers of the real estate will generally be able to defer the realization of gains until they redeem the limited partnership units. Limited partners who hold limited partnership units in our Operating Partnership will be entitled to redeem these units for cash or, at our election, shares of our common stock on a one-for-one basis at any time. Whenever we issue common stock for cash, we will be obligated to contribute any net proceeds we receive from the sale of the stock to our Operating Partnership and our Operating Partnership will, in turn, be obligated to issue an equivalent number of limited partnership units to us. Our Operating Partnership will distribute the income it generates from its operations to Gladstone Commercial Partners, LLC and its limited partners, including us, on a pro rata basis. We will, in turn, distribute the amounts we receive from our Operating Partnership to our stockholders in the form of monthly cash distributions. We have historically operated, and intend to continue to operate, so as to qualify as a REIT for federal tax purposes, thereby generally avoiding federal and state income taxes on the distributions we make to our stockholders.

Gladstone Management Corporation, a registered investment adviser and an affiliate of ours, serves as our external adviser (our "Adviser"). Our Adviser is responsible for managing our business on a day-to-day basis and for identifying and making acquisitions and dispositions that it believes meet our investment criteria.

Recent Events

On February 10, 2005, we acquired a 60,245 square foot flexible office building in San Antonio, Texas for $9.0 million, including transaction costs. Upon acquisition of the property, we were assigned the previously existing triple net lease with the sole tenant, which had a remaining term of approximately nine years at the time of assignment. The lease provides for annual rents of approximately $753,000 through 2008, with prescribed escalations thereafter.

On February 10, 2005, we acquired a 39,000 square foot industrial building in Columbus, Ohio for $3.4 million, including transaction costs. Upon acquisition of the property, we were assigned the previously existing triple net lease with the sole tenant, which had a remaining term of approximately ten years at the time of assignment. The lease provides for annual rents of approximately $318,000 through 2006, with prescribed escalations thereafter.

On March 16, 2005 we borrowed $3,150,000 pursuant to a long-term note payable from Key Bank National Association, which is collateralized by a security interest in our Canton, North Carolina property. The note accrues interest at an initial interest rate of 6.33% per year until the anticipated repayment date of April 1, 2010. Monthly payments on the note are based upon a twenty-five year term, with both principal and interest being paid each month. If the note is not repaid before the anticipated repayment date, interest will accrue on the remaining outstanding principal balance from and after the anticipated repayment date at the greater of the initial interest rate plus 2%, or the treasury rate for the week ending prior to the anticipated repayment date plus 2%. We may repay this note at any time after June 23, 2009 and not be subject to a prepayment penalty. The note matures on April 1, 2030, however we expect to repay the note in full prior to the anticipated repayment date. We intend to use the proceeds from the note to acquire additional investments for our portfolio.

On April 15, 2005, we acquired a 120,000 square foot industrial building in Big Flats, New York for $7.1 million, including transaction costs, and the purchase was funded using a portion of the net proceeds from our initial public offering. Upon acquisition of the property, we were assigned the previously existing triple net lease with the sole tenant, which had a remaining term of approximately eight years at the time of assignment. The lease provides for annual rents of approximately $616,000 through 2006, with prescribed escalations thereafter.

On April 15, 2005, we extended a mortgage loan in the amount of $10.0 million on an office building in McLean, Virginia, where our Adviser is a subtenant in the building. The loan was funded using a portion of the net proceeds from our initial public offering. This 12 year mortgage loan, collateralized by the McLean property, accrues interest at the greater of 7.5% per year or the one month LIBOR rate plus six percent per year, with a ceiling of 10.0%.

Expenses

Prior to October 1, 2004, our Adviser had an expense sharing arrangement with Gladstone Capital Advisers, a wholly-owned subsidiary of our affiliate, Gladstone Capital Corporation, through which our entire workforce was employed. Under that relationship, our Adviser reimbursed Gladstone Capital Advisers for a portion of Gladstone Capital Advisers' total payroll and benefits expenses (based on the percentage of total hours worked by Gladstone Capital Advisers' employees on our matters on an employee-by-employee basis) and a portion of Gladstone Capital Advisers' total overhead expense (based on the percentage of total hours worked by all Gladstone Capital Advisers' employees on our matters). In turn, subject to the terms and conditions of our advisory agreement, our Adviser passed these charges on to us. Effective October 1, 2004, the expense sharing arrangement with Gladstone Capital Advisers was terminated, and all of our personnel are now directly employed by our Adviser. Pursuant to the terms of our advisory agreement, we continue to be responsible for a portion of our Adviser's total payroll and benefits expenses (based on the percentage of time our Adviser's employees devote to our matters on an employee-by-employee basis) and a portion of our Adviser's total overhead expense (based on the percentage of time worked by all of our Adviser's employees on our matters). The termination of the arrangement between our Adviser and Gladstone Capital Advisers is not expected to materially change the level of our expenses.

During the three months ended March 31, 2005 and 2004, payroll and benefits expenses, which are part of the management fee paid to our Adviser, were approximately $347,000 and $165,000, respectively. The actual amount of payroll and benefits expenses which we will be required to reimburse our Adviser in the future is not determinable, but we currently estimate that during the year ending December 31, 2005 this amount will be approximately $1,500,000. This estimate is based on our current expectations regarding our Adviser's payroll and benefits expenses and the proportion of our Adviser's time we believe will be spent on matters relating to our business. To the extent that our Adviser's payroll and benefits expenses are greater than we expect or our Adviser allocates a greater percentage of its time to our business, our actual reimbursement of our Adviser for our share of its payroll and benefits expenses could be materially greater than we currently project.

Under the terms of our advisory agreement, we will only be required to reimburse our Adviser for our portion of its general overhead expenses if the amount of payroll and benefits we reimburse to our Adviser is less than 2.0% of our average invested assets for the year. Additionally, we will only be required to reimburse our Adviser for overhead expenses up to the point that reimbursed overhead expenses and payroll and benefits expenses, on a combined basis, equal 2.0% of our average invested assets for the year. However, to the extent that payroll and benefits reimbursements exceed the annual management fee cap of 2.0%, these payroll amounts will be reimbursed by us. Our Adviser will bill us on a monthly basis for these amounts. Our Adviser must reimburse us annually for the amount by which amounts billed to and paid by us exceed this 2.0% limit during a given year. To the extent that overhead expenses payable or reimbursable by us exceed this limit and our independent directors determine that the excess expenses were justified based on unusual and nonrecurring factors which they deem sufficient, we may reimburse our Adviser in future years for the full amount of the excess expenses, or any portion thereof, but only to the extent that the reimbursement would not cause our overhead expense reimbursements to exceed the 2.0% limitation in any year. To date, the advisory fee has not exceeded the annual cap.

During the three months ended March 31, 2005 and 2004, the amount of overhead expenses that we reimbursed our Adviser was approximately $125,000 and $64,000, respectively. The actual amount of overhead expenses for which we will be required to reimburse our Adviser in the future is not determinable, but we currently estimate that during the year ending December 31, 2005 this amount will be approximately $500,000.

Under the terms of the advisory agreement, we are responsible for all expenses incurred for our direct benefit. Examples of these expenses include, legal, accounting, tax preparation, directors and officers insurance, consulting and related fees. During the three months ended March 31, 2005 and 2004, the total amount of these expenses that we incurred was approximately $699,000 and $388,000, respectively.

In addition, we are also responsible for all fees charged by third parties that are directly related to our business, which may include real estate brokerage fees, mortgage placement fees, lease-up fees and transaction structuring fees (although we may be able to pass some or all of such fees on to our tenants and borrowers). During the three months ended March 31, 2005 and 2004, we passed all such fees along to our tenants, and accordingly we did not incur any such fees during this time. The actual amount of such fees that we incur in the future will depend largely upon the aggregate costs of the properties we acquire, the aggregate amount of mortgage loans we make, and the extent to which we are able to shift the burden of such fees to our tenants and borrowers. Accordingly, the amount of these fees that we will pay in the future is not determinable at this time.

Critical Accounting Policies

Management believes our most critical accounting policies are revenue recognition (including straight-line rent), purchase price allocation, determining the risk rating of our potential tenants, accounting for our investments in real estate, provision for loans losses, the accounting for our derivative and hedging activities, if any, income taxes and stock based compensation. Each of these items involves estimates that require management to make judgments that are subjective in nature. Management relies on its experience, collects historical data and current market data, and analyzes these assumptions in order to arrive at what it believes to be reasonable estimates. Under different conditions or assumptions, materially different amounts could be reported related to the accounting policies described below. In addition, application of these accounting policies involves the exercise of judgments on the use of assumptions as to future uncertainties and, as a result, actual results could materially differ from these estimates.

Revenue Recognition

Rental revenues include rents that each tenant pays in accordance with the terms of its respective lease reported on a straight-line basis over the initial term of the lease. Because certain of our leases contain

rental increases at specified intervals, straight-line basis accounting requires us to record as an asset, and include in revenues, deferred rent receivable that we will only receive if the tenant makes all rent payments required through the expiration of the initial term of the lease. Deferred rent receivable in the accompanying balance sheets represents the cumulative difference between rental revenue as recorded on a straight-line basis and rents received from the tenants in accordance with the lease terms. Accordingly, our management must determine, in its judgment, to what extent the deferred rent receivable applicable to each specific tenant is collectible. We review deferred rent receivable on a quarterly basis and take into consideration the tenant's payment history, the financial condition of the tenant, business conditions in the industry in which the tenant operates and economic conditions in the area in which the property is located. In the event that the collectability of deferred rent with respect to any given tenant is in doubt, we would record an increase in our allowance for uncollectible accounts or record a direct write-off of the specific rent receivable, which would have an adverse effect on our net income for the year in which the reserve is increased or the direct write-off is recorded and would decrease our total assets and stockholders' equity.

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

Purchase Price Allocation

We record above-market and below-market in-place lease values for owned properties based on the present value (using an interest rate which reflects the risks associated with the leases acquired) of the difference between (i) the contractual amounts to be paid pursuant to the in-place leases and (ii) management's estimate of fair market lease rates for the corresponding in-place leases, measured over a period equal to the remaining non-cancelable term of the lease. We amortize the capitalized above-market lease values as a reduction of rental income over the remaining non-cancelable terms of the respective leases. We amortize the capitalized below-market lease values (presented in the accompanying balance sheet as value of assumed lease obligations) as an increase to rental income over the initial term and any fixed-rate renewal periods in the respective leases. Since our strategy to a large degree involves sale-leaseback transactions with newly originated leases at market rates, the above-market and below-market in-place lease values are generally not significant.

In accordance with Statement of Financial Accounting Standards ("SFAS") No. 141 "Business Combinations," the total amount of other intangible assets acquired are further allocated to in-place lease values and customer relationship intangible values based on management's evaluation of the specific characteristics of each tenant's lease and our overall relationship with that respective tenant. Characteristics to be considered by management in allocating these values include the nature and extent of our existing business relationships with the tenant, growth prospects for developing new business with the tenant, the tenant's credit quality and expectations of lease renewals (including those existing under the terms of the lease agreement), among other factors.

Management's estimates of value are made using methods similar to those used by independent appraisers (e.g., discounted cash flow analysis). Factors considered by management in its analysis include an estimate of carrying costs during hypothetical expected lease-up periods considering current market conditions, and costs to execute similar leases. We also consider information obtained about each property as a result of our pre-acquisition due diligence, marketing and leasing activities in estimating the fair value of the tangible and intangible assets acquired. In estimating carrying costs, management also includes real estate taxes, insurance and other operating expenses and estimates of lost rentals at market rates during the

expected lease-up periods, which primarily range from six to eighteen months, depending on specific local market conditions. Management also estimates costs to execute similar leases including leasing commissions, legal and other related expenses to the extent that such costs are not already incurred in connection with a new lease origination as part of the transaction.

We amortize the value of in-place leases to expense over the initial term of the respective leases, which generally range from five to twenty years. The value of customer relationship intangibles are amortized to expense over the initial term and any renewal periods in the respective leases, but in no event will the amortization period for intangible assets exceed the remaining depreciable life of the building. Should a tenant terminate its lease, the unamortized portion of the in-place lease value and customer relationship intangibles would be charged to expense.

Risk Rating

In evaluating each transaction that it considers for investment, our Adviser seeks to assess the risk associated with the potential tenant or borrower. For companies that have debt that has been rated by a national credit ratings agency, our Adviser uses the rating as determined by such ratings agency. For companies that do not have publicly rated debt, our Adviser calculates and assigns to our borrowers and tenants a risk rating under our ten-point risk rating scale. Our risk rating system is designed to assess qualitative and quantitative risks associated with our prospective tenants and borrowers. We have developed our risk rating system to approximate the risk rating systems of major credit ratings agencies. While we seek to mirror the systems of these credit ratings agencies, we cannot assure you that our risk rating system provides the same risk rating for a particular tenant or borrower as a credit ratings agency would. The following chart is an estimate of the relationship of our risk rating system to the designations used by two credit ratings agencies to rate the risk of public debt securities of major companies. Because we have established our system to rate the risk associated with mortgage loans and real estate leases to private companies that are unrated by any credit ratings agency, we cannot assure you that the correlation between our system and the credit ratings set out below is accurate.

Our System	First Ratings Agency	Second Ratings Agency	Description (a)
>10	Baa2	BBB	Probability of default during the next ten years is 4% and the expected loss is 1% or less
10	Baa3	BBB-	Probability of default during the next ten years is 5% and the expected loss is 1% to 2%
9	Ba1	BB+	Probability of default during the next ten years is 10% and the expected loss is 2% to 3%
8	Ba2	BB	Probability of default during the next ten years is 16% and the expected loss is 3% to 4%
7	Ba3	BB-	Probability of default during the next ten years is 17.8% and the expected loss is 4% to 5%
6	B1	B+	Probability of default during the next ten years is 22% and the expected loss is 5% to 6.5%
5	B2	B	Probability of default during the next ten years is 25% and the expected loss is 6.5% to 8%

Our System	First Ratings Agency	Second Ratings Agency	Description (a)
4	B3	B-	Probability of default during the next ten years is 27% and the expected loss is 8% to 10%
3	Caa1	CCC+	Probability of default during the next ten years is 30% and the expected loss is 10% to 13.3%
2	Caa2	CCC	Probability of default during the next ten years is 35% and the expected loss is 13.3% to 16.7%
1	Caa3	CC	Probability of default during the next ten years is 65% and the expected loss is 16.7% to 20%
0	N/a	D	Probability of default during the next ten years is 85%, or there is a payment default, and the expected loss is greater than 20%

(a) the default rates set forth above assume a ten year lease or mortgage loan. If the particular investment has a term other than ten years, the probability of default is adjusted to reflect the reduced risk associated with a shorter term or the increased risk associated with a longer term.

As stated above, we generally anticipate entering into transactions with tenants or borrowers that have a risk rating of at least 4 based on the above scale or, for tenants or borrowers whose debt rating is at least B3 or B-. Once we have entered into a transaction, we periodically re-evaluate the risk rating, or debt rating as applicable, of the investment for purposes of determining whether we should increase our reserves for loan losses or allowance for uncollectible rent. To date there have been no allowances for uncollectible rent or reserves for loan losses. Our board of directors may alter our risk rating system from time to time.

The following table reflects the average risk rating of our tenants and borrowers:

Rating	3/31/2005	12/31/2004
Average	8.1	7.8
Weighted Average	8.0	7.6
Highest	10.0	10.0
Lowest	6.0	6.0

Investments in Real Estate

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

We are required to make subjective assessments as to the useful lives of our properties for purposes of determining the amount of depreciation to record on an annual basis with respect to our investments in real estate. These assessments have a direct impact on our net income because, if we were to shorten the expected useful lives of our investments in real estate, we would depreciate these investments over fewer years, resulting in more depreciation expense and lower net income on an annual basis.

We have adopted SFAS No. 144, “Accounting for the Impairment or Disposal of Long-Lived Assets,” which establishes a single accounting model for the impairment or disposal of long-lived assets including discontinued operations. SFAS No. 144 requires that the operations related to properties that have been sold or that we intend to sell be presented as discontinued operations in the statement of operations for all periods presented, and properties we intend to sell be designated as “held for sale” on our balance sheet.

When circumstances such as adverse market conditions indicate a possible impairment of the value of a property, we review the recoverability of the property's carrying value. The review of recoverability is based on our estimate of the future undiscounted cash flows, excluding interest charges, expected to result from the property's use and eventual disposition. Our forecast of these cash flows considers factors such as expected future operating income, market and other applicable trends and residual value, as well as the effects of leasing demand, competition and other factors. If impairment exists due to the inability to recover the carrying value of a property, an impairment loss is recorded to the extent that the carrying value exceeds the estimated fair value of the property. We are required to make subjective assessments as to whether there are impairments in the values of our investments in real estate.

Provision for Loan Losses

Our accounting policies require that we reflect in our financial statements an allowance for estimated credit losses with respect to mortgage loans we have made based upon our evaluation of known and inherent risks associated with our private lending assets. We have extended one mortgage loan and have not experienced any actual losses in connection with our lending investments. Management reflects provisions for loan losses on a portfolio basis based upon our assessment of general market conditions, our internal risk management policies and credit risk rating system, industry loss experience, our assessment of the likelihood of delinquencies or defaults, and the value of the collateral underlying our investments. Actual losses, if any, could ultimately differ from these estimates.

Accounting for Derivative Financial Investments and Hedging Activities

We will account for our derivative and hedging activities, if any, using SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended by SFAS No. 137, "Accounting for Derivative Instruments and Hedging Activities-Deferral of the Effective Date of FASB Statement No. 133, an amendment of FASB Statement No. 133" and SFAS No. 149 "Amendment of Statement 133 on Derivative Instruments and Hedging Activities," which requires all derivative instruments to be carried at fair value on the balance sheet.

Derivative instruments designated in a hedge relationship to mitigate exposure to variability in expected future cash flows, or other types of forecasted transactions, will be considered cash flow hedges. We will formally document all relationships between hedging instruments and hedged items, as well as our risk-management objective and strategy for undertaking each hedge transaction. We will periodically review the effectiveness of each hedging transaction, which involves estimating future cash flows. Cash flow hedges will be accounted for by recording the fair value of the derivative instrument on the balance sheet as either an asset or liability, with a corresponding amount recorded in other comprehensive income within stockholders' equity. Amounts will be reclassified from other comprehensive income to the income statement in the period or periods the hedged forecasted transaction affects earnings. Derivative instruments designated in a hedge relationship to mitigate exposure to changes in the fair value of an asset, liability, or firm commitment attributable to a particular risk, such as interest rate risk, will be considered fair value hedges under SFAS No. 133. As of March 31, 2005, we were not a party to any separate derivatives contract. Certain of our leases and loans contain embedded derivatives, principally LIBOR floors, which do not require separate accounting.

Income Taxes

Our financial results generally do not reflect provisions for current or deferred income taxes. Management believes that we have operated and will operate in a manner that will allow us to qualify as a REIT and, as a result, we do not expect to pay substantial corporate-level income taxes. Many of the requirements for REIT qualification, however, are highly technical and complex. If we were to fail to meet these requirements, we would be subject to federal income tax which could have a material adverse impact on our results of operations and amounts available for distributions to our stockholders.

Stock Based Compensation

We currently apply the intrinsic value method to account for the issuance of stock options under our 2003 Equity Incentive Plan in accordance with APB Opinion No. 25, "*Accounting for Stock Issued to Employees,*" where appropriate. In this regard, the substantial portion of these options were granted to individuals who are our officers and who qualify as leased employees under FASB Interpretation No. 44, "*Accounting for Certain Transactions involving Stock Compensation, an interpretation of APB Opinion No. 25.*" Accordingly, because the grants were at exercise prices equal to the fair value of the stock at date of grant, we did not record any expense related to the issuance of these options under the intrinsic value method. We will adopt SFAS No. 123(R), "Share-Based Payment" effective January 1, 2006, which will require us to begin expensing stock options as compensation cost. Dependent upon the method chosen by our management for implementation of SFAS No. 123(R), prior periods may need to be adjusted.

Results of Operations

Comparison of the three months ended March 31, 2005 to the three months ended March 31, 2004

Revenues

For the three months ended March 31, 2005, we earned $1,847,007 of rental revenue as compared to $197,773 for the three months ended March 31, 2004. The increase of $1,649,234, or 834%, in rental revenue is primarily a result of the acquisition of twelve properties subsequent to March 31, 2004.

Interest income from the mortgage loan increased to $295,583 for the three months ended March 31, 2005 as compared to $133,149 for the three months ended March 31, 2004. The increase of $162,434, or 122%, is due to the fact that the mortgage loan was originated during the first quarter of 2004, and interest was only earned for a portion of the first quarter of 2004.

For the three months ended March 31, 2005, we earned $2,043 of tenant recovery revenue. Tenant recovery revenue results from franchise taxes we paid that will be recovered for the 2005 tax year from the tenant of our Canton, North Carolina property.

Expenses

The management advisory fee for the three months ended March 31, 2005 increased to $471,861, as compared to $229,416 for the three months ended March 31, 2004. The increase of $242,445, or 106%, is primarily a result of the increased time that our Adviser's employees spent on our company matters. The management advisory fee consists of the reimbursement of expenses, including direct allocation of employee salaries and benefits, as well as general overhead expense, to our Adviser in accordance with the terms of the advisory agreement.

