

Whitestone REIT
Form 10-K
March 15, 2019

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

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2018

OR

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

For the transition period from _____ to _____

Commission File Number: 001-34855

WHITESTONE REIT

(Exact Name of Registrant as Specified in Its Charter)

Maryland	76-0594970
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

2600 South Gessner, Suite 500, Houston, Texas	77063
(Address of Principal Executive Offices)	(Zip Code)

Registrant's telephone number, including area code: (713) 827-9595

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

Title of each class of common shares of Beneficial Interest, par value \$0.001 per share	Name of each exchange on which registered
	New York Stock Exchange

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

None

(Title of Class)

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

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

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No
The aggregate market value of the common shares held by nonaffiliates of the registrant as of June 29, 2018 (the last business day of the registrant's most recently completed second fiscal quarter) was \$490,696,053.

As of March 15, 2019, the registrant had 39,766,240 common shares of beneficial interest, \$0.001 par value per share, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE: We incorporate by reference in Part III of this Annual Report on Form 10-K portions of our definitive proxy statement for our 2019 Annual Meeting of Shareholders, which proxy statement will be filed no later than 120 days after the end of our fiscal year ended December 31, 2018.

EXPLANATORY NOTE

On February 26, 2019, the Audit Committee of the Board of Trustees (the “Audit Committee”) of Whitestone REIT (“we,” “us,” “our” or the “Company”), after consultation with members of senior management of the Company, concluded that the Company’s unaudited consolidated financial statements as of and for the periods ended March 31, 2018, June 30, 2018 and September 30, 2018 (collectively, the “2018 Quarterly Financial Statements”) included in the Company’s Quarterly Reports on Form 10-Q for the quarterly periods ended March 31, 2018, June 30, 2018 and September 30, 2018, respectively, should be restated to correct the accounting error described below under “Background on the Quarterly Restatement” and should no longer be relied upon.

In this comprehensive Annual Report on Form 10-K for the fiscal year ended December 31, 2018 (this “Annual Report on Form 10-K”), the Company is presenting its audited consolidated financial statements as of and for the fiscal years ended December 31, 2018, 2017 and 2016, as well as restated 2018 Quarterly Financial Statements, which are included in Note 19 (Selected Quarterly Financial Data (Unaudited)) to the Company’s consolidated financial statements included in this Annual Report on Form 10-K. The Company refers to the restatement of the 2018 Quarterly Financial Statements included herein as the “Quarterly Restatement.”

We do not intend to file separate amended Quarterly Reports on Form 10-Q for the quarterly periods ended March 31, 2018, June 30, 2018 and September 30, 2018.

Background on the Quarterly Restatement

As previously disclosed in the Company’s Current Form 8-K filed with the Securities and Exchange Commission (“SEC”) on February 27, 2019 (the “Form 8-K”), on January 1, 2018, the Company adopted Accounting Standard Update (“ASU”) 2014-09 (“Topic 606”), as subsequently amended, using the modified retrospective method and applied Topic 606 to those contracts that were not completed as of January 1, 2018. We applied Topic 606 to account for contracts (that do not meet the definition of a business) to customers. We accounted for contracts (that do not meet the definition of a business) to noncustomers under Accounting Standards Codification 610, “Other Income-Gains and Losses from the Derecognition of Nonfinancial Assets” (“ASC 610”), which requires the application of certain concepts from Topic 606. In August 2018, the Company received a comment letter from the Staff of the SEC relating to its Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2018. The Staff requested that the Company provide them with an analysis of the Company’s determination that the contribution of assets to Pillarstone Capital REIT Operating Partnership LP (“Pillarstone” or “Pillarstone OP”) (as described in the Form 8-K) did not meet the requirements for derecognition of the underlying assets under Topic 606 and ASC 610, and an explanation of the Company’s consideration of the immaterial accounting errors related to Pillarstone OP in its conclusion that the Company’s disclosure controls and procedures and internal controls over financial reporting were effective as of June 30, 2018 and December 31, 2017. In September 2018, the Company responded to the Staff’s letter with the requested analysis and explanation. In October 2018, the Company received a comment letter from the Staff with certain follow up questions. Subsequently, the Company engaged in verbal discussions with the Staff regarding its responses, and in February 2019, the Staff verbally informed the Company that it objected to the Company’s conclusion regarding the assessment of the transfer of control criteria in Topic 606 with respect to the contribution and objected to the Company’s continued recognition of the underlying assets and liabilities associated with the contribution subsequent to the adoption of Topic 606 and ASC 610 on January 1, 2018. Accordingly, the Company concluded that the 2018 Quarterly Financial Statements should be restated. Because this change from the profit sharing method is only applicable for periods ending after giving effect to the implementation of Topic 606 and ASC 610, no periods prior to January 1, 2018 are affected by this error.

As described in more detail in this Annual Report on Form 10-K, as a result of the adoption of Topic 606 and ASC 610 and as reflected in the Quarterly Restatement, the Company has derecognized the underlying assets and liabilities associated with the contribution as of January 1, 2018 and has recognized the Company’s investment in Pillarstone OP under the equity method of accounting. As a part of the Quarterly Restatement, the Company has made the following adjustments to the 2018 Quarterly Financial Statements, which increased the Company’s retained earnings as of January 1, 2018 by \$19.1 million:

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For the three months ended March 31, 2018, the change decreased revenue by \$3.8 million, decreased total expenses by \$3.3 million, increased equity in earnings of real estate partnership by \$0.7 million and increased net income by \$0.2 million.

For the three months ended June 30, 2018, the change decreased revenue by \$3.6 million, decreased total expenses by \$3.2 million, increased equity in earnings of real estate partnership by \$0.6 million and increased net income by \$0.2 million. For the six months ended June 30, 2018, the change decreased revenue by \$7.4 million, decreased total expenses by \$6.5 million, increased equity in earnings of real estate partnership by \$1.3 million and increased net income by \$0.4 million.

For the three months ended September 30, 2018, the change decreased revenue by \$3.9 million, decreased total expenses by \$3.6 million, increased equity in earnings of real estate partnership by \$0.5 million and increased net income by \$0.2 million.

For the nine months ended September 30, 2018, the change decreased revenue by \$11.3 million, decreased total expenses by \$10.1 million, increased equity in earnings of real estate partnership by \$1.8 million and increased net income by \$0.6 million.

Internal Control Over Financial Reporting and Disclosure Controls and Procedures

The Company identified a material weakness in its internal control over financial reporting as of December 31, 2018. As a result of the material weakness, management concluded that the Company's internal control over financial reporting was not effective as of December 31, 2018 and determined that its disclosure controls and procedures were not effective as of March 31, 2018, June 30, 2018, September 30, 2018 and December 31, 2018. The Company has implemented and continues to implement measures to remediate the material weakness. See Part II, Item 9A, "Controls and Procedures" of this Annual Report on Form 10-K for more information about the material weakness and our remediation activities.

WHITESTONE REIT
FORM 10-K
Year Ended December 31, 2018

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Unless the context otherwise requires, all references in this Annual Report on Form 10-K to the “Company,” “we,” “us” or “our” are to Whitestone REIT and its consolidated subsidiaries.

Forward-Looking Statements

The following discussion should be read in conjunction with our audited consolidated financial statements and the notes thereto in this Annual Report on Form 10-K.

This Annual Report on Form 10-K contains forward-looking statements within the meaning of the federal securities laws, including discussion and analysis of our financial condition, anticipated capital expenditures required to complete projects, amounts of anticipated cash distributions to our shareholders in the future and other matters. These forward-looking statements are not historical facts but are the intent, belief or current expectations of our management based on its knowledge and understanding of our business and industry. Forward-looking statements are typically identified by the use of terms such as “may,” “will,” “should,” “potential,” “predicts,” “anticipates,” “expects,” “intends,” “plans,” “believes,” “seeks,” “estimates” or the negative of such terms and variations of these words and similar expressions, although not all forward-looking statements include these words. These statements are not guarantees of future performance and are subject to risks, uncertainties and other factors, some of which are beyond our control, are difficult to predict and could cause actual results to differ materially from those expressed or forecasted in the forward-looking statements.

Forward-looking statements that were true at the time made may ultimately prove to be incorrect or false. You are cautioned not to place undue reliance on forward-looking statements, which reflect our management’s view only as of the date of this Annual Report on Form 10-K. We undertake no obligation to update or revise forward-looking statements to reflect changed assumptions, the occurrence of unanticipated events or changes to future operating results. Factors that could cause actual results to differ materially from any forward-looking statements made in this Annual Report on Form 10-K include:

- the imposition of federal taxes if we fail to qualify as a real estate investment trust (“REIT”) in any taxable year or forego an opportunity to ensure REIT status;
- uncertainties related to the national economy, the real estate industry in general and in our specific markets;
- legislative or regulatory changes, including changes to laws governing REITs;
- adverse economic or real estate developments or conditions in Texas, Arizona or Illinois;
- increases in interest rates, operating costs or general and administrative expenses, including those incurred in connection with the Quarterly Restatement;
 - availability and terms of capital and financing to fund our operations, distributions to shareholders and to refinance our indebtedness as it matures;
- decreases in rental rates or increases in vacancy rates;
- litigation risks, including potential litigation as a result of the Quarterly Restatement and its effects;
- lease-up risks, including leasing risks arising from exclusivity and consent provisions in leases with significant tenants;

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our inability to renew tenants or obtain new tenants upon the expiration of existing leases;

our inability to generate sufficient cash flows due to market conditions, competition, uninsured losses, changes in tax or other applicable laws;

- the need to fund tenant improvements or other capital expenditures out of operating cash flow;

the risk that we are unable to raise capital for working capital, acquisitions or other uses on attractive terms or at all; and

our inability to improve our internal control over financial reporting and disclosure controls and procedures, including our inability to remediate the identified material weakness, and the costs and time associated with such efforts.

The forward-looking statements should be read in light of these factors and the factors identified in the “Risk Factors” section of this Annual Report on Form 10-K.

PART I

Item 1. Business.

General

We are a Maryland REIT engaged in owning and operating commercial properties in culturally diverse markets in major metropolitan areas. Founded in 1998, we changed our state of organization from Texas to Maryland in December 2003. We have elected to be taxed as a REIT under the Internal Revenue Code of 1986, as amended (the “Code”).

We are internally managed and, as of December 31, 2018, we wholly-owned a real estate portfolio of 57 properties that meet our Community Centered Property[®] strategy containing approximately 4.8 million square feet of gross leasable area (“GLA”), located in Texas, Arizona and Illinois. Our consolidated property portfolio has a gross book value of approximately \$1.1 billion and book equity, including noncontrolling interests, of approximately \$359 million as of December 31, 2018.

Further, as of December 31, 2018, we, through our investment in Pillarstone OP, owned a majority interest in 11 properties that do not meet our Community Centered Property[®] strategy containing approximately 1.3 million square feet of GLA (the “Pillarstone Properties”). We own 81.4% of the total outstanding units of Pillarstone OP, which we account for using the equity method. We also manage the day-to-day operations of Pillarstone OP. In this Annual Report on Form 10-K, unless otherwise indicated, we do not include the Pillarstone Properties when we refer to our properties.

Our common shares of beneficial interest, par value \$0.001 per share, are traded on the New York Stock Exchange (the “NYSE”) under the ticker symbol “WSR.” Our offices are located at 2600 South Gessner, Suite 500, Houston, Texas 77063. Our telephone number is (713) 827-9595 and we maintain a website at www.whitstonereit.com. The contents of our website are not incorporated into this filing.

Our Strategy

In October 2006, our current management team joined the Company and adopted a strategic plan to acquire, redevelop, own and operate Community Centered Properties[®]. We define Community Centered Properties[®] as visibly located properties in established or developing culturally diverse neighborhoods in our target markets. We market, lease and manage our centers to match tenants with the shared needs of the surrounding neighborhood. Those needs may include specialty retail, grocery, restaurants and medical, educational and financial services. Our goal is for each property to become a Whitestone-branded retail community that serves a neighboring five-mile radius around our property. We employ and develop a diverse group of associates who understand the needs of our multicultural communities and tenants.

Our primary business objective is to increase shareholder value by acquiring, owning and operating Community Centered Properties[®]. The key elements of our strategy include:

Strategically Acquiring Properties.

Seeking High Growth Markets. We seek to strategically acquire commercial properties in high-growth markets. Our acquisition targets are located in densely populated, culturally diverse neighborhoods, primarily in and around Austin, Chicago, Dallas-Fort Worth, Houston, Phoenix and San Antonio.

Diversifying Geographically. Our current portfolio is concentrated in Houston and Phoenix. As of December 31, 2018, we wholly-owned 57 commercial properties, including 15 properties in Houston, seven properties in Dallas-Fort Worth, three properties in San Antonio, four properties in Austin, 27 properties in the Scottsdale and Phoenix, Arizona metropolitan areas, and one property in Buffalo Grove, Illinois, a suburb of Chicago.

We believe that continued geographic diversification in markets where we have substantial knowledge and experience will help offset the economic risk from a single market concentration. We intend to continue to focus our expansion efforts on the Austin, Chicago, Dallas-Fort Worth, Houston, Phoenix and San Antonio markets. We believe our management infrastructure and capacity can accommodate substantial growth in those markets. We may also pursue opportunities in other regions that are consistent with our Community Centered Property® strategy. Markets in which we have developed some knowledge and contacts include Orlando, Florida and Denver, Colorado, both of which have economic, demographic and cultural profiles similar to our Arizona and Texas markets.

Capitalizing on Availability of Reasonably Priced Acquisition Opportunities. We believe that currently and during the next several years there will continue to be excellent opportunities in our target markets to acquire quality properties at historically attractive prices. We intend to acquire assets in off-market transactions negotiated directly with owners or financial institutions holding foreclosed real estate and debt instruments that are either in default or on bank watch lists. Many of these assets may benefit from our Community Centered Property[®] strategy and our management team's experience in turning around distressed properties, portfolios and companies. We have extensive relationships with community banks, attorneys, title companies and others in the real estate industry with whom we regularly work to identify properties for potential acquisition.

Redeveloping and Re-tenanting Existing Properties. We have substantial experience in repositioning underperforming properties and seek to add value through renovating and re-tenanting our properties to create Whitestone-branded Community Centered Properties[®]. We seek to accomplish this by (1) stabilizing occupancy, with per property occupancy goals of 90% or higher; (2) adding leasable square footage to existing structures; (3) developing and building new leasable square footage on excess land; (4) upgrading and renovating existing structures; and (5) investing significant effort in recruiting tenants whose goods and services meet the needs of the surrounding neighborhood.

Recycling Capital for Greater Returns. We seek to continually upgrade our portfolio by opportunistically selling properties that do not have the potential to meet our Community Centered Property[®] strategy and redeploying the sale proceeds into properties that better fit our strategy. Some of our properties that we owned at the time our current management team assumed the management of the Company (the "Legacy Portfolio" or "Non-Core Properties") may not fit our Community Centered Property[®] strategy, and we may look for opportunities to dispose of these properties as we continue to execute our strategy. For example, on December 31, 2016, we contributed to Pillarstone the 14 Pillarstone Properties located in Dallas and Houston that were part of the Legacy Portfolio.

Prudent Management of Capital Structure. Of our 57 properties, we currently have 48 properties that are unencumbered. We may seek to add mortgage indebtedness to existing and newly acquired unencumbered properties to provide additional capital for acquisitions. As a general policy, we intend to maintain a ratio of total indebtedness to undepreciated book value of real estate assets that is at or less than 60%. As of December 31, 2018, our ratio of total indebtedness to undepreciated book value of real estate assets was 58%.

Investing in People. We believe that our people are the heart of our culture, philosophy and strategy. We continually focus on developing associates who are self-disciplined and motivated and display, at all times, a high degree of character and competence. We provide them with equity incentives to align their interests with those of our shareholders.

Our Structure

Substantially all of our business is conducted through Whitestone REIT Operating Partnership, L.P., a Delaware limited partnership organized in 1998 (the "Operating Partnership"). We are the sole general partner of the Operating Partnership. As of December 31, 2018, we owned a 97.7% interest in the Operating Partnership.

As of December 31, 2018, we wholly-owned a real estate portfolio consisting of 57 properties located in three states. The aggregate occupancy rate of our portfolio was 90% based on GLA as of December 31, 2018.

We are hands-on owners who directly manage the operations and leasing of our properties. Substantially all of our revenues consist of base rents received under varying term leases. For the year ended December 31, 2018, our total revenues were approximately \$119.9 million.

Additionally, we, through our investment in Pillarstone, owned a majority interest in 11 properties located in Dallas and Houston, Texas. The aggregate occupancy rate of the Pillarstone properties was 80% based on GLA as of December 31, 2018.

Our largest property, BLVD Place (“BLVD”), a retail community purchased on May 26, 2017 and located in Houston, Texas, accounted for 12.7% of our total revenues for the year ended December 31, 2018. BLVD also accounted for 17.4% of our consolidated real estate assets, net of accumulated depreciation, as of the year ended December 31, 2018. Of our 57 properties, 15 and 27 are located in the Houston, Texas and Phoenix, Arizona metropolitan areas, respectively.

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Economic Environment

Low interest rates and desire for higher yielding investments with moderate risk has resulted in lower capitalization rates and higher prices for commercial real estate acquisitions. Each of these factors could negatively impact the value of public real estate companies, including ours. However, the majority of our retail properties are located in densely populated metropolitan areas and are occupied by tenants that generally provide basic necessity-type items and services which have tended to be less affected by economic changes. Furthermore, a substantial portion of our portfolio is in metropolitan areas in Texas that have been impacted less by the economic slowdown compared to other metropolitan areas.

Competition

All of our properties are located in areas that include competing properties. The amount of competition in a particular area could impact our ability to acquire additional real estate, sell current real estate, lease space and the amount of rent we are able to charge. We may be competing with owners, developers and operators, including, but not limited to, real estate investors, other REITs, insurance companies and pension funds.

Should we decide to dispose of a property, we may compete with third-party sellers of similar types of commercial properties for suitable purchasers, which may result in our receiving lower net proceeds from a sale or in our not being able to dispose of such property at a time of our choosing due to the lack of an acceptable return. In operating and managing our properties, we compete for tenants based upon a number of factors including, but not limited to, location, rental rates, security, flexibility, expertise to design space to meet prospective tenants' needs and the manner in which the property is operated, maintained and marketed. We may be required to provide rent concessions, incur charges for tenant improvements and other inducements, or we may not be able to timely lease vacant space, all of which could adversely impact our results of operations.

Many of our competitors have greater financial and other resources than us and also may have more operating experience. Generally, there are other neighborhood and community retail centers within relatively close proximity to each of our properties. There is, however, no dominant competitor in the Austin, Chicago, Dallas-Fort Worth, Houston, Phoenix and San Antonio metropolitan areas. Our retail tenants also face increasing competition from outlet malls, internet retailers, catalog companies, direct mail and telemarketing.