Depreciation and amortization expenses of $537,755 were recorded for the three months ended March 31, 2005, as compared to $79,330 for the three months ended March 31, 2004. The increase of $458,425, or 578%, is primarily a result of the increased number of acquisitions since March 31, 2004.

Professional fees, consisting primarily of legal and accounting fees, were $331,244 for the three months ended March 31, 2005, as compared to $208,457 for the three months ended March 31, 2004. The increase of $122,787, or 59%, was primarily a result of the increased accounting fees related to the audit of our internal controls performed in order to comply with the The Sarbanes –Oxley Act of 2002.

Taxes and licenses for the three months ended March 31, 2005 were $128,273, an increase of $117,953, or 1143%, from $10,320 for the three months ended March 31, 2004. This increase is primarily attributable to the payment of $119,853 of franchise taxes paid for doing business in certain states. Approximately $100,000 of these franchise taxes relate to taxes incurred in 2004, however management has determined that these expenses were immaterial to the 2004 earnings, and were expensed in the quarter ending March 31, 2005. We expect to reduce future incurrance of these types of taxes next year by restructuring our entities in these specific states, however we can not assure that this restructuring will reduce the taxes in all states.

Insurance expense increased to $70,383 for the three months ended March 31, 2005, as compared to $64,487 for the three months March 31, 2004. The increase of $5,896, or 9%, is a result of an increase in insurance premiums year over year.

Interest expense was $36,219 for the three months ended March 31, 2005. This amount consisted of $11,111 in unused line of credit fees accrued on the line of credit obtained in February of 2005, $8,862 of interest expense on the mortgage note payable issued in March of 2005, and $16,246 of deferred financing fees from the line of credit. There was no interest expense incurred for the three months ended March 31, 2004.

General and administrative expenses were $132,828 for the three months ended March 31, 2005, as compared to $104,949 and consisted mainly of directors' fees and stockholder-related expenses. The increase of $27,879, or 27%, was primarily a result of an increase in stockholder-related expenses, and other general expenses that have increased as the number of properties has increased year over year.

Because we have only recently begun our operations, we do not believe that our current level of operating expenses relative to revenues is indicative of our operating expenses in the future. As we continue to expand our real estate investments, we expect our revenues and operating expenses to increase and that ultimately our annual management advisory fee will be approximately 2% of our invested assets.

Interest Income

Interest income on cash and cash equivalents decreased during the three months ended March 31, 2005 to $94,521, as compared to $172,462 for the three months ended March 31, 2004. The decrease of $77,491, or 45%, is primarily a result of the increase in our portfolio of investments in real estate and mortgage loans, resulting in lower average cash balances invested. This interest represents the interest earned on the investment of the net proceeds from our initial public offering in short-term investment grade securities, primarily U.S. Treasury Bills.

During the three months ended March 31, 2005, we earned interest income on employee loans of $4,685. This interest represents the interest earned on a loan extended to an employee in September of 2004 in connection with the exercise of stock options.

Net Income

For the three months ended March 31, 2005, we recorded net income of $535,184, as compared to a net loss of $193,305 for the three months ended March 31, 2004. This increase of $728,489, or 377%, is primarily a result in the increase in our portfolio of investments in the past year and the other events described above. Based on the basic and diluted weighted average common shares outstanding of 7,667,000 and 7,733,335, respectively, for the three months ended March 31, 2005, the basic and diluted earnings per weighted average common share were both $0.07. Based on the basic and diluted weighted average common shares outstanding of 7,642,000, for the three months ended March 31, 2004, the basic and diluted loss per weighted average common share were both $0.03.

Liquidity and Capital Resources

Cash and Cash Equivalents

At March 31, 2005, we had approximately $18.1 million in cash and cash equivalents available to make investments and fund our continuing operations, a decrease of $11.1 million from $29.2 million at December 31, 2004. The funds on hand were predominantly raised though our initial public offering in 2003.

Operating Activities

Net cash provided by operating activities during the three months ended March 31, 2005 was approximately $1.3 million, consisting primarily of net income, decreases in other assets, increases in rent received in advance and security deposits, increases in amounts due our Adviser and an increase in accrued expenses and accounts payable, partially offset by increases in mortgage interest receivable, increases in deferred rent receivable and prepaid expenses.

Net cash provided by operating activities during three months ended March 31, 2004 was $495,502, consisting primarily of an increase in the amount due to Adviser, increases in rent received in advance and security deposits and an increase in accrued expenses and other liabilities.

Investing Activities

Net cash used in investing activities during the three months ended March 31, 2005 was $12.7 million, which consisted of our purchases of the San Antonio, Texas flexible office property, and the Columbus, Ohio industrial building, both purchased in February of 2005, and deposits placed on future acquisitions, partially offset by principal repayments from our mortgage note receivable.

Net cash used in investing activities during the three months ended March 31, 2004 was $14.8 million, and consisted of our purchase of the Canton, Ohio commercial office and warehouse property in January 2004 and our extension of a mortgage loan of approximately $11.2 million in February 2004.

Financing Activities

Net cash provided by financing activities for the three months ended March 31, 2005 was approximately $220,000. This amount consisted of the proceeds received from the long-term financing of our Canton, North Carolina property of $3.1 million, partially offset by the dividend payments to our stockholders of $2.3 million and approximately $630,000 of financing costs paid in connection with our line of credit and mortgage note payable.

Net cash used in financing activities was $84,150 for the three months ended March 31, 2004. These amounts consisted of the dividend payments to our stockholders of $76,420 and of $7,730 in costs associated with our initial public offering.

Future Capital Needs

We had a purchase commitment for one property at March 31, 2005 in the aggregate amount of $13.4 million, where a deposit had been placed on the real estate as of March 31, 2005. Subsequent to March 31, 2005, we made two investments in the aggregate amount of $17.1 million.

As of May 4, 2005, we have invested approximately $105.4 million, or substantially all of the net proceeds from our initial public offering in real properties and mortgage loans. Investments in fifteen real properties account for approximately $84.2 million of the currently invested net proceeds, and investments in two mortgage loans account for approximately $21.2 million of the currently invested net proceeds. During the remainder of 2005 and beyond, we expect to complete additional acquisitions of real estate and to extend additional mortgage notes. The net proceeds of our initial public offering have been fully invested, and we intend to acquire additional properties by borrowing all or a portion of the purchase price and collateralizing the loan with mortgages secured by some or all of our real property, or by borrowing against our existing line of credit. If we are unable to make any required debt payments on any borrowings we make in the future, our lenders could foreclose on the properties collateralizing their loans, which could cause us to lose part or all of our investments in such properties. We also may issue additional equity securities in the future to finance future investment although there can be no assurance that we would be able to do so on favorable terms if at all.

Line of Credit

On February 28, 2005 we entered into a line of credit agreement with a syndicate of banks led by Branch Banking & Trust Company, which provides us with up to $50 million of financing. The line of credit matures on February 28, 2008. We have the option of increasing the line of credit up to an additional $25 million, for a total of $75 million, upon agreement of the syndicate of banks. The interest rate charged on the advances under the facility is based on LIBOR, the prime rate or the federal funds rate, depending on market conditions, and adjusts periodically. The unused portion of the line of credit is subject to a fee of 0.25% per year. Our ability to access this funding source is subject to our continuing to meet customary lending requirements such as compliance with financial and operating covenants and meeting certain lending limits. For example, as is customary with such line of credit facilities, the maximum amount we may draw under this agreement is based on the percentage of the value of our properties meeting agreed-upon eligibility standards that we have pledged as collateral to the banks. As we arrange for long-term mortgages for these properties, the banks will release the properties from the line of credit and reduce the availability under the line of credit by the advanced amount of the removed property. Conversely, as we purchase new properties meeting the eligibility standards, we may pledge these new properties to obtain additional advances under this agreement . As of May 4, 2005, we may draw up to $38.2 million under this agreement. As of May 4, 2005 we had no borrowings outstanding under the line of credit.

Mortgage Note Payable

On March 16, 2005 we borrowed $3,150,000 pursuant to a long-term note payable from Key Bank National Association, which is collateralized by a security interest in our Canton, North Carolina property. The note accrues interest at an initial interest rate of 6.33% per year until the anticipated repayment date of April 1, 2010. Monthly payments on the note are based upon a twenty-five year term, with both principal and interest being paid each month. If the note is not repaid before the anticipated repayment date, interest will accrue on the remaining outstanding principal balance from and after the anticipated repayment date at the greater of the initial interest rate plus 2%, or the treasury rate for the week ending prior to the anticipated repayment date plus 2%. We may repay this note at any time after June 23, 2009 and not be subject to a prepayment penalty. The note matures on April 1, 2030, however we expect to repay the note in full prior to the anticipated repayment date. We intend to use the proceeds from the note to acquire additional investments for our portfolio.

Contractual Obligations

The following table reflects our significant contractual obligations as of March 31, 2005:

		Payments Due by Period			
Contractual Obligations	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Long-Term Debt Obligations	3,150,000	47,000	110,000	126,000	2,867,000
Capital Lease Obligations	—	—	—	—	—
Operating Lease Obligations (1)	—	—	—	—	—
Purchase Obligations (2)	13,400,000	13,400,000	—	—	—
Other Long-Term Liabilities Reflected on the Registrant's Balance Sheet under GAAP	—	—	—	—	—
Total	$ 16,550,000	$ 13,447,000	$ 110,000	$ 126,000	$ 2,867,000

(1) This does not include the portion of the operating lease on office space that is allocated to us by our adviser in connection with our advisory agreement.

(2) The purchase obligations reflected in the above table represents committiments outstanding at March 31, 2005 to purchase real estate.

Funds from Operations

The National Association of Real Estate Investment Trusts (NAREIT) developed Funds from Operations ("FFO"), as a relative non-GAAP (Generally Accepted Accounting Principles in the United States) supplemental measure of operating performance of an equity REIT in order to recognize that income-producing real estate historically has not depreciated on the basis determined under GAAP. FFO, as defined by NAREIT, is net income (loss) (computed in accordance with GAAP), excluding gains (or losses) from sales of property, plus depreciation and amortization of real estate assets, and after adjustments for unconsolidated partnerships and joint ventures.

FFO does not represent cash flows from operating activities in accordance with GAAP (which, unlike FFO, generally reflects all cash effects of transactions and other events in the determination of net income (loss)) and should not be considered an alternative to net income (loss) as an indication of our performance or to cash flow from operations as a measure of liquidity or ability to make distributions. Comparison of FFO, using the NAREIT definition, to similarly titled measures for other REITs may not necessarily be meaningful due to possible differences in the application of the NAREIT definition used by such REITs.

Diluted funds from operations per share ("Diluted FFO per share") is FFO divided by weighted average common shares outstanding on a diluted basis during a period. We believe that FFO and Diluted FFO per share are useful to investors because they provide investors with a further context for evaluating our FFO results in the same manner that investors use net income and earnings per share ("EPS") in evaluating net income available to common shareholders. In addition, since most REITs provide FFO and Diluted FFO per share information to the investment community, we believe FFO and Diluted FFO per share are useful supplemental measures for comparing us to other REITs. We believe that net income is the most directly comparable GAAP measure to FFO and that diluted EPS is the most directly comparable GAAP measure to Diluted FFO per share.

The following table provides a reconciliation of our FFO for the three months ended March 31, 2005 and 2004 to the most directly comparable GAAP measure, net income, and a computation of diluted FFO per weighed average common share and diluted net income per weighted average common share:

	For the three months ended March 31, 2005	For the three months ended March 31, 2004
Net income (loss)	$ 535,184	$ (193,305)
Real estate depreciation and amortization	537,755	79,330
Funds from operations	1,072,939	(113,975)
Weighted average shares outstanding - diluted	7,733,335	7,642,000
Diluted net income (loss) per weighted average common share	$ 0.07	$ (0.03)
Diluted funds from operations per weighted average common share	$ 0.14	$ (0.01)

Item 3. Quantitative and Qualitative Disclosure About Market Risk

Market risk includes risks that arise from changes in interest rates, foreign currency exchange rates, commodity prices, equity prices and other market changes that affect market sensitive instruments. The primary risk that we believe we will be exposed to is interest rate risk. We currently have one variable rate loan and certain of our leases contain escalations based on market interest rates. We seek to mitigate this risk by structuring such provisions to contain a minimum interest rate or escalation rate, as applicable. We are also exposed to the effects of interest rate changes as a result of the holding of our cash and cash equivalents in short-term, interest-bearing investments.

To illustrate the potential impact of changes in interest rates on our net income, we have performed the following analysis, which assumes that our balance sheet remains constant and no further actions beyond a minimum interest rate or escalation rate are taken to alter our existing interest rate sensitivity.

Under this analysis, a hypothetical increase in the one month LIBOR rate by 1% would increase our net income by approximately $22,630 or 1.0% over the next twelve months, compared to net income for the latest twelve months ended March 31, 2005. A hypothetical decrease in the one month LIBOR by 1% would have no impact on our net income over the next twelve months, due to the existing minimum interest rates in place on the loans and in our leases. Although management believes that this analysis is indicative of our existing interest rate sensitivity, it does not adjust for potential changes in credit quality, size and composition of our loan and lease portfolio on the balance sheet and other business developments that could affect net income. Accordingly, no assurances can be given that actual results would not differ materially from the results under this hypothetical analysis.

In the future, we may be exposed to additional effects of interest rate changes primarily as a result of our line of credit or long-term debt used to maintain liquidity and fund expansion of our real estate investment portfolio and operations. Our interest rate risk management objectives are to limit the impact of interest rate changes on earnings and cash flows and to lower overall borrowing costs. To achieve this objective, we will borrow primarily at fixed rates or variable rates with the lowest margins available and, in some cases, with the ability to convert variable rates to fixed rates. We may also enter into derivative financial instruments such as interest rate swaps and caps in order to mitigate the interest rate risk on a related financial instrument. We will not enter into derivative or interest rate transactions for speculative purposes.

We have purchased two properties in Canada, and the monthly rental payments on these properties are received in Canadian dollars. In order to mitigate the risk of foreign currency rate fluctuations, we are currently exploring the possibility of securing one or more loans on the real estate properties in which the mortgage payments would be denominated in Canadian dollars. Until one or more loans has been secured on the properties, we are exposed to foreign currency risk. However, exchange rate movements to date have not had a significant effect on our financial position or results of operations. For the three months ended March 31, 2005, we had a $92 foreign currency transaction loss in connection with the translation of monthly rental payments denominated in a foreign currency.

To illustrate the potential impact of changes in exchange rates on our net income, we have performed the following analysis, which assumes that our balance sheet remains constant and no further actions beyond a minimum exchange rate fluctuation are taken to alter our existing foreign currency sensitivity.

Under this analysis, a hypothetical increase or decrease in the Canadian exchange rate by 10% would increase or decrease our net income by approximately $60,453 or 2.6% over the next twelve months, compared to net income for the latest twelve months ended March 31, 2005. Although management believes that this analysis is indicative of our existing exchange rate sensitivity, no assurances can be given that actual results would not differ materially from the results under this hypothetical analysis.

In addition to changes in interest rates, the value of our real estate is subject to fluctuations based on changes in local and regional economic conditions and changes in the creditworthiness of lessees, all of which may affect our ability to refinance debt if necessary.

Item 4. Controls and Procedures

a) Evaluation of Disclosure Controls and Procedures

As of March 31, 2005, our management, including the chief executive officer and chief financial officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures. Based on that evaluation, management, including the chief executive officer and chief financial officer, concluded that the disclosure controls and procedures were effective in timely alerting management of material information about the company required to be included in our periodic Securities and Exchange Commission filings. However, while evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply judgment in evaluating the cost-benefit relationship of possible controls and procedures.

b) Changes in Internal Control over Financial Reporting

There were no changes in internal controls for the period ended March 31, 2005 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings

Neither we nor any of our subsidiaries are currently subject to any material legal proceedings, nor, to our knowledge, is any material legal proceeding threatened against us or our subsidiaries.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

As of March 31, 2005, we had invested approximately $88.3 million of the net proceeds from our initial public offering in fourteen real properties and one mortgage loan. As of March 31, 2005, we had used approximately $4.0 million in our operating activities, of which approximately $2.0 million has been paid to our Adviser (which is an affiliate of ours) in partial payment of amounts owed under our advisory agreement. As of March 31, 2005, substantially all of the remaining net proceeds from our initial public offering were invested in short-term, investment grade, interest-bearing instruments.

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. Submission of Matters to a Vote of Security Holders

Not applicable.

Item 5. Other Information

Not applicable.

Item 6. Exhibits

Exhibit Index

Exhibit	Description of Document
3.1†	Amended and Restated Articles of Incorporation, incorporated by reference to Exhibit 3.1 to the Registration Statement on Form S-11 (File No. 333-106024), filed June 11, 2003.
3.2†	Bylaws, incorporated by reference to Exhibit 3.2 to the Registration Statement on Form S-11 (File No. 333-106024), filed June 11, 2003.
10.1	Promissory Note between Key Bank National Association and CMI04 Canton NC LLC, dated March 14, 2005.
10.2	First Amendment to Credit Agreement and Waiver by and among Gladstone Commercial Corporation, Gladstone Commercial Limited Partnership, Branch Banking and Trust Company and certain other parties, dated as of April 21, 2005.
11	Computation of Per Share Increase in Stockholders' Equity from Operations (included in the notes to the unaudited financial statements contained in this report).
31.1	Certification of Chief Executive Officer pursuant to Section 302 of The Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of The Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer pursuant to Section 906 of The Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer pursuant to Section 906 of The Sarbanes-Oxley Act of 2002.

† Previously filed and incorporated by reference.

SIGNATURES

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

Gladstone Commercial Corporation

Date: May 4, 2005

By: /s/ Harry Brill

Harry Brill
Chief Financial Officer and Treasurer

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Exhibit 10.1

PROMISSORY NOTE

LOAN TERMS TABLE

Lender: KeyBank National Association, a national banking association, its successors and assigns

Loan No.: 10026291

Lender's Address: 911 Main Street, Suite #1500, Kansas City, Missouri 64105

Lender's Facsimile No.: (816) 221-8848

Borrower: CMI04 CANTON NC LLC, a Delaware limited liability company

Borrower's Address: c/o Gladstone Commercial Corporation, 1616 Anderson Road, Second Floor, McLean, Virginia, 22102

Borrower's Facsimile No.: (973) 993-1954

Borrower's Tax Identification Number: 91-2198700

Property: Real property located at 171 Great Oak Drive, Canton, North Carolina 28716, in Haywood County, North Carolina and certain personal property

Note Date: March 14, 2005

Original Principal Amount: $3,150,000.00

Maturity Date: April 1, 2030

Anticipated Repayment Date: April 1, 2010

Interest Rate: See Section 25.2

Initial Interest Payment Per Diem: $553.88

Monthly Payment: $ 20,935.63

Monthly Payment Date: May 1, 2005 and on the first day of each successive month thereafter

Financial Statement Reporting Deposit: $130.00

1. **Loan Amount and Rate.** FOR VALUE RECEIVED, Borrower promises to pay to the order of Lender, the Original Principal Amount (or so much thereof as is outstanding from time to time, which is referred to herein as the "**Outstanding Principal Balance**" or "**OPB**"), with interest on the unpaid OPB from the date of disbursement of the Loan (as hereinafter defined) evidenced by this Promissory Note ("**Note**") at the Interest Rate. Interest shall be calculated based on the daily rate which is produced assuming a three hundred sixty (360) day year multiplied by the actual number of days elapsed. The loan evidenced by this Note will sometimes hereinafter be called the "**Loan**". The above Loan Terms Table (hereinafter referred to as the "**Table**") is a part of the Note and all terms used in this Note that are defined in the Table shall have the meanings set forth therein.

2. **Principal and Interest Payments.** Payments of principal and interest shall be made as follows:

(a) An interest payment on the date of disbursement of the Loan proceeds in an amount calculated by multiplying the Initial Interest Payment Per Diem by the number of days from (and including) the date of the disbursement of the Loan proceeds through the last day of the calendar month in which the disbursement was made;

(b) A Monthly Payment on each Monthly Payment Date until the Maturity Date, each of such payments to be applied: (i) to the payment of interest computed at the Interest Rate; and (ii) the balance applied toward the reduction of the principal balance of the Loan; and

(c) If not sooner paid, the balance of the principal amount of the Loan, all unpaid interest thereon, and all other amounts owed to Lender pursuant to this Note or any other Loan Document (as hereinafter defined) or otherwise in connection with the Loan or the security for the Loan shall be due and payable on the Maturity Date.

3. **Security for Note**. This Note is secured by a first deed of trust, mortgage, or deed to secure debt (which is herein called the "**Security Instrument**") encumbering the Property. This Note, the Security Instrument, and all other documents and instruments existing now or after the date hereof that evidence, secure or otherwise relate to the Loan, including any assignments of leases and rents, other assignments, security agreements, financing statements, guaranties, indemnity agreements (including environmental indemnity agreements), letters of credit, or escrow/holdback or similar agreements or arrangements, together with all amendments, modifications, substitutions or replacements thereof, are sometimes herein collectively referred to as the "**Loan Documents**" or individually as a "**Loan Document**". All amounts that are now or in the future become due and payable under this Note, the Security Instrument, or any other Loan Document, including any Prepayment Consideration (as hereinafter defined) and all applicable expenses, costs, charges, and fees, will be referred to herein as the "**Debt**." The remedies of Lender as provided in this Note, any other Loan Document, or under applicable law shall be cumulative and concurrent, may be pursued singularly, successively, or together at the discretion of Lender, and may be exercised as often as an occasion shall occur. The failure to exercise any right or remedy shall not be construed as a waiver or release of the right or remedy respecting the same or any subsequent default.

4. **Financial Statement Reporting Deposit; Rebate of Deposit.** In order to further protect the collateral for the Loan and to secure payment thereof, in addition to and concurrently with each Monthly Payment, Borrower shall also pay to Lender a constant monthly amount equal to the Financial Statement Reporting Deposit. On the first day of the fourteenth (14th) month following the date of the initial disbursement of funds under this Note (the "**Disbursement Date**"), and on an annual basis thereafter during the term of this Note, Lender shall remit to Borrower a portion of the Financial Statement Reporting Deposit then held by Lender in an amount equal to the aggregate amount of the Financial Statement Reporting Deposit actually received by Lender during the twelve (12) month period ending upon the immediately prior annual anniversary of the Disbursement Date (the "**Annual Compliance Period**") provided that no Event of Default (as hereinafter defined), including any failure by Borrower to strictly comply with the financial reporting requirements set forth in the Security Instrument, is currently existing or has occurred in the Annual Compliance Period.

5. **Payments.** All amounts payable hereunder shall be payable in lawful money of the United States of America to Lender at Lender's Address or such other place as the holder hereof may designate in writing. Each payment made hereunder shall be made in immediately

available funds and must state the Borrower's Loan Number. If any payment of principal or interest on this Note is due on a day other than a Business Day (as hereinafter defined), such payment shall be made on the next succeeding Business Day. Any payment on this Note received after 2:00 o'clock p.m. local time at the place then designated as the place for receipt of payments hereunder shall be deemed to have been made on the next succeeding Business Day. All amounts due under this Note shall be payable without set off, counterclaim, or any other deduction whatsoever. All payments from Borrower to Lender following the occurrence of an Event of Default shall be applied in such order and manner as Lender elects in reduction of costs, expenses, charges, disbursements and fees payable by Borrower hereunder or under any other Loan Document, in reduction of interest due on unpaid principal, or in reduction of principal. Lender may, without notice to Borrower or any other person, accept one or more partial payments of any sums due or past due hereunder from time to time while an uncured Event of Default exists hereunder, after Lender accelerates the indebtedness evidenced hereby, and/or after Lender commences enforcement of its remedies under any Loan Document or applicable law, without thereby waiving any Event of Default, rescinding any acceleration, or waiving, delaying, or forbearing in the pursuit of any remedies under the Loan Documents. Lender may endorse and deposit any check or other instrument tendered in connection with such a partial payment without thereby giving effect to or being bound by any language purporting to make acceptance of such instrument an accord and satisfaction of the indebtedness evidenced hereby. As used herein, the term "Business Day" shall mean a day upon which commercial banks are not authorized or required by law to close in the city designated from time to time as the place for receipt of payments hereunder.

6. **Late Charge.** If any sum payable under this Note or any other Loan Document is not received by Lender by close of business on the fifth (5th) day after the date on which it was due, Borrower shall pay to Lender an amount (the "**Late Charge**") equal to the lesser of (a) five percent (5%) of the full amount of such sum or (b) the maximum amount permitted by applicable law in order to help defray the expenses incurred by Lender in handling and processing such delinquent payment and to compensate Lender for the loss of the use of such delinquent payment. Any such Late Charge shall be secured by the Security Instrument and other Loan Documents. The collection of any Late Charge shall be in addition to, and shall not constitute a waiver of or limitation of, a default or Event of Default hereunder or a waiver of or limitation of any other rights or remedies that Lender may be entitled to under any Loan Document or applicable law.

7. **Default Rate.** Upon the occurrence of an Event of Default (including the failure of Borrower to make full payment on the Maturity Date), Lender shall be entitled to receive and Borrower shall pay interest on the Outstanding Principal Balance at the rate of five percent (5%) per annum above the Interest Rate ("**Default Rate**") but in no event greater than the maximum rate permitted by applicable law. Interest shall accrue and be payable at the Default Rate from the occurrence of an Event of Default until all Events of Default have been fully cured. Such accrued interest shall be added to the Outstanding Principal Balance, and interest shall accrue thereon at the Default Rate until fully paid. Such accrued interest shall be secured by the Security Instrument and other Loan Documents. Borrower agrees that Lender's right to collect interest at the Default Rate is given for the purpose of compensating Lender at reasonable amounts for Lender's added costs and expenses that occur as a result of Borrower's default and that are difficult to predict in amount, such as increased general overhead, concentration of

management resources on problem loans, and increased cost of funds. Lender and Borrower agree that Lender's collection of interest at the Default Rate is not a fine or penalty, but is intended to be and shall be deemed to be reasonable compensation to Lender for increased costs and expenses that Lender will incur if there occurs an Event of Default hereunder. Collection of interest at the Default Rate shall not be construed as an agreement or privilege to extend the Maturity Date or to limit or impair any rights and remedies of Lender under any Loan Documents. If judgment is entered on this Note, interest shall continue to accrue post-judgment at the greater of (a) the Default Rate or (b) the applicable statutory judgment rate.

8. **Origination, Administration, Enforcement, and Defense Expenses** Borrower shall pay Lender, on demand, all Administration and Enforcement Expenses (as hereinafter defined) now or hereafter incurred by Lender, together with interest thereon at the Default Rate, from the date paid or incurred by Lender until such fees and expenses are paid by Borrower, whether or not an Event of Default or Default then exists. For the purpose of this Note, "**Administration and Enforcement Expenses**" shall mean all fees and expenses incurred at any time or from time to time by Lender, including legal (whether for the purpose of advice, negotiation, documentation, defense, enforcement or otherwise), accounting, financial advisory, auditing, rating agency, appraisal, valuation, title or title insurance, engineering, environmental, collection agency, or other expert or consulting or similar services, in connection with: (a) the origination of the Loan, including the negotiation and preparation of the Loan Documents and any amendments or modifications of the Loan or the Loan Documents, whether or not consummated; (b) the administration, servicing or enforcement of the Loan or the Loan Documents, including any request for interpretation or modification of the Loan Documents or any matter related to the Loan or the servicing thereof (which shall include the consideration of any requests for consents, waivers, modifications, approvals, lease reviews or similar matters and any proposed transfer of the Property or any interest therein), (c) any litigation, contest, dispute, suit, arbitration, mediation, proceeding or action (whether instituted by or against Lender, including actions brought by or on behalf of Borrower or Borrower's bankruptcy estate or any indemnitor or guarantor of the Loan or any other person) in any way relating to the Loan or the Loan Documents including in connection with any bankruptcy, reorganization, insolvency, or receivership proceeding; (d) any attempt to enforce any rights of Lender against Borrower or any other person that may be obligated to Lender by virtue of any Loan Document or otherwise whether or not litigation is commenced in pursuance of such rights; and (e) protection, enforcement against, or liquidation of the Property or any other collateral for the Loan, including any attempt to inspect, verify, preserve, restore, collect, sell, liquidate or otherwise dispose of or realize upon the Loan, the Property or any other collateral for the Loan. All Administration and Enforcement Expenses shall be additional Debt hereunder secured by the Property, and may be funded, if Lender so elects, by Lender paying the same to the appropriate persons and thus making an advance on Borrower's behalf.

9. **Prepayment; Defeasance.**

(a) **Restrictions.** Voluntary prepayment of this Note is prohibited except during the last ninety (90) days of the term when prepayment may be made in whole, but not in part, without payment of any Prepayment Consideration (as hereinafter defined), on any Monthly Payment Date. Notwithstanding anything contained in this Article 9 to the contrary, provided no Default (as hereinafter defined) or Event of Default has occurred, no Prepayment Consideration

shall be due in connection with a complete or partial prepayment resulting from: (i) the application of insurance proceeds or condemnation awards pursuant to the Security Instrument; or (ii) changes in tax or debt credit laws as may be required pursuant to the Security Instrument, but Borrower shall be required to pay all other sums due hereunder together with all interest accrued thereon. Any such partial prepayments shall reduce the Outstanding Principal Balance, but shall not reduce the amount of the Monthly Payment.

(b) **Defeasance.**

(i) Provided that as of the Release Date (as hereinafter defined) the Debt has not been accelerated, no Event of Default exists, and no event has occurred that with the passage of time, giving of notice, or modification or termination of the automatic stay of Section 362 of the United States Bankruptcy Code may become an Event of Default ("**Default**"), Borrower may cause the release of the Property from the lien of the Security Instrument and the other Loan Documents ("**Defeasance**") on any Monthly Payment Date following the date that is two (2) years and fifteen (15) days after the "startup day" within the meaning of Section 860G(a)(9) of the Internal Revenue Code of 1986, as amended (together with any successor statute and the related Treasury Department Regulations including temporary regulations, the "**Code**") of any "real estate mortgage investment conduit" within the meaning of Section 860D of the Code ("**REMIC**") that holds this Note upon Borrower's satisfaction of the following conditions:

(A) Borrower shall provide Lender not less than thirty (30) days prior written notice specifying a Monthly Payment Date (such Date, or any extended date upon which Borrower and Lender may mutually agree is referred to herein as the "**Release Date**") on which the Defeasance Collateral (as hereinafter defined) is to be delivered;

(B) On the Release Date Borrower shall pay in full all accrued and unpaid interest and all other sums due under this Note and under the other Loan Documents up to the Release Date, including all costs and expenses (including attorneys' fees) incurred by Lender or its servicers or other agent(s) or to or on behalf of any rating agencies or other third parties in connection with such release and related transactions (including the review of the proposed Defeasance Collateral and the preparation of the Defeasance Security Agreement (as hereinafter defined) and related documentation), together with a defeasance processing fee in an amount equal to one-half of one percent (0.5%) of the then Outstanding Principal Balance but in no event less than (A) $7,500 or greater than (B) $20,000; and

(C) Borrower shall deliver the following, all of which must be satisfactory to Lender, at or prior to the release of the Property and substitution of the Defeasance Collateral:

(1) Direct, non-callable and non-redeemable securities evidencing an obligation to pay principal and interest in a full and timely manner that are direct obligations of the United States of America for the payment of which its full faith and credit is pledged (the "**Defeasance Collateral**") in amounts sufficient to pay all scheduled principal and interest payments required under this Note, which securities provide for payments prior, but as close as possible, to the Business Day prior to each

successive Monthly Payment Date occurring after the Release Date, with each such payment being equal to or greater than the amount of the corresponding Monthly Payment required to be made hereunder for the balance of the term hereof plus the amount required to be paid on the Maturity Date (the "**Scheduled Defeasance Payments**"), each of which shall be duly endorsed by the holder thereof as directed by Lender or accompanied by a written instrument of transfer in form and substance satisfactory to Lender (including such instruments as may be required by the depository institution or other entity holding such securities or the issuer thereof, as the case may be, to effectuate book-entry transfers and pledges through the book-entry facilities of such institution) in order to perfect upon the delivery of the Defeasance Security Agreement (as hereinafter defined) a valid, first priority lien and security interest therein in favor of Lender in conformity with all applicable state and federal laws governing granting of such security interest;

(2) any and all agreements, certificates, opinions, documents or instruments required by Lender in connection with the Defeasance including (a) a pledge and security agreement, in form and substance satisfactory to Lender, creating a first priority security interest in favor of Lender in the Defeasance Collateral (the "**Defeasance Security Agreement**"), and (b) any and all agreements, certificates, opinions, documents, or instruments required by Lender that affect or relate in any way to the maintenance by any REMIC that holds this Note of its qualification and status for tax purposes as a REMIC;

(3) a certificate of Borrower certifying that (a) all of the requirements set forth in this Section 9(b) have been satisfied, (b) the transactions that are being carried out pursuant to this Section 9(b) (including specifically the release of the lien of the Security Instrument) are being effected to facilitate the disposition of the Property or any other customary commercial transaction and not as part of an arrangement to collateralize a REMIC offering with obligations that are not real estate mortgages, and (c) the amounts of the Defeasance Collateral comply with all the requirements of this section including the requirement that the Defeasance Collateral shall generate monthly amounts equal to or greater than the Scheduled Defeasance Payments required to be paid under this Note through the Maturity Date;

(4) an opinion of counsel for Borrower, delivered by counsel acceptable to Lender, stating, among other things but without substantive qualification, that (a) Lender has a valid, duly perfected, first priority security interest in the Defeasance Collateral and that the Defeasance Security Agreement is enforceable against Borrower in accordance with its terms, (b) neither the Defeasance nor any other transaction that occurs pursuant to the provisions of this Section 9(b) has caused or will cause the Loan (including for this purpose the Loan Documents) to cease to be a "qualified mortgage" within the meaning of Section 860G of the Code, either under the provisions of Treasury Regulation Sections 1.860G-2(a)(8) or 1.860G-2(b) (as such regulations may be amended or superseded from time to time) or under any other provision of the Code or otherwise, and (c) the tax qualification and status of any REMIC or any other entity that holds this Note will not be adversely impaired or affected as a result of the Defeasance and/or any other transaction that occurs pursuant to the provisions of this Section 9(b). The opinions set forth in clauses (b) and (c) above may, in Lender's discretion, be rendered by counsel to Lender at Borrower's sole cost and expense;

(5) a certificate and opinion delivered by an independent certified public accounting firm acceptable to Lender certifying that the amounts of the Defeasance Collateral comply with all the requirements of this Section including the requirement that the Defeasance Collateral shall generate monthly amounts equal to or greater than the Scheduled Defeasance Payments required to be paid under this Note through the Maturity Date. Upon Lender's request, such accounting firm shall also certify the change in the yield of the Loan that results from the Defeasance and any other transactions that occur pursuant to the provisions of this Section 9(b), including supporting computations which shall be made in a manner that is consistent with the provisions of Treasury Regulation Sections 1.1001-3(e)(1) and (2);

(6) Upon Lender's request, written confirmation from the rating agencies that have rated any of the securities issued by any REMIC that holds this Note to the effect that the Defeasance will not result in a downgrading, withdrawal or qualification of the respective ratings in effect immediately prior to such Defeasance for any rated securities then outstanding or a waiver from any such rating agency stating that it has declined to review the Defeasance. If required by any rating agency or Lender, a non-consolidation opinion with respect to the Defeasance Obligor (as hereinafter defined) in form and substance satisfactory to Lender and such rating agency; and

(7) Borrower shall (unless otherwise agreed to in writing by Lender), at Borrower's expense, assign all of its obligations under this Note, together with the Defeasance Collateral, to a successor entity ("**Defeasance Obligor**") designated by Lender (which may include an entity that is owned and/or controlled by Lender) that is a single purpose, bankruptcy remote entity as determined by Lender in its discretion. The Defeasance Obligor shall execute an assumption agreement pursuant to which it shall assume Borrower's obligations under this Note, the Loan Documents, and the Defeasance Security Agreement. As conditions to such assignment and assumption, Borrower shall (a) deliver to Lender an opinion of counsel delivered by counsel acceptable to Lender stating, among other things, that such assumption agreement has been duly authorized and is enforceable against Borrower and the Defeasance Obligor in accordance with its terms, that the Note, the Defeasance Security Agreement and the other Loan Documents, as so assumed, have been duly authorized and are enforceable against the Defeasance Obligor in accordance with their respective terms, and that the delivery of the Defeasance Collateral to the Defeasance Obligor does not constitute a fraudulent transfer, preferential payment, or other voidable transfer under applicable bankruptcy law and (b) pay all costs and expenses including attorneys' fees incurred by Lender or its servicer or other agent(s) in connection with such assignment and assumption (including the review of the proposed transferee and the preparation of the assumption agreement and related documentation). Upon such assumption, Borrower shall be relieved of its obligations under this Note, the Defeasance Security Agreement and the other Loan Documents, other than those obligations which are specifically intended to survive the payment of this Note and the termination, satisfaction or assignment of this Note, the Defeasance Security Agreement or the other Loan Documents or the exercise of Lender's rights and remedies under any of such documents and instruments.

(ii) Upon compliance with the requirements of this Section, Lender shall release the Property from the lien of the Security Instrument and the other Loan Documents, and the Defeasance Collateral shall secure this Note and all other obligations under the Loan Documents. Lender will, at Borrower's expense, execute and deliver any agreements reasonably requested by Borrower to release the lien of the Security Instrument from the Property. Borrower, pursuant to the Defeasance Security Agreement, shall authorize and direct that the payments received from Defeasance Collateral be made directly to Lender and applied to satisfy the obligations of Borrower under this Note.

(iii) Upon the release of the Property in accordance with this Section 9(b), Borrower shall have no further right to prepay this Note. Borrower shall pay all costs and expenses incurred or to be incurred in connection with the Defeasance and related transactions, including all charges imposed by any rating agencies and any revenue, documentary stamp or intangible taxes or any other tax or charge due in connection with the transfer of this Note or otherwise required to accomplish the Defeasance and related transactions.

(iv) If any notice of defeasance is given pursuant to Section 9(b)(i)(A), Borrower shall be required to defease the Loan on the Release Date (unless such notice is revoked by Borrower prior to the Release Date in which event Borrower shall immediately reimburse Lender for any and all reasonable costs and expenses incurred by Lender in connection with Borrower's giving of such notice and revocation).

(v) At Borrower's request, Lender may agree that Lender or its servicer or other agent, acting on Borrower's behalf as Borrower's agent and attorney-in-fact, shall purchase the Defeasance Collateral that Borrower is required to deliver to Lender pursuant to Section 9(b)(i)(C)(1). If such an agreement is made then Borrower shall deposit with Lender or Lender's servicer or other agent, as directed by Lender or Lender's agent(s), on or prior to the Release Date a sum of money sufficient to purchase the Defeasance Collateral. By making such deposit Borrower shall thereby appoint Lender or Lender's servicer or other agent as Borrower's agent and attorney-in-fact, with full power of substitution, for the purpose of purchasing the Defeasance Collateral with the funds so provided and delivering the Defeasance Collateral to Lender pursuant to Section 9(b)(i)(C)(1).

(vi) Notwithstanding any release of the Security Instrument or any Defeasance hereunder, the Defeasance Obligor shall be bound by and obligated under Sections 3.1 (Payment of Debt), 7.2 (Further Acts Etc.), 7.4(a) (Estoppel Certificates), 11.2 (Application of Proceeds), 11.7 (Other Rights Etc.) and 14.2 (Marshalling and Other Matters) and Article 13 (Indemnification) of the Security Instrument; provided, however, that all references therein to "**Property**" or "**Personal Property**" shall be deemed to refer only to the Defeasance Collateral delivered to Lender.

(c) **Default Prepayment.** If a Default Prepayment (as hereinafter defined) occurs, such Default Prepayment shall be deemed to be a voluntary prepayment under this Note and in such case the applicable Prepayment Consideration (as hereinafter defined) shall be due and

payable to Lender in connection with such Default Prepayment (unless Lender voluntarily and expressly waives in writing the right to collect such Prepayment Consideration). The Prepayment Consideration shall be secured by all security and collateral for the Loan and shall, after it becomes due and payable, be treated as if it were added to the Outstanding Principal Balance for all purposes including accrual of interest, judgment on the Note, foreclosure (whether through power of sale, judicial proceeding, or otherwise) ("**Foreclosure Sale**"), redemption, and bankruptcy (including pursuant to Section 506 of the United States Bankruptcy Code or any successor provision); without limiting the generality of the foregoing, it is understood and agreed that the Prepayment Consideration may be added to Lender's bid at any Foreclosure Sale. If Prepayment Consideration is due hereunder, Lender shall deliver to Borrower a statement setting forth the amount and determination of the Prepayment Consideration, and, provided that Lender shall have in good faith applied the formula described below, Borrower shall not have the right to challenge the calculation or the method of calculation set forth in any such statement in the absence of manifest error, which calculation may be made by Lender on any day during the thirty (30) day period preceding the date of such prepayment.

The term "**Default Prepayment**" shall mean a prepayment of any portion of the principal amount of this Note made after occurrence of a Default or Event of Default under any circumstances including a prepayment in connection with (i) reinstatement of the Security Instrument provided by statute under foreclosure proceedings or exercise of power of sale, (ii) any statutory right of redemption exercised by Borrower or any other party having a statutory right to redeem or prevent foreclosure or power of sale, (iii) any sale in foreclosure or under exercise of a power of sale or otherwise (including pursuant to a credit bid made by Lender in connection with such sale), (iv) any other collection action by Lender, or (v) exercise by any governmental authority of any civil or criminal forfeiture action with respect to any collateral for the Loan. Prepayment Consideration shall be due and payable upon acceleration of the Loan in accordance with the terms of this Note, and the "Prepayment Date", for the purpose of computing Prepayment Consideration, shall be the date of acceleration of the Loan in accordance with the terms of this Note. Exchange of this Note for a different instrument or modification of the terms of this Note, including classification and treatment of Lender's claim (other than non-impairment under Section 1124 of the United States Bankruptcy Code or any successor provision) pursuant to a plan of reorganization in bankruptcy shall also be deemed to be a Default Prepayment hereunder.