Compliance with Governmental Regulations

Under various federal and state environmental laws and regulations, as an owner or operator of real estate, we may be required to investigate and clean up certain hazardous or toxic substances, asbestos-containing materials, or petroleum product releases at our properties. We may also be held liable to a governmental entity or to third parties for property damage and for investigation and cleanup costs incurred by those parties in connection with any such contamination. In addition, some environmental laws create a lien on a contaminated site in favor of the government for damages and costs the government incurs in connection with contamination on the site. The presence of contamination or the failure to remediate contamination at any of our properties may adversely affect our ability to sell or lease the properties or to borrow using the properties as collateral. We could also be liable under common law to third parties for damages and injuries resulting from environmental contamination coming from our properties.

We will not purchase any property unless we are generally satisfied with the environmental status of the property. We typically obtain a Phase I environmental site assessment for each new acquisition, which includes a visual survey of the building and the property in an attempt to identify areas of potential environmental concerns, visually observing neighboring properties to assess surface conditions or activities that may have an adverse environmental impact on the

property, and contacting local governmental agency personnel and performing a regulatory agency file search in an attempt to determine any known environmental concerns in the immediate vicinity of the property. A Phase I environmental site assessment does not include any sampling or testing of soil, groundwater or building materials from the property.

We believe that our properties are in compliance in all material respects with all applicable federal, state and local laws and regulations regarding the handling, discharge and emission of hazardous or toxic substances. Because release of chlorinated solvents can occur as a result of dry cleaning operations, we participate in the Texas Commission on Environmental Quality Dry Cleaner Remediation Program (“DCRP”) with respect to four of our properties that currently or previously had a dry cleaning facility as a tenant. The DCRP administers the Dry Cleaning Remediation fund to assist with remediation of contamination caused by dry cleaning solvents.

We have not been notified by any governmental authority, and are not otherwise aware of any material noncompliance, liability or claim relating to hazardous or toxic substances in connection with any of our present or former properties. Nevertheless, it is possible that the environmental assessments conducted thus far and currently available to us do not reveal all potential environmental liabilities. It is also possible that subsequent investigations will identify material contamination or other adverse conditions, that adverse environmental conditions have arisen subsequent to the performance of the environmental assessments, or that there are material environmental liabilities of which management is unaware.

Under the Americans with Disabilities Act (“ADA”), all places of public accommodation are required to meet certain federal requirements related to access and use by disabled persons. Our properties must comply with the ADA to the extent that they are considered “public accommodations” as defined by the ADA. The ADA may require removal of structural barriers to access by persons with disabilities in public areas of our properties where such removal is readily achievable. We believe that our properties are in substantial compliance with the ADA and that we will not be required to make substantial capital expenditures to address the requirements of the ADA. In addition, we will continue to assess our compliance with the ADA and to make alterations to our properties as required.

Employees

As of December 31, 2018, we had 98 employees.

Materials Available on Our Website

Copies of our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports, proxy statements with respect to meetings of our shareholders, as well as Reports on Forms 3, 4 and 5 regarding our officers, trustees or 10% beneficial owners, filed or furnished pursuant to Section 13(a), 15(d) or 16(a) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), are available free of charge through our website (www.whitstonereit.com) as soon as reasonably practicable after we electronically file the material with, or furnish it to, the SEC. We have also made available on our website copies of our Audit Committee Charter, Compensation Committee Charter, Nominating and Governance Committee Charter, Corporate Governance Guidelines, Insider Trading Compliance Policy, and Code of Business Conduct and Ethics Policy. In the event of any changes to these documents, revised copies will also be made available on our website. The SEC maintains an internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC as we do. The website address is <http://www.sec.gov>. Materials on our website are not part of our Annual Report on Form 10-K. The contents of these websites are not incorporated into this filing.

Financial Information

Additional financial information related to the Company is included in Item 8 “Financial Statements and Supplementary Data.”

Item 1A. Risk Factors.

In addition to the other information contained in this Annual Report on Form 10-K, the following risk factors should be considered carefully in evaluating our business. Our business, financial condition, results of operations or the trading price of our common shares could be materially adversely affected by any of these risks. Please note that additional risks not presently known to us or which we currently consider immaterial may also impair our business and operations.

Risks Associated with Real Estate

Market disruptions may significantly and adversely affect our financial condition and results of operations.

World financial markets have, from time to time, experienced significant disruption. While many U.S. real estate markets have generally stabilized since the pervasive and fundamental disruptions associated with the last recession, which resulted in increased unemployment, weakening of tenant financial condition, large-scale business failures and tight credit markets, the financial markets have been volatile recently, and oil prices have declined dramatically over the past year. Our results of operations may be sensitive to changes in overall economic conditions that impact tenants of our properties or tenant leasing practices. Adverse economic conditions affecting tenant income, such as employment levels, business conditions, interest rates, tax rates, fuel and energy costs and other matters, could reduce overall tenant leasing or cause tenants to shift their leasing practices. In addition, periods of economic slowdown or recession, rising interest rates or declining demand for real estate, or the public perception that any of these events may occur, could result in a general decline in rents or an increased incidence of defaults under existing leases. Although the U.S. economy generally appears to have emerged from the worst aspects of the last recession, rental rates and valuations for retail space have not fully recovered to pre-recession levels and may not for a number of years. In addition, financial markets may again experience significant and prolonged disruption, including as a result of unanticipated events, or as a result of recent uncertainty regarding legislative and regulatory shifts relating to, among other things, taxation and trade, which could adversely affect our tenants and our business in general. For example, a general reduction in consumer spending and the level of tenant leasing could adversely affect our ability to maintain our current tenants and gain new tenants, affecting our growth and profitability. Accordingly, if financial and macroeconomic conditions deteriorate, or if financial markets experience significant disruption, it could have a significant adverse effect on our cash flows, profitability, results of operations and the trading price of our common shares.

Real estate property investments are illiquid due to a variety of factors and therefore we may not be able to dispose of properties when appropriate or on favorable terms.

Our strategy includes opportunistically selling properties that do not have the potential to meet our Community Centered Property[®] strategy. However, real estate property investments generally cannot be disposed of quickly. In addition, the Code imposes certain restrictions on the ability of a REIT to dispose of properties that are not applicable to other types of real estate companies. Therefore, we may not be able to vary our portfolio in response to economic or other conditions promptly or on favorable terms, which could cause us to incur extended losses, reduce our cash flows and adversely affect distributions to shareholders.

We cannot predict whether we will be able to sell any property for the price or on the terms set by us or whether any price or other terms offered by a prospective purchaser would be acceptable to us. We also cannot predict the length of time needed to find a willing purchaser and to close the sale of a property. To the extent we are unable to sell any properties for our book value, we may be required to take a non-cash impairment charge or loss on the sale, either of which would reduce our net income.

We may be required to expend funds and time to correct defects or to make improvements before a property can be sold. We cannot assure you that we will have funds available to correct those defects or to make those improvements, which may impede our ability to sell a property. Further, we may agree to transfer restrictions that materially restrict us from selling a property for a period of time or impose other restrictions, such as a limitation on the amount of debt that can be placed or repaid on that property. These transfer restrictions could impede our ability to sell a property even if we deem it necessary or appropriate. These facts and any others that would further contribute to the illiquid character of real estate properties and impede our ability to respond to adverse changes in the performance of our properties may have a material adverse effect on our business, financial condition, results of operations, our ability to make distributions to our shareholders and the trading price of our common shares.

Our business is dependent upon our tenants successfully operating their businesses, and their failure to do so could have a material adverse effect on our ability to successfully and profitably operate our business.

We depend on our tenants to operate their businesses in a manner that generates revenues sufficient to allow them to meet their obligations to us, including their obligations to pay rent, maintain certain insurance coverage, pay real estate taxes and maintain the properties in a manner so as not to jeopardize their operating licenses or regulatory status. The ability of our tenants to fulfill their obligations under our leases may depend, in part, upon the overall profitability of their operations. Cash flow generated by the businesses of certain tenants may not be sufficient for such tenants to meet their obligations to us. Our financial position could be weakened and our ability to fulfill our obligations under our indebtedness and make distributions to our shareholders could be limited if a number of our tenants were unable to meet their obligations to us or failed to renew or extend their relationships with us as their lease terms expire, or if we were unable to lease or re-lease our properties on economically favorable terms.

Disruption in capital markets could adversely impact acquisition activities and pricing of real estate assets.

Volatility or other disruption in capital markets could adversely affect our access to or the cost of debt and equity capital, which could adversely affect our acquisition and other investment activities. Disruptions could include price volatility or decreased demand in equity markets, as seen in recent months, rising interest rates, tightening of underwriting standards by lenders and credit rating agencies and the significant inventory of unsold collateralized mortgage backed securities in the market. As a result, we may not be able to obtain favorable equity and debt financing in the future or at all. This may impair our ability to acquire properties at favorable returns or adversely affect our returns on investments in development and re-development projects, which may adversely affect our results of operations and distributions to shareholders. Furthermore, any turmoil in the capital markets could adversely impact the overall amount of capital available to invest in real estate, which may result in price or value decreases of real estate assets.

The value of investments in our common shares will be directly affected by general economic and regulatory factors we cannot control or predict.

Investments in real estate typically involve a high level of risk as the result of factors we cannot control or predict. One of the risks of investing in real estate is the possibility that our properties will not generate income sufficient to meet operating expenses or will generate income and capital appreciation, if any, at rates lower than those anticipated or available through investments in comparable real estate or other investments. The following factors may affect income from properties and yields from investments in properties and are generally outside of our control:

- conditions in financial markets;
- continuing deterioration of the brick-and-mortar retail industry;
- over-building in our markets;
- a reduction in rental income as the result of the inability to maintain occupancy levels;
- adverse changes in applicable tax, real estate, environmental or zoning laws;
- changes in general economic conditions or economic conditions in our markets;
- a taking of any of our properties by eminent domain;

adverse local conditions (such as changes in real estate zoning laws that may reduce the desirability of real estate in the area);

acts of God, such as hurricanes, earthquakes or floods and other uninsured losses;

changes in supply of or demand for similar or competing properties in an area;

changes in interest rates and availability of permanent debt capital, which may render the sale of a property difficult or unattractive; and

periods of high interest rates, inflation or tight money supply.

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Some or all of these factors may affect our properties, which could adversely affect our operations and ability to make distributions to shareholders.

All of our properties are subject to property taxes that may increase in the future, which could adversely affect our cash flow.

Our properties are subject to property taxes that may increase as property tax rates change and as the properties are assessed or reassessed by taxing authorities. As the owner of the properties we are ultimately responsible for payment of the taxes to the government. If property taxes increase, our tenants may be unable to make the required tax payments, ultimately requiring us to pay the taxes. In addition, we will generally be responsible for property taxes related to any vacant space in our properties.

Our assets may be subject to impairment charges.

We periodically evaluate our real estate investments and other assets for impairment indicators. The judgment regarding the existence of impairment indicators is based on factors such as market conditions, tenant performance and legal structure. If we determine that a significant impairment has occurred, we would be required to make an adjustment to the net carrying value of the asset, which could have a material adverse effect on our results of operations and funds from operations in the period in which the write-off occurs.

Compliance or failure to comply with laws requiring access to our properties by disabled persons could result in substantial cost.

The ADA and other federal, state and local laws generally require public accommodations be made accessible to disabled persons. Noncompliance with these laws could result in the imposition of fines by the government or the award of damages to private litigants. These laws may require us to modify our existing properties, which could require a significant investment of our cash resources that could otherwise be invested in more productive assets. These laws may also restrict renovations by requiring improved access to such buildings by disabled persons or may require us to add other structural features which increase our construction costs. Legislation or regulations adopted in the future may impose further obligations, restrictions or increased compliance costs on us with respect to improved access by disabled persons. We may incur unanticipated expenses that may be material to our financial condition or results of operations to comply with ADA and other federal, state and local laws, or in connection with lawsuits brought by private litigants.

We face intense competition, which may decrease, or prevent increases of, the occupancy and rental rates of our properties.

We compete with a number of developers, owners and operators of commercial real estate, many of whom own properties similar to ours in the same markets in which our properties are located. If our competitors offer space at rental rates below current market rates, or below the rental rates we currently charge our tenants, we may lose existing or potential tenants and we may be pressured to reduce our rental rates below those we currently charge or to offer more substantial rent abatements, tenant improvements, early termination rights or below-market renewal options in order to retain tenants when our tenants' leases expire. This competitive environment could have a material adverse effect on our ability to lease our properties or any newly developed or acquired property, as well as on the rents charged.

Our acquisition strategy includes acquiring distressed commercial real estate, and we could face significant competition from other investors, REITs, hedge funds, private equity funds and other private real estate investors with

greater financial resources and access to capital than us. Therefore, we may not be able to compete successfully for investments. In addition, the number of entities and the amount of purchasers competing for suitable investments may increase, all of which could result in competition for accretive acquisition opportunities and adversely affect our business plan and our ability to maintain our current dividend rate.

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Risks Associated with Our Operations

Because a majority of our GLA is in the Houston and Phoenix metropolitan areas, an economic downturn in either area could adversely impact our operations and ability to make distributions to our shareholders.

The majority of our assets and revenues are currently derived from properties located in the Houston and Phoenix metropolitan areas. As of December 31, 2018, 26% and 48% of our GLA was located in Houston and Phoenix, respectively. Our results of operations are directly affected by our ability to attract financially sound commercial tenants. A significant economic downturn in the Houston or Phoenix metropolitan area may adversely impact our ability to locate and retain financially sound tenants, could have an adverse impact on our existing tenants' revenues, costs and results of operations and may adversely affect their ability to meet their obligations to us. Likewise, we may be required to lower our rental rates to attract desirable tenants in such an environment. Consequently, because of the geographic concentration among our current assets, if either the Houston or Phoenix metropolitan area experiences an economic downturn, our operations and ability to make distributions to our shareholders could be adversely impacted. In addition, a substantial component of the Houston economy is the oil and gas industry, and the current low prices of oil and natural gas could adversely affect companies in that industry and their employees, which could adversely affect the businesses of our Houston tenants.

We lease our properties to approximately 1,300 tenants and leases for approximately 10% to 20% of our GLA expire annually. Each year we face the risk of non-renewal of a significant percentage of our leases and the cost of re-leasing a significant amount of our available space, and our failure to meet leasing targets and control the cost of re-leasing our properties could adversely affect our rental revenue, operating expenses and results of operations.

Our Community Centered Property® business model produces shorter term leases to smaller, non-national tenants, and substantially all of our revenues consist of base rents received under these leases. As of December 31, 2018, approximately 29% of the aggregate GLA of our properties is subject to leases that expire prior to December 31, 2020. We are subject to the risk that:

- tenants may choose not to, or may not have the financial resources to, renew these leases;
- we may experience significant costs associated with re-leasing a significant amount of our available space;
- we may experience difficulties and significant time lags re-leasing vacated space, which may cause us to fail to meet our occupancy and average base rent targets and experience increased costs of re-leasing; and
- the terms of any renewal or re-lease may be less favorable than the terms of the current leases.

We routinely seek to renew leases with our existing tenants prior to their expiration and typically begin discussions with tenants as early as 18 months prior to the expiration date of the existing lease. While our early renewal program and other leasing and marketing efforts provide early focus on expiring leases, and have generally been effective in producing lease renewals prior to expiration of the leases at rates comparable to or slightly in excess of the current rates, market conditions, including new supply of properties, and macroeconomic conditions in our markets and nationally could adversely impact our renewal rate and/or the rental rates we are able to negotiate. If any of these risks materialize, our rental revenue, operating expenses and results of operations could be adversely affected.

Many of our tenants are small businesses, which may have a higher risk of bankruptcy or insolvency.

Many of our tenants are small businesses that depend primarily on cash flows from their operations to pay their rent and without other resources could be at a higher risk of bankruptcy or insolvency than larger, national tenants. If

tenants are unable to comply with the terms of our leases, we may be forced to modify the leases in ways that are unfavorable to us. Alternatively, the failure of a tenant to perform under a lease could require us to declare a default, repossess the space and find a suitable replacement tenant. There is no assurance that we would be able to lease the space on substantially equivalent or better terms than the prior lease, or at all, or successfully reposition the space for other uses. If one or more of our tenants files for bankruptcy relief, the Bankruptcy Code provides that a debtor has the option to assume or reject the unexpired lease within a certain period of time.

Any bankruptcy filing by or relating to one or more of our tenants could bar all efforts by us to collect pre-bankruptcy debts from that tenant or seize its property. A tenant bankruptcy could also delay our efforts to collect past due balances under the lease and could ultimately preclude collection of all or a portion of these sums. It is possible that we may recover substantially less than the full value of any unsecured claims we hold, if any. Furthermore, dealing with a tenant's bankruptcy or other default may divert management's attention and cause us to incur substantial legal and other costs. The bankruptcy or insolvency of a number of smaller tenants may have an adverse impact on our business, financial condition and results of operations, our ability to make distributions to our shareholders and the trading price of our common shares.

Uninsured losses relating to real property or excessively expensive premiums for insurance coverage may adversely affect our returns.

We attempt to adequately insure all of our properties to cover casualty losses. However, there are types of losses, generally catastrophic in nature, such as losses due to wars, acts of terrorism, earthquakes, floods, hurricanes, pollution or environmental matters, which are uninsurable or not economically insurable, or may be insured subject to limitations, such as large deductibles or co-payments. Our current geographic concentration in the Houston metropolitan area potentially increases the risk of damage to our portfolio due to hurricanes. Insurance risks associated with potential terrorism acts could sharply increase the premiums we pay for coverage against property and casualty claims. In some instances, we may be required to provide other financial support, either through financial assurances or self-insurance, to cover potential losses. We cannot assure you that we will have adequate coverage for these losses. Also, to the extent we must pay unexpectedly large insurance premiums, we could suffer reduced earnings that would result in less cash to be distributed to shareholders.

Discovery of previously undetected environmentally hazardous conditions may adversely affect our operating results.

Under various federal, state and local environmental laws, ordinances and regulations, a current or previous owner or operator of real property may be liable for the cost of removal or remediation of hazardous or toxic substances on, under or in its property. The costs of removal or remediation could be substantial. These laws often impose liability whether or not the owner or operator knew of, or was responsible for, the presence of any hazardous or toxic substances. Environmental laws also may impose restrictions on the manner in which a property may be used or businesses may be operated, and these restrictions may require substantial expenditures. Environmental laws provide for sanctions in the event of noncompliance and may be enforced by governmental agencies or, in certain circumstances, by private parties. Certain environmental laws and common law principles could be used to impose liability for release of and exposure to hazardous substances, including asbestos containing materials into the air. In addition, third parties may seek recovery from owners or operators of real properties for personal injury or property damage associated with exposure to released hazardous substances. The cost of defending against claims of liability, of compliance with environmental regulatory requirements, of remediating any contaminated property, or of paying personal injury claims could materially adversely affect our business, assets or results of operations and, consequently, amounts available for distributions to our shareholders.