The "**Prepayment Consideration**" (as the term is used in this Note) shall mean the present value, as of the date of the occurrence of the Default, of the remaining scheduled payments of principal and interest from the date of the occurrence of the Default through the Maturity Date (including any balloon payment), which shall be determined by discounting such payments at the Discount Rate (hereinafter defined) less the amount of principal being prepaid. The term "**Discount Rate**" shall mean the rate that, when compounded monthly, is equivalent to the Treasury Rate (hereinafter defined) when compounded semi-annually. The term "**Treasury Rate**" shall mean the yield calculated by the linear interpolation of the yields, as reported in Federal Reserve Statistical Release H.15-Selected Interest Rates under the heading U.S. Government Securities/Treasury Constant Maturities for the week ending prior to the Prepayment Date, of U.S. Treasury constant maturities with maturity dates (one longer and one shorter) most nearly approximating the Maturity Date. (If Release H.15 is no longer published, Lender shall select a comparable publication to determine the Treasury Rate.).

Borrower acknowledges that: (i) Lender has made the Loan to Borrower in reliance on, and the Loan has been originated for the purpose of selling the Loan in the secondary market to investors who will purchase the Loan or direct or indirect interests therein in reliance on, the actual receipt over time of the stream of payments of principal and interest agreed to by Borrower herein; and (ii) Lender or any subsequent investor in the Loan will incur substantial additional costs and expenses in the event of a prepayment of the Loan; and (iii) the Prepayment Consideration is reasonable and is a bargained for consideration and not a penalty and the terms of the Loan are in various respects more favorable to Borrower than they would have been absent Borrower's agreement to pay Prepayment Consideration as provided herein. Borrower agrees that Lender shall not, as a condition to receiving the Prepayment Consideration, be obligated to actually reinvest the amount prepaid in any treasury obligation or in any other manner whatsoever. Nothing contained herein shall be deemed to be a waiver by Lender of any right it may have to require specific performance of any obligation of Borrower hereunder including to make payments hereunder strictly according to the terms hereof or to furnish Defeasance Collateral.

In addition to Prepayment Consideration, Borrower shall pay all hedging and breakage costs of any kind and in any amount incurred by Lender due to any prepayment (including a Default Prepayment).

10. **Maximum Rate Permitted by Law.** All agreements in this Note and all other Loan Documents are expressly limited so that in no contingency or event whatsoever, whether by reason of acceleration of maturity of the indebtedness evidenced hereby or otherwise, shall the amount agreed to be paid hereunder for the use, forbearance, or detention of money exceed the highest lawful rate permitted under applicable usury laws. If, from any circumstance whatsoever, fulfillment of any provision of this Note or any other Loan Document at the time performance of such provision shall be due shall involve exceeding any usury limit prescribed by law that a court of competent jurisdiction may deem applicable hereto, then, ipso facto, the obligations to be fulfilled shall be reduced to allow compliance with such limit, and if, from any circumstance whatsoever, Lender shall ever receive as interest an amount that would exceed the highest lawful rate, the receipt of such excess shall be deemed a mistake and shall be canceled automatically or, if theretofore paid, such excess shall be credited against the principal amount of the indebtedness evidenced hereby to which the same may lawfully be credited, and any portion of such excess not capable of being so credited shall be refunded immediately to Borrower.

11. **Events of Default; Acceleration of Amount Due.** Lender may in its discretion, without notice to Borrower, declare the entire Debt, including the principal balance of the Loan, all accrued interest, all costs, expenses, charges and fees payable under any Loan Document, and Prepayment Consideration immediately due and payable, and Lender shall have all remedies available to it at law or equity for collection of the amounts due, if any of the following (the "**Events of Default**") occurs:

(a) Borrower fails to make full and punctual payment of any Monthly Payment or any other amount payable on a monthly basis under this Note, the Security Instrument or any other Loan Document within five (5) days of the date on which such payment was due; or

(b) Borrower fails to make full payment of the Debt when due, whether on the Maturity Date, upon acceleration or prepayment, or otherwise; or

(c) Borrower fails to make full and punctual payment of any Late Charges, costs and expenses due hereunder, or any other sum of money required to be paid to Lender under this Note, the Security Instrument or under any other Loan Document (other than any payment described in subclauses (a) and (b) immediately above), which failure is not cured on or before the fifth (5th) day after Lender's written notice to Borrower that such payment is required.

(d) an Event of Default occurs under the Security Instrument or any other Loan Document that has continued beyond any applicable cure period therefor.

12. **Time of Essence.** Time is of the essence with regard to each provision contained in this Note.

13. **Transfer and Assignment.** This Note may be freely transferred and assigned by Lender. Borrower's right to transfer its rights and obligations with respect to the Debt, and to be released from liability under this Note, shall be governed by the Security Instrument.

14. **Authority of Persons Executing Note.** Borrower warrants and represents that the persons or officers who are executing this Note and the other Loan Documents on behalf of Borrower have full right, power and authority to do so, and that this Note and the other Loan Documents constitute valid and binding documents, enforceable against Borrower in accordance with their terms, and that no other person, entity, or party is required to sign, approve, or consent to, this Note.

15. **Severability.** The terms of this Note are severable, and should any provision be declared by a court of competent jurisdiction to be invalid or unenforceable, the remaining provisions shall, at the option of Lender, remain in full force and effect and shall in no way be impaired.

16. **Borrower's Waivers.** Borrower and all others liable hereon hereby waive presentation for payment, demand, notice of dishonor, protest, and notice of protest, notice of intent to accelerate, and notice of acceleration, stay of execution and all other suretyship defenses to payment generally. No release of any security held for the payment of this Note, or extension of any time periods for any payments due hereunder, or release of collateral that may be granted by Lender from time to time, and no alteration, amendment or waiver of any provision of this Note or of any of the other Loan Documents, shall modify, waive, extend, change, discharge, terminate or affect the liability of Borrower and any others that may at any time be liable for the payment of this Note or the performance of any covenants contained in any of the Loan Documents.

17. **Governing Law.** This Note shall be governed and construed generally according to the laws of the jurisdiction in which the real property collateral for this Note is located without regard to the conflicts of law provisions thereof ("**Governing State**").

18. **JURISDICTION AND VENUE.** BORROWER HEREBY CONSENTS TO PERSONAL JURISDICTION IN THE GOVERNING STATE. VENUE OF ANY ACTION BROUGHT TO ENFORCE THIS NOTE OR ANY OTHER LOAN DOCUMENT OR ANY ACTION RELATING TO THE LOAN OR THE DEBT OR THE RELATIONSHIPS CREATED BY OR UNDER THE LOAN DOCUMENTS ("**ACTION**") SHALL, AT THE ELECTION OF LENDER, BE IN (AND IF ANY ACTION IS ORIGINALLY BROUGHT IN ANOTHER VENUE, THE ACTION SHALL AT THE ELECTION OF LENDER BE TRANSFERRED TO) A STATE OR FEDERAL COURT OF APPROPRIATE JURISDICTION LOCATED IN THE GOVERNING STATE. BORROWER HEREBY CONSENTS AND SUBMITS TO THE PERSONAL JURISDICTION OF THE STATE COURTS OF THE GOVERNING STATE AND OF FEDERAL COURTS LOCATED IN THE GOVERNING STATE IN CONNECTION WITH ANY ACTION AND HEREBY WAIVES ANY AND ALL PERSONAL RIGHTS UNDER THE LAWS OF ANY OTHER STATE TO OBJECT TO JURISDICTION WITHIN SUCH STATE FOR PURPOSES OF ANY ACTION. Borrower hereby waives and agrees not to assert, as a defense to any Action or a motion to transfer venue of any Action, (i) any claim that it is not subject to such jurisdiction, (ii) any claim that any Action may not be brought against it or is not maintainable in those courts or that this Note or any of the other Loan Documents may not be enforced in or by those courts, or that it is exempt or immune from execution, (iii) that the Action is brought in an inconvenient forum, or (iv) that the venue for the Action is in any way improper.

19. **Notices.** Any notice required or permitted to be given hereunder must be in writing and given (a) by depositing same in the United States mail, addressed to the party to be notified, postage prepaid and registered or certified with return receipt requested; (b) by delivering the same in person to such party; (c) by transmitting a facsimile copy to the correct facsimile phone number of the intended recipient (with a second copy to be sent to the intended recipient by any other means permitted under this Section 19); or (d) by depositing the same into the custody of a nationally recognized overnight delivery service addressed to the party to be notified. In the event of mailing, notices shall be deemed effective three (3) days after posting; in the event of overnight delivery, notices shall be deemed effective on the next Business Day following deposit with the delivery service; in the event of personal service or facsimile transmissions, notices shall be deemed effective when delivered. For purposes of notice, the addresses of the parties shall be as set forth in the Table. From time to time either party may designate another address than the address set forth for all purposes of this Note by giving the other party no less than ten (10) days advance notice of such change of address in accordance with the notice provisions hereof. A copy of any notice sent, transmitted or delivered to Lender shall also be delivered to Daniel Flanigan, Esq., Polsinelli Shalton Welte Suelthaus, 700 W. 47th Street, Suite 1000, Kansas City, Missouri 64112, facsimile number: (816) 753-1536.

20. **Avoidance of Debt Payments.** To the extent that any payment to Lender and/or any payment or proceeds of any collateral received by Lender in reduction of the Debt is subsequently invalidated, declared to be fraudulent or preferential, set aside and/or required to be repaid to a trustee, to Borrower (or Borrower's successor) as a debtor in possession, or to a receiver, creditor, or any other party under any bankruptcy law, state or federal law, common law or equitable cause, then the portion of the Debt intended to have been satisfied by such payment or proceeds shall remain due and payable hereunder, be evidenced by this Note, and shall continue in full force and effect as if such payment or proceeds had never been received by Lender whether or not this Note has been marked "paid" or otherwise cancelled or satisfied and/or has been delivered to Borrower, and in such event Borrower shall be immediately obligated to return the original Note to Lender and any marking of "paid" or other similar marking shall be of no force and effect.

21. **Nonrecourse.**

(a) Subject to the provisions of subsections (b) and (c) of this Section 21, Lender shall not be entitled to recover any deficiency judgment against Borrower or any general partner (if any) of Borrower on this Note, provided, however, the foregoing shall not be interpreted to: (i) impair or affect the right of Lender to enforce any of its rights or remedies (other than any right to a deficiency judgment) provided for in any of the Loan Documents or under applicable law in full accordance with the terms thereof including the right of Lender to name Borrower or any general partner of Borrower as a party defendant in any action or suit for specific performance, foreclosure, or sale (or similar remedy) under the Security Instrument or any other Loan Document; (ii) impair or affect the validity or enforceability of any guaranty, indemnity agreement (including any environmental indemnity agreement), letter of credit, or other similar third party agreement or undertaking made in connection with this Note, the Security Instrument, or any other Loan Document; (iii) impair or affect Lender's right to offset any and all amounts outstanding under any of the Loan Documents against any claim or amount that may be asserted against Lender by Borrower or any partners, members, shareholders, or other owners of legal or beneficial interests in Borrower; or (iv) affect the validity or enforceability of or impair the right of Lender to bring suit and obtain specific performance or personal, recourse judgment to enforce the liability of Borrower or any other person or entity to the extent of, and Borrower hereby agrees to be personally liable for, any loss, damage, cost, expense or liability incurred by Lender (including all attorneys' fees and expenses and other collection and litigation expenses) arising out of or in connection with any of the following:

(A) Borrower or any affiliate, agent, or employee of Borrower misappropriates any rents or other Property income or collateral proceeds including insurance or condemnation proceeds or awards;

(B) Borrower or any affiliate, agent, or employee of Borrower fails to apply or pay over any tenant security deposits or other refundable deposits in accordance with the terms of the applicable lease or other agreement or the Security Instrument or any other Loan Document;

(C) Borrower or any affiliate, agent, or employee of Borrower receives rents or other payments from tenants more than one month in advance and fails to apply them in accordance with the Loan Documents;

(D) following the occurrence of an Event of Default, Borrower or any affiliate, agent, or employee of Borrower (including Borrower in its capacity as a debtor or debtor in possession in a bankruptcy proceeding) fails either to apply rents or other Property income, whether collected before or after such Event of Default, to the ordinary, customary, and necessary expenses of operating the Property or, upon demand, to deliver such rents or other Property income to Lender;

(E) waste is committed on the Property during a period while Borrower or any affiliate, agent, or employee of Borrower is in possession thereof ("waste" meaning the diminution in the Property's value resulting from Borrower's negligent or willful failure to manage, maintain, repair and otherwise operate the Property in a commercially reasonable manner);

(F) any damage to the Property or the Lender is caused as a result of the intentional misconduct or gross negligence of Borrower or any affiliate, agent, or employee of Borrower;

(G) any Property is removed in violation of the terms of the Loan Documents;

(H) Borrower fails, in accordance with the terms of the Loan Documents, to maintain insurance or to pay taxes, assessments, or other liens or claims that could create liens affecting the Property (unless Lender is escrowing funds therefor and fails to make such payments or has taken possession of the Property following an Event of Default, has received all rents from the Property applicable to the period for which such insurance, taxes or other items are due, and thereafter fails to make such payments);

(I) there is any fraud or material misrepresentation by Borrower or any of its affiliates, any guarantor, any indemnitor or any agent, employee, or other person with actual or apparent authority to make statements or representations on behalf of Borrower, any affiliate of Borrower, or any guarantor or indemnitor ("apparent authority" meaning such authority as the principal knowingly or negligently permits the agent to assume, or which he holds the agent out as possessing); or

(J) Borrower fails, following an Event of Default, to deliver to Lender on demand all security deposits, books and records relating to the Property and in the possession or control of Borrower or any affiliate, agent, or employee of Borrower.

(b) Notwithstanding anything to the contrary in the provisions of subsection (a) of this Section, subsection (a) of this Section shall not apply and Borrower and any general partner of Borrower shall be personally liable for the Debt if (i) there shall be any violation of the due-on-sale or due-on-encumbrance provisions of the Security Instrument, (ii) Borrower shall at any time hereafter make an assignment for the benefit of its creditors, or (iii) the Property or any part thereof shall at any time hereafter become property of the estate or an asset in (a) a voluntary bankruptcy, insolvency, receivership, liquidation, winding up, or other similar type of proceeding, or (b) an involuntary bankruptcy or insolvency proceeding (other than one filed by Lender) that is not dismissed within sixty (60) days of filing.

(c) Nothing herein shall be deemed to constitute a waiver by Lender of any right Lender may have under Sections 506(a), 506(b), 1111(b) or any other provision of the United States Bankruptcy Code to file a claim for the full amount of the Debt (as defined in the Security Instrument) or to require that all collateral shall continue to secure all of the Debt.

22. **Miscellaneous.** Neither this Note nor any of the terms hereof, including the provisions of this Section, may be terminated, amended, supplemented, waived or modified orally, but only by an instrument in writing executed by the party against which enforcement of the termination, amendment, supplement, waiver or modification is sought, and the parties hereby: (a) expressly agree that it shall not be reasonable for any of them to rely on any alleged, non-written amendment to this Note; (b) irrevocably waive any and all right to enforce any alleged, non-written amendment to this Note; and (c) expressly agree that it shall be beyond the scope of authority (apparent or otherwise) for any of their respective agents to agree to any non-written modification of this Note. This Note may be executed in several counterparts, each of which counterpart shall be deemed an original instrument and all of which together shall constitute a single Note. The failure of any party hereto to execute this Note, or any counterpart hereof, shall not relieve the other signatories from their obligations hereunder. If Borrower consists of more than one person or entity, then the obligations and liabilities of each person or entity shall be joint and several and in such case, the term "Borrower" shall mean individually and collectively, jointly and severally, each Borrower. As used in this Note, (i) the terms "include," "including" and similar terms shall be construed as if followed by the phrase "without being limited to," (ii) any pronoun used herein shall be deemed to cover all genders, and words importing the singular number shall mean and include the plural number, and vice versa, (iii) all captions to the Sections hereof are used for convenience and reference only and in no way define, limit or describe the scope or intent of, or in any way affect, this Note, (iv) no inference in favor of, or against, Lender or Borrower shall be drawn from the fact that such party has drafted any portion hereof or any other Loan Document, (v) the words "Lender" and "Borrower" shall include their respective successors (including, in the case of Borrower, any subsequent owner or owners of the Property or any part thereof or any interest therein and Borrower in its capacity as debtor-in-possession after the commencement of any bankruptcy proceeding), assigns, heirs, personal representatives, executors and administrators, (vi) the term "or" has, except where otherwise indicated, the inclusive meaning represented by the phrase "and/or", (vii) the words "hereof", "herein", "hereby", "hereunder", and similar terms in this Note refer to this Note as a whole and not to any particular provision or section of this Note, and (viii) an Event of Default shall "continue" or be "continuing" until such Event of Default has been waived in writing by Lender. Wherever Lender's judgment, consent, approval or discretion is required under this Note or Lender shall have an option, election, or right of determination or any other power to decide any matter relating to the terms of this Note, including any right to determine that something is satisfactory or not ("**Decision Power**"), such Decision Power shall be exercised in the sole and absolute discretion of Lender except as may be otherwise expressly and specifically provided herein. Such Decision Power and each other power granted to Lender upon this Note or any other Loan Document may be exercised by Lender or by any authorized agent of Lender (including any servicer and/or attorney-in-fact), and Borrower hereby expressly agrees to recognize the exercise of such Decision Power by such authorized agent. In the event of a conflict between or among the terms, covenants, conditions or provisions of the Loan Documents, the term(s), covenant(s), condition(s) and/or provision(s) that Lender may elect to enforce from time to time so as to enlarge the interest of Lender in its security, afford Lender the maximum financial benefits or security for the Debt, and/or provide Lender the maximum assurance of payment of the Debt in full shall control. BORROWER ACKNOWLEDGES AND AGREES THAT IT HAS BEEN PROVIDED WITH SUFFICIENT AND NECESSARY TIME AND OPPORTUNITY TO REVIEW THE TERMS OF THIS NOTE, THE SECURITY INSTRUMENT, AND EACH OF THE LOAN DOCUMENTS, WITH ANY AND ALL COUNSEL IT DEEMS APPROPRIATE, AND THAT NO INFERENCE IN FAVOR OF, OR AGAINST, LENDER OR BORROWER SHALL BE DRAWN FROM THE FACT THAT EITHER SUCH PARTY HAS DRAFTED ANY PORTION HEREOF, OR THE SECURITY INSTRUMENT, OR ANY OF THE LOAN DOCUMENTS.

23. **Waiver of Counterclaim and Jury Trial. BORROWER HEREBY KNOWINGLY WAIVES THE RIGHT TO ASSERT ANY COUNTERCLAIM, OTHER THAN A COMPULSORY COUNTERCLAIM, IN ANY ACTION OR PROCEEDING BROUGHT AGAINST BORROWER BY LENDER OR ITS AGENTS. ADDITIONALLY, BORROWER AND LENDER HEREBY KNOWINGLY, VOLUNTARILY AND INTENTIONALLY WAIVE ANY RIGHT THEY MAY HAVE TO A TRIAL BY JURY IN RESPECT OF ANY LITIGATION BASED ON THE LOAN OR ARISING OUT OF, UNDER, OR IN CONNECTION WITH THE LOAN, THIS NOTE, THE SECURITY INSTRUMENT, OR ANY OTHER LOAN DOCUMENT, OR ANY COURSE OF CONDUCT, COURSE OF DEALING, STATEMENT (WHETHER VERBAL OR WRITTEN), OR ACTION OF BORROWER OR LENDER. THIS PROVISION IS A MATERIAL INDUCEMENT FOR LENDER'S MAKING OF THE LOAN.**

24. **Local Law Provisions.** In the event of any inconsistencies between the terms and conditions of this Section and any other terms and conditions of this Note (other than the terms and conditions of Section 25), the terms and conditions of this Section shall be binding.

24.1 **Business Purpose.** This Loan is intended to be for commercial or business purposes.

24.2 **Late Charge**. The first sentence of Section 6 is modified by adding the following between "due", and "Borrower": "or on a later date if required by applicable law,".

24.3 **Waiver of Counterclaim and Jury Trial.** The second sentence of Section 23 is hereby modified by adding the following to the beginning thereof: "TO THE EXTENT PERMITTED BY APPLICABLE LAW,".

25. **Additional Provisions.** In the event of any inconsistencies between the terms and conditions of this Section and any other terms and conditions of this Note, the terms and conditions of this Section shall be binding.

25.1 **Financial Statement Reporting Deposit; Rebate of Deposit**. Borrower's obligation under Section 4 to pay the monthly Financial Statement Reporting Deposit stated in the Loan Terms Table is hereby waived so long as Gladstone Commercial Corporation, a Maryland corporation, is a publicly traded company.

25.2 **Interest Rate.** From the date of disbursement of the Loan proceeds, until the Anticipated Repayment Date (as hereinafter defined) interest shall accrue on the OPB at a rate of 6.33 percent (6.33%) per annum ("**Initial Interest Rate**"). From and after the Anticipated Repayment Date (as hereinafter defined), interest shall accrue on the OPB at a rate equal to the greater of: (i) Initial Interest Rate plus two (2) percent per annum; or (ii) the Treasury Rate for the week ending prior to the Anticipated Repayment Date plus two (2) percent per annum ("**Adjusted Interest Rate**"). As used in this Note, the term "Interest Rate" shall mean the Initial Interest Rate or the Adjusted Interest Rate, as applicable.

25.3 **Prepayment Restrictions.** The first sentence of Section 9(a) is amended in its entirety to provide as follows: Voluntary prepayment of this Note is prohibited except during the period commencing on June 23, 2009 and ending on the Maturity Date when prepayment may be made in whole, but not in part, without payment of any Prepayment Consideration (as hereinafter defined) on any Monthly Payment Date.

The fifth line of Section 9(a) is hereby modified by adding "and is continuing" between "occurred" and ",".

The following is added to the end of Section 9(a): "Borrower's right to cause a Defeasance (as hereinafter defined) in accordance with Section 9(b) shall end on the Anticipated Repayment Date (as hereinafter defined)." In the tenth line of Section 9(b)(i)(C)(1), and the final line of Section 9(b)(i)(C)(3), and the sixth line of Section 9(b)(i)(C)(5), and the fourth line of the third paragraph of Section 9(c), and the second to last line of the third paragraph of Section 9(c) the phrase "Maturity Date" is deleted and the phrase "Anticipated Repayment Date" is substituted therefor.

The third line of Section 9(b)(i)(B) is hereby modified by inserting "reasonable" between "including" and "attorneys'".

The second line of Section 9(b)(i)(C)(2) is hereby modified by inserting "reasonably" between "instruments" and "required".

The seventeenth line of the first paragraph of Section 9(b)(i)(C)(7) is hereby modified by inserting "reasonable" between "including" and "attorneys'".

The second and third lines of the second paragraph of Section 9(b)(i)(C)(7) is hereby modified by deleting the words "under any circumstances" and substituting "that has not been waived in writing by Lender" therefor.

25.4 **Hyperamortization.** In the event that Borrower does not pay to Lender on or before the Anticipated Repayment Date, the outstanding principal balance of this Note together with all unpaid interest thereon and all other amounts owed to Lender pursuant to this Note or any other Loan Document, the following provisions shall apply:

(a) From and after the Anticipated Repayment Date, interest shall accrue on the OPB at the Adjusted Interest Rate. Interest accrued at the Adjusted Interest Rate and not paid pursuant to this Section 25.4 shall be deferred and added to the OPB of this Note (together with all accrued interest thereon) and shall earn interest at the Adjusted Interest Rate to the extent permitted by applicable law (such accrued interest, together with any interest accrued thereon is hereinafter defined as "**Accrued Interest**"). All of the OPB, including any Accrued Interest, shall be due and payable on the Maturity Date.

(b) Contemporaneously herewith, Borrower has executed a Collection and Disbursement Agreement (the "**Disbursement Agreement**") pursuant to which Borrower has agreed that, commencing on the first day of the month preceding the Anticipated Repayment Date, Borrower shall cause all rents and all other income, proceeds and other revenues generated or otherwise derived from or attributable to the Property (collectively, "**Rents and Profits**") to be deposited in a deposit account with a financial institution named by Lender (the "**Disbursement Account**"). The Disbursement Agreement provides that all sums deposited in the Disbursement Account shall be applied as set forth therein. From and after the Anticipated Repayment Date, provided no Event of Default has occurred and no event has occurred which, with the passage of time, notice or both, would constitute an Event of Default, all funds in the Disbursement Account shall be disbursed, unless Lender in its sole discretion determines otherwise, by Lender from such account for the payment of the following items in the specified order of payment:

(i) First, payments to be made to the tax and insurance escrow funds in accordance with the terms and conditions of the Security Instrument;

(ii) Second, payment of the Monthly Payment (plus, if applicable, interest at the Default Rate and any other charges then due to Lender under the Loan Documents) to be applied first to the payment of interest computed at the Initial Interest Rate with the remainder applied to the reduction of the OPB of this Note;

(iii) Third, payments required to be made to any other escrow or reserve funds established pursuant to any of the Loan Documents;

(iv) Fourth, payments of the monthly operating expenses incurred for the Property ("**Monthly Operating Expenses**"), pursuant to the terms of the approved Annual Budget (as hereinafter defined), but excluding any Affiliate Expenses (as hereinafter defined);

(v) Fifth, payment of Extraordinary Expenses (as hereinafter defined) approved in writing by Lender, if any;

(vi) Sixth, payment of any other amounts due under any of the Loan Documents, including, without limitation, any advances made by Lender thereunder for the protection of the Property or Lender's liens and security interests;

(vii) Seventh, payment to Lender to be applied against the OPB of this Note (but not including any Accrued Interest) until such principal amount (not including any Accrued Interest) is paid in full;

(viii) Eighth, payment of Accrued Interest;

(ix) Ninth, payment of Affiliate Expenses; and

(x) Tenth, payment to Borrower of any remaining funds.

(c) Nothing provided above with respect to the Disbursement Account shall limit, reduce or otherwise affect Borrower's obligations under the Loan Documents including, without limitation, the obligations of Borrower to: (i) operate and maintain (and to pay currently all expenses to operate and maintain) the Property; (ii) make the Monthly Payments; (iii) fund all escrows or reserves established or required under the Loan Documents; and (iv) pay all other amounts due at any time under this Note, the Security Instrument, and the other Loan Documents, even though the sums available in the Disbursement Account may be insufficient at any time to make such payments.

(d) For each fiscal year commencing with the fiscal year in which the Anticipated Repayment Date occurs, Borrower shall submit to Lender for Lender's written approval an operating budget for the next succeeding fiscal year, on a month by month basis, including cash flow projections and all proposed capital replacements and improvements and other expenses of the Property (the "**Annual Budget**") not later than sixty (60) days prior to the commencement of such fiscal year, in form and substance satisfactory to Lender. Lender shall have the right to approve such Annual Budget and in the event that Lender objects to the proposed Annual Budget submitted by Borrower, Lender shall advise Borrower of such objections and Borrower shall within five (5) days after receipt of notice of any such objections, revise such Annual Budget and resubmit the same to Lender. This procedure shall be repeated until Lender approves an Annual Budget. Until such time as Lender approves a proposed Annual Budget, the most recently approved Annual Budget shall apply; provided that such approved Annual Budget shall be adjusted to reflect actual increases in real estate taxes, insurance premiums, and utility expenses and to defer any management fees, leasing commissions, or other payments to, or any personal expenses of, Borrower or any person or entity which is directly or indirectly controlling, controlled by, or under common control with, Borrower or any guarantor or indemnitor with respect to the Loan ("**Affiliate Expenses**"). In the event that Borrower proposes to incur an extraordinary operating expense or capital expense not set forth in the approved Annual Budget then in effect (an "**Extraordinary Expense**"), then Borrower shall promptly deliver to Lender a reasonably detailed explanation of such proposed Extraordinary Expense for Lender's written approval. Borrower covenants and agrees to incur costs only in accordance with the approved Annual Budget.

25.5 **Notices**. In addition to the requirements of Section 19 hereof, Lender shall use reasonable efforts to provide a courtesy copy of any notice required or permitted to be given by Lender to Borrower hereunder to the following addressee: James D. Kelly, Esq., Dickstein Shapiro Marin & Oshinsky LLP, 2101 L Street N.W., Washington, D.C. 20037, facsimile number (202) 887-0689.

Lender's failure to send such courtesy copies shall not impair the effect of the notice sent to Borrower.

25.6 **Nonrecourse**. The second and seventh lines of Section 21(a), and the second line of Section 21(b) are hereby modified by inserting the words "member or" between "any" and "general". The third line of Section 21(a) is hereby modified by inserting the phrase "or any person or entity having an ownership and/or equity, or legal and/or beneficial interest in any member or general partner of Borrower" between "Note" and ",".

[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK]

Intending to be fully bound, Borrower has executed this Note under seal effective as of the day and year first above written.

Borrower:

By: **CMI04 CANTON NC LLC**, (SEAL)
a Delaware limited liability company

By: GLADSTONE COMMERCIAL LIMITED (SEAL)
PARTNERSHIP, a Delaware limited
Partnership, its managing member

By: GLADSTONE COMMERCIAL (SEAL)
PARTNERS, LLC, a Delaware limited
liability company, its General Partner

By: GLADSTONE COMMERCIAL (SEAL)
CORPORATION, a Maryland
corporation, its manager

By: _____
Name: Robert J. Corry
Title: Principal

[CORPORATE SEAL]

Pay to the order of _____, without recourse.

KEYBANK NATIONAL ASSOCIATION,
a national banking association

By: _____
Print Name: _____
Print Title: _____

STATE OF _____

COUNTY OF_____

I,_____ , a Notary Public of the County and State aforesaid, certify that Robert J. Corry personally came before me this day and acknowledged that he is the Principal of GLADSTONE COMMERCIAL CORPORATION, a Maryland corporation, who is the Manager of GLADSTONE COMMERCIAL PARTNERS, LLC, a Delaware limited liability company, who is the General Partner of GLADSTONE COMMERCIAL LIMITED PARTNERSHIP, a Delaware limited partnership, who is the Managing Member of CMI04 CANTON NC LLC, a Delaware limited liability company, and that by authority duly given and as the act of the corporation, in its capacity as Manager of GLADSTONE COMMERCIAL PARTNERS, LLC, the General Partner of GLADSTONE COMMERCIAL LIMITED PARTNERSHIP, which in turn is the Managing Member of CMI04 CANTON NC LLC, the foregoing instrument was signed in its name by the said Robert J. Corry in such capacity sealed with its corporate seal and attested by him as its principal.

Witness my hand and official stamp or seal, this_____ day of March, 2005.

_____
Notary Public

My Commission Expires:

_____
(Affix official seal or stamp)

Exhibit 10.2

FIRST AMENDMENT TO CREDIT AGREEMENT AND WAIVER

THIS FIRST AMENDMENT TO CREDIT AGREEMENT AND WAIVER (this "Amendment") is made as of the 21st day of April, 2005, by and among GLADSTONE COMMERCIAL CORPORATION and GLADSTONE COMMERCIAL LIMITED PARTNERSHIP, as Borrowers (together, the "Borrowers"), the GUARANTORS signatory hereto, as guarantors (collectively, the "Guarantors"), and BRANCH BANKING AND TRUST COMPANY, as Administrative Agent (the "Administrative Agent") and a Bank, FIRST HORIZON BANK, as a Bank, and COMPASS BANK, as a Bank (collectively, the "Banks").

R E C I T A L S:

The Borrowers, the Guarantors, the Administrative Agent and the Banks have entered into a certain Credit Agreement dated as of February 28, 2005 (referred to herein as the "Credit Agreement"). Capitalized terms used in this Amendment which are not otherwise defined in this Amendment shall have the respective meanings assigned to them in the Credit Agreement.

The Borrowers have requested the Administrative Agent and the Banks to amend the Credit Agreement and the Membership Pledge Agreement to modify certain provisions thereof (i) to permit certain subleases of Eligible Properties, (ii) to permit certain of Borrowers' Subsidiaries which own Borrowing Base Assets or prospective Borrowing Base Assets to be organized as limited partnerships and (iii) to permit certain limited guaranties by Gladstone Commercial Corporation of Long Term Limited Recourse Mortgage Loans by its Subsidiaries, all as more fully set forth herein. The Borrowers have further requested the Administrative Agent and the Banks to waive the provision of the Credit Agreement requiring immediate delivery of tenant estoppel and subordination and nondisturbance agreements to allow the Borrowers an additional forty-five (45) days to obtain such documents. The Administrative Agent, the Banks, the Borrowers and the Guarantors desire to amend and waive the Credit Agreement upon the terms and conditions hereinafter set forth.

NOW, THEREFORE, in consideration of the Recitals and the mutual promises contained herein and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the Borrowers, the Guarantors, the Administrative Agent and the Banks, intending to be legally bound hereby, agree as follows:

SECTION 1. Recitals. The Recitals are incorporated herein by reference and shall be deemed to be a part of this Amendment.

SECTION 2. Amendments. The Credit Agreement is hereby amended as set forth in thisSection 2.

SECTION 2.01. Amendment to Section 1.01. Section 1.01 of the Credit Agreement is amended by amending and restating the definitions of "Eligible Property," "Eligible Property Owner" or "Eligible Mortgage Owner," "Eligible Tenant," "Membership

Pledge Agreement" and "Mortgaged Property Support Documents" to read in their entirety as follows:

"Eligible Property" means a Property which satisfies all of the following requirements:

(a) such Property is located in one of the 48 contiguous states of the United States of America or in the District of Columbia;

(b) neither such Property, nor any interest of the Company or any Subsidiary thereof (including without limitation any Eligible Property Owner) therein, is subject to any Lien (other than Permitted Liens) or any Negative Pledge;

(c) such Property is owned by an Eligible Property Owner and is a Wholly Owned Property;

(d) none of the Company's direct or indirect ownership interest in such Eligible Property Owner is subject to any Lien or any Negative Pledge (other than any Liens pursuant to the Loan Documents);

(e) the Company directly, or indirectly through a Wholly Owned Subsidiary, has the right to take the following actions without the need to obtain the consent of any Person: (A) to create Liens on such Property as security for Debt of the Company, any Loan Parties or such Subsidiary, as applicable and (B) to sell, transfer or otherwise dispose of such Property;

(f) such Property is free of all structural defects or architectural deficiencies, title defects, environmental conditions or other adverse matters except for defects, deficiencies, conditions or other matters individually or collectively which are fully insured against (subject to reasonable and customary deductibles) or are not material to the profitable operation of such Property;

(g) such Property was acquired: (1) except for Properties proposed to be included as Borrowing Base Assets within ninety (90) days after the Closing Date, by the Eligible Property Owner within three months of the date such Property is proposed to be included as a Borrowing Base Asset; (2) by the Eligible Property Owner in accordance with the terms of the Acquisition, Credit and Collection Policy; and (3) in the ordinary course of the Company's business through a sale-leaseback transaction;

(h) good and indefeasible fee simple title to such Property is owned by the Eligible Property Owner free and clear of any liens (other than Permitted Liens) and 100% of the membership interests of such

Eligible Property Owner have been pledged pursuant to the Membership Pledge Agreement;

(i) the tenant (or, in the case of a Property which has been subleased and the Company has underwritten the subtenant in lieu of the tenant, the subtenant): (a) has an internal risk rating of 4 or higher on the Company's 10 point risk rating scale set forth in the Acquisition, Credit and Collection Policy and (b) is otherwise deemed an Eligible Tenant;

(j) substantially all of the Property is leased or subleased to an Eligible Tenant pursuant to a lease or sublease substantially in the form previously approved by the Administrative Agent and the Required Lenders, except with respect to Properties acquired by an Eligible Property Owner subject to an existing lease that has not been entered into in contemplation of such sale to the Eligible Property Owner and which is in compliance with the Acquisition, Credit and Collection Policy and except for subleases of nonmaterial portions of the Property which shall not be subject to the requirements of this paragraph;

(k) each Eligible Tenant is in material compliance with the terms of the lease or sublease and related documents;

(l) such property has been a Borrowing Base Asset for less than 12 months;

(m) lease and sublease payments on such Property are in U.S. Dollars; and

(n) all of the representations and warranties set forth in the Mortgage with respect to such Property are true and correct.

"Eligible Property Owner" or "Eligible Mortgage Owner" means (i) any limited liability company which is a Domestic Subsidiary and a Wholly Owned Subsidiary, all of the membership interests (and all other ownership interests) of which are pledged to the Secured Parties pursuant to the Membership Pledge Agreement or (ii) any limited partnership which is a Domestic Subsidiary and a Wholly Owned Subsidiary, and whose general partner is a corporation and a Domestic Subsidiary and a Wholly Owned Subsidiary, all of the limited partnership interests of which limited partnership and all of the stock of the corporate general partner of which limited partnership are pledged to the Secured Parties pursuant to the Membership Pledge Agreement.

"Eligible Tenant" means on any day with respect to a Mortgaged Property, the tenant (or, in the case of a Property which has been subleased and the Company has underwritten the subtenant in lieu of the tenant, the subtenant): obligated to make payments pursuant to a lease or sublease of all or any portion of such Mortgaged Property (which lease or sublease shall be in form and content satisfactory to the Administrative Agent), including any guarantor thereof that satisfies each of the following requirements at all times: (i) such tenant or subtenant is not a natural person and is a legal operating

entity, duly organized and validly existing under the laws of its jurisdiction of organization; (ii) the business of such tenant or subtenant has a Operating History of at least twenty-four (24) months from the date of its incorporation or formation; (iii) such tenant or subtenant is not the subject of any Insolvency Event and such tenant or subtenant has not experienced a material adverse change, in its business, financial condition, operations, properties or prospects since the date of the lease or sublease; (iv) no default, event of default or event which with the giving of notice or the expiration of time would constitute a default or event of default has occurred with respect to any other lease or sublease included within the Collateral to which such tenant or subtenant is a party; (v) such tenant or subtenant is not a Governmental Authority; (vi) such tenant or subtenant is in compliance with all material terms and conditions of such lease or sublease; (vii) such tenant's or subtenant's principal office is located in the United States; and (viii) such tenant or subtenant has an internal risk rating of 4 or higher on the Company's 10 point risk rating scale set forth in the Acquisition, Credit and Collection Policy.

"Membership Pledge Agreement" means collectively (or individually as the context may indicate): (i) a Membership Pledge Agreement by the Operating Partnership in favor of the Administrative Agent for the benefit of the Secured Parties dated the date hereof and (ii) any joinders thereto or any additional Equity Pledge Agreement (as such Membership Pledge Agreement has been retitled pursuant to the First Amendment to Credit Agreement dated as of April 21, 2005) in substantially the form of Exhibit R hereto delivered to the Administrative Agent pursuant to Section 5.25."

"Mortgaged Property Support Documents" means, for each Mortgaged Property, (i) the Title Policy pertaining thereto, (ii) such appraisals, surveys, flood hazard certifications and environmental assessments thereof as the Administrative Agent may require prepared by recognized experts in their respective fields selected by the Administrative Agent, (iii) as to Mortgaged Properties located in a flood hazard area, such flood hazard insurance as the Administrative Agent may require, (iv) with respect to facilities leased or subleased to third parties, such lessees' or sublessees' (in the case of sublessees of any material portion of the Property) estoppel, waiver and consent certificates and subordination, nondisturbance and attornment agreements, (v) such owner's or lessee's or sublessees' (in the case of sublessees of any material portion of the Property) affidavits as the Administrative Agent may require, (vi) such opinions of local counsel with respect to the Mortgages or leasehold mortgages, as applicable, as the Administrative Agent may require, and (vii) such other documentation as the Administrative Agent may reasonably require, in each case as shall be in form and substance reasonably acceptable to the Administrative Agent.

SECTION 2.02. Amendment to Section 3.01(c). Paragraph (c) of Section 3.01 of the Credit Agreement is amended and restated to read in its entirety as follows:

"(c) receipt by the Administrative Agent of an opinion (together with any opinions of local counsel relied on therein, to the extent that an opinion of local counsel in the applicable state has not been previously provided with respect to another Property in the same state) of Cooley Godward LLP, counsel for the Borrowers and Guarantors,

dated as of the Closing Date (or in the case of an opinion delivered pursuant to Section 2.14(d) such later date as specified by the Administrative Agent), substantially in the form of Exhibit P hereto and covering such additional matters relating to the transactions contemplated hereby as the Administrative Agent or any Bank may reasonably request;"

SECTION 2.03. Amendment to Section 4.01. Section 4.01 of the Credit Agreement is amended and restated to read in its entirety as follows:

"SECTION 4.01. Existence and Power. The Company is a corporation, the Operating Partnership is a limited partnership and each Guarantor is a limited liability company or limited partnership duly organized, validly existing and in good standing under the laws of the jurisdiction of its incorporation or organization, as the case may be, is duly qualified to transact business in every jurisdiction where, by the nature of its business, such qualification is necessary, and has all organizational powers and all governmental licenses, authorizations, consents and approvals required to carry on its business as now conducted."

SECTION 2.04. Amendment to Section 4.08. Section 4.08 of the Credit Agreement is amended and restated to read in its entirety as follows:

"SECTION 4.08. Subsidiaries. Each of the Subsidiaries is a limited liability company or limited partnership duly organized, validly existing and in good standing under the laws of its jurisdiction of organization, is duly qualified to transact business in every jurisdiction where, by the nature of its business, such qualification is necessary, and has all organizational powers and all governmental licenses, authorizations, consents and approvals required to carry on its business as now conducted. Each Subsidiary other than the Operating Partnership is organized and governed pursuant to Organizational Documents, the form and contents of which are attached hereto as Exhibit G. No Loan Party has any Subsidiaries except those Subsidiaries listed on Schedule 4.08 and as set forth in any Compliance Certificate provided to the Administrative Agent and Banks pursuant to Section 5.01(c) after the Closing Date, which accurately sets forth each such Subsidiary's complete name and jurisdiction of organization."