Certain of our properties currently include or have in the past included a dry cleaning facility as a tenant. See "Business - Compliance with Governmental Regulations."

We may not be successful in consummating suitable acquisitions or investment opportunities, which may impede our growth and adversely affect the trading price of our common shares.

Our ability to expand through acquisitions is integral to our business strategy and requires us to consummate suitable acquisition or investment opportunities that meet our criteria and are compatible with our growth strategy. We may not be successful in consummating acquisitions or investments in properties that meet our acquisition criteria on

satisfactory terms or at all. Failure to consummate acquisitions or investment opportunities, the failure of an acquired property to perform as expected, or the failure to integrate successfully any acquired properties without substantial expense, delay or other operational or financial problems, would slow our growth, which could in turn adversely affect the trading price of our common shares.

Our ability to acquire properties on favorable terms may be constrained by the following significant risks:

- competition from other real estate investors with significant capital, including other REITs and institutional investment funds;

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

- unsatisfactory results of our due diligence investigations or failure to meet other customary closing conditions;

the failure of an acquired property to perform as expected; and
failure to finance an acquisition on favorable terms or at all.

If any of these risks are realized, our business, financial condition and results of operations, our ability to make distributions to our shareholders and the trading price of our common shares may be materially and adversely affected.

Our success depends in part on our ability to execute our Community Centered Property® strategy.

Our Community Centered Property® strategy requires intensive management of a large number of small spaces and small tenant relationships. Our success depends in part upon our management's ability to identify potential Community Centered Properties® and find and maintain the appropriate tenants to create such a property. Lack of market acceptance of our Community Centered Property® strategy or our inability to successfully attract and manage a large number of tenant relationships could adversely affect our occupancy rates, operating results and dividend rate.

Our business is significantly influenced by demand for retail space generally, and a decrease in such demand may have a greater adverse effect on our business than if we owned a more diversified real estate portfolio.

Because our portfolio of properties consists primarily of community and neighborhood shopping centers, a decrease in the demand for retail space, due to the economic factors discussed above or otherwise, may have a greater adverse effect on our business and financial condition than if we owned a more diversified real estate portfolio. The market for retail space has been, and could continue to be, adversely affected by weakness in the national, regional and local economies, the adverse financial conditions of some retailing companies, the ongoing consolidation in the retail sector, the excess amount of retail space in a number of markets and increasing online consumer purchases.

Loss of our key personnel, particularly our senior managers, could threaten our ability to execute our strategy and operate our business successfully.

We are dependent on the experience and knowledge of our key executive personnel, particularly certain of our senior managers who have been instrumental in setting our strategic direction, operating our business, identifying, recruiting and training key personnel and arranging necessary financing. Losing the services of any of these individuals could adversely affect our business until qualified replacements could be found. We also believe that they could not quickly be replaced with managers of equal experience and capabilities and their successors may not be as effective.

Our systems may not be adequate to support our growth, and our failure to successfully oversee our portfolio of properties could adversely affect our results of operations.

We make no assurances that we will be able to adapt our portfolio management, administrative, accounting and operational systems, or hire and retain sufficient operational staff, to support our growth. Our failure to successfully oversee our current portfolio of properties or any future acquisitions or developments could have a material adverse effect on our results of operations and financial condition and our ability to make distributions.

We face risks relating to cybersecurity attacks, loss of confidential information and other business disruptions.

Our business is at risk from and may be impacted by cybersecurity attacks, including attempts to gain unauthorized access to our confidential data and other electronic security breaches. Such cyber-attacks can range from individual attempts to gain unauthorized access to our information technology systems to more sophisticated security threats.

While we employ a number of measures to prevent, detect and mitigate these threats, there is no guarantee such efforts will be successful in preventing a cyber-attack. Cybersecurity incidents could compromise the confidential information of our tenants, employees and third party vendors and affect the efficiency of our business operations, which in turn could have a material adverse effect on our reputation, competitiveness and results of operations.

There can be no assurance that we will be able to pay or maintain cash distributions or that distributions will increase over time.

There are many factors that can affect the availability and timing of cash distributions to shareholders. Distributions are based upon our funds from operations, financial condition, cash flows and liquidity, debt service requirements, capital expenditure requirements for our properties and other matters our board of trustees may deem relevant from time to time. If we do not have sufficient cash available for distributions, we may need to fund the shortage out of working capital or borrow to provide funds for such distributions, which would reduce the amount of capital available for real estate investments and increase our future interest costs.

We can give no assurance that we will be able to continue to pay distributions or that distributions will increase over time. In addition, we can give no assurance that rents from our properties will increase, or that future acquisitions of real properties, mortgage loans or our investments in securities will increase our cash available for distributions to shareholders. Our actual results may differ significantly from the assumptions used by our board of trustees in establishing the distribution rate to shareholders. Our inability to make distributions, or to make distributions at expected levels, could result in a decrease in the trading price of our common shares.

We have identified a material weakness in our system of internal controls pursuant to Section 404 of the Sarbanes-Oxley Act of 2002. If not remediated, this material weakness could result in additional material misstatements in our consolidated financial statements. We may be unable to develop, implement and maintain appropriate controls in future periods.

Section 404 of the Sarbanes-Oxley Act of 2002 requires that public companies evaluate and report on their systems of internal control over financial reporting. In addition, our independent registered public accounting firm must report on management's evaluation of those controls. As disclosed in Part II, Item 9A, "Controls and Procedures" of this Form 10-K, our management, including our Chief Executive Officer and our Chief Financial Officer, has determined that we had a material weakness in the Company's internal control over financial reporting as of December 31, 2018. The material weakness contributed to the material misstatement in our previously filed interim unaudited consolidated financial statements, which were restated as part of the Quarterly Restatement. As a result of the material weakness, the Company's management, under the supervision of the Audit Committee and with participation of the Company's Chief Executive Officer and Chief Financial Officer, concluded that the Company's internal control over financial reporting was not effective as of December 31, 2018 and determined that its disclosure controls and procedures were not effective as of March 31, June 30, September 30 and December 31, 2018.

Although we are working to remedy the ineffectiveness of the Company's internal control over financial reporting and disclosure controls and procedures, there can be no assurance as to when the remediation plan will be fully developed and implemented. Until our remediation plan is fully implemented, our management will continue to devote significant time, attention and financial resources to these efforts. If we do not complete our remediation in a timely fashion, or at all, or if our remediation plan is inadequate, there will continue to be an increased risk that our future consolidated financial statements could contain errors that will be undetected. Further and continued determinations that there are one or more material weaknesses in the effectiveness of the Company's internal control over financial reporting could also reduce our ability to obtain financing or could increase the cost of any financing we obtain and require additional expenditures of both money and our management's time to comply with applicable requirements. For more information relating to the Company's internal control over financial reporting, the material weakness that existed as of December 31, 2018 and the remediation activities undertaken by us, see Part II, Item 9A, "Controls and Procedures" of this Annual Report on Form 10-K.

We have restated certain of our prior interim unaudited financial statements, which may lead to additional risks and uncertainties, including loss of investor confidence and negative impacts on our share price.

We have restated our unaudited financial statements for the periods ended March 31, 2018, June 30, 2018 and September 30, 2018. We have filed this comprehensive Annual Report on Form 10-K to, among other things, reflect the restatement of our 2018 interim financial statements.

As a result of the Quarterly Restatement, we have become subject to a number of additional costs and risks, including costs for accounting and legal fees in connection with or related to the Quarterly Restatement and the remediation of our material weakness in internal control over financial reporting. In addition, the attention of our management team has been diverted by these efforts. We may be subject to shareholder and other actions in connection with the Quarterly Restatement and related matters. In addition, the Quarterly Restatement and related matters could impair our reputation or could cause our counterparties to lose confidence in us. Each of these occurrences could have a material adverse effect on our business, financial condition, results of operations and share price.

Risks Associated with Our Indebtedness and Financing

Current market conditions could adversely affect our ability to refinance existing indebtedness or obtain additional financing for growth on acceptable terms or at all, which could adversely affect our ability to grow, our interest cost and our results of operations.

The United States credit markets have experienced significant dislocations and liquidity disruptions, including the bankruptcy, insolvency or restructuring of certain financial institutions. These circumstances have materially impacted liquidity in the debt markets, making financing terms for borrowers less attractive, and in certain cases have resulted in the unavailability of various types of debt financing. Reductions in our available borrowing capacity, or inability to refinance our revolving credit facility when required or when business conditions warrant, could have a material adverse effect on our business, financial condition and results of operations. In addition, we mortgage many of our properties to secure payment of indebtedness. If we are not successful in refinancing our mortgage debt upon maturity, then the property could be foreclosed upon or transferred to the mortgagee, or we might be forced to dispose of some of our properties upon disadvantageous terms, with a consequent loss of income and asset value. A foreclosure or disadvantageous disposal on one or more of our properties could adversely affect our ability to grow, financial condition, interest cost, results of operations, cash flow and ability to make distributions to our shareholders. In addition, our universal shelf registration statement on Form S-3 expired in April 2018. Until our new shelf registration statement is declared effective by the SEC, we will not have access to the public capital markets.

Furthermore, if prevailing interest rates or other factors at the time of refinancing result in higher interest rates upon refinancing, then the interest expense relating to that refinanced indebtedness would increase. Higher interest rates on newly incurred debt may negatively impact us as well. If interest rates increase, our interest costs and overall costs of capital will increase, which could adversely affect our transaction and development activity, financial condition, results of operation, cash flow, our ability to pay principal and interest on our debt and our ability to make distributions to our shareholders.

Our failure to hedge effectively against interest rate changes may adversely affect results of operations.

We currently have mortgages that bear interest at variable rates and we may incur additional variable rate debt in the future. Accordingly, increases in interest rates on variable rate debt would increase our interest expense, which could reduce net earnings and cash available for payment of our debt obligations and distributions to our shareholders.

We may seek to manage our exposure to interest rate volatility by using interest rate hedging arrangements, such as interest cap agreements and interest rate swap agreements. These agreements involve risks, such as the risk that counterparties may fail to honor their obligations under these arrangements, that these arrangements may not be effective in reducing our exposure to interest rate changes and that a court could rule that such an agreement is not legally enforceable. In the past, we have used derivative financial instruments to hedge interest rate risks related to our variable rate borrowings. We will not use derivatives for speculative or trading purposes and intend only to enter into contracts with major financial institutions based on their credit rating and other factors, but we may choose to change this practice in the future. As of December 31, 2018, we had fixed rate hedges on \$209.5 million of our variable rate debt, including \$200 million of our unsecured credit facility. We may enter into additional interest rate swap agreements for our variable rate debt not currently subject to hedges, which totaled \$241.2 million as of December 31, 2018. Hedging may reduce the overall returns on our investments. Failure to hedge effectively against interest rate changes may materially and adversely affect our results of operations.

We currently have and may incur additional mortgage indebtedness and other borrowings, which may increase our business risks and may adversely affect our ability to make distributions to our shareholders.

If we determine it to be in our best interests, we may, in some instances, acquire real properties by using either existing financing or borrowing new funds. In addition, we may incur or increase our current mortgage debt to obtain funds to acquire additional properties. We may also borrow funds if necessary to satisfy the REIT distribution requirement described above, or otherwise as may be necessary or advisable to ensure that we maintain our qualification as a REIT for federal income tax purposes.

On November 7, 2014, we, through our Operating Partnership, entered into an unsecured revolving credit facility (the “2014 Facility”) with the lenders party thereto, with BMO Capital Markets Corp., Wells Fargo Securities, LLC, Merrill Lynch, Pierce, Fenner & Smith Incorporated and U.S. Bank, National Association, as co-lead arrangers and joint book runners, and Bank of Montreal, as administrative agent (the “Agent”). The 2014 Facility amended and restated our previous unsecured revolving credit facility. On October 30, 2015, we, through our Operating Partnership, entered into the First Amendment to the 2014 Facility (the “First Amendment”) with the guarantors party thereto, the lenders party thereto and the Agent. We refer to the 2014 Facility, as amended by the First Amendment, as the “2018 Facility.”

On January 31, 2019, we, through our Operating Partnership, entered into an unsecured credit facility (the “2019 Facility”) with the lenders party thereto, Bank of Montreal, as administrative agent (the “Agent”), SunTrust Robinson Humphrey, as syndication agent, and BMO Capital Markets Corp., U.S. Bank National Association, SunTrust Robinson Humphrey and Regions Capital Markets, as co-lead arrangers and joint book runners. The 2019 Facility amended and restated the 2018 Facility (as defined herein).

The 2019 Facility is comprised of the following three tranches:

\$250.0 million unsecured revolving credit facility with a maturity date of January 1, 2023 (the “2019 Revolver”);

\$165.0 million unsecured term loan with a maturity date of January 31, 2024 (“Term Loan A”); and

\$100.0 million unsecured term loan with a maturity date of October 30, 2022 (“Term Loan B” and together with Term Loan A, the “2019 Term Loans”).

The 2019 Facility includes an accordion feature that will allow the Operating Partnership to increase the borrowing capacity by \$200.0 million, upon the satisfaction of certain conditions. The Company used \$446.2 million of proceeds from the 2019 Facility to repay amounts outstanding under the 2018 Facility and intends to use the remaining proceeds from the 2019 Facility for general corporate purposes, including property acquisitions, debt repayment, capital expenditures, the expansion, redevelopment and re-tenanting of properties in its portfolio and working capital.

The Company, each direct and indirect material subsidiary of the Operating Partnership and any other subsidiary of the Operating Partnership that is a guarantor under any unsecured ratable debt will serve as a guarantor for funds borrowed by the Operating Partnership under the 2019 Facility. The 2019 Facility contains customary terms and conditions, including, without limitation, customary representations and warranties and affirmative and negative covenants including, without limitation, information reporting requirements, limitations on investments, acquisitions, loans and advances, mergers, consolidations and sales, incurrence of liens, dividends and restricted payments. In addition, the 2019 Facility contains certain financial covenants including the following:

• maximum total indebtedness to total asset value ratio of 0.60 to 1.00;

• maximum secured debt to total asset value ratio of 0.40 to 1.00;

• minimum EBITDA (earnings before interest, taxes, depreciation, amortization or extraordinary items) to fixed charges ratio of 1.50 to 1.00;

• maximum other recourse debt to total asset value ratio of 0.15 to 1.00; and

• maintenance of a minimum tangible net worth (adjusted for accumulated depreciation and amortization) of \$372 million plus 75% of the net proceeds from additional equity offerings.

The 2019 Facility also contains customary events of default with customary notice and cure, including, without limitation, nonpayment, breach of covenant, misrepresentation of representations and warranties in a material respect, cross-default to other major indebtedness, change of control, bankruptcy and loss of REIT tax status. If an event of default occurs and is continuing under the 2019 Facility, the lenders may, among other things, terminate their commitments under the 2019 Facility and require the immediate payment of all amounts owed thereunder.

We may also incur mortgage debt on a particular property if we believe the property's projected cash flow is sufficient to service the mortgage debt. As of December 31, 2018, we had approximately \$178.2 million of mortgage debt secured by 9 of our properties. If there is a shortfall in cash flow, however, the amount available for distributions to shareholders may be affected. In addition, incurring mortgage debt increases the risk of loss because defaults on such indebtedness may result in loss of property in foreclosure actions initiated by lenders. For tax purposes, a foreclosure of any of our properties would be treated as a sale of the property for a purchase price equal to the outstanding balance of the debt secured by the mortgage. If the outstanding balance of the debt secured by the mortgage exceeds our tax basis in the property, we would recognize taxable income on foreclosure, but would not receive any cash proceeds. We may give lenders full or partial guarantees for mortgage debt incurred by the entities that own our properties. When we give a guaranty on behalf of an entity that owns one of our properties, we will be responsible to the lender for satisfaction of the debt if it is not paid by that entity. If any mortgages contain cross-collateralization or cross-default provisions, there is a risk that more than one property may be affected by a default. If any of our properties are foreclosed upon due to a default, our ability to pay cash distributions to our shareholders may be adversely affected. For more discussion, see "Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources."

If we set aside insufficient working capital or are unable to secure funds for future tenant improvements, we may be required to defer necessary property improvements, which could adversely impact the quality of our properties and our results of operations.

When tenants do not renew their leases or otherwise vacate their space, it is possible that, in order to attract replacement tenants, we may be required to expend substantial funds for tenant improvements and refurbishments to the vacated space. If we have insufficient working capital reserves, we will have to obtain financing from other sources. Because most of our leases provide for tenant reimbursement of operating expenses, we have not established a permanent reserve for maintenance and repairs for our properties. However, to the extent that we have insufficient funds for such purposes, we may establish reserves for maintenance and repairs of our properties out of cash flow generated by operating properties or out of non-liquidating net sale proceeds. If these reserves or any reserves otherwise established are insufficient to meet our cash needs, we may have to obtain financing from either affiliated or unaffiliated sources to fund our cash requirements. We cannot assure you that sufficient financing will be available or, if available, will be available on economically feasible terms or on terms acceptable to us. Additional borrowing for working capital purposes will increase our interest expense, and therefore our financial condition and our ability to pay cash distributions to our shareholders may be adversely affected. In addition, we may be required to defer necessary improvements to our properties that may cause our properties to suffer from a greater risk of obsolescence or a decline in value, or a greater risk of decreased cash flow as a result of fewer potential tenants being attracted to our properties. If this happens, we may not be able to maintain projected rental rates for affected properties, and our results of operations may be negatively impacted.

We have in the past and may continue to structure acquisitions of property in exchange for limited partnership units in our Operating Partnership on terms that could limit our liquidity or our flexibility.

We have in the past and may continue to acquire properties by issuing limited partnership units in our Operating Partnership ("OP units") in exchange for a property owner contributing property to the Operating Partnership. If we enter into such transactions, in order to induce the contributors of such properties to accept OP units, rather than cash, in exchange for their properties, it may be necessary for us to provide them with additional incentives. For instance, our Operating Partnership's limited partnership agreement provides that any holder of OP units may redeem such units for cash, or, at our option, common shares on a one-for-one basis. We may, however, enter into additional contractual arrangements with contributors of property under which we would agree to redeem a contributor's OP units for our common shares or cash, at the option of the contributor, at set times. If the contributor required us to redeem OP units

for cash pursuant to such a provision, it would limit our liquidity and thus our ability to use cash to make other investments, satisfy other obligations or pay distributions. Moreover, if we were required to redeem OP units for cash at a time when we did not have sufficient cash to fund the redemption, we might be required to sell one or more properties to raise funds to satisfy this obligation. Furthermore, we might agree that if distributions the contributor received as a limited partner in our Operating Partnership did not provide the contributor with a defined return, then upon redemption of the contributor's OP units, we would pay the contributor an additional amount necessary to achieve that return. Such a provision could further negatively impact our liquidity and flexibility. Finally, in order to allow a contributor of a property to defer taxable gain on the contribution of property to our Operating Partnership, we might agree not to sell a contributed property for a defined period of time or until the contributor redeemed the contributor's OP units for cash or our common shares. Such an agreement would prevent us from selling those properties, even if market conditions made such a sale favorable to us.