SECTION 2.05. Amendment to Section 5.12. Section 5.12 of the Credit Agreement is amended and restated to read in its entirety as follows:

"SECTION 5.12. Maintenance of Existence, etc. Each Loan Party shall, and shall cause each Subsidiary of a Loan Party to, maintain its organizational existence and carry on its business in substantially the same manner and in substantially the same fields as such business is now carried on and maintained. The Operating Partnership shall at all times remain a limited partnership and meet all requirements to maintain its tax qualification as such. Any Subsidiary pledging Collateral hereunder shall be organized as a limited liability company or limited partnership pursuant to Organizational Documents in substantially the form attached hereto as Exhibits G-1 or G-2, respectively."

SECTION 2.06. Amendment to Sections 5.25(b) and (c). Sections 5.25(b) and (c) of the Credit Agreement are amended and restated to read in their entirety as follows:

"(b) The Borrowers shall, and shall cause any Person owning membership or limited partnership interests in a Mortgaged Property Owner or Pledged Mortgage Receivable Owner and each Person owning stock in a corporate general partner of a Mortgaged Property Owner or Pledged Mortgage Receivable Owner that is a limited partnership (each, a "Pledgor Owner") to: (i) to the extent not already a Borrower or Guarantor hereunder, join this Agreement as a Guarantor by executing a Joinder Agreement in the form attached hereto as Exhibit Q; (ii) pledge 100% of the membership or limited partnership interests of any Person which becomes a Mortgaged Property Owner or Pledged Mortgage Receivable Owner after the Closing Date and, in the case of a Mortgaged Property Owner or Pledged Mortgage Receivable Owner that is a limited partnership, also pledge 100% of the stock of the corporate general partner thereof, in each case pursuant to a Membership Pledge Agreement in the form attached hereto as Exhibit R executed and delivered by the Borrower or such Pledgor Owner to the Administrative Agent within ten (10) Domestic Business Days after the day on which such Person became a Mortgaged Property Owner or Pledged Mortgage Receivable Owner; and (iii) deliver to the Administrative Agent such Certificates evidencing such membership interests, limited partnership interests or stock together with transfer powers executed in blank. The Borrowers shall also cause the items specified in Section 3.01(c), (e), (g), (h) and (l) to be delivered to the Administrative Agent concurrently with the Joinder Agreement and Membership Pledge Agreement referred to above, modified appropriately to refer to such Membership Pledge Agreement, Pledgor Owner and such Mortgaged Property Owner or Pledged Mortgage Receivable Owner.

(c) Once any Subsidiary becomes a Mortgaged Property Owner or Pledged Mortgage Receivable Owner and therefore becomes a party to this Agreement and a Guarantor in accordance with Section 5.25(a) or any membership or limited partnership interests of a Mortgaged Property Owner or Pledged Mortgage Receivable Owner are pledged by the Pledgor Owner thereof to the Administrative Agent in accordance with Section 5.25(b) and such Pledgor Owner becomes a party to this Agreement and a Guarantor in accordance with Section 5.25(b), (and, in the case of a Mortgaged Property Owner or Pledged Mortgage Receivable Owner which is a limited partnership, the common stock of the corporate general partner is pledged by the Pledgor Owner thereof pursuant to paragraph (b) above and such Pledgor Owner becomes a party to this Agreement and a Guarantor in accordance with Section 5.25(b)) such Subsidiary or Pledgor Owner (including, without limitation, all Initial Guarantors) thereafter shall remain a party to this Agreement and a Guarantor hereunder and the membership or limited partnership interests in such Mortgaged Property Owner or Pledged Mortgage Receivable Owner (including, without limitation, all initial Mortgaged Property Owners and all initial Pledged Mortgage Receivable Owners) and the common stock of any corporate general partner of a limited partnership pledged hereunder shall remain subject to the pledge to the Administrative Agent, as the case may be, even if such Mortgaged Property Owner or Pledged Mortgage Receivable Owner ceases to be a Mortgaged Property Owner or Pledged Mortgage Receivable Owner, as the case may be; provided that if a Mortgaged Property Owner or Pledged Mortgage Receivable Owner ceases to be

a Subsidiary of the Borrowers as a result of a Borrower's transfer or sale of one hundred percent (100%) of the Capital Securities of such Subsidiary in accordance with and to the extent permitted by the terms of Section 5.14, the Administrative Agent and the Banks agree to release such Subsidiary from the Guaranty and release the membership or limited partnership interests of such Subsidiary from the Membership Pledge Agreement, and, in the case of a corporate general partner of a Mortgaged Property Owner or Pledged Mortgage Receivable Owner which is a limited partnership, release the common stock of such corporate general partner, provided, however, that, notwithstanding the foregoing, if the corporate general partner is also a corporate general partner in another Mortgaged Property Owner or Pledged Mortgage Receivable Owner, the Collateral of which is not required to be released, then the common stock of such corporate general partner shall remain subject to the Membership Pledge Agreement and shall not be released."

SECTION 2.07. Amendment to Section 5.27. Section 5.27 of the Credit Agreement is amended and restated to read in its entirety as follows:

"SECTION 5.27. Partnerships and Joint Ventures. No Loan Party shall become a general partner in any general or limited partnership or a joint venturer in any joint venture except that (i) the Company shall remain the indirect general partner in the Operating Partnership and (ii) corporate Loan Parties which are Wholly Owned Subsidiaries may be general partners in Subsidiaries which are limited partnerships."

SECTION 2.08. Amendment to Section 5.28. Section 5.28 of the Credit Agreement is amended to substitute a comma for the word "and" immediately preceding clause (d) thereof and to add the following new clause (e) at the end of said Section:

"(e) unsecured Guarantees by the Company of Long Term Limited Recourse Mortgage Loans to its Subsidiaries so long as (i) the scope of the Guarantee is limited to a "make-whole" for specifically enumerated (A) acts of malfeasance by the Subsidiary borrower of the Long Term Limited Recourse Mortgage Loan or its Affiliates or (B) intentional or negligent acts or omissions by such Subsidiary borrower or its affiliates resulting in a breach of such borrower's obligations under such mortgage loan documents and (ii) the amount of the Guarantee is limited to the actual damages, losses, costs, liabilities or expenses of the mortgage lender resulting from such malfeasance or breach, provided that, notwithstanding the foregoing, said Guarantees may have full recourse to the Company in the event of any violation of the due on sale or due on encumbrance clauses of the applicable mortgage or upon the voluntary or involuntary bankruptcy of the Subsidiary borrower (other than an involuntary bankruptcy initiated by the mortgage lender), so long as the aggregate principal amount of Long Term Limited Recourse Mortgage Loans guaranteed by Guarantees which contain any full recourse provision upon the voluntary or involuntary bankruptcy of the Subsidiary borrower shall at no time exceed fifty (50) percent of the aggregate principal amount of all Long Term Limited Recourse Mortgage Loans."

SECTION 2.09. Amendment to Section 6.01(r). Paragraph (r) of Section 6.01 of the Credit Agreement is amended and restated to read in its entirety as follows:

"(r) if (i) the Company or the Operating Partnership at any time fails to own (directly or indirectly, through Wholly Owned Subsidiaries) 100% of the outstanding shares of the voting stock (in the case of a corporation) or membership interests (in the case of a limited liability company) or general and limited partnership interests (in the case of a limited partnership) (or equivalent equity interests) of each Subsidiary of the Company or the Operating Partnership or (ii) the Company, or any Wholly Owned Subsidiary of the Company, shall cease to be the sole general partner of the Operating Partnership with full power and discretion to manage and control the business of the Operating Partnership or (iii) any other holder of any interest (limited partnership or otherwise) in the Operating Partnership shall acquire the right (a) to remove the general partner for reasons other than bankruptcy or dissolution of the general partner or (b) to participate in the management or control of, transact business for, or sign for or bind, the Operating Partnership."

SECTION 2.10. Exhibit G – Organizational Documents for Subsidiaries. Exhibit G to the Credit Agreement is hereby amended (i) to add a new first page to such exhibit as set forth on Exhibit G hereto, (ii) to retitle the existing Exhibit G as "Exhibit G-1" and (iii) to add a new Exhibit G-2 as set forth on Exhibit G-2 hereto.

SECTION 2.11. Exhibit R – Membership Pledge Agreement. Exhibit R to the Credit Agreement is hereby amended and restated to read in its entirety as set forth on Exhibit R hereto.

SECTION 3. Waiver of SNDA and Tenant Estoppel Delivery Deadline. The requirements of Section 3.01(g) of the Credit Agreement are hereby waived to the extent necessary to extend the deadline by which the Borrowers must deliver executed tenant estoppel certificates and Subordination Nondisturbance and Attornment Agreements from the date hereof to not later than forty-five (45) days from the date hereof.

SECTION 4. Conditions to Effectiveness. The effectiveness of this Amendment and the obligations of the Administrative Agent and the Banks hereunder are subject to the following conditions, unless the Required Banks waive such conditions:

(a) receipt by the Administrative Agent from each of the parties hereto of a duly executed counterpart of this Amendment signed by such party;

(b) the fact that the representations and warranties of the Borrower contained in Section 6 of this Amendment shall be true on and as of the date hereof.

SECTION 5. No Other Amendment or Waiver. Except for the amendments and waiver set forth above, the text of the Credit Agreement shall remain unchanged and in full force and effect. This Amendment is not intended to effect, nor shall it be construed as, a novation. The Credit Agreement and this Amendment shall be construed together as a single agreement. Nothing herein contained shall waive, annul, vary or affect any provision, condition, covenant or agreement contained in the Credit Agreement, except as herein amended or waived, nor affect nor impair any rights, powers or remedies under the Credit Agreement as hereby amended and waived. The Banks and the Administrative Agent do hereby reserve all of their rights and

remedies against all parties who may be or may hereafter become secondarily liable for the repayment of the Obligations. The Borrower promises and agrees to perform all of the requirements, conditions, agreements and obligations under the terms of the Credit Agreement, as heretofore and hereby amended and waived, the Credit Agreement, as amended, and the other Loan Documents being hereby ratified and affirmed. The Borrower hereby expressly agrees that the Credit Agreement, as amended, and the other Loan Documents are in full force and effect.

SECTION 6. Representations and Warranties. The Borrowers and the Guarantors hereby represent and warrant to the Administrative Agent and each of the Banks as follows:

(a) No Default or Event of Default, nor any act, event, condition or circumstance which with the passage of time or the giving of notice, or both, would constitute an Event of Default, under the Credit Agreement or any other Loan Document has occurred and is continuing.

(b) The Borrowers and the Guarantors each have the power and authority to enter into this Amendment and to do all acts and things as are required or contemplated hereunder to be done, observed and performed by them.

(c) This Amendment has been duly authorized, validly executed and delivered by one or more authorized officers or managers of the Borrowers and the Guarantors and constitutes the legal, valid and binding obligations of the Borrowers and the Guarantors enforceable against each of them in accordance with its terms, provided that such enforceability is subject to general principles of equity.

(d) The execution and delivery of this Amendment and the performance by the Borrowers and the Guarantors hereunder do not and will not require the consent or approval of any regulatory authority or governmental authority or agency having jurisdiction over the Borrowers or the Guarantors nor be in contravention of or in conflict with the articles of incorporation, bylaws, operating agreement or other organizational documents of the Borrower or the Guarantors or the provision of any statute, or any judgment, order or indenture, instrument, agreement or undertaking, to which the Borrowers or the Guarantors is party or by which the assets or properties of the Borrower or the Guarantors are or may become bound.

SECTION 7. Counterparts. This Amendment may be executed in multiple counterparts, each of which shall be deemed to be an original and all of which, taken together, shall constitute one and the same agreement.

SECTION 8. Governing Law. This Amendment shall be construed in accordance with and governed by the laws of the State of North Carolina.

SECTION 9. Effective Date. This Amendment shall be effective as of the date hereof.

IN WITNESS WHEREOF, the parties hereto have executed and delivered, or have caused their respective duly authorized officers or representatives to execute and deliver, this Amendment as of the day and year first above written.

GLADSTONE COMMERCIAL CORPORATION

By: _____ (SEAL)

George Stelljes III
Executive Vice President
and Chief Investment Officer

GLADSTONE COMMERCIAL LIMITED PARTNERSHIP

By: Gladstone Commercial Partners, LLC
its General Partner

By: Gladstone Commercial Corporation
its Manager

By: _____ (SEAL)

George Stelljes III
Executive Vice President
and Chief Investment Officer

EE, 208 SOUTH ROGERS LANE, RALEIGH, NC LLC

By: Gladstone Commercial Limited Partnership
its Manager

By: Gladstone Commercial Partners, LLC
its General Partner

By: Gladstone Commercial Corporation
its Manager

By: _____ (SEAL)

George Stelljes III
Executive Vice President
and Chief Investment Officer

LITTLE ARCH CHARLOTTE NC LLC

By: Gladstone Commercial Limited Partnership
its Manager

By: Gladstone Commercial Partners, LLC
its General Partner

By: Gladstone Commercial Corporation
its Manager

By: _____ (SEAL)

George Stelljes III
Executive Vice President
and Chief Investment Officer

OB CRENSHAW PA GLADSTONE COMMERCIAL LLC

By: Gladstone Commercial Limited Partnership
its Manager

By: Gladstone Commercial Partners, LLC
its General Partner

By: Gladstone Commercial Corporation
its Manager

By: _____ (SEAL)

George Stelljes III
Executive Vice President
and Chief Investment Officer

OB MIDWAY NC GLADSTONE COMMERCIAL LLC

By: Gladstone Commercial Limited Partnership
its Manager

By: Gladstone Commercial Partners, LLC
its General Partner

By: Gladstone Commercial Corporation
its Manager

By: _____ (SEAL)

George Stelljes III
Executive Vice President
and Chief Investment Officer

GCC POCONO LLC

By: Gladstone Commercial Limited Partnership
its Manager

By: Gladstone Commercial Partners, LLC
its General Partner

By: Gladstone Commercial Corporation
its Manager

By: _____ (SEAL)

George Stelljes III
Executive Vice President
and Chief Investment Officer

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BRANCH BANKING AND TRUST COMPANY, as
Administrative Agent and as a Bank

By: _____ (SEAL)

James C. Stallings III
Vice President

[Remainder of this page intentionally left blank]

FIRST HORIZON BANK,
a Division of First Tennessee Bank, NA

By: _____ (SEAL)

J. Jordan O'Neill, III,
Senior Vice President

[Remainder of this page intentionally left blank]

COMPASS BANK

By: _____ (SEAL)

T. Ray Sandefur
Senior Vice President

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EXHIBIT G

[FORM OF ORGANIZATIONAL DOCUMENTS FOR NEW SUBSIDIARIES]

EXHIBIT G-1 — ORGANIZATIONAL DOCUMENTS FOR LLC SUBSIDIARIES

EXHIBIT G-2 — ORGANIZATIONAL DOCUMENTS FOR LIMITED PARTNERSHIP SUBSIDIARIES

AGREEMENT OF LIMITED PARTNERSHIP
OF
[GLADSTONE ENTITY], L.P.

THIS AGREEMENT OF LIMITED PARTNERSHIP ("Agreement") is made and effective for all purposes as of the ___day of ___, 200_, by and between [Gladstone Entity], INC., a Delaware corporation (the "General partner"), and GLADSTONE COMMERCIAL LIMITED PARTNERSHIP, a Delaware limited partnership (the "Limited Partner", and together with the General Partner, the "Partners").

WHEREAS, the Partners desire to join together and form a limited partnership under and pursuant to the Act (as hereinafter defined), and other relevant laws of the State of Delaware, for the purposes and upon the terms and conditions hereinafter set forth.

NOW THEREFORE, the Partners, intending to be legally bound, hereby agree as follows.

SECTION 1
DEFINITIONS

Capitalized words and phrases used in this Operating Agreement have the following meanings:

"**Act**" means the Delaware Revised Uniform Limited Partnership Act, Title 6, Chapter 17 of the Annotated Code of Delaware, as such act may from time to time be amended, including any successor statute.

"**Affiliate**" means, with respect to any Person (i) any individual, corporation, limited liability company, partnership, trust or other legal entity directly or indirectly controlling, controlled by or under common control with such Person, (ii) any officer, director, general partner, member or trustee of such Person or (iii) any individual who is an officer, director, general partner, member or trustee of any Person described in clauses (i) or (ii) of this sentence. For purposes of this definition, the terms "controlling," "controlled by" or "under common control with" shall mean the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a Person, whether through the ownership of voting securities, by contract or otherwise, or the power to elect at least 50% of the directors, general partners, members or persons exercising similar authority with respect to such Person.

"**Agreement**" means this Agreement of Limited Partnership of [GLADSTONE ENTITY], L.P., as amended from time to time, which shall constitute the limited partnership agreement of the Partnership for all purposes of the Act. Words such as "herein," "hereinafter," "hereof," "hereto" and "hereunder" refer to this Agreement as a whole, unless the context otherwise requires.

"**Bankruptcy**" means, with respect to any Person, a "**Voluntary Bankruptcy**" or an "**Involuntary Bankruptcy**." A "**Voluntary Bankruptcy**" means, with respect to any Person (i) the inability of such Person generally to pay its debts as such debts become due, or an admission in writing by such Person of its inability to pay its debts generally or a general assignment by such Person for the benefit of creditors, (ii) the filing of any petition or answer by such Person seeking to adjudicate itself as bankrupt or insolvent, or seeking for itself any liquidation, winding up, reorganization, arrangement, adjustment, protection, relief, or composition of such Person or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking, consenting to, or acquiescing in the entry of an order for relief or the appointment of a receiver, trustee, custodian or other similar official for such Person or for any substantial part of its property or (iii) corporate or other action taken by such Person to authorize any of the actions set forth above. An "**Involuntary Bankruptcy**" means, with respect to any Person, without the consent or acquiescence of such Person, (i) the entering of an order for relief or approving a petition for relief or reorganization or any other petition seeking any reorganization, arrangement, composition, readjustment, liquidation, dissolution or other similar relief under any present or future bankruptcy, insolvency or similar statute, law or regulation, (ii) the filing of any such petition against such Person which petition shall not be dismissed within ninety (90) days, or (iii) without the consent or acquiescence of such' Person, the entering of an order appointing a trustee, custodian, receiver or liquidator of such Person or of all or any substantial part of the property of such Person which order shall not be dismissed within ninety (90) days.

"**Certificate**" means the certificate of formation for the Partnership filed in the office of the Secretary of State of Delaware pursuant to the Act, as originally executed and as amended, modified, supplemented or restated from time to time, as the context requires.

"**General Partner**" means [Gladstone Entity], INC., a Delaware corporation, or any Person who is admitted as a General Partner pursuant to the terms of this Agreement.

"**Indemnified Person**" means the General Partner, any officer of the Partnership appointed by the General Partner, and any Affiliate which performs services for the benefit of the Partnership, each of their respective partners, officers, directors, shareholders, members or employees and such other Persons as the General Partner may designate from time to time, in its sole and absolute discretion.

"**Limited Partner**" means GLADSTONE COMMERCIAL LIMITED PARTNERSHIP, a Delaware limited partnership, or such other Person who is admitted as a limited partner pursuant to the terms of this Agreement.

"**Liquidator**" means the General Partner or such other Person appointed by the Partners acting in the capacity of liquidating trustee of the Partnership.

"**Partners**" means General Partner(s) and Limited Partner(s).

"**Partnership**" means the limited partnership, known as [GLADSTONE ENTITY], L.P., formed pursuant to this Agreement and the Certificate.

"**Person**" means any individual, partnership (whether general or limited), limited liability company, corporation, trust, estate, association, nominee or other entity.

"**Property**" means all real, and if any, personal property acquired by the Partnership and shall include both tangible and intangible property.

SECTION 2
THE PARTNERSHIP

2.1 Name.

The name of the Partnership is [GLADSTONE ENTITY], L.P., and all business of the Partnership shall be conducted in such name or in such other name as the General Partner may designate.

2.2 Purpose; Powers.

(a) The purpose and nature of the business to be conducted by the Partnership is to acquire, own, hold, maintain, manage, operate, improve, develop, construct, finance, pledge, encumber, mortgage, sell, exchange, lease, dispose of and otherwise deal with the Property.

(b) The Partnership shall have the power to do any and all acts necessary, appropriate, proper, advisable, incidental or convenient to or in furtherance of the purposes of the Partnership set forth in this Section 2.2 and has, without limitation, any and all powers that may be exercised on behalf of the Partnership by the General Partner pursuant to Section 6 hereof.

2.3 Principal Place of Business; Agent for Service of Process.

(a) The principal place of business of the Partnership shall be located at such place as determined by the General Partner.

(b) The registered agent for service of process on the Partnership in the State of Delaware shall be Corporation Service Company or any successor as appointed by the General Partner in accordance with the Act. The address for the registered agent shall be

Corporation Service Company
2711 Centerville Road, Suite 400
Wilmington, Delaware 19808

(c) The initial registered office of the Partnership in the State of Delaware is:

[GLADSTONE ENTITY], L.P.
c/o Corporation Service Company
2711 Centerville Road, Suite 400
Wilmington, Delaware 19808

(d) The Partnership may maintain other offices, as determined by the General Partner.

2.4 Term.

The term of the Partnership commenced on the date the Certificate was filed in the Office of the Secretary of State of State of Delaware in accordance with the Act. The Partners intend that the

existence of the Partnership shall continue until the earlier to occur of (i) winding up and liquidation of the Partnership and the completion of its business following a Dissolution Event, as provided in Section 7.1 hereof or (ii) December 31, 2073.

2.5 Title to Property.

All Property owned by the Partnership shall be owned by the Partnership as an entity, and no Partner shall have any ownership interest in such Property in its individual name, and each Partner's interest in the Partnership shall be personal property for all purposes. The Partnership shall hold title to its Property in the name of the Partnership and not in the name of any Partner.

2.6 Payments of Individual Obligations.

The Partnership's credit and assets shall be used solely for the benefit of the Partnership, and no asset of the Partnership shall be transferred or encumbered for, or in payment of, any individual obligation of any Partner.

SECTION 3
CAPITAL CONTRIBUTIONS AND OTHER MATTERS

3.1 Capital Contributions.

The General Partner shall not make any capital contribution to the Partnership and shall receive no ownership interest in the Partnership. The Limited Partnership has or will cause the Property to be deeded to the Partnership as an initial capital contribution. In consideration of such capital contribution, the Limited Partner has received 100% of the partnership interest in the Partnership. Upon the request of the General Partner, the Limited Partner may, but shall not be required to, make subsequent capital contributions to the Partnership.

3.2 Other Matters.

(a) No Partner shall receive any interest, salary or drawing with respect to its capital contribution or for services rendered on behalf of the Partnership or otherwise, in its capacity as a Partner, except as otherwise provided in this Agreement.

(b) The Limited Partner shall not be liable for the debts or any other obligations of the Partnership, nor shall any Partner be required to guarantee any debts, liabilities, contracts or obligations of the Partnership.

(c) No Partner shall be required to lend any funds to the Partnership.

(d) No Partner shall receive any salary or other compensation for services rendered on behalf of the Partnership. Notwithstanding the foregoing, the Partnership may enter into a property management agreement or other services agreement with a Partner or an Affiliate of a Partner.

SECTION 4
PROFIT, LOSS, INCOME AND DEDUCTIONS; DISTRIBUTIONS

4.1 Determination of Profit and Loss. The profit and loss of the Partnership shall be determined in accordance with the accounting methods followed for federal income tax purposes and otherwise in accordance with sound accounting principles and procedures applied in a consistent manner. An accounting shall be made for each taxable year by the accountants employed by the Partnership as soon as possible after the close of each such taxable year to determine the profit or loss of the Partnership, which shall be credited or debited, as the case may be, 100% to the Limited Partner.

4.2 Allocation of Profits, Losses, Income and Deductions; Distributions.

(a) One hundred percent (100%) of the profits, losses, income and deductions of the Partnership shall be allocated to the Limited Partner. One hundred percent (100%) of all cash of the Partnership available for distribution shall be distributed to the Limited Partner. The General Partner may make distributions of available cash or other assets to the Limited Partner from time to time in its discretion, and shall make a distribution of available cash or other assets to the Limited Partner upon any written request therefor from the Limited Partner.

(b) It is the intent of the Partners that the Partnership shall be treated as a disregarded entity for income tax purposes, with all items of profit, loss, income and deduction of the Partnership allocated to and reported by the Limited Partner. In the event that the Partnership is treated as a partnership for income tax purposes, the provisions of Section 4.2(c) below shall apply.

(c) In the event that the Partnership is treated as a partnership for income tax purposes, the following provision shall apply:

(i) Subject to (ii) through (v) below, one hundred percent (100%) of the profits, losses, income and deductions of the Partnership shall be allocated to the Limited Partner.

(ii) Notwithstanding anything to the contrary contained in this Section 4.2(c), the Partnership shall comply with Treasury Regulation section 1.704-2, as amended, with respect to the allocation of deductions and the charge back of minimum gain on nonrecourse debts of the Partnership.

(iii) Notwithstanding anything to the contrary contained in this Section 4.2(c), no Partner shall be allocated a net loss which would cause or increase a deficit balance in its capital account in excess of any actual or deemed obligation of such Partner to restore deficits (as defined in Treasury Regulation Section 1.704-1(b)(2)(ii)(c) and the penultimate sentences of Treasury Regulation Sections 1.704-2(g)(1) and 1.704 2(i)(5)). If any Partner shall receive with respect to the Partnership an adjustment, allocation or distribution in the

nature described in Treasury Regulation section 1.704-1(b)(2)(ii)(d)(4)-(6), as amended, which causes or increases a deficit in such Partner's capital account, such Partner shall be allocated items of income and gain in an amount and manner as will eliminate such deficit balance as quickly as possible. It is intended that this Section 4.2(c)(iii) shall constitute a "qualified income offset" within the meaning of Treasury Regulation section 1.704-1(b)(2)(ii)(d)(3), as amended.

(iv) Any allocations required pursuant to Section 4.2(c)(iii) above shall be taken into account in allocating profits, losses, income and deductions pursuant to Section 4.2(c)(i) above, so that, to the extent possible, the cumulative amount of such allocations shall be equal to the cumulative amount that would have been allocated to the Limited Partner if the allocations pursuant to Section 4.2(c)(iii) above had not occurred.

(v) Notwithstanding anything to the contrary contained in this Section 4.2(c), any portion of any income, gain, loss or deduction with respect to property contributed to the Partnership by a Partner shall be allocated among the Partners in accordance with Internal Revenue Code section 704(c) and Treasury Regulation section 1.704-3, as amended, so as to take account of the variation, if any, between the adjusted tax basis of such property to the Partnership and its fair market value at the time of the contribution, provided, however, that allocation to Partners under this Section 4.2(c)(v) shall not affect a Partner's capital account to the extent such amounts have previously been reflected in such capital account.

(vi) A capital account (which shall be a book account) shall be established and maintained for each Partner in a manner determined by the General Partner to be in compliance with Treasury Regulation section 1.704-1(b)(2)(iv), as amended. All distributions to the Partners made in connection with a liquidation of the Partnership shall be made to the Partners based on their respective positive capital account balances, after such balances have been adjusted to reflect all allocations and distributions for all periods (and the Partners hereby acknowledge that it is their intent that all such distributions in liquidation shall be made solely to the Limited Partner).

(vii) The General Partner shall be the Tax Matters Partner of the Partnership as provided in section 6231 of the Internal Revenue Code. The Partnership shall reimburse the Tax Matters Partner for any expenses incurred by the Tax Matters Partner in connection with the performance of its duties as Tax Matters Partner. The General Partner shall have the power to make such elections under

the tax laws of the United States, the several states and other relevant jurisdictions as to the treatment of items of Partnership income, gain, loss, deduction and credit, and to all other relevant matters, as it deems necessary or desirable.

SECTION 5
ADMISSION OF ADDITIONAL OR SUBSTITUTE PARTNERS

5.1 Admission of Additional or Substitute Partners. No additional or substitute General or Limited Partner may be admitted to the Partnership without the consent of all Partners. Each additional or substitute Partner shall, upon its admission as a Partner, agree in writing to be bound by all of the terms, provisions and conditions of this Agreement.

SECTION 6
MANAGEMENT AND INDEMNIFICATION.

6.1 Actions by the Limited Partner. The Limited Partner, in its capacity as a Limited Partner, shall not have authority to act for or on behalf of the Partnership, or to bind the Partnership in any way solely by virtue of being a partner of the Partnership.

6.2 Authority of the General Partner.

(a) The General Partner shall manage the business and affairs of the Partnership. The General Partner shall have full, exclusive and complete discretion, power and authority, subject in all cases to the provisions of this Agreement and the requirements of applicable law, to manage, control, administer and operate the business and affairs of the Partnership for the purposes herein stated, to make all decisions affecting such business and affairs, to adopt such accounting rules and procedures as it deems appropriate in the conduct of the business and affairs of the Partnership and to do all things it deems necessary or desirable in the conduct of the business and affairs of the Partnership. The General Partner has full power and discretion to cause the Partnership to borrow money, pledge, mortgage, and assign the Property and to enter into guarantees. The General Partner may appoint and delegate responsibilities to such officers and other agents, as it deems appropriate in its sole discretion.

(b) Any Person dealing with the Partnership shall be entitled to assume that the General Partner has full power and authority to encumber, sell or otherwise use in any manner any and all assets of the Partnership and to enter into any contracts on behalf of the Partnership, and such Person shall be entitle to deal with the General Partner as if it were the Partnership's sole party in interest, both legally and beneficially. In no event shall any Person dealing with the General Partner or its representatives be obligated to ascertain that the terms of this Agreement have been complied with or to inquire into the necessity or expedience of any act or action of the General Partner or its representatives. Each and every certificate, document or other instrument executed on behalf of the Partnership by the General Partner or its representatives shall be conclusive evidence in favor of any and every Person relying thereon or claiming thereunder that (i) at the time of the execution and delivery of such certificate, document or instrument, this Agreement was in full force and effect, (ii) the Person executing

and delivering such certificate, document or instrument was duly authorized and empowered to do for and on behalf of the Partnership, and (iii) such certificate, document or instrument was duly executed and delivered in accordance with the terms and provisions of this Agreement and is binding upon the Partnership.

6.3 Indemnification of Indemnified Persons. The Partnership shall defend, indemnify, and save harmless each Indemnified Person for all loss, liability, damage, cost, or expense (including reasonable attorneys' fees) incurred by reason of any demands, claims, suits, actions, or proceedings arising out of (a) the Indemnified Person's relationship to the Partnership or (b) such Indemnified Person's capacity as the General Partner or an officer, except for such loss, liability, damage, cost, or expense as arises out of the theft, fraud, willful misconduct, or gross negligence by such Indemnified Person. Expenses incurred in defending a civil or criminal action, suit or proceeding shall be paid by the Partnership in advance of the final disposition of such action, suit or proceeding, and not less often than monthly upon receipt of an undertaking by and on behalf of the. Indemnified Person to repay such amount if it shall be ultimately determined that he or she is not entitled to be indemnified by the Partnership.

SECTION 7
DISSOLUTION AND WINDING UP

7.1 Dissolution Events. The Partnership shall be dissolved and its affairs wound up upon the expiration of the term of the Partnership as provided in Section 2.4 or upon the happening of any of the following:

(a) the sale or disposition of all or substantially all of the Partnership assets, and the distribution of the proceeds thereof to the Limited Partner;

(b) the decision by the Partners to dissolve;

(c) the occurrence of an event that makes it unlawful for the Partnership's business to be continued;

(d) the entry by a court of competent jurisdiction of a decree of judicial dissolution of the Partnership; or

(e) the liquidation, dissolution or Bankruptcy of the General Partner, unless within 90 days after such occurrence the Limited Partner elects to continue the Partnership and elects a new general partner, and such new general partner agrees in writing to be bound by all of the terms, provisions and conditions of the Agreement.

7.2 Winding Up. Upon dissolution under Section 7.1, no further business shall be conducted by the Partnership except for the taking of such action as shall be necessary for the winding-up of the affairs of the Partnership and the distribution of its assets to the Limited Partner pursuant to the provisions hereof, and thereupon the General Partner (or such other Person approved by the Partners) shall act as the Liquidator of the Partnership within the meaning of the Act and immediately proceed to wind up and terminate the business and affairs of the Partnership.

7.3 Sale of Partnership Assets. Upon dissolution, the Liquidator shall sell such of the Partnership assets as it deems necessary or appropriate. In lieu of the sale of the Property, the Liquidator may convey, distribute and assign all or any part of Property to the Limited Partner in such form of ownership as shall be determined by the Liquidator to be applicable to the jurisdiction where the Property is located. A full accounting shall be made of the accounts of the Partnership and of the Partnership's assets, liabilities and income, from the date of the last accounting to the date of such dissolution. The profits and losses of the Partnership shall be determined to the date of dissolution and transferred as provided in Section 4, to the Limited Partner.

7.4 Distribution of Assets. The Liquidator shall apply the remaining Partnership assets, in the following order of priority:

(a) first, to the payment and discharge of, or the making of reasonable provisions for, all of the Partnership's debts and liabilities to Persons other than the Limited Partner, including contingent, conditional and unmatured liabilities of the Partnership, and the expenses of dissolution and winding-up, in the order of priority as provided by law, including the establishment of a reserve fund for contingent, conditional and unmatured claims as deemed necessary and reasonable by the Liquidator;

(b) second, to the payment and discharge of, or the making of reasonable provisions for, all of the Partnership's debts and liabilities to the Limited Partner; and

(c) third, all remaining assets to the Limited Partner.

SECTION 8
SEPARATENESS COVENANTS

8.1 Affirmative Covenants. The Partnership shall (i) maintain its accounts, books and records separate from any other person or entity, (ii) maintain its books, records, resolutions and agreements as official records, (iii) hold its assets in its own name, (iv) conduct its business in its own name (provided that any Partner or its Affiliates may provide management or other services for the Partnership), (v) maintain its internal financial statements, accounting records and other entity documents separate from any other person or entity (provided that its external financial statements and tax returns may be prepared on a consolidated basis with other entities), (vi) hold itself out and identify itself as a separate and distinct entity under its own name and not as a part of any person or entity, (vii) correct any known misunderstanding regarding its separate identity, and (viii) observe all limited partnership formalities.

SECTION 9
MISCELLANEOUS

9.1 Variation of Terms. All terms and any variations thereof shall be deemed to refer to masculine, feminine, or neuter, singular or plural, as the identity of the Person or Persons may require.

9.2 Governing Law. The laws of the State of Delaware (other than the choice of law provisions thereat) shall govern the validity of this Agreement, the construction of its terms, and the interpretation of the rights and duties arising hereunder.

9.3 Waiver. Any of the terms and conditions of this Agreement may be waived in whole or in part, but only by an agreement in writing making specific reference to this Agreement and executed by the party entitled to the benefit thereof.

9.4 Binding Agreement and Successors. This Agreement shall be binding upon and shall inure to the benefit of the Partners and their successors and assigns.

9.5 No Third-Party Beneficiaries. Except as otherwise expressly provided in this Agreement, nothing in this Agreement is intended to confer upon any Person other than the parties hereto any rights or remedies.

9.6 Section Headings. Section headings contained in this Agreement are for convenience of reference only and shall not limit or otherwise affect the meaning or interpretation of this Agreement or any of its terms and conditions.

9.7 Interest Held for Investment. The Limited Partner does hereby represent and warrant by the execution of this Agreement that its interest in the Partnership was obtained for investment purposes only and not for resale or distribution.

9.8 Securities Laws Restrictions. The interests described. in this Agreement have not been registered under the Securities Act of 1933, as amended, or under the securities laws of the

State of Delaware or any other jurisdiction. Consequently, these interests may not be sold, transferred, assigned, pledged, hypothecated or otherwise disposed of, except in accordance with the provisions of such laws and this Agreement.

IN WITNESS WHEREOF, the undersigned parties have executed and entered into this Agreement effective as of the day first above set forth.

GENERAL PARTNER:

[GLADSTONE ENTITY], INC., a Delaware corporation

By: _____
[Name], [Title]

LIMITED PARTNER:

GLADSTONE COMMERCIAL LIMITED PARTNERSHIP, a Delaware limited partnership

By: Gladstone Commercial Partners, LLC, its General Partner

By: Gladstone Commercial Corporation, its Manager

By: _____
[Name], [Title]

EXHIBIT G-2

STATE *of* DELAWARE
CERTIFICATE *of* LIMITED PARTNERSHIP

- **The Undersigned**, desiring to form a limited partnership pursuant to the Delaware Revised Uniform Limited Partnership Act, 6 Delaware Code, Chapter 17, do hereby certify as follows:

- **First**: The name of the limited partnership is [Gladstone entity] L.P.

- **Second**: The name and address of the Registered Agent is:

  Corporation Service Company
  2711 Centerville Road, Suite 400
  Wilmington, Delaware 19805

- Third: The name and mailing address of the general partner is as follows:

  ___, Inc.
  1251 West Branch Road
  Suite 200
  McLean, Virginia 22102

- **In Witness Whereof**, the undersigned has executed this Certificate of Limited Partnership as of the ___day of ___200_.

BY: ___, INC., a Delaware corporation
(General Partner)

NAME: _____

[Name], [Title]

EXHIBIT G-2

WRITTEN CONSENT

OF THE GENERAL PARTNER OF

[GLADSTONE ENTITY], L.P.

Dated as of _____ __, 200_

The undersigned, being the general partner of **[Gladstone Entity], L.P.**, a Delaware limited partnership (the "Partnership"), pursuant to the partnership agreement of the Partnership does hereby consent in writing, without a meeting, to the following actions, and directs that this Consent be filed with the minutes of proceedings of the Partnership:

WHEREAS, the Company was formed pursuant to filing of the Certificate of Formation with the Secretary of State of the State of Delaware on ___, 200___ (the "Formation Date").

RESOLVED, that all of the acts and transactions of the manager and officers of the Company which have been taken or made prior to or since the Formation Date and all other acts and transactions taken or made in furtherance of the purposes of the Company be, and they hereby are, ratified and approved.

[Gladstone Entity], INC.

By: _____
[Name], [Title]

EXHIBIT R

EQUITY PLEDGE AGREEMENT

[Formerly Titled "Membership Pledge Agreement"]

THIS EQUITY PLEDGE AGREEMENT (this "Agreement") dated as of this ___day of March, 2005, between Gladstone Commercial Corporation, a Maryland corporation, Gladstone Commercial Limited Partnership, a Delaware limited partnership (together, the "Pledgors") and Branch Banking and Trust Company, a national banking association ("BB&T"), acting as Administrative Agent (in such capacity, the "Administrative Agent") for itself and the other Secured Parties (as defined in the Credit Agreement referred to below).

W I T N E S S E T H

WHEREAS, the Administrative Agent and the Banks (as defined in the Credit Agreement) have agreed to extend credit to the Pledgors pursuant to the terms of that certain Credit Agreement of even date herewith (as amended, restated, or otherwise modified from time to time, the "Credit Agreement") among the Pledgors, the Administrative Agent and the Banks signatory thereto;

WHEREAS, the Pledgors beneficially and legally own the limited liability company membership interests, limited partnership interests and stock in the Subsidiaries of the Borrowers described on Exhibit A attached hereto (the "Pledged Subsidiaries"), which membership interests, limited partnership interests and stock comprise all of the outstanding membership interests, limited partnership interests and stock in each such Subsidiary;

WHEREAS, Pledgors, as Borrowers under the Credit Agreement and as holders of all the outstanding equity interests of each Pledged Subsidiary (other than the general partnership interests in the Pledged Subsidiaries which are limited partnerships) will derive material benefit from Banks' extension of credit to the Pledgors pursuant to the Credit Agreement; and

WHEREAS, it is a condition of Banks' agreement to extend credit to Borrowers pursuant to the Credit Agreement that the Administrative Agent, on behalf of the Secured Parties (as defined in the Credit Agreement), receive a pledge of the Collateral (as defined below) hereunder by the Pledgors' execution and delivery of this Agreement to secure: (a) the due and punctual payment by the Borrowers of: (i) the principal of and interest on the Notes, when and as due, whether at maturity, by acceleration, upon one or more dates set for prepayment or otherwise and any renewals, modifications or extensions thereof, in whole or in part; (ii) each payment required to be made by the Borrowers under the Credit Agreement and Letter of Credit Agreements in respect of any of the Letters of Credit, when and as due, including payments in respect of reimbursement of disbursements, interest thereon, and obligations, if any, to provide cash collateral and any renewals, modifications or extensions thereof, in whole or in part; and (iii) all other monetary obligations of the Borrowers to the Secured Parties under the Credit Agreement and the other Loan Documents to which the Borrowers are or are to be a party and any renewals, modifications or extensions thereof, in whole or in part; (b) the due and punctual performance of all other obligations of the Borrowers under the Credit Agreement and the other Loan

Documents to which the Borrowers are or are to be a party, and any renewals, modifications or extensions thereof, in whole or in part and (c) the due and punctual payment and performance of all obligations of each of the Guarantors under the Credit Agreement and the other Loan Documents to which they are or are to be a party and any and all renewals, modifications or extensions thereof, in whole or in part (all of the foregoing indebtedness, liabilities and obligations being collectively called the "Obligations").

NOW, THEREFORE, in consideration of the premises and of the mutual covenants herein contained, and for other good and valuable consideration, the receipt and adequacy of which are hereby acknowledged, the parties hereby agree as follows:

SECTION 1. Definitions. Any capitalized terms used but not defined herein shall have the meanings assigned to them in the Credit Agreement.