We may issue preferred shares with a preference in distributions over our common shares, and our ability to issue preferred shares and additional common shares may deter or prevent a sale of our common shares in which you could profit.

Our declaration of trust authorizes our board of trustees to issue up to 400,000,000 common shares and 50,000,000 preferred shares. Our board of trustees may amend our declaration of trust from time to time to increase or decrease the aggregate number of shares or the number of any class or series that we have authority to issue. In addition, our board of trustees may classify or reclassify any unissued common shares or preferred shares and may set the preferences, rights and other terms of the classified or reclassified shares. The terms of preferred shares could include a preference in distributions senior to our common shares. If we authorize and issue preferred shares with a distribution preference senior to our common shares, payment of any distribution preferences of outstanding preferred shares would reduce the amount of funds available for the payment of distributions on our common shares. Further, holders of preferred shares are normally entitled to receive a preference payment in the event we liquidate, dissolve or wind up before any payment is made to our common shareholders, likely reducing the amount our common shareholders would otherwise receive upon such an occurrence. In addition, under certain circumstances, the issuance of preferred shares or a separate class or series of common shares may render more difficult or tend to discourage:

- a merger, tender offer or proxy contest;
- assumption of control by a holder of a large block of our shares; or
- removal of incumbent management.

Risks Associated with Income Tax Laws

If we fail to qualify as a REIT, our operations and distributions to shareholders would be adversely impacted.

We intend to continue to be organized and to operate so as to qualify as a REIT under the Code. A REIT generally is not taxed at the corporate level on income it currently distributes to its shareholders. Qualification as a REIT involves the application of highly technical and complex rules for which there are only limited judicial or administrative interpretations. The determination of various factual matters and circumstances not entirely within our control may affect our ability to continue to qualify as a REIT. In addition, new legislation, new regulations, administrative interpretations or court decisions could significantly change the tax laws, possibly with retroactive effect, with respect to qualification as a REIT or the federal income tax consequences of such qualification.

If we were to fail to qualify as a REIT in any taxable year:

- we would not be allowed to deduct our distributions to shareholders when computing our taxable income;
- we would be subject to federal income tax on our taxable income at regular corporate rates;
- we would be disqualified from being taxed as a REIT for the four taxable years following the year during which qualification was lost, unless entitled to relief under certain statutory provisions;
- our cash available for distributions to shareholders would be reduced; and
- we may be required to borrow additional funds or sell some of our assets in order to pay corporate tax obligations that we may incur as a result of our disqualification.

We may need to incur additional borrowings to meet the REIT minimum distribution requirement and to avoid excise tax.

In order to maintain our qualification as a REIT, we are required to distribute to our shareholders at least 90% of our annual real estate investment trust taxable income (excluding any net capital gain and before application of the dividends paid deduction). In addition, we are subject to a 4% nondeductible excise tax on the amount, if any, by which certain distributions paid by us with respect to any calendar year are less than the sum of (i) 85% of our ordinary income for that year, (ii) 95% of our net capital gain for that year and (iii) 100% of our undistributed taxable income from prior years. Although we intend to pay distributions to our shareholders in a manner that allows us to meet the 90% distribution requirement and avoid this 4% excise tax, we cannot assure you that we will always be able to do so.

Our income consists almost solely of our share of our Operating Partnership's income, and the cash available for distribution by us to our shareholders consists of our share of cash distributions made by our Operating Partnership. Because we are the sole general partner of our Operating Partnership, our board of trustees determines the amount of any distributions made by our Operating Partnership. Our board of trustees may consider a number of factors in authorizing distributions, including:

- the amount of cash available for distribution;
- our Operating Partnership's financial condition;
- our Operating Partnership's capital expenditure requirements; and
- our annual distribution requirements necessary to maintain our qualification as a REIT.

Differences in timing between the actual receipt of income and actual payment of deductible expenses and the inclusion of income and deduction of expenses when determining our taxable income, as well as the effect of nondeductible capital expenditures and the creation of reserves or required debt amortization payments could require us to borrow funds on a short-term or long-term basis or make taxable distributions to our shareholders of our shares or debt securities to meet the REIT distribution requirement and to avoid the 4% excise tax described above. In these circumstances, we may need to borrow funds to avoid adverse tax consequences even if our management believes that the then prevailing market conditions generally are not favorable for borrowings or that borrowings would not be advisable in the absence of the tax consideration.

If our Operating Partnership were classified as a "publicly traded partnership" taxable as a corporation for federal income tax purposes under the Code, we would cease to qualify as a REIT and would suffer other adverse tax consequences.

We structured our Operating Partnership so that it would be classified as a partnership for federal income tax purposes. In this regard, the Code generally classifies "publicly traded partnerships" (as defined in Section 7704 of the Code) as associations taxable as corporations (rather than as partnerships), unless substantially all of their taxable income consists of specified types of passive income. In order to minimize the risk that the Code would classify our Operating Partnership as a "publicly traded partnership" for tax purposes, we placed certain restrictions on the transfer and/or redemption of partnership units in our Operating Partnership. If the Internal Revenue Service were to assert successfully that our Operating Partnership is a "publicly traded partnership," and substantially all of its gross income did not consist of the specified types of passive income, the Code would treat our Operating Partnership as an association taxable as a corporation.

In such event, the character of our assets and items of gross income would change and would prevent us from continuing to qualify as a REIT. In addition, the imposition of a corporate tax on our Operating Partnership would reduce our amount of cash available for payment of distributions by us to our shareholders.

Complying with REIT requirements may cause us to forego otherwise attractive opportunities or liquidate otherwise attractive investments.

To qualify as a REIT for federal income tax purposes, we must continually satisfy tests concerning, among other things, the sources of our income, the nature and diversification of our assets, the amounts we distribute to our shareholders and the ownership of our shares. In order to meet these tests, we may be required to forego investments we might otherwise make. Thus, compliance with the REIT requirements may hinder our performance.

In particular, we must ensure that at the end of each calendar quarter, at least 75% of the value of our assets consists of cash, cash items, government securities and qualified real estate assets. The remainder of our investment in securities (other than government securities and qualified real estate assets) generally cannot include more than 10% of the outstanding voting securities of any one issuer or more than 10% of the total value of the outstanding securities of any one issuer. In addition, in general, no more than 5% of the value of our assets (other than government securities and qualified real estate assets) can consist of the securities of any one issuer, and no more than 20% of the value of our total assets can be represented by the securities of one or more taxable REIT subsidiaries. If we fail to comply with these requirements at the end of any calendar quarter, we must correct the failure within 30 days after the end of the calendar quarter or qualify for certain statutory relief provisions to avoid losing our REIT qualification and suffering adverse tax consequences. As a result, we may be required to liquidate otherwise attractive investments. These actions could have the effect of reducing our income and amounts available for distribution to our shareholders.

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

For non-corporate taxpayers the maximum tax rate applicable to “qualified dividend income” paid by regular “C” corporations to U.S. shareholders generally is 20%. Dividends payable by REITs, however, generally are not eligible for the reduced rates on qualified dividend income. Instead, our ordinary dividends generally are taxed at the higher tax rates applicable to ordinary income, the current maximum rate of which is 37%. However, for taxable years prior to 2026, individual stockholders are generally allowed to deduct 20% of the aggregate amount of ordinary dividends distributed by us, subject to certain limitations, which would reduce the maximum marginal effective tax rate for individuals on the receipt of such ordinary dividends to 29.6%.

Complying with REIT requirements may limit our ability to hedge effectively and may cause us to incur tax liabilities.

The REIT provisions of the Code substantially limit our ability to hedge our liabilities. Any income from a hedging transaction that we enter into to manage risk of interest rate changes, price changes or currency fluctuations with respect to borrowings made or to be made to acquire or carry real estate assets does not constitute “gross income” for purposes of the 75% or 95% gross income tests. To the extent that we enter into other types of hedging transactions, the income from those transactions is likely to be treated as non-qualifying income for purposes of both of the gross income tests. As a result of these rules, we may need to limit our use of advantageous hedging techniques or implement those hedges through taxable REIT subsidiaries. This could increase the cost of our hedging activities because any taxable REIT subsidiary that we may form would be subject to tax on gains or expose us to greater risks associated with changes in interest rates than we would otherwise want to bear. In addition, losses in taxable REIT subsidiaries will generally not provide any tax benefit, except for being carried forward against future taxable income in the taxable REIT subsidiaries.

Pursuant to the Tax Protection Agreement, the amount that Pillarstone is required to indemnify the Operating Partnership for certain tax liabilities reduces over the term of the Tax Protection Agreement.

In connection with the Contribution (as defined below), on December 8, 2016, the Operating Partnership entered into a Tax Protection Agreement (the “Tax Protection Agreement”) with Pillarstone Capital REIT (“Pillarstone REIT”), the general partner of Pillarstone, and Pillarstone pursuant to which Pillarstone agreed to indemnify the Operating Partnership for certain tax liabilities resulting from its recognition of income or gain prior to December 8, 2021 (a) if such liabilities result from a transaction involving a direct or indirect taxable disposition of all or a portion of the Pillarstone Properties or (b) if Pillarstone fails to maintain and allocate to the Operating Partnership for taxation purposes minimum levels of liabilities as specified in the Tax Protection Agreement, the result of which causes such recognition of income or gain and the Company incurs taxes that must be paid to maintain its REIT status for federal tax purposes. However, the Tax Protection Agreement expires on the earlier of (x) December 8, 2021 and (y) the date on which the Operating Partnership disposes of 50% or more of the Pillarstone OP Units (as defined below) issued in connection with the Contribution. Further, the amount that Pillarstone is required to indemnify the Operating Partnership reduces over the term of the Tax Protection Agreement as follows: on December 8th of each year, the amount of tax liability recognized by the Operating Partnership during that year that Pillarstone is required to indemnify is reduced by 20 percentage points. Once the Tax Protection Agreement has expired, the Company could be subject to additional taxes upon the occurrence of certain events that must be paid to maintain its REIT status for federal tax purposes.

Risks Related to Ownership of our Common Shares

Increases in market interest rates may result in a decrease in the value of our common shares.

One of the factors that may influence the price of our common shares will be the dividend distribution rate on the common shares (as a percentage of the price of our common shares) relative to market interest rates. If market interest rates rise, prospective purchasers of shares of our common shares may expect a higher distribution rate. Higher interest rates would not, however, result in more funds being available for distribution and, in fact, would likely increase our borrowing costs and might decrease our funds available for distribution. We therefore may not be able, or we may not choose, to provide a higher distribution rate. As a result, prospective purchasers may decide to purchase other securities rather than our common shares, which would reduce the demand for, and result in a decline in the market price of, our common shares.

Broad market fluctuations could negatively impact the market price of our common shares.

The stock market has experienced extreme price and volume fluctuations that have affected the market price of many companies in industries similar or related to ours and that have been unrelated to these companies' operating performances. These broad market fluctuations could reduce the market price of our common shares. Furthermore, our operating results and prospects may be below the expectations of public market analysts and investors or may be lower than those of companies with comparable market capitalizations. Either of these factors could lead to a material decline in the market price of our common shares.

Maryland takeover statutes may deter others from seeking to acquire us and prevent shareholders from making a profit in such transactions.

The Maryland General Corporation Law ("MGCL") contains many provisions, such as the business combination statute and the control share acquisition statute, that are designed to prevent, or have the effect of preventing, someone from acquiring control of us. The business combination statute, subject to limitations, prohibits certain business combinations between us and an "interested shareholder" (defined generally as any person who beneficially owns 10% or more of the voting power of our outstanding voting shares or an affiliate or associate of our Company who, at any time within the two-year period prior to the date in question, was the beneficial owner of 10% or more of the voting power of our then outstanding shares) or an affiliate of an interested shareholder for five years after the most recent date on which the person becomes an interested shareholder and thereafter imposes super-majority voting requirements on these combinations. The control share acquisition statute provides that "control shares" of our Company (defined as shares which, when aggregated with other shares controlled by the shareholder (except solely by virtue of a revocable proxy), entitle the shareholder to exercise one of three increasing ranges of voting power in electing trustees) acquired in a "control share acquisition" (defined as the direct or indirect acquisition of ownership or control of issued and outstanding control shares) have no voting rights except to the extent approved by our shareholders by the affirmative vote of at least two-thirds of all the votes entitled to be cast on the matter, excluding all interested shares.

We are currently subject to the control share acquisition statute, although our board of trustees may amend our Amended and Restated Bylaws, or our bylaws, without shareholder approval, to exempt any acquisition of our shares from the statute. Our board of trustees has adopted a resolution exempting any business combination with any person from the business combination statute. The business combination statute (if our board of trustees revokes the foregoing exemption) and the control share acquisition statute could delay or prevent offers to acquire us and increase the difficulty of consummating any such offers, even if such a transaction would be in our shareholders' best interest.

The MGCL, the Maryland REIT Law and our organizational documents limit shareholders' rights to bring claims against our officers and trustees.

The MGCL and the Maryland REIT Law provide that a trustee will not have any liability as a trustee so long as he performs his duties in good faith, in a manner he reasonably believes to be in our best interests, and with the care that an ordinarily prudent person in a like position would use under similar circumstances. In addition, our declaration of trust provides that no trustee or officer will be liable to us or to any shareholder for money damages except to the extent that (a) the trustee or officer actually received an improper benefit or profit in money, property or services, for the amount of the benefit or profit in money, property, or services actually received; or (b) a judgment or the final adjudication adverse to the trustee or officer is entered in a proceeding based on a finding in the proceeding the trustee's or officer's action or failure to act was the result of active and deliberate dishonesty and was material to the cause of action adjudicated in the proceeding. Finally, our declaration of trust authorizes our Company to obligate itself, and our bylaws obligate us, to indemnify and advance expenses to our trustees and officers to the maximum extent permitted by Maryland law.

Our board of trustees is currently classified. Although our board of trustees has voted to recommend that our shareholders approve a proposal to declassify our board of trustees at our 2019 annual meeting of shareholders, there can be no assurance that such proposal will be approved at that the board of trustees will be declassified. A classified board of trustees may prevent others from effecting a change in the control of our board of trustees.

Our board of trustees is currently classified into three classes, with each trustee elected for a three-year term. Although our board of trustees has voted unanimously to submit a proposal to our shareholders to declassify the board of trustees at our 2019 annual meeting of shareholders, the approval of the holders of at least a majority of the outstanding common shares will be required to approve the proposal and there can be no assurance that the proposal will be approved and that the board will be declassified on the timeline anticipated, or at all. The full text of the proposal will be included in our proxy statement, which will be filed in advance of our 2019 annual meeting of shareholders. If our board remains classified, the classified board provision could have the effect of making the replacement of incumbent trustees more time-consuming and difficult. At least two annual meetings of shareholders, instead of one, will generally be required to effect a change in a majority of our board of trustees. Thus, the classified board provision could increase the likelihood that incumbent trustees will retain their positions. The staggered terms of trustees may delay, defer or prevent a transaction or a change in control that might involve a premium price for our common shares or otherwise be in the best interest of the shareholders.

The terms of our employment agreements with our executive officers and severance arrangements with other employees and the terms of certain equity awards granted to our employees may deter others from seeking to acquire us or reduce the price of any such acquisition.

We have entered into employment agreements with our executive officers and severance arrangements with other of our employees, and have granted equity awards to a number of our employees. In certain cases, upon a change of control acquisition of us, such agreements and awards would entitle the officer or employee to severance payments and vesting of otherwise unvested awards. The cost of these payments and the impact of the vesting of such awards could deter a third party from seeking to acquire us or could cause the price payable to shareholders in connection with any such acquisition to be lower than it otherwise may have been. These effects could delay or prevent offers to acquire us and increase the difficulty in consummating any such offers, even if such a transaction would be in our shareholders' best interests.

Future offerings of debt, which would be senior to our common shares upon liquidation, and/or preferred equity securities that may be senior to our common shares for purposes of distributions or upon liquidation, may adversely affect the market price of our common shares.

In the future, we may attempt to increase our capital resources by making additional offerings of debt or preferred equity securities, including medium-term notes, trust preferred securities, senior or subordinated notes and preferred shares. Upon liquidation, holders of our debt securities and preferred shares and lenders with respect to other borrowings will receive distributions of our available assets prior to the holders of our common shares. Additional equity offerings may dilute the holdings of our existing shareholders or reduce the market price of our common shares, or both. Holders of our common shares are not entitled to preemptive rights or other protections against dilution. Our preferred shares, if issued, could have a preference on liquidating distributions or a preference on distribution payments that could limit our ability to pay distributions to the holders of our common shares. Because our decision to issue securities in any future offering will depend on market conditions and other factors beyond our control, we cannot predict or estimate the amount, timing or nature of our future offerings. Thus, our common shareholders bear the risk of our future offerings reducing the market price of our common shares and diluting their share holdings in us.

Item 1B. Unresolved Staff Comments.

None.

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Item 2. Properties.

General

As of December 31, 2018, we wholly-owned 57 commercial properties, including 15 properties in Houston, seven properties in Dallas-Fort Worth, three properties in San Antonio, four properties in Austin, 27 properties in the Scottsdale and Phoenix, Arizona metropolitan areas, and one property in Buffalo Grove, Illinois, a suburb of Chicago.

Our tenants consist of national, regional and local businesses. Our properties generally attract a mix of tenants who provide basic staples, convenience items and services tailored to the specific cultures, needs and preferences of the surrounding community. These types of tenants are the core of our strategy of creating Whitestone-branded Community Centered Properties®. We also believe daily sales of these basic items are less sensitive to fluctuations in the business cycle than higher priced retail items. Our largest tenant represented only 3.0% of our total revenues for the year ended December 31, 2018.

Substantially all of our revenues consist of base rents received under leases that generally have terms that range from less than one year to 15 years. The following table summarizes certain information relating to our properties as of December 31, 2018:

Commercial Properties	GLA	Average Occupancy as of 12/31/18	Annualized Base Rental Revenue (in thousands) (1)	Average Annualized Base Rental Revenue Per Sq. Ft. (2)
Whitestone	4,841,660	90 %	\$ 82,055	\$ 18.83

Calculated as the tenant's actual December 31, 2018 base rent (defined as cash base rents including abatements) multiplied by 12. Excludes vacant space as of December 31, 2018. Because annualized base rental revenue is not derived from historical results that were accounted for in accordance with GAAP, historical results differ from the annualized amounts. Total abatements for leases in effect as of December 31, 2018 equaled approximately \$152,000 for the month ended December 31, 2018.

(2) Calculated as annualized base rent divided by GLA leased as of December 31, 2018. Excludes vacant space as of December 31, 2018.

Our largest property, BLVD Place, a retail community purchased on May 26, 2017 and located in Houston, Texas, accounted for 12.7% of our total revenues for the year ended December 31, 2018. BLVD also accounted for 17.4% of our real estate assets, net of accumulated depreciation, for the year ended December 31, 2018.

As of December 31, 2018, approximately \$178.2 million of our total debt of \$619.4 million was secured by 9 of our properties with a combined net book value of \$279.1 million.

Location of Properties

Of our 57 wholly-owned properties, 15 are located in the greater Houston metropolitan statistical area. These 15 properties represent 29% of our revenue for the year ended December 31, 2018. An additional 27 of our wholly-owned properties are located in the greater Phoenix metropolitan statistical area and represent 42% of our

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revenue for the year ended December 31, 2018.

According to the United States Census Bureau, Houston and Phoenix ranked sixth and twelfth, respectively, in the largest United States metropolitan statistical areas as of December 31, 2018. The following table sets forth information about the unemployment rate in Houston, Phoenix and nationally during the last six months of 2018.

	July	Aug.	Sept.	Oct.	Nov.	Dec.
National ⁽¹⁾	3.9%	3.8%	3.7%	3.8%	3.7%	3.9%
Houston ⁽²⁾	4.4%	4.3%	4.1%	3.8%	3.8%	3.9% ⁽³⁾
Phoenix ⁽²⁾	4.3%	4.5%	4.2%	3.9%	3.9%	4.5% ⁽³⁾

(1) Seasonally adjusted.

(2) Not seasonally adjusted.

(3) Represents estimate.

Source: Bureau of Labor Statistics

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General Physical and Economic Attributes

The following table sets forth certain information relating to each of our properties owned as of December 31, 2018.

Whitestone REIT and Subsidiaries

Property Details

As of December 31, 2018

Community Name	Location	Year Built/ Renovated	Gross Leasable Square Feet	Percent Occupied at 12/31/2018		Annualized Base Rental Revenue (in thousands) (1)	Average Base Rental Revenue Per Sq. Ft. (2)	Average Net Effective Annual Base Rent Per Leased Sq. Ft.(3)
Whitestone Properties:								
Ahwatukee Plaza	Phoenix	1979	72,650	86	%	\$ 801	\$ 12.82	\$ 12.76
Anthem Marketplace	Phoenix	2000	113,293	96	%	1,735	15.95	15.56
Bissonnet Beltway	Houston	1978	29,205	80	%	335	14.34	13.78
BLVD Place	Houston	2014	216,944	99	%	8,277	38.54	43.30
The Citadel	Phoenix	2013	28,547	89	%	466	18.34	16.14
City View Village	San Antonio	2005	17,870	100	%	488	27.31	28.60
Davenport Village	Austin	1999	128,934	100	%	3,334	25.86	25.74
Desert Canyon	Phoenix	2000	62,533	87	%	799	14.69	14.70
Eldorado Plaza	Dallas	2004	221,577	98	%	3,217	14.81	15.27
Fountain Hills	Phoenix	2009	111,289	85	%	1,586	16.77	16.89
Fountain Square	Phoenix	1986	118,209	88	%	1,851	17.79	17.31
Fulton Ranch Towne Center	Phoenix	2005	120,575	87	%	1,746	16.64	17.96
Gilbert Tuscany Village	Phoenix	2009	49,415	100	%	954	19.31	18.82
Gilbert Tuscany Village Hard Corner	Phoenix	2009	14,603	100	%	124	8.49	8.90
Heritage Trace Plaza	Dallas	2006	70,431	91	%	1,407	21.95	23.22
Headquarters Village	Dallas	2009	89,134	84	%	2,148	28.69	29.49
Keller Place	Dallas	2001	93,541	95	%	889	10.00	10.29
Kempwood Plaza	Houston	1974	91,302	89	%	949	11.68	12.31
La Mirada	Phoenix	1997	147,209	81	%	2,515	21.09	21.95
Lion Square	Houston	2014	117,592	98	%	1,501	13.02	12.70
The Marketplace at Central	Phoenix	2012	111,130	99	%	1,001	9.10	8.69
Market Street at DC Ranch	Phoenix	2003	242,459	92	%	4,417	19.80	19.74
Mercado at Scottsdale Ranch	Phoenix	1987	118,730	87	%	1,620	15.68	16.24
Paradise Plaza	Phoenix	1983	125,898	87	%	1,551	14.16	13.96
Parkside Village North	Austin	2005	27,045	100	%	811	29.99	30.58
Parkside Village South	Austin	2012	90,101	100	%	2,338	25.95	26.78
Pima Norte	Phoenix	2007	35,110	68	%	426	17.84	18.56
Pinnacle of Scottsdale	Phoenix	1991	113,108	100	%	2,411	21.32	21.87
Pinnacle Phase II	Phoenix	2017	27,063	100	%	648	23.94	23.69
The Promenade at Fulton Ranch	Phoenix	2007	98,792	87	%	1,138	13.24	15.01
Providence	Houston	1980	90,327	99	%	804	8.99	9.01
Quinlan Crossing	Austin	2012	109,892	98	%	2,339	21.72	23.92

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Seville	Phoenix	1990	90,042	72	%	2,202	33.97	34.17
Shaver	Houston	1978	21,926	94	%	292	14.17	14.07
Shops at Pecos Ranch	Phoenix	2009	78,767	80	%	1,678	26.63	26.14
Shops at Starwood	Dallas	2006	55,385	92	%	1,455	28.56	29.69
The Shops at Williams Trace	Houston	1985	132,991	96	%	1,980	15.51	15.40
South Richey	Houston	1980	69,928	97	%	715	10.54	10.72
Spoerlein Commons	Chicago	1987	41,455	79	%	639	19.51	19.51
Starwood Phase II	Dallas	2016	35,351	72	%	866	34.02	37.17
The Strand at Huebner Oaks	San Antonio	2000	73,920	98	%	1,464	20.21	22.06
SugarPark Plaza	Houston	1974	95,032	100	%	1,126	11.85	13.80

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Whitestone REIT and Subsidiaries
Property Details
As of December 31, 2018

Community Name	Location	Year Built/ Renovated	Gross Leasable Square Feet	Percent Occupied at 12/31/2018	Annualized Base Rental Revenue (in thousands) (1)	Average Base Rental Revenue Per Sq. Ft. (2)	Average Net Effective Annual Base Rent Per Leased Sq. Ft. ⁽³⁾
Sunridge	Houston	1979	49,359	83 %	531	12.96	12.50
Sunset at Pinnacle Peak	Phoenix	2000	41,530	82 %	611	17.94	18.24
Terravita Marketplace	Phoenix	1997	102,733	50 %	1,142	22.23	22.35
Town Park	Houston	1978	43,526	100 %	946	21.73	21.71
Village Square at Dana Park	Phoenix	2009	323,026	87 %	6,107	21.73	21.54
Westchase	Houston	1978	50,332	86 %	633	14.62	14.30
Williams Trace Plaza	Houston	1983	129,222	94 %	1,780	14.65	15.19
Windsor Park	San Antonio	2012	196,458	97 %	1,876	9.84	9.65
Woodlake Plaza	Houston	1974	106,169	80 %	1,386	16.32	15.99
Total/Weighted Average - Whitestone Properties			4,841,660	90 %	82,055	18.83	19.35
Land Held for Development:							
Anthem Marketplace	Phoenix	N/A	—	—	\$ —	\$ —	\$ —
BLVD Phase II-B	Houston	N/A	—	—	—	—	—
Dana Park Development	Phoenix	N/A	—	—	—	—	—
Eldorado Plaza Development	Dallas	N/A	—	—	—	—	—
Fountain Hills	Phoenix	N/A	—	—	—	—	—
Market Street at DC Ranch	Phoenix	N/A	—	—	—	—	—
Total/Weighted Average - Land Held For Development ⁽⁴⁾			—	—	—	—	—
Grand Total/Weighted Average - Whitestone Properties			4,841,660	90 %	\$ 82,055	\$ 18.83	\$ 19.35

Calculated as the tenant's actual December 31, 2018 base rent (defined as cash base rents including abatements) multiplied by 12. Excludes vacant space as of December 31, 2018. Because annualized base rental revenue is not

(1) derived from historical results that were accounted for in accordance with generally accepted accounting principles, historical results differ from the annualized amounts. Total abatements for leases in effect as of December 31, 2018 equaled approximately \$152,000 for the month ended December 31, 2018.

(2) Calculated as annualized base rent divided by gross leasable area leased as of December 31, 2018. Excludes vacant space as of December 31, 2018.

(3)

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Represents (i) the contractual base rent for leases in place as of December 31, 2018, adjusted to a straight-line basis to reflect changes in rental rates throughout the lease term and amortize free rent periods and abatements, but without regard to tenant improvement allowances and leasing commissions, divided by (ii) square footage under commenced leases of December 31, 2018.

- (4) As of December 31, 2018, these parcels of land were held for development and, therefore, had no gross leasable area.

Significant Tenants

The following table sets forth information about our 15 largest tenants as of December 31, 2018, based upon consolidated annualized rental revenues at December 31, 2018.

Tenant Name	Location	Annualized of Total Rental Revenue (in thousands)	Percentage		Initial Lease Date	Year Expiring
			Base	Annualized		
		(in thousands)	Revenues	(1)		
Safeway Stores Incorporated ⁽²⁾	Austin, Houston and Phoenix	\$ 2,447	3.0	%	11/14/1982, 5/8/1991, 7/1/2000, 4/1/2014, 4/1/2014 and 10/19/16	2020, 2020, 2021, 2022, 2024 and 2034
Whole Foods Market	Houston	2,042	2.5	%	9/3/2014	2035
Frost Bank	Houston	1,872	2.3	%	7/1/2014	2024
Newmark Real Estate of Houston LLC	Houston	1,188	1.4	%	10/1/2015	2026
Walgreens & Co. ⁽³⁾	Houston and Phoenix	946	1.1	%	11/14/1982, 11/2/1987, 8/24/1996 and 11/3/1996	2022, 2027, 2049 and 2056
Verizon Wireless ⁽⁴⁾	Houston and Phoenix	875	1.1	%	8/16/1994, 2/1/2004, 5/10/2004, 1/27/2006 and 5/1/2014	2019, 2019, 2022, 2023 and 2024
Bashas' Inc. ⁽⁵⁾	Phoenix	823	1.0	%	10/9/2004 and 4/1/2009	2024 and 2029
Alamo Drafthouse Cinema	Austin	690	0.8	%	2/1/2012	2027
Dollar Tree ⁽⁶⁾	Houston and Phoenix	677	0.8	%	3/1/1998, 8/10/1999, 6/29/2001, 11/8/2009, 12/17/2009, and 5/21/2013	2020, 2020, 2021, 2022, 2023 and 2027
Wells Fargo & Company ⁽⁷⁾	Phoenix	553	0.7	%	10/24/1996 and 4/16/1999	2022 and 2023
Kroger Co.	Dallas	483	0.6	%	12/15/2000	2022
Ruth's Chris Steak House Inc.	Phoenix	466	0.6	%	1/1/1991	2030
Regus Corporation	Houston	434	0.5	%	5/23/2014	2025
Paul's Ace Hardware	Phoenix	427	0.5	%	3/1/2008	2023
Ross Dress for Less, Inc. ⁽⁸⁾	Phoenix and San Antonio	362	0.4	%	2/11/2009 and 6/18/2012	2020, 2023
		\$ 14,285	17.3	%		

(1) Annualized Base Rental Revenues represents the monthly base rent as of December 31, 2018 for each applicable tenant multiplied by 12.

As of December 31, 2018, we had six leases with the same tenant occupying space at properties located in Phoenix, Houston and Austin. The annualized rental revenue for the lease that commenced on April 1, 2014, and is scheduled to expire in 2034, was \$997,000, which represents approximately 1.2% of our total annualized base rental revenue. The annualized rental revenue for the lease that commenced on April 1, 2014, and is scheduled to expire in 2024, was \$42,000, which represents less than 0.1% of our annualized base rental revenue. The annualized rental revenue for the lease that commenced on May 8, 1991, and is scheduled to expire in 2021, was (2) \$344,000, which represents approximately 0.4% of our total annualized base rental revenue. The annualized rental revenue for the lease that commenced on July 1, 2000, and is scheduled to expire in 2020, was \$321,000, which represents approximately 0.4% of our total annualized base rental revenue. The annualized rental revenue for the lease that commenced on November 14, 1982, and is scheduled to expire in 2022, was \$318,000, which represents approximately 0.4% of our total annualized base rental revenue. The annualized rental revenue for the lease that commenced on October 19, 2016, and is scheduled to expire in 2020, was \$425,000, which represents approximately 0.5% of our total annualized base rental revenue.

As of December 31, 2018, we had four leases with the same tenant occupying space at properties located in Phoenix and Houston. The annualized rental revenue for the lease that commenced on November 3, 1996, and is scheduled to expire in 2049, was \$279,000, which represents approximately 0.3% of our total annualized base rental revenue. The annualized rental revenue for the lease that commenced on November 2, 1987, and is (3) scheduled to expire in 2027, was \$188,000, which represents approximately 0.2% of our total annualized base rental revenue. The annualized rental revenue for the lease that commenced on November 14, 1982, and is scheduled to expire in 2022, was \$181,000, which represents approximately 0.2% of our total annualized base rental revenue. The annualized rental revenue for the lease that commenced on August 24, 1996, and is scheduled to expire in 2056, was \$298,000, which represents approximately 0.4% of our total annualized rental revenue.

As of December 31, 2018, we had five leases with the same tenant occupying space at properties located in Phoenix and Houston. The annualized rental revenue for the lease that commenced on August 16, 1994, and is scheduled to expire in 2019, was \$21,000, which represents less than 0.1% of our total annualized base rental revenue. The annualized rental revenue for the lease that commenced on January 27, 2006, and is scheduled to expire in 2023, was \$130,000, which represents approximately 0.2% of our total annualized base rental revenue. (4) The annualized rental revenue for the lease that commenced on February 1, 2004, and is scheduled to expire in 2019, was \$37,000, which represents less than 0.1% of our total annualized base rental revenue. The annualized rental revenue for the lease that commenced on May 1, 2014, and is scheduled to expire in 2024, was \$681,000, which represents approximately 0.8% of our total annualized rental revenue. The annualized rental revenue for the lease that commenced on May 10, 2004, and is scheduled to expire in 2022, was \$6,000, which represents less than 0.1% of our total annualized base rental revenue.

As of December 31, 2018, we had two leases with the same tenant occupying space at properties located in Phoenix. The annualized rental revenue for the lease that commenced on October 9, 2004, and is scheduled to (5) expire in 2024, was \$119,000, which represents approximately 0.1% of our total annualized base rental revenue. The annualized rental revenue for the lease that commenced on April 1, 2009, and is scheduled to expire in 2029, was \$704,000, which represents approximately 0.9% of our total annualized base rental revenue.

(6) As of December 31, 2018, we had six leases with the same tenant occupying space at properties in Houston and Phoenix. The annualized rental revenue for the lease that commenced on March 1, 1998, and is scheduled to expire in 2022, was \$73,000, which represents less than 0.1% of our total annualized base rental revenue. The annualized rental revenue for the lease that commenced on August 10, 1999, and is scheduled to expire in 2020, was \$88,000, which represents approximately 0.1% of our total annualized base rental revenue. The annualized rental revenue for the lease that commenced on December 17, 2009, and is scheduled to expire in 2020, was \$110,000, which represents approximately 0.1% of our total annualized base rental revenue. The annualized rental revenue for the

lease that commenced on June 29, 2001, and is scheduled to expire in 2021, was \$145,000, which represents approximately 0.2% of our total annualized base rental revenue. The annualized rental revenue for the lease that commenced on May 21, 2013, and is scheduled to expire in 2023, was \$111,000, which represents approximately 0.1% of our total annualized base rental revenue. The annualized rental revenue for the lease that commenced on November 8, 2009, and is scheduled to expire in 2027, was \$151,000, which represents approximately 0.2% of our total annualized base rental revenue.

As of December 31, 2018, we had two leases with the same tenant occupying space at properties located in Phoenix. The annualized rental revenue for the lease that commenced on October 24, 1996, and is scheduled to expire in 2022, was \$131,000, which represents approximately 0.2% of our total annualized base rental revenue.⁽⁷⁾ The annualized rental revenue for the lease that commenced on April 16, 1999, and is scheduled to expire in 2023, was \$421,000, which represents approximately 0.5% of our total annualized base rental revenue.

As of December 31, 2018, we had two leases with the same tenant occupying space at properties located in San Antonio and Phoenix. The annualized rental revenue for the lease that commenced on June 18, 2012, and is scheduled to expire in 2023, was \$175,000, which represents approximately 0.2% of our total annualized base rental revenue.⁽⁸⁾ The annualized rental revenue for the lease that commenced on February 11, 2009, and is scheduled to expire in 2020, was \$187,000, which represents approximately 0.2% of our total annualized base rental revenue.

Lease Expirations

The following table lists, on an aggregate basis, all of our consolidated scheduled lease expirations over the next 10 years.

Year	Number of Leases	GLA Approximate Square Feet	Percent of Total	Annualized Base Rent as of December 31, 2018	
				Amount (in thousands)	Percent of Total
2019	370	633,907	13.1 %	\$12,998	15.8 %
2020	219	786,854	16.3 %	13,032	15.8 %
2021	198	512,859	10.6 %	9,994	12.1 %
2022	167	626,485	12.9 %	11,220	13.6 %
2023	154	474,322	9.8 %	9,437	11.4 %
2024	79	477,378	9.9 %	7,664	9.3 %
2025	43	156,796	3.2 %	3,614	4.4 %
2026	26	172,237	3.6 %	3,309	4.0 %
2027	26	173,391	3.6 %	3,457	4.2 %
2028	21	98,415	2.0 %	2,131	2.6 %
Total	1,303	4,112,644	85.0 %	\$76,856	93.2 %

Insurance

We believe that we have property and liability insurance with reputable, commercially rated companies. We also believe that our insurance policies contain commercially reasonable deductibles and limits, adequate to cover our properties. We expect to maintain this type of insurance coverage and to obtain similar coverage with respect to any additional properties we acquire in the near future. Further, we have title insurance relating to our properties in an aggregate amount that we believe to be adequate.

Item 3. Legal Proceedings.

We are a participant in various legal proceedings and claims that arise in the ordinary course of our business. These matters are generally covered by insurance. While the resolution of these matters cannot be predicted with certainty, we believe that the final outcome of these matters will not have a material effect on our financial position, results of operations or cash flows.