SECTION 2. Pledge. As collateral security for the due and punctual payment of the Obligations, each Pledgor hereby pledges, hypothecates, delivers and assigns and grants unto Administrative Agent, as Administrative Agent for itself and the Secured Parties, a security interest (which security interest shall constitute a first priority security interest), in all of the Pledgor's membership interests, limited partnership interests and common stock in the Pledged Subsidiaries and all securities instruments or other rights convertible into or exercisable for the foregoing (the "Equity Interests"), together with all proceeds, profits, interests, capital accounts, accounts, contract rights, general intangibles, deposits, funds, dividends, distributions, rights to distributions, including both distributions of money and of property, and other rights, claims and interests relating to or arising out of Pledgor's Equity Interests, now owned or hereafter acquired, in the Pledged Subsidiaries, together with any and all replacements or substitutions for or proceeds of all of the foregoing (collectively, the "Collateral"), and each Pledgor hereby delivers to Administrative Agent, on behalf of the Secured Parties, including itself, the certificates, instruments or other documents, if any, evidencing or representing the Collateral. This Agreement is not intended to place Administrative Agent or any Secured Party in a position of being a member or partner of any Pledged Subsidiary, but is intended to grant Administrative Agent, on behalf of the Secured Parties, a lien on and security interest in Pledgor's Equity Interests in the Pledged Subsidiaries including, without limitation, any and all of the Collateral but specifically excluding any general partnership interests.

SECTION 3. Representations and Warranties. Each Pledgor hereby represents and warrants that:

(a) Pledgor has all requisite power and authority to enter into this Agreement, to grant a security interest in the Collateral for the purposes described in Section 2 and to carry out the transactions contemplated by this Agreement;

(b) No approval of or consent from any person or entity (other than the acknowledgement and consent of the Pledged Subsidiaries as evidenced by their signature hereto) is required in connection with the execution and delivery by Pledgor of this Agreement, the granting of the security interests in the Collateral, or the carrying out of the transactions contemplated by this Agreement;

(c) Pledgor is the direct and beneficial owner of the Collateral as of the date hereof;

(d) All of the Collateral is owned by the Pledgor free and clear of any pledge, mortgage, hypothecation, lien, charge, encumbrance or any security interest in such Collateral or the proceeds thereof, except for the security interest granted to the Administrative Agent on behalf of the Secured Parties hereunder;

(e) The execution, delivery and performance by Pledgor of this Agreement do not and will not contravene or constitute a default under or result in any violation of any agreement (including, without limitation, the operating or partnership agreement of any Pledged Subsidiary), indenture or other instrument, license, judgment, decree, order, law, statute, ordinance or other governmental rule or regulation applicable to Pledgor;

(f) Each Pledged Subsidiary is a limited liability company, limited partnership or corporation duly formed, validly existing and in good standing as such under the laws of the State of its organization as set forth on Exhibit A hereto, and the execution and delivery of this Agreement are within the limited liability company, partnership or corporate powers of such Pledged Subsidiary, have been duly authorized by all necessary limited liability company, partnership or corporate action, require no action by or in respect of, or filing with, any governmental body, agency or official (except for the Uniform Commercial Code filings set forth in paragraph (g) below) and do not contravene, or constitute a default under, the operating agreement, partnership agreement, charter or by-laws of such Pledged Subsidiary;

(g) Upon filing of a Uniform Commercial Code Financing Statement with the Maryland Secretary of State, in the case of Gladstone Commercial Corporation and with the Delaware Secretary of State, in the case of Gladstone Commercial Limited Partnership, this Agreement creates and grants a valid lien on and perfected security interest in the Collateral and the proceeds thereof, subject to no prior security interest, lien, charge or encumbrance, or to any agreement purporting to grant to any third party a security interest in the property or assets of the Pledgor which would include the Collateral; and

(h) A true, correct and complete copy of the operating agreement, limited partnership agreement, charter and by-laws, as the case may be, of each Pledged Subsidiary (together with all amendments thereto) has been provided to the Administrative Agent.

SECTION 4. Voting Rights; Distributions, Etc.

(a) So long as no Event of Default, as defined in the Credit Agreement, shall have occurred and be continuing:

(i) each Pledgor shall be entitled to exercise any and all voting and/or consensual rights and powers relating or pertaining to the Collateral or any part thereof, provided, however, that no vote shall be cast or right exercised or other action taken which would impair the Collateral or which would be inconsistent

with or result in any violation of the provisions of this Agreement, the Credit Agreement or any other Loan Document,

(ii) except to the extent limited by this Agreement, the Credit Agreement or any other Loan Document, each Pledgor shall be entitled to receive and retain any and all cash dividends or cash distributions payable on the Collateral, but any and all equity interests and/or liquidating dividends, distributions in property, returns of capital, or other distributions made on or in respect of the Collateral, whether resulting from a subdivision, combination, or reclassification of the outstanding ownership units or other interests of the Pledged Subsidiaries or received in exchange for the Collateral or any part thereof or as a result of any merger, consolidation, acquisition, or other exchange of assets to which any Pledged Subsidiary may be a party or otherwise, and any and all cash and other property received in redemption of or in exchange for any Collateral (either upon call for redemption or otherwise), shall be and become part of the Collateral pledged hereunder and, if received by the Pledgor, shall forthwith be delivered to Administrative Agent (accompanied by proper instruments of assignment and/or powers of attorneys executed by the Pledgor) to be held subject to the terms of this Agreement;

(b) Upon the occurrence and during the continuance of an Event of Default, all rights of either Pledgor to exercise the voting and/or consensual rights and powers that such Pledgor is entitled to exercise pursuant to Section 4(a)(i) hereof and/or to receive the payments that such Pledgor is authorized to receive and retain pursuant to Section 4(a)(ii) hereof shall cease, and all such rights shall thereupon become vested in Administrative Agent for the benefit of the Secured Parties, who shall have the sole and exclusive right and authority to exercise such voting and/or consensual rights and powers and/or to receive and retain such payments; provided, that nothing herein shall obligate Administrative Agent to exercise such voting and/or consensual rights, all such action in such regard being solely in Administrative Agent's or Secured Parties' discretion. Any and all money and other property paid over to or received by Administrative Agent pursuant to the provisions of this paragraph (b) shall be retained by Administrative Agent as additional Collateral hereunder and be applied in accordance with the provisions hereof.

SECTION 5. Covenants. Each Pledgor hereby covenants that until such time as the Obligations shall have been indefeasibly paid in full:

(a) Pledgor will not, without the prior written consent of the Administrative Agent, sell, convey, assign, or otherwise dispose of all or any part of the Collateral or any interest therein, except that prior to an Event of Default, Pledgor shall be permitted to receive and dispose of distributions to the extent permitted by Section 4 above; nor will the Pledgor create, incur or permit to exist any pledge, mortgage, lien, charge, encumbrance or security interest whatsoever with respect to all or any part of the Collateral or the proceeds thereof, other than that created hereby; nor will the Pledgor amend the operating agreement, limited partnership agreement or charter of any Pledged Subsidiary or consent to or permit any amendment thereof; nor will Pledgor consent to or

permit the issuance of any additional Equity Interests in any Pledged Subsidiary (unless pledged to Administrative Agent hereunder), or any securities or instruments exercisable or exchangeable for Equity Interests in any Pledged Subsidiary or otherwise representing any right to acquire any Equity Interest in any Pledged Subsidiary or any general partnership interests in any Pledged Subsidiary that is a limited partnership.

(b) Pledgor will not permit any Pledged Subsidiary to change its entity form and will give to Administrative Agent not less than 30 days prior written notice of (i) any change in its name or the name of any Pledged Subsidiary or (ii) any change in the location of the principal place of business of Pledgor or any Pledged Subsidiary.

(c) Pledgor will, at Pledgor's own expense, defend Administrative Agent's and Secured Parties' right, title, special property and security interest in and to the Collateral and any distributions with respect thereto against the claims of any person, firm, corporation or other entity.

(d) Pledgor will preserve and protect the Collateral.

(e) Pledgor will promptly pay and discharge before the same become delinquent, all taxes, assessments and governmental charges or levies imposed on Pledgor or the Collateral, except for taxes timely disputed in good faith, for which adequate reserves have been made.

(f) The Secured Parties shall have the right, upon request, to review, examine and audit the books and records of any Pledged Subsidiary and of any Pledgor with regard to the Collateral and any distributions with respect thereto. Each Secured Party's costs and expenses incurred in connection with any such review, examination or audit shall be paid by Pledgors.

SECTION 6. Remedies upon Default. Upon the occurrence of an Event of Default as defined in the Credit Agreement, Administrative Agent may, in addition to the exercise by Administrative Agent of its rights and remedies under any other Section of this Agreement or under the Credit Agreement or any other agreement relating to the Obligations or otherwise available to it at law or in equity:

(a) declare the principal of and all accrued interest on and any other amounts owing with respect to the Obligations immediately due and payable, without demand, protest, notice of default, notice of acceleration or of intention to accelerate or other notices of any kind, and

(b) exercise all the rights and remedies of a secured party under the Uniform Commercial Code in effect in the State of North Carolina at that time and sell (in compliance with applicable laws, including securities laws) the Collateral, or any part thereof, at public or private sale, at any broker's board, upon any securities exchange, or elsewhere, for cash, upon credit, or for future delivery, as Administrative Agent may deem appropriate in the circumstances and commercially reasonable. Administrative Agent shall have the right to impose limitations and restrictions on the sale of the Collateral as Administrative Agent may deem to be necessary or appropriate to comply

with any law, rule, or regulation (Federal, state, or local) having applicability to the sale, including, but without limitation, restrictions on the number and qualifications of the offerees and requirements for any necessary governmental approvals, and Administrative Agent shall be authorized at any such sale (if it deems it necessary or advisable to do so) to restrict the prospective offerees or purchasers to persons who will represent and agree that they are purchasing securities included in the Collateral for their own account and not with a view to the distribution or sale thereof in violation of applicable securities laws and each Pledgor hereby waives, to the maximum extent permitted by law, any claim arising because the price at which the Collateral may have been sold at such private sale was less than the price that might have been obtained at public sale, even if Administrative Agent accepts the first offer received and does not offer such Collateral to more than one offeree. Upon consummation of any such sale, Administrative Agent shall have the right to assign, transfer, and deliver to the purchaser or purchasers thereof the Collateral so sold. Each such purchaser at any such sale shall hold the property sold absolutely free from any claim or right on the part of each Pledgor, and the Pledgor hereby waives (to the extent permitted by law) all rights of redemption, stay, and/or appraisal that the Pledgor now has or may at any time in the future have under any rule of law or statute now existing or hereafter enacted. To the extent that notice of sale shall be required to be given by law, Administrative Agent shall give the Pledgor at least ten (10) days' prior written notice of its intention to make any such public or private sale. Such notice shall state the time and place fixed for sale, and the Collateral, or portion thereof, to be offered for sale. Any such sale shall be held at such time or times within ordinary business hours and at such place or places as Administrative Agent may fix in the notice of such sale. At any such sale, the Collateral, or portion thereof, to be sold may be sold in one lot as an entirety or in separate parcels, as Administrative Agent may determine, and Administrative Agent may itself bid (which bid may be in whole or in part in the form of cancellation of the Obligations) for and purchase the whole or any part of the Collateral. Administrative Agent shall not be obligated to make any sale of the Collateral if it shall determine not to do so, regardless of the fact that notice of sale of the Collateral may have been given. Administrative Agent may, without notice or publication, adjourn any public or private sale or cause the same to be adjourned from time to time by announcement at the time and place fixed for sale, and such sale may, without further notice, be made at the time and place to which the same was so adjourned. In case sale of all or any part of the Collateral is made on credit or for future delivery, the Collateral so sold may be retained by Administrative Agent until the sale price is paid by the purchaser or purchasers thereof, but Administrative Agent shall not incur any liability in case any such purchaser or purchasers shall fail to take up and pay for the Collateral so sold and, in case of any such failure, such Collateral may be sold again upon like notice. Each Pledgor hereby agrees that any sale or disposition of the Collateral conducted in conformity with reasonable commercial practices of banks, insurance companies or other financial institutions in the city and state where Administrative Agent is located in disposing of property similar to the Collateral shall be deemed to be commercially reasonable.

SECTION 7. Application of Proceeds of Sale. The proceeds of sale of the Collateral sold pursuant to Section 6 hereof shall be applied by Administrative Agent as set forth in Section 6.04 of the Credit Agreement.

SECTION 8. Administrative Agent Appointed Attorney-in-Fact. Each Pledgor hereby appoints Administrative Agent the Pledgor's attorney-in-fact, with full power of substitution, for the purpose of carrying out the provisions of this Agreement and taking any action and executing any instrument that Administrative Agent may deem necessary or advisable to accomplish the purposes hereof, which appointment is coupled with an interest and is irrevocable. Without limiting the generality of the foregoing, after the occurrence of an Event of Default as defined in the Credit Agreement, Administrative Agent shall have the right and power to receive, endorse, and collect all checks and other orders for the payment of money made payable to Pledgor representing any dividend or other distribution payable or distributable in respect of the Collateral or any part thereof, and to give full discharge for same.

SECTION 9. Responsibility. Notwithstanding the provisions of Section 4(b) hereof, Administrative Agent shall have no duty to exercise any voting and/or consensual rights and powers becoming vested in Administrative Agent with respect to the Collateral or any part thereof, to exercise any right to redeem, convert, or exchange any securities included in the Collateral, to enforce or see to the payment of any dividend or any other distribution payable or distributable on or with respect to the Collateral or any part thereof, or otherwise to preserve any rights in respect of the Collateral against any third parties.

SECTION 10. No Waiver: Cumulative Remedies. No failure on the part of Administrative Agent to exercise, and no delay in exercising, any right, power, or remedy hereunder shall operate as a waiver thereof, nor shall any single or partial exercise of any such right, power or remedy by Administrative Agent preclude any other or further exercise thereof or the exercise of any other right, power or remedy. All remedies of Administrative Agent hereunder are cumulative and are not exclusive of any other remedies available to Administrative Agent at law or in equity.

SECTION 11. Termination. This Agreement shall terminate upon the complete performance of each Loan Party's obligations under each Loan Document and the final and indefeasible payment in full of the Obligations. Upon termination of this Agreement, Administrative Agent shall reassign and redeliver (or cause to be reassigned or redelivered) to the Pledgors such Collateral (if any) as shall not have been sold or otherwise applied by Administrative Agent pursuant to the terms hereof and as shall still be held by it hereunder together with appropriate instruments of assignment and release.

SECTION 12. Notices. Any notice or communication required or permitted hereunder shall be given in the manner prescribed in the Credit Agreement.

SECTION 13. Further Assurances. Each Pledgor agrees to do such further acts and things, and to execute and deliver such agreements and instruments, as Administrative Agent may at any time reasonably request in connection with the administration or enforcement of this Agreement or related to the Collateral or any part thereof or in order better to assure and confirm unto Administrative Agent and the Secured Parties their rights, powers and remedies hereunder. Each Pledgor hereby authorizes Administrative Agent to file one or more Uniform Commercial Code financing or continuation statements, or amendments thereto, relative to all or any part of the Collateral.

SECTION 14. Binding Agreement. This Agreement and the terms, covenants, and conditions hereof, shall be binding upon and inure to the benefit of the parties hereto, and their respective heirs, executors, administrators, successors and assigns.

SECTION 15. Modification. Neither this Agreement nor any provisions hereof may be amended, modified, waived, discharged, or terminated, nor may any of the Collateral be released or the pledge or the security interest created hereby extended, except by an instrument in writing signed by the parties hereto.

SECTION 16. Severability. In case any lien, security interest, or other right of Administrative Agent hereunder shall be held to be invalid, illegal, or unenforceable, such invalidity, illegality, and/or unenforceability shall not affect any other lien, security interest, or other right of Administrative Agent hereunder.

SECTION 17. Governing Law. This Agreement (including matters of construction, validity, and performance) , the rights, remedies, and obligations of the parties with respect to the Collateral to the extent not provided for herein, and all matters concerning the validity, perfection, and the effect of non-perfection of the pledge contemplated hereby, shall be governed by and construed in accordance with the laws of the State of North Carolina or other mandatory applicable laws. Notwithstanding anything herein, EACH PLEDGOR AGREES TO SUBMIT TO THE JURISDICTION OF THE COURTS OF THE STATE OF NORTH CAROLINA AND THE UNITED STATES DISTRICT COURTS SITTING THEREIN IN ANY ACTION TAKEN BY ADMINISTRATIVE AGENT RELATING TO THIS AGREEMENT OR ANY PROVISIONS, RIGHTS OR REMEDIES HEREOF. EACH PLEDGOR FURTHER AGREES THAT ANY ACTION TAKEN BY PLEDGOR RELATING TO THIS AGREEMENT OR ANY PROVISIONS, RIGHTS OR REMEDIES HEREOF SHALL BE TAKEN IN SAID COURTS AND SHALL NOT BE TAKEN IN ANY OTHER JURISDICTION. PLEDGOR RECOGNIZES THAT THIS COVENANT IS AN ESSENTIAL PROVISION OF THIS AGREEMENT, THE ABSENCE OF WHICH WOULD MATERIALLY ALTER THE CONSIDERATION GIVEN BY ADMINISTRATIVE AGENT AND SECURED PARTIES TO PLEDGOR AND GLADSTONE COMMERCIAL CORPORATION.

IN WITNESS WHEREOF, the parties hereto have caused this Pledge Agreement to be duly executed and delivered as of the date first above written.

PLEDGORS:

GLADSTONE COMMERCIAL CORPORATION

By: _____ (SEAL)
George Stelljes III
Executive Vice President
and Chief Investment Officer

GLADSTONE COMMERCIAL LIMITED PARTNERSHIP

By Gladstone Commercial Partners, LLC, its general partner

By Gladstone Commercial Corporation, its manager

_____
Name: George Stelljes III
Executive Vice President
and Chief Investment Officer

ADMINISTRATIVE AGENT:

BRANCH BANK AND TRUST COMPANY,
as Administrative Agent for itself and the other Secured Parties

By: _____
James C. Stallings III
Vice President

Acknowledged and Consented to:

PLEDGED SUBSIDIARIES:

GCC NORFOLK LLC

GLADSTONE LENDING LLC

By: **Gladstone Commercial Limited Partnership**
its Manager

By: **Gladstone Commercial Partners, LLC**
its General Partner

By: **Gladstone Commercial Corporation Manager of each of the above LLCs**

By: _____ (SEAL)
Name: George Stelljes III
Title: Executive Vice President
and Chief Investment Officer

TUSCANY AUSTIN GCC L.P.

By: **GCC COCO, Inc.**
its General Partner

By: _____
Arthur S. Cooper, President

FIRST PARK TEN COCO SAN ANTONIO, L.P.
(SEAL)
By: **GCC COCO, Inc.**
its General Partner

By: _____
Arthur S. Cooper, President

Exhibit A

NAMES, ADDRESSES, PLEDGED EQUITY INTERESTS AND STATES OF ORGANIZATION OF PLEDGED SUBSIDIARIES

Pledged Subsidiary	Address	Equity Interest	State of Organization
Tuscany Austin GCC L.P.	1616 Anderson Road, Suite 208 McLean, VA 22101 Attn: George Stelljes III	100% of Limited Partnership Interests (Uncertificated)	Delaware
GCC Norfolk LLC	1616 Anderson Road, Suite 208 McLean, VA 22101 Attn: George Stelljes III	100% of Membership Interests (Uncertificated)	Delaware
First Park Ten Coco San Antonio, L.P.	1616 Anderson Road, Suite 208 McLean, VA 22101 Attn: George Stelljes III	100% of Limited Partnership Interests (Uncertificated)	Delaware
Gladstone Lending LLC	1616 Anderson Road, Suite 208 McLean, VA 22101 Attn: George Stelljes III	100% of Membership Interests (Uncertificated)	Delaware
GCC COCO, Inc.	1616 Anderson Road, Suite 208 McLean, VA 22101 Attn: George Stelljes III	100% of Common Stock, no par value	Delaware

Exhibit 31.1

CERTIFICATION
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, David Gladstone, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Gladstone Commercial Corporation;

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 annual 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 we 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 controls over financial reporting, or caused such internal controls 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 changes 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 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 controls 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: May 4, 2005

/s/ DAVID GLADSTONE
David Gladstone
Chief Executive Officer and
Chairman of the Board of Directors

Exhibit 31.2

CERTIFICATION
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Harry Brill, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Gladstone Commercial Corporation;

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 annual 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 we 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 controls over financial reporting, or caused such internal controls 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 changes 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 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 controls 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: May 4, 2005

/s/ HARRY BRILL
Harry Brill
Chief Financial Officer and Treasurer

Exhibit 32.1

CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

The undersigned, the Chief Executive Officer of Gladstone Commercial Corporation (the "Company"), hereby certifies on the date hereof, pursuant to 18 U.S.C. §1350(a), as adopted pursuant to Section 906 of The Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 ("Form 10-Q"), filed concurrently herewith by the Company, fully complies with the requirements of Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934, as amended, and that the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

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 Exchange Commission or its staff upon request.

Dated: May 4, 2005

/s/ David Gladstone
David Gladstone
Chief Executive Officer

Exhibit 32.2

CERTIFICATION OF THE CHIEF FINANCIAL OFFICER PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

The undersigned, the Chief Financial Officer of Gladstone Commercial Corporation (the "Company"), hereby certifies on the date hereof, pursuant to 18 U.S.C. §1350(a), as adopted pursuant to Section 906 of The Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 ("Form 10-Q"), filed concurrently herewith by the Company, fully complies with the requirements of Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934, as amended, land that the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

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 Exchange Commission or its staff upon request.

Dated: May 4, 2005

/s/ Harry Brill
Harry Brill
Chief Financial Officer