Item 4. Mine Safety Disclosures.

Not applicable.

PART II

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

Market Information

Common Shares

Our common shares are traded on the NYSE under the ticker symbol "WSR." As of March 15, 2019, we had 39,766,240 common shares of beneficial interest outstanding held by a total of 1,123 shareholders of record.

On March 15, 2019, the closing price of our common shares reported on the NYSE was \$11.88 per share.

Distributions

U.S. federal income tax law generally requires that a REIT distribute annually to its shareholders at least 90% of its REIT taxable income, without regard to the deduction for dividends paid and excluding net capital gains, and that it pay tax at regular corporate rates on any taxable income that it does not distribute. We currently, and intend to continue to, accrue distributions quarterly and make distributions in three monthly installments following the end of each quarter. For a discussion of our cash flow as compared to dividends, see "Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources."

The timing and frequency of our distributions are authorized and declared by our board of trustees in exercise of its business judgment based upon a number of factors, including:

- our funds from operations;
- our debt service requirements;
- our capital expenditure requirements for our properties;
- our taxable income, combined with the annual distribution requirements necessary to maintain REIT qualification;
- requirements of Maryland law;
- our overall financial condition; and
- other factors deemed relevant by our board of trustees.

Any distributions we make will be at the discretion of our board of trustees and we cannot provide assurance that our distributions will be made or sustained in the future.

The following table reflects the total distributions we have paid (including the total amount paid and the amount paid per share/unit) in each indicated quarter (in thousands, except per share/unit data):

Quarter Paid	Common Shares		Noncontrolling OP Unit Holders		Total
	Distributions Per Common Share	Total Amount Paid	Distributions Per OP Unit	Total Amount Paid	Total Amount Paid
2018					
Fourth Quarter	\$0.2850	\$ 11,302	\$0.2850	\$ 265	\$ 11,567
Third Quarter	0.2850	11,294	0.2850	286	11,580
Second Quarter	0.2850	11,203	0.2850	295	11,498
First Quarter	0.2850	11,145	0.2850	309	11,454
Total	\$ 1.1400	\$ 44,944	\$ 1.1400	\$ 1,155	\$ 46,099
2017					
Fourth Quarter	\$0.2850	\$ 11,002	\$0.2850	\$ 309	\$ 11,311
Third Quarter	0.2850	10,948	0.2850	309	11,257
Second Quarter	0.2850	10,093	0.2850	310	10,403
First Quarter	0.2850	8,429	0.2850	313	8,742
Total	\$ 1.1400	\$ 40,472	\$ 1.1400	\$ 1,241	\$ 41,713

Equity Compensation Plan Information

Please refer to Item 12 of this Annual Report on Form 10-K for information concerning securities authorized under our equity incentive plan.

Issuer Purchases of Equity Securities

During the three months ended December 31, 2018, certain of our employees tendered owned common shares to satisfy the tax withholding on the lapse of certain restrictions on restricted common shares issued under our 2008 Long-Term Equity Incentive Ownership Plan (the "2008 Plan"). The following table summarizes all of these repurchases during the three months ended December 31, 2018.

Period	Total Number of Shares Purchased (1)	Average Price Paid for Shares	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet be Purchased Under the Plans or Programs
October 1, 2018 through October 31, 2018	—	\$ —	N/A	N/A
November 1, 2018 through November 30, 2018	—	—	N/A	N/A
December 1, 2018 through December 31, 2018	21,414	12.26	N/A	N/A
Total	21,414	\$ 12.26		

(1) The number of shares purchased represents common shares held by employees who tendered owned common shares to satisfy the tax withholding on the lapse of certain restrictions on restricted common shares issued under the 2008 Plan. With respect to these shares, the price paid per share is based on the fair market value at the time of tender.

Performance Graph

The following graph compares the total shareholder returns of the Company's common shares to the Standard & Poor's 500 Index ("S&P 500 Index") and to the Morgan Stanley Capital International US REIT Index ("REIT Index") from December 31, 2013 to December 31, 2018. The graph assumes that the value of the investment in our common shares and in the S&P 500 Index and REIT Index was \$100 at December 31, 2013 and that all dividends were reinvested. The closing price of our common shares on December 31, 2013 (on which the graph is based) was \$13.37. The past shareholder return shown on the following graph is not necessarily indicative of future performance. The performance graph and related information shall not be deemed "filed" with the SEC, nor shall such information be incorporated by reference into any future filing, except to the extent the Company specifically incorporates it by reference into such filing.

Item 6. Selected Financial Data.

The following table sets forth our selected consolidated financial information and should be read in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and our audited consolidated financial statements and the notes thereto, both of which appear elsewhere in this Annual Report on Form 10-K.

	Year Ended December 31,				
	(in thousands, except per share and per square foot data)				
	2018	2017	2016	2015	2014
Operating Data:					
Revenues	\$119,863	\$125,959	\$104,437	\$93,416	\$72,382
Property expenses	37,431	42,110	34,092	31,335	25,152
General and administrative	23,281	23,949	23,922	20,312	15,274
Depreciation and amortization	25,679	27,240	22,457	19,761	15,725
Equity in earnings of real estate partnership	(8,431)	—	—	—	—
Interest expense	25,177	23,651	19,239	14,910	10,579
Interest, dividend and other investment income	(1,055)	(410)	(429)	(313)	(90)
Income from continuing operations before loss on disposal of assets and income taxes	17,781	9,419	5,156	7,411	5,742
Provision for income taxes	(347)	(386)	(289)	(372)	(282)
Gain on sale of property	4,629	16	3,357	—	—
Profit sharing expense	—	(278)	(15)	—	—
Loss on disposal of assets	(82)	(183)	(96)	(185)	(111)
Income from continuing operations	21,981	8,588	8,113	6,854	5,349
Income from discontinued operations	—	—	—	11	510
Gain on sale of properties from discontinued operations	—	—	—	—	1,887
Net income	21,981	8,588	8,113	6,865	7,746
Less: net income attributable to noncontrolling interests	550	254	182	116	160
Net income attributable to Whitestone REIT	\$21,431	\$8,334	\$7,931	\$6,749	\$7,586

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	Year Ended December 31, (in thousands, except per share data and per square foot and occupancy)				
	2018	2017	2016	2015	2014
Earnings per share - basic					
Income from continuing operations attributable to Whitestone REIT excluding amounts attributable to unvested restricted shares	\$0.54	\$0.22	\$0.26	\$0.25	\$0.23
Income from discontinued operations attributable to Whitestone REIT	—	—	—	—	0.10
Net income attributable to common shareholders excluding amounts attributable to unvested restricted shares	\$0.54	\$0.22	\$0.26	\$0.25	\$0.33
Earnings per share - diluted					
Income from continuing operations attributable to Whitestone REIT excluding amounts attributable to unvested restricted shares	\$0.52	\$0.22	\$0.26	\$0.24	\$0.22
Income from discontinued operations attributable to Whitestone REIT	—	—	—	—	0.10
Net income attributable to common shareholders excluding amounts attributable to unvested restricted shares	\$0.52	\$0.22	\$0.26	\$0.24	\$0.32
Balance Sheet Data:					
Real estate (net)	\$938,938	\$1,018,420	\$813,052	\$745,958	\$602,068
Other assets	89,934	51,748	38,327	36,127	30,137
Total assets	\$1,028,872	\$1,070,168	\$851,379	\$782,085	\$632,205
Liabilities	\$669,722	\$711,764	\$583,751	\$535,094	\$418,882
Whitestone REIT shareholders' equity	350,456	347,604	255,687	242,974	210,072
Noncontrolling interest in subsidiary	8,694	10,800	11,941	4,017	3,251
	\$1,028,872	\$1,070,168	\$851,379	\$782,085	\$632,205
Other Data:					
Proceeds from issuance of common shares	\$—	\$118,412	\$30,014	\$49,649	\$6,458
Acquisitions of and additions to real estate ⁽¹⁾	\$11,638	\$231,120	\$91,785	\$163,050	\$142,065
Distributions per share ⁽²⁾	\$1.14	\$1.13	\$1.13	\$1.13	\$1.13
Funds from operations ⁽³⁾	\$39,398	\$35,039	\$27,031	\$26,696	\$21,920
Total occupancy at year end	90	% 88	% 87	% 87	% 87
Average aggregate GLA	4,925	6,403	5,837	5,734	5,075
Average rent per square foot	\$18.81	\$16.81	\$15.45	\$14.62	\$13.57

⁽¹⁾ Including amounts for discontinued operations.

⁽²⁾ The distributions per share represent total cash payments

divided by
weighted
average
common
shares.

(3) We believe
that Funds
From
Operations
("FFO") is an
appropriate
supplemental
measure of
operating
performance
because it
helps our
investors
compare our
operating
performance
relative to
other
REITs. The
National
Association of
Real Estate
Investment
Trusts
("NAREIT")
defines FFO as
net income
(loss) available
to common
shareholders
computed in
accordance
with GAAP,
excluding
gains or losses
from sales of
operating
properties and
extraordinary
items, plus
depreciation
and
amortization of
real estate
assets,

including our share of equity method investments and joint ventures. We calculate FFO in a manner consistent with the NAREIT definition. For more information, see “Management’s Discussion and Analysis of Financial Condition and Results of Operations - Reconciliation of Non-GAAP Financial Measures.”

The following table sets forth a reconciliation of net income to FFO, the nearest GAAP measure, for the periods presented:

	Year Ended December 31,				
	(in thousands)				
	2018	2017	2016	2015	2014
Net income attributable to Whitestone REIT	\$21,431	\$8,334	\$7,931	\$6,749	\$7,586
Adjustments to reconcile to FFO: ⁽¹⁾					
Depreciation and amortization of real estate assets ⁽²⁾	25,401	26,290	22,179	19,646	15,950
Depreciation and amortization of real estate assets of real estate partnership (pro rata) ⁽³⁾	2,903	—	—	—	—
Loss (gain) on sale or disposal of assets ⁽²⁾	(4,547)	167	(3,261)	185	(1,776)
Gain on sale or disposal of properties or assets of real estate partnership (pro rata) ⁽³⁾	(6,340)	—	—	—	—
Net income attributable to redeemable operating partnership units ⁽²⁾	550	254	182	116	160
FFO	\$39,398	\$35,045	\$27,031	\$26,696	\$21,920

⁽¹⁾ Includes pro rata share attributable to real estate partnership in 2018.

⁽²⁾ Including amounts for discontinued operations.

⁽³⁾ Included in equity in earnings of real estate partnership on the consolidated statements of operations and comprehensive income.

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

You should read the following discussion of our financial condition and results of operations in conjunction with our audited consolidated financial statements and the notes thereto included in this Annual Report on Form 10-K. For more detailed information regarding the basis of presentation for the following information, you should read the notes to our audited consolidated financial statements included in this Annual Report on Form 10-K.

On February 26, 2019, our Audit Committee, after consultation with members of senior management of the Company, concluded that the Company's unaudited consolidated financial statements as of and for the periods ended March 31, 2018, June 30, 2018 and September 30, 2018 (collectively, the "2018 Quarterly Financial Statements") included in the Company's Quarterly Reports on Form 10-Q for the quarterly periods ended March 31, 2018, June 30, 2018 and September 30, 2018, respectively, should be restated to correct the accounting error described below.

As previously disclosed in the Company's Current Form 8-K filed with the SEC on February 27, 2019, on January 1, 2018, the Company adopted Topic 606, as subsequently amended, using the modified retrospective method and applied Topic 606 to those contracts that were not completed as of January 1, 2018. We applied Topic 606 to account for contracts (that do not meet the definition of a business) to customers. We accounted for contracts (that do not meet the definition of a business) to noncustomers under ASC 610, which requires the application of certain concepts from Topic 606. In August 2018, the Company received a comment letter from the Staff relating to its Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2018. The Staff requested that the Company provide them with an analysis of the Company's determination that the contribution of assets to Pillarstone OP (as described in the Form 8-K) did not meet the requirements for derecognition of the underlying assets under Topic 606 and ASC 610, and an explanation of the Company's consideration of the immaterial accounting errors related to Pillarstone OP in its conclusion that the Company's disclosure controls and procedures and internal controls over financial reporting were effective as of June 30, 2018 and December 31, 2017. In September 2018, the Company responded to the Staff's letter with the requested analysis and explanation. In October 2018, the Company received a comment letter from the Staff with certain follow up questions. Subsequently, the Company engaged in verbal discussions with the Staff regarding its responses, and in February 2019, the Staff verbally informed the Company that it objected to the Company's conclusion regarding the assessment of the transfer of control criteria in Topic 606 with respect to the contribution and objected to the Company's continued recognition of the underlying assets and liabilities associated with the contribution subsequent to the adoption of Topic 606 and ASC 610 on January 1, 2018. Accordingly, the Company concluded that the 2018 Quarterly Financial Statements should be restated. Because this change from the profit sharing method is only applicable for periods ending after giving effect to the implementation of Topic 606 and ASC 610, no periods prior to January 1, 2018 are affected by this error.

Overview of Our Company

We are a fully integrated real estate company that owns and operates commercial properties in culturally diverse markets in major metropolitan areas. Founded in 1998, we are internally managed with a portfolio of commercial properties in Texas, Arizona and Illinois.

In October 2006, our current management team joined the Company and adopted a strategic plan to acquire, redevelop, own and operate Community Centered Properties®. We define Community Centered Properties® as visibly located properties in established or developing culturally diverse neighborhoods in our target markets. We market, lease, and manage our centers to match tenants with the shared needs of the surrounding neighborhood. Those needs may include specialty retail, grocery, restaurants and medical, educational and financial services. Our goal is for each property to become a Whitestone-branded retail community that serves a neighboring five-mile radius around our property. We employ and develop a diverse group of associates who understand the needs of our multicultural

communities and tenants.

As of December 31, 2018, we wholly-owned 57 commercial properties consisting of:

Consolidated Operating Portfolio

51 properties that meet our Community Centered Properties® strategy containing approximately 4.8 million square feet of GLA and having a total carrying amount (net of accumulated depreciation) of \$921.1 million; and

Redevelopment, New Acquisitions Portfolio

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six parcels of land held for future development that meet our Community Centered Properties® strategy having a total carrying amount of \$17.8 million.

As of December 31, 2018, we had an aggregate of 1,337 tenants. We have a diversified tenant base with our largest tenant comprising only 3.0% of our total revenues for the year ended December 31, 2018. Lease terms for our properties range from less than one year for smaller tenants to more than 15 years for larger tenants. Our leases generally include minimum monthly lease payments and tenant reimbursements for taxes, insurance and maintenance. We completed 308 new and renewal leases during 2018, totaling 727,440 square feet and \$82.7 million in total lease value.

We employed 98 full-time employees as of December 31, 2018. As an internally managed REIT, we bear our own expenses of operations, including the salaries, benefits and other compensation of our employees, office expenses, legal, accounting and investor relations expenses and other overhead costs.

Real Estate Partnership

As of December 31, 2018, we, through our investment in Pillarstone OP, owned a majority interest in 11 properties that do not meet our Community Centered Property® strategy containing approximately 1.3 million square feet of GLA (the “Pillarstone Properties”). We own 81.4% of the total outstanding units of Pillarstone OP, which we account for using the equity method. We also manage the day-to-day operations of Pillarstone OP.

Recent Developments

On January 31, 2019, we, through our Operating Partnership, entered into an unsecured credit facility (the “2019 Facility”) with the lenders party thereto, Bank of Montreal, as administrative agent (the “Agent”), SunTrust Robinson Humphrey, as syndication agent, and BMO Capital Markets Corp., U.S. Bank National Association, SunTrust Robinson Humphrey and Regions Capital Markets, as co-lead arrangers and joint book runners. The 2019 Facility amended and restated the 2018 Facility.

The 2019 Facility is comprised of the following three tranches:

\$250.0 million unsecured revolving credit facility with a maturity date of January 1, 2023 (the “2019 Revolver”);

\$165.0 million unsecured term loan with a maturity date of January 31, 2024 (“Term Loan A”); and

\$100.0 million unsecured term loan with a maturity date of October 30, 2022 (“Term Loan B” and together with Term Loan A, the “2019 Term Loans”).

The 2019 Facility includes an accordion feature that will allow the Operating Partnership to increase the borrowing capacity by \$200.0 million, upon the satisfaction of certain conditions. The Company used \$446.2 million of proceeds from the 2019 Facility to repay amounts outstanding under the 2018 Facility and intends to use the remaining proceeds from the 2019 Facility for general corporate purposes, including property acquisitions, debt repayment, capital expenditures, expansion, redevelopment and re-tenanting of properties in its portfolio and working capital.

The Company, each direct and indirect material subsidiary of the Operating Partnership and any other subsidiary of the Operating Partnership that is a guarantor under any unsecured ratable debt will serve as a guarantor for funds borrowed by the Operating Partnership under the 2019 Facility. The 2019 Facility contains customary terms and conditions, including, without limitation, customary representations and warranties and affirmative and negative covenants including, without limitation, information reporting requirements, limitations on investments, acquisitions,

loans and advances, mergers, consolidations and sales, incurrence of liens, dividends and restricted payments. In addition, the 2019 Facility contains certain financial covenants including the following:

• maximum total indebtedness to total asset value ratio of 0.60 to 1.00;

• maximum secured debt to total asset value ratio of 0.40 to 1.00;

• minimum EBITDA (earnings before interest, taxes, depreciation, amortization or extraordinary items) to fixed charges ratio of 1.50 to 1.00;

• maximum other recourse debt to total asset value ratio of 0.15 to 1.00; and

• maintenance of a minimum tangible net worth (adjusted for accumulated depreciation and amortization) of \$372 million plus 75% of the net proceeds from additional equity offerings (as defined).

The 2019 Facility also contains customary events of default with customary notice and cure, including, without limitation, nonpayment, breach of covenant, misrepresentation of representations and warranties in a material respect, cross-default to other major indebtedness, change of control, bankruptcy and loss of REIT tax status. If an event of default occurs and is continuing under the 2019 Facility, the lenders may, among other things, terminate their commitments under the 2019 Facility and require the immediate payment of all amounts owed thereunder.

How We Derive Our Revenue

Substantially all of our revenue is derived from rents received from leases at our properties. We had rental income and tenant reimbursements of approximately \$119,863,000 for the year ended December 31, 2018 as compared to \$125,959,000 for the year ended December 31, 2017, a decrease of \$6,096,000, or 5%. The year ended December 31, 2018 included \$6,486,000 in increased revenues from Non-Same Store operations and \$15,441,000 in decreased revenues from the Pillarstone Properties (as defined below) due to the accounting change from the profit sharing method to the equity method. We define “Non-Same Stores” as properties acquired since the beginning of the period being compared and properties that have been sold, but not classified as discontinued operations. During the twelve months ended December 31, 2018, Same Store revenues increased \$2,859,000. We define “Same Stores” as properties owned during the entire period being compared. For purposes of comparing the year ended December 31, 2018 to the year ended December 31, 2017, Same Stores include properties owned from January 1, 2016 to December 31, 2017. Same Store average occupied square feet increased from 3,959,354 for the year ended December 31, 2017 to 3,967,881 for the year ended December 31, 2018, increasing Same Store revenue by \$201,000. Same Store average occupancy decreased from 90.2% for the year ended December 31, 2017 to 90.1% for the year ended December 31, 2018. Same Store revenue rate per average leased square foot increased \$0.67 for the year ended December 31, 2018 to \$25.10 per average leased square foot as compared to the year ended December 31, 2017 revenue rate per average leased square foot of \$24.43, increasing Same Store revenue by \$2,658,000. The revenue rate per average leased square feet is calculated by dividing the total revenue by the average square feet leased during the period.

Known Trends in Our Operations; Outlook for Future Results

Rental Income

We expect our rental income to increase year-over-year due to the addition of properties and rent increases on renewal leases. The amount of net rental income generated by our properties depends principally on our ability to maintain the occupancy rates of currently leased space and to lease currently available space, newly acquired properties with vacant space, and space available from unscheduled lease terminations. The amount of rental income we generate also depends on our ability to maintain or increase rental rates in our submarkets. Over the past three years, we have seen modest improvement in the overall economy in our markets, which has allowed us to maintain overall occupancy rates, with slight increases in occupancy at certain of our properties, and to recognize modest increases in rental rates. We expect this trend to continue in 2019.

Scheduled Lease Expirations

We tend to lease space to smaller businesses that desire shorter term leases. As of December 31, 2018, approximately 29% of our GLA was subject to leases that expire prior to December 31, 2020. Over the last three years, we have

renewed expiring leases with respect to approximately 80% of our GLA. We routinely seek to renew leases with our existing tenants prior to their expiration and typically begin discussions with tenants as early as 18 months prior to the expiration date of the existing lease. Inasmuch as our early renewal program and other leasing and marketing efforts target these expiring leases, we hope to re-lease most of that space prior to expiration of the leases. In the markets in which we operate, we obtain and analyze market rental rates through review of third-party publications, which provide market and submarket rental rate data and through inquiry of property owners and property management companies as to rental rates being quoted at properties that are located in close proximity to our properties and we believe display similar physical attributes as our nearby properties. We use this data to negotiate leases with new tenants and renew leases with our existing tenants at rates we believe to be competitive in the markets for our individual properties. Due to the short term nature of our leases, and based upon our analysis of market rental rates, we believe that, in the aggregate, our current leases are at market rates. Market conditions, including new supply of properties, and macroeconomic conditions in our markets and nationally affecting tenant income, such as employment levels, business conditions, interest rates, tax rates, fuel and energy costs and other matters, could adversely impact our renewal rate

and/or the rental rates we are able to negotiate. We continue to monitor our tenants' operating performances as well as overall economic trends to evaluate any future negative impact on our renewal rates and rental rates, which could adversely affect our cash flow and ability to make distributions to our shareholders.

Acquisitions

We have continued to successfully grow our GLA through the acquisition of additional properties, and we expect to actively pursue and consummate additional acquisitions in the foreseeable future. We believe that over the next few years we will continue to have excellent opportunities to acquire quality properties at historically attractive prices. We have extensive relationships with community banks, attorneys, title companies and others in the real estate industry, which we believe enables us to take advantage of these market opportunities and maintain an active acquisition pipeline.

Property Acquisitions and Dispositions

We seek to acquire commercial properties in high-growth markets. Our acquisition targets are properties that fit our Community Centered Properties® strategy. We define Community Centered Properties® as visibly located properties in established or developing, culturally diverse neighborhoods in our target markets, primarily in and around Phoenix, Chicago, Dallas, Fort Worth, San Antonio and Houston. We may acquire properties in other high growth cities in the future. We market, lease and manage our centers to match tenants with the shared needs of the surrounding neighborhood. Those needs may include specialty retail, grocery, restaurants and medical, educational and financial services. Our goal is for each property to become a Whitestone-branded business center or retail community that serves a neighboring five-mile radius around our property.

Property Dispositions. We seek to continually upgrade our portfolio by opportunistically selling properties that do not have the potential to meet our Community Centered Property® strategy and redeploying the sale proceeds into properties that better fit our strategy. Some of our properties that we owned at the time our current management team assumed the management of the Company may not fit our Community Centered Property® strategy, and we may look for opportunities to dispose of these properties as we continue to execute our strategy. For example, in December 2014, we sold three suburban office properties in Clear Lake, Texas that were part of the Legacy Portfolio. In 2016, we sold three properties in the greater Houston area. In 2018, we sold two properties in the greater Houston area, and Pillarstone OP, through an indirect wholly owned subsidiary, Whitestone Industrial-Office, LLC, sold a portfolio of three properties in the greater Houston area.

On December 8, 2016, we, through our Operating Partnership, entered into a Contribution Agreement (the "Contribution Agreement") with Pillarstone and Pillarstone REIT pursuant to which we contributed all of the equity interests in four of our wholly-owned subsidiaries: Whitestone CP Woodland Ph. 2, LLC, a Delaware limited liability company ("CP Woodland"); Whitestone Industrial-Office, LLC, a Texas limited liability company ("Industrial-Office"); Whitestone Offices, LLC, a Texas limited liability company ("Whitestone Offices"); and Whitestone Uptown Tower, LLC, a Delaware limited liability company ("Uptown Tower", and together with CP Woodland, Industrial-Office and Whitestone Offices, the "Entities") that own 14 non-core properties (the "Pillarstone Properties") that do not fit our Community Centered Property® strategy, to Pillarstone for aggregate consideration of approximately \$84.0 million, consisting of (1) approximately \$18.1 million Class A units representing limited partnership interests in Pillarstone ("Pillarstone OP Units"), issued at a price of \$1.331 per Pillarstone OP Unit; and (2) the assumption of approximately \$65.9 million of liabilities, consisting of (a) approximately \$15.5 million of our liability under the 2018 Facility (see Note 9 to the accompanying consolidated financial statements); (b) an approximately \$16.3 million promissory note of Uptown Tower under the Loan Agreement, dated as of September 26, 2013, between Uptown Tower, as borrower, and U.S. Bank, National Association, as successor to Morgan Stanley Mortgage Capital Holdings LLC, as lender; and (c) an approximately \$34.1 million promissory note (the "Industrial-Office Promissory Note") of Industrial-Office issued

under the Loan Agreement, dated as of November 26, 2013 (the “Industrial-Office Loan Agreement”), between Industrial-Office, as borrower, and Jackson National Life Insurance Company, as lender (collectively, the “Contribution”).

In connection with the Contribution, on December 8, 2016, the Operating Partnership entered into an OP Unit Purchase Agreement (the “OP Unit Purchase Agreement”) with Pillarstone REIT and Pillarstone pursuant to which the Operating Partnership agreed to purchase up to an aggregate of \$3.0 million of Pillarstone OP Units at a price of \$1.331 per Pillarstone OP Unit over the two-year term of the OP Unit Purchase Agreement on the terms set forth therein. The OP Unit Purchase Agreement contains customary closing conditions and the parties have made certain customary representations, warranties and indemnifications to each other in the OP Unit Purchase Agreement. In addition, pursuant to the OP Unit Purchase Agreement, in the event of a Change of Control (as defined therein) of the Company, Pillarstone shall have the right, but not the obligation, to repurchase the Pillarstone OP Units issued thereunder from the Operating Partnership at their initial issue price of \$1.331 per Pillarstone OP Unit.

In connection with the Contribution, (1) with respect to each Pillarstone Property (other than Uptown Tower), Whitestone TRS, Inc., a subsidiary of the Company (“Whitestone TRS”), entered into a Management Agreement with the Entity that owns such Pillarstone Property and (2) with respect to Uptown Tower, Whitestone TRS entered into a Management Agreement with Pillarstone (collectively, the “Management Agreements”). Pursuant to the Management Agreements with respect to each Pillarstone Property (other than Uptown Tower), Whitestone TRS agreed to provide certain property management, leasing and day-to-day advisory and administrative services to such Pillarstone Property in exchange for (x) a monthly property management fee equal to 5.0% of the monthly revenues of such Pillarstone Property and (y) a monthly asset management fee equal to 0.125% of GAV (as defined in each Management Agreement as, generally, the purchase price of the respective Pillarstone Property based upon the purchase price allocations determined pursuant to the Contribution Agreement, excluding all indebtedness, liabilities or claims of any nature) of such Pillarstone Property. Pursuant to the Management Agreement with respect to Uptown Tower, Whitestone TRS agreed to provide certain property management, leasing and day-to-day advisory and administrative services to Pillarstone in exchange for (x) a monthly property management fee equal to 3.0% of the monthly revenues of Uptown Tower and (y) a monthly asset management fee equal to 0.125% of GAV of Uptown Tower.

In connection with the Contribution, on December 8, 2016, the Operating Partnership entered into a Tax Protection Agreement with Pillarstone REIT and Pillarstone pursuant to which Pillarstone agreed to indemnify the Operating Partnership for certain tax liabilities resulting from its recognition of income or gain prior to December 8, 2021 if such liabilities result from a transaction involving a direct or indirect taxable disposition of all or a portion of the Pillarstone Properties or if Pillarstone fails to maintain and allocate to the Operating Partnership for taxation purposes minimum levels of liabilities as specified in the Tax Protection Agreement, the result of which causes such recognition of income or gain and the Company incurs taxes that must be paid to maintain its REIT status for federal tax purposes.

As of December 31, 2018, we owned approximately 81.4% of the total outstanding Pillarstone OP Units, which we account for under the equity method. Additionally, certain of our officers and trustees serve as officers and trustees of Pillarstone REIT. See Note 5 Investment in Real Estate Partnership to the accompanying consolidated financial statements for more information on our accounting treatment of our investment in Pillarstone OP.

Property Acquisitions. On December 29, 2017, we acquired a 1.83 acre parcel of undeveloped land for \$0.9 million in cash and net prorations. The undeveloped land parcel is the hard corner at our Eldorado Plaza property.

On May 26, 2017, we acquired BLVD Place, a property that meets our Community Centered Property® strategy, for \$158.0 million, including \$80.0 million of asset level mortgage financing and \$78.0 million in cash and net prorations using borrowings under our 2014 Facility and a portion of the net proceeds from the April 2017 Offering (as defined below). BLVD Place, a 216,944 square foot property, was 99% leased at the time of purchase and is located in Houston, Texas. Included in the purchase of BLVD Place is approximately 1.43 acres of developable land.

On May 3, 2017, we acquired Eldorado Plaza, a property that meets our Community Centered Property® strategy, for \$46.6 million in cash and net prorations using borrowings under our 2014 Facility and a portion of the net proceeds from the April 2017 Offering. Eldorado Plaza, a 221,577 square foot property, was 96% leased at the time of purchase and is located in McKinney, Texas, a suburb of Dallas, Texas.

Hurricane Harvey. In August 2017, Hurricane Harvey impacted the South Texas region, including Houston, Texas. The majority of our Houston properties incurred minor damage and as a result, we recorded approximately \$0.5 million in Harvey related repairs recorded in property operation and maintenance expense for the year ended December 31, 2017.

Leasing Activity

As of December 31, 2018, we wholly-owned 57 properties with 4,841,660 square feet of GLA, which were approximately 90% occupied. The following is a summary of the Company's leasing activity for the year ended December 31, 2018:

	Number of Leases Signed	GLA Signed	Weighted Average Lease Term ⁽²⁾	TI and Incentives per Sq. Ft. ⁽³⁾	Contractual Rent Per Sq. Ft ⁽⁴⁾	Prior Contractual Rent Per Sq. Ft. ⁽⁵⁾	Straight-lined Basis Increase (Decrease) Over Prior Rent	
Comparable ⁽¹⁾								
Renewal Leases	177	409,217	4.5	\$ 3.98	\$ 20.57	\$ 19.97	11.1	%
New Leases	48	84,504	4.9	9.08	22.94	23.65	7.0	%
Total/Average	225	493,721	4.5	\$ 4.85	\$ 20.98	\$ 20.60	10.3	%
Total								
Renewal Leases	177	409,217	4.5	\$ 3.98	\$ 20.57			
New Leases	131	318,223	5.6	12.05	20.00			
Total/Average	308	727,440	5.0	\$ 7.51	\$ 20.32			

(1) Comparable leases represent leases signed on spaces for which there was a former tenant within the last twelve months and the new or renewal square footage was within 25% of the expired square footage.

(2) Weighted average lease term (in years) is determined on the basis of square footage.

Estimated amount per signed leases. Actual cost of construction may vary. Does not include first generation costs for tenant improvements ("TI") and leasing commission costs needed for new acquisitions, development or redevelopment of a property to bring to operating standards for its intended use.

(4) Contractual minimum rent under the new lease for the first month, excluding concessions.

(5) Contractual minimum rent under the prior lease for the final month.

Capital Expenditures

The following is a summary of the Company's capital expenditures for the years ended December 31 (in thousands):

	2018	2017
Capital expenditures:		
Tenant improvements and allowances	\$4,622	\$6,646
Developments / redevelopments	4,142	6,519
Leasing commissions and costs	2,113	3,118
Maintenance capital expenditures	2,874	4,410
Total capital expenditures	\$13,751	\$20,693

Summary of Critical Accounting Policies

Our discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements. We prepared these financial statements in conformity with GAAP. The preparation of these financial statements required us to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. We based our estimates on historical experience and on various other assumptions we believe to be reasonable under the circumstances. Our results may differ from these estimates. Currently, we believe that our accounting policies do not require us to make estimates using assumptions about matters that are highly uncertain. For a better understanding of our accounting policies, you should read Note 2 to our accompanying consolidated financial statements in conjunction with this “Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

We have described below the critical accounting policies that we believe could impact our consolidated financial statements most significantly.

Revenue Recognition. All leases on our properties are classified as operating leases, and the related rental income is recognized on a straight-line basis over the terms of the related leases. Differences between rental income earned and amounts due per the respective lease agreements are capitalized or charged, as applicable, to accrued rents and accounts receivable. Percentage rents are recognized as rental income when the thresholds upon which they are based have been met. Recoveries from tenants for taxes, insurance, and other operating expenses are recognized as revenues in the period the corresponding costs are incurred. We have established an allowance for doubtful accounts against the portion of tenant accounts receivable which is estimated to be uncollectible.

Profit-sharing Method. In accordance with the Financial Accounting Standards Board’s (“FASB”) guidance applicable to sales of real estate or interests therein, specifically FASB Accounting Standards Codification (“ASC”) 360-20, “Real Estate Sales,” Topic 606, “Revenue from Contracts with Customers” and ASC 610, “Other Income–Gains and Losses from the Derecognition of Nonfinancial Assets,” we did not recognize the sale of assets to Pillarstone OP in the Contribution and accounted for the transaction under the profit-sharing method for the year ended December 31, 2017. We recognized Pillarstone OP’s real estate assets and notes payables in our consolidated balance sheets. Additionally, the profits and losses of Pillarstone OP not attributable to the Company are reported as profit sharing expense. As a result of the adoption of Topic 606 and ASC 610, the Company derecognized the underlying assets and liabilities associated with the Contribution as of January 1, 2018 and recognized the Company’s investment in Pillarstone OP under the equity method.

Equity Method. For the year ended December 31, 2017, we accounted for the Contribution under the profit-sharing method. As a result of the adoption of Topic 606 and ASC 610, the Company derecognized the underlying assets and liabilities associated with the Contribution as of January 1, 2018 and recognized the Company’s investment in Pillarstone OP under the equity method. See Note 5 and Note 19 to our accompanying consolidated financial statements for additional disclosure on Pillarstone OP.

Development Properties. Land, buildings and improvements are recorded at cost. Expenditures related to the development of real estate are carried at cost which includes capitalized carrying charges and development costs. Carrying charges (interest and real estate taxes) are capitalized as part of construction in progress. The capitalization of such costs ceases when the property, or any completed portion, becomes available for occupancy. For the year ended December 31, 2018, approximately \$574,000 and \$365,000 in interest expense and real estate taxes, respectively, were capitalized. For the year ended December 31, 2017, approximately \$439,000 and \$277,000 in interest expense and real estate taxes, respectively, were capitalized. For the year ended December 31, 2016, approximately \$324,000 and \$71,000 in interest expense and real estate taxes, respectively, were capitalized.

Acquired Properties and Acquired Lease Intangibles. We allocate the purchase price of the acquired properties to land, building and improvements, identifiable intangible assets and to the acquired liabilities based on their respective fair values at the time of purchase. Identifiable intangibles include amounts allocated to acquired out-of-market leases, the value of in-place leases and customer relationship value, if any. We determine fair value based on estimated cash flow projections that utilize appropriate discount and capitalization rates and available market information. Estimates of future cash flows are based on a number of factors including the historical operating results, known trends and specific market and economic conditions that may affect the property. Factors considered by management in our analysis of determining the as-if-vacant property value include an estimate of carrying costs during the expected lease-up periods considering market conditions, and costs to execute similar leases. In estimating carrying costs, management includes real estate taxes, insurance and estimates of lost rentals at market rates during the expected lease-up periods, tenant demand and other economic conditions. Management also estimates costs to execute similar leases including leasing commissions, tenant improvements, legal and other related expenses.

Intangibles related to out-of-market leases and in-place lease value are recorded as acquired lease intangibles and are amortized as an adjustment to rental revenue or amortization expense, as appropriate, over the remaining terms of the underlying leases. Premiums or discounts on acquired out-of-market debt are amortized to interest expense over the remaining term of such debt.

Depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of 5 to 39 years for improvements and buildings, respectively. Tenant improvements are depreciated using the straight-line method over the life of the improvement or remaining term of the lease, whichever is shorter.

Impairment. We review our properties for impairment at least annually or whenever events or changes in circumstances indicate that the carrying amount of the assets, including accrued rental income, may not be recoverable through operations. We determine whether an impairment in value has occurred by comparing the estimated future cash flows (undiscounted and without interest charges), including the estimated residual value of the property, with the carrying cost of the property. If impairment is indicated, a loss will be recorded for the amount by which the carrying value of the property exceeds its fair value. Management has determined that there has been no impairment in the carrying value of our real estate assets as of December 31, 2018.

Accrued Rents and Accounts Receivable. Included in accrued rent and accounts receivable are base rents, tenant reimbursements and receivables attributable to recording rents on a straight-line basis. An allowance for the uncollectible portion of accrued rents and accounts receivable is determined based upon customer credit-worthiness (including expected recovery of our claim with respect to any tenants in bankruptcy), historical bad debt levels, and current economic trends. As of December 31, 2018 and 2017, we had an allowance for uncollectible accounts of \$9.7 million and \$8.6 million, respectively. As of December 31, 2018, 2017 and 2016, we recorded bad debt expense in the amount of \$1.4 million, \$2.3 million and \$1.6 million, respectively, related to tenant receivables that we specifically identified as potentially uncollectible based on our assessment of each tenant's credit-worthiness. Bad debt expenses and any related recoveries are included in property operation and maintenance expense.

Unamortized Lease Commissions and Loan Costs. Leasing commissions are amortized using the straight-line method over the terms of the related lease agreements. Loan costs are amortized on the straight-line method over the terms of the loans, which approximates the interest method. Costs allocated to in-place leases whose terms differ from market terms related to acquired properties are amortized over the remaining life of the respective leases.

Prepays and Other Assets. Prepays and other assets include escrows established pursuant to certain mortgage financing arrangements for real estate taxes and insurance and acquisition deposits which include earnest money deposits on future acquisitions.

Federal Income Taxes. We elected to be taxed as a REIT under the Code beginning with our taxable year ended December 31, 1999. As a REIT, we generally are not subject to federal income tax on income that we distribute to our shareholders. If we fail to qualify as a REIT in any taxable year, we will be subject to federal income tax on our taxable income at regular corporate rates. We believe that we are organized and operate in such a manner as to qualify to be taxed as a REIT, and we intend to operate so as to remain qualified as a REIT for federal income tax purposes.

State Taxes. We are subject to the Texas Margin Tax which is computed by applying the applicable tax rate (1% for us) to the profit margin, which, generally, will be determined for us as total revenue less a 30% standard deduction. Although the Texas Margin Tax is not an income tax, Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") ASC 740, "Income Taxes" ("ASC 740") applies to the Texas Margin Tax. As of December 31, 2018, 2017 and 2016, we recorded a margin tax provision of \$0.4 million, \$0.4 million and \$0.2 million, respectively.

Fair Value of Financial Instruments. Our financial instruments consist primarily of cash, cash equivalents, accounts receivable, accounts and notes payable and investments in marketable securities. The carrying value of cash, cash equivalents, accounts receivable and accounts payable are representative of their respective fair values due to their short-term nature. The fair value of our long-term debt, consisting of fixed rate secured notes, variable rate secured notes and an unsecured revolving credit facility aggregate to approximately \$618.6 million and \$659.6 million as compared to the book value of approximately \$619.4 million and \$660.9 million as of December 31, 2018 and 2017, respectively. The fair value of our long-term debt is estimated on a Level 2 basis (as provided by ASC 820, “Fair Value Measurements and Disclosures”), using a discounted cash flow analysis based on the borrowing rates currently available to us for loans with similar terms and maturities, discounting the future contractual interest and principal payments.

The fair value of our loan guarantee to Pillarstone OP is estimated on a Level 3 basis (as provided by ASC 820, “Fair Value Measurements and Disclosures”), using a probability-weighted discounted cash flow analysis based on a discount rate, discounting the loan balance.

Disclosure about fair value of financial instruments is based on pertinent information available to management as of December 31, 2018 and 2017. Although management is not aware of any factors that would significantly affect the fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since December 31, 2018 and current estimates of fair value may differ significantly from the amounts presented herein.

Derivative Instruments and Hedging Activities. We occasionally utilize derivative financial instruments, principally interest rate swaps, to manage our exposure to fluctuations in interest rates. We have established policies and procedures for risk assessment, and the approval, reporting and monitoring of derivative financial instruments. We recognize our interest rate swaps as cash flow hedges with the effective portion of the changes in fair value recorded in comprehensive income and subsequently reclassified into earnings in the period that the hedged transaction affects earnings. Any ineffective portion of a cash flow hedge’s change in fair value is recorded immediately into earnings. Our cash flow hedges are determined using Level 2 inputs under ASC 820. Level 2 inputs represent quoted prices in active markets for similar assets or liabilities; quoted prices in markets that are not active; and model-derived valuations whose inputs are observable. As of December 31, 2018, we consider our cash flow hedges to be highly effective.

Recent Accounting Pronouncements. In May 2014, the FASB issued guidance, as amended in subsequent updates, establishing a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most of the existing revenue recognition guidance. The standard also requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services and also requires certain additional disclosures. This guidance became effective for the reporting periods beginning on or after December 15, 2017, and interim periods within those fiscal years. We adopted this guidance on a modified retrospective basis beginning January 1, 2018 and have derecognized the underlying assets and liabilities associated with the Contribution as of January 1, 2018 and have recognized the Company’s investment in Pillarstone OP under the equity method of accounting. The Company made an adjustment which decreased the Company’s accumulated deficit as of January 1, 2018 by \$19.1 million. See Note 5 and Note 19 to our accompanying consolidated financial statements for further details.

In February 2016, the FASB issued guidance requiring lessees to recognize a lease liability and a right-of-use asset for all leases. Lessor accounting will remain largely unchanged with the exception of changes related to costs which qualify as initial direct costs. The guidance will also require new qualitative and quantitative disclosures to help financial statement users better understand the timing, amount and uncertainty of cash flows arising from leases. This guidance is effective for reporting periods beginning on or after December 15, 2018, with early adoption permitted. We adopted the guidance and its related amendments as of January 1, 2019 using the transition practical expedient which allows us to recognize a cumulative-effect adjustment to the opening balance of retained earnings as of the adoption date as well as other elected practical expedients. Additionally, we have elected the optional transition practical expedient for lessors that permits lessors to make an accounting policy election to not separate nonlease components from the associated lease components, if the following two criteria are met: (1) the timing and pattern of transfer of the lease and nonlease components are the same and (2) the lease component would be classified as an operating lease if accounted for separately. As a result, leases where we are the lessor are accounted for in a similar manner to existing standards with the underlying leased asset being reported and recognized as a real estate asset.

We have identified our lease commitments and finalized our evaluation on our consolidated financial statements and on our internal accounting processes. Substantially all of our real estate lessor commitments continued to be accounted for as operating leases, and the new leasing standard did not have a material impact on rental revenues. Our lessee operating lease commitments are subject to the standard and recognized as operating lease liabilities and right-of-use assets upon adoption. Our adoption of the new leasing standard did not have a material impact on our consolidated financial statements. Upon our adoption of the guidance as of January 1, 2019, we increased lease liabilities and corresponding right-of-use assets. Such adoption resulted in certain costs (primarily legal costs related to lease negotiations) being expensed rather than capitalized. We capitalized \$406,000 in legal related costs for the year ended December 31, 2018. These transition adjustments did not have a material impact on our consolidated balance sheet. Additionally, this guidance did not have a material impact on our consolidated statement of income upon adoption.

In November 2016, the FASB issued guidance requiring that the statement of cash flows explain the change during the period in the total cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash

equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. This guidance became effective for the reporting periods beginning on or after December 15, 2017, and interim periods within those fiscal years. We adopted this guidance effective January 1, 2018, and we have reconciled cash and cash equivalents and restricted cash and restricted cash equivalents on a retrospective basis, whereas under the previous guidance, we reported restricted cash and restricted cash equivalents under cash flows from financing activities.

In January 2017, the FASB issued guidance clarifying the definition of a business with the objective of adding guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions (or dispositions) of assets or businesses. This guidance became effective for the reporting periods beginning on or after December 15, 2017, and interim periods within those fiscal years. We adopted this guidance on a prospective basis beginning January 1, 2018 and believe the majority of our future acquisitions will qualify as asset acquisitions and the associated transaction costs will be capitalized as opposed to expensed under previous guidance.

In February 2017, the FASB issued guidance clarifying the scope of asset derecognition guidance, adds guidance for partial sales of nonfinancial assets and clarifies recognizing gains and losses from the transfer of nonfinancial assets in contracts with noncustomers. This guidance became effective for the reporting periods beginning on or after December 15, 2017, and interim periods within those fiscal years. We adopted this guidance on a modified retrospective basis beginning January 1, 2018 and have derecognized the underlying assets and liabilities associated with the Contribution as of January 1, 2018 and have recognized the Company's investment in Pillarstone OP under the equity method of accounting. The Company made an adjustment which decreased the Company's accumulated deficit as of January 1, 2018 by \$19.1 million. See Note 5 and Note 19 to our accompanying consolidated financial statements for further details.

Liquidity and Capital Resources

Our short-term liquidity requirements consist primarily of distributions to holders of our common shares and OP units, including those required to maintain our REIT status and satisfy our current quarterly distribution target of \$0.2850 per share and OP unit, recurring expenditures, such as repairs and maintenance of our properties, non-recurring expenditures, such as capital improvements and tenant improvements, debt service requirements, and, potentially, acquisitions of additional properties.

During the year ended December 31, 2018, our cash provided from operating activities was \$39,557,000 and our total dividends and distributions paid were \$46,099,000. Therefore, we had distributions in excess of cash flow from operations of approximately \$6,542,000. The 2019 Facility included a \$300 million unsecured borrowing capacity under a revolving credit facility, two \$50 million term loans and one \$100 million term loan. The 2019 Facility also included an accordion feature that allowed the Operating Partnership to increase the borrowing capacity to \$700 million, upon the satisfaction of certain conditions. We anticipate that cash flows from operating activities and our borrowing capacity under the 2019 Facility will provide adequate capital for our distributions, working capital requirements, anticipated capital expenditures and scheduled debt payments in the short term. We also believe that cash flows from operating activities and our borrowing capacity will allow us to make all distributions required for us to continue to qualify to be taxed as a REIT for federal income tax purposes.

Our long-term capital requirements consist primarily of maturities under our longer-term debt agreements, development and redevelopment costs, and potential acquisitions. We expect to meet our long-term liquidity requirements with net cash from operations, long-term indebtedness, sales of common shares, issuance of OP units, sales of underperforming and Non-Core Properties and other financing opportunities, including debt financing. We believe we have access to multiple sources of capital to fund our long-term liquidity requirements, including the incurrence of additional debt and the issuance of additional equity. However, our ability to incur additional debt will be dependent on a number of factors, including our degree of leverage, the value of our unencumbered assets and borrowing restrictions that may be imposed by lenders. Our ability to access the equity markets will be dependent on a number of factors as well, including general market conditions for REITs and market perceptions about our Company. In addition, our universal shelf registration statement on Form S-3 expired in April 2018. Until our new shelf registration statement is declared effective by the SEC, we will not have access to the public capital markets.

We expect that our rental income will increase as we continue to acquire additional properties, subsequently increasing our cash flows generated from operating activities. We intend to finance the continued acquisition of such additional properties through equity issuances and through debt financing.

Our capital structure includes non-recourse secured debt that we assumed or originated on certain properties. We may hedge the future cash flows of certain debt transactions principally through interest rate swaps with major financial institutions.

As discussed in Note 2 to the accompanying consolidated financial statements, pursuant to the term of our \$15.1 million 4.99% Note, due January 6, 2024 (see Note 9 to the accompanying consolidated financial statements), which is collateralized by our Anthem Marketplace property, we were required by the lenders thereunder to establish a cash management account controlled by the lenders to collect all amounts generated by our Anthem Marketplace property in order to collateralize such promissory note. Amounts in the cash management account are classified as restricted cash.

Cash and Cash Equivalents

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We had cash and cash equivalents of approximately \$13,786,000 at December 31, 2018, as compared to \$5,210,000 at December 31, 2017. The increase of \$8,576,000 was primarily the result of the following:

Sources of Cash

• Cash flow from operations of \$39,557,000 for the year ended December 31, 2018;

• Net proceeds of \$9,000,000 from the 2018 Facility;

• Net proceeds from financed receivable due from related party of \$9,812,000;

• Net proceeds of \$12,574,000 from sales of properties;

• Net proceeds of \$30,000 from sales of marketable securities;

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Uses of Cash

Payment of dividends and distributions to common shareholders and OP unit holders of \$46,099,000;

Additions to real estate of \$11,638,000;

Payments of loan origination costs of \$30,000;

Payments of notes payable of \$2,543,000;

Payments of exchange offer costs of \$126,000; and

Repurchase of common shares of \$1,961,000.

We place all cash in short-term, highly liquid investments that we believe provide appropriate safety of principal.

Equity Offerings

On April 25, 2017, we completed the sale of 8,018,500 common shares, including 1,018,500 common shares purchased by the underwriters upon exercise of their option to purchase additional common shares, at a public offering price per share of \$13.00 (the “April 2017 Offering”). Total net proceeds from the April 2017 Offering, after deducting offering expenses, were approximately \$99.9 million, which we contributed to the Operating Partnership in exchange for OP units. The Operating Partnership used the net proceeds from the April 2017 Offering to repay a portion of the 2018 Facility and for general corporate purposes, including funding a portion of the purchase price of BLVD Place and Eldorado Plaza.

On June 4, 2015, we entered into nine amended and restated equity distribution agreements (the “2015 equity distribution agreements”) for an at-the-market distribution program. Pursuant to the terms and conditions of the 2015 equity distribution agreements, we could issue and sell up to an aggregate of \$50 million of our common shares pursuant to our Registration Statement on Form S-3 (File No. 333-203727), which expired on April 29, 2018. Actual sales depended on a variety of factors determined by us from time to time, including (among others) market conditions, the trading price of our common shares, capital needs and our determinations of the appropriate sources of funding for us, and were made in transactions that will be deemed to be “at-the-market” offerings as defined in Rule 415 under the Securities Act. We had no obligation to sell any of our common shares, and could at any time suspend offers under the 2015 equity distribution agreements or terminate the 2015 equity distribution agreements. For the year ended December 31, 2018, we did not sell any common shares under the 2015 equity distribution agreements. For the year ended December 31, 2017, we sold 1,324,038 common shares under the 2015 equity distribution agreements, with net proceeds to us of approximately \$18.6 million. In connection with such sales, we paid compensation of approximately \$0.3 million to the sales agents. For the year ended December 31, 2016, we sold 2,063,697 common shares under the 2015 equity distribution agreements, with net proceeds to us of approximately \$30.0 million. In connection with such sales, we paid compensation of approximately \$0.5 million to the sales agents.

Debt

Mortgages and other notes payable consist of the following (in thousands):

Description	December 31,	
	2018	2017
Fixed rate notes		
\$10.5 million, LIBOR plus 2.00% Note, due September 24, 2020 ⁽¹⁾	\$9,500	\$9,740
\$50.0 million, 1.75% plus 1.35% to 1.90% Note, due October 30, 2020 ⁽²⁾	50,000	50,000
\$50.0 million, 1.50% plus 1.35% to 1.90% Note, due January 29, 2021 ⁽³⁾	50,000	50,000
\$100.0 million, 1.73% plus 1.65% to 2.25% Note, due October 30, 2022 ⁽⁴⁾	100,000	100,000
\$80.0 million, 3.72% Note, due June 1, 2027	80,000	80,000
\$37.0 million 3.76% Note, due December 1, 2020 ⁽⁵⁾	—	33,148
\$6.5 million 3.80% Note, due January 1, 2019	5,657	5,842
\$19.0 million 4.15% Note, due December 1, 2024	19,000	19,000
\$20.2 million 4.28% Note, due June 6, 2023	18,996	19,360
\$14.0 million 4.34% Note, due September 11, 2024	13,718	13,944
\$14.3 million 4.34% Note, due September 11, 2024	14,300	14,300
\$16.5 million 4.97% Note, due September 26, 2023 ⁽⁵⁾	—	16,058
\$15.1 million 4.99% Note, due January 6, 2024	14,643	14,865
\$2.6 million 5.46% Note, due October 1, 2023	2,430	2,472
Floating rate notes		
Unsecured line of credit, LIBOR plus 1.40% to 1.95%, due October 30, 2019 ⁽⁶⁾	241,200	232,200
Total notes payable principal	619,444	660,929
Less deferred financing costs, net of accumulated amortization	(1,239)	(1,861)
	\$618,205	\$659,068

- (1) Promissory note includes an interest rate swap that fixed the interest rate at 3.55% for the duration of the term through September 24, 2018 and 4.85% beginning September 24, 2018 through September 24, 2020.
- (2) Promissory note includes an interest rate swap that fixed the LIBOR portion of Term Loan 1 (as defined below) at 0.84% through February 3, 2017 and 1.75% beginning February 3, 2017 through October 30, 2020.
- (3) Promissory note includes an interest rate swap that fixed the LIBOR portion of Term Loan 2 (as defined below) at 1.50%.
- (4) Promissory note includes an interest rate swap that fixed the LIBOR portion of Term Loan 3 (as defined below) at 1.73%.
- (5) Promissory notes were assumed by Pillarstone OP in December 2016 and included in our consolidated balance sheet under the profit-sharing method of accounting through December 31, 2017 as discussed in Note 5.
- (6) Unsecured line of credit includes certain Pillarstone Properties (as defined and described in more detail below) in determining the amount of credit available under the 2018 Facility (as defined and described in more detail below).

On May 26, 2017, we, through our subsidiary, Whitestone BLVD Place LLC, a Delaware limited liability company, issued a \$80.0 million promissory note to American General Life Insurance Company (the “BLVD Note”). The BLVD Note has a fixed interest rate of 3.72% and a maturity date of June 1, 2027. Proceeds from the BLVD Note were used to fund a portion of the purchase price of the acquisition of BLVD Place (See Note 4 to our accompanying

consolidated financial statements).

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On November 7, 2014, we, through our Operating Partnership, entered into an unsecured revolving credit facility (the “2014 Facility”) with the lenders party thereto, with BMO Capital Markets Corp., Wells Fargo Securities, LLC, Merrill Lynch, Pierce, Fenner & Smith Incorporated and U.S. Bank, National Association, as co-lead arrangers and joint book runners, and Bank of Montreal, as administrative agent (the “Agent”). The 2014 Facility amended and restated our previous unsecured revolving credit facility. On October 30, 2015, we, through our Operating Partnership, entered into the First Amendment to the 2014 Facility (the “First Amendment”) with the guarantors party thereto, the lenders party thereto and the Agent. We refer to the 2014 Facility, as amended by the First Amendment, as the “2018 Facility.”

Pursuant to the First Amendment, the Company made the following amendments to the 2014 Facility:

- extended the maturity date of the \$300 million unsecured revolving credit facility under the 2014 Facility (the “Revolver”) to October 30, 2019 from November 7, 2018;
- converted \$100 million of outstanding borrowings under the Revolver to a new \$100 million unsecured term loan under the 2014 Facility (“Term Loan 3”) with a maturity date of October 30, 2022;
- extended the maturity date of the first \$50 million unsecured term loan under the 2014 Facility (“Term Loan 1”) to October 30, 2020 from February 17, 2017; and
- extended the maturity date of the second \$50 million unsecured term loan under the 2014 Facility (“Term Loan 2” and together with Term Loan 1 and Term Loan 3, the “Term Loans”) to January 29, 2021 from November 7, 2019.

Borrowings under the 2018 Facility accrued interest (at the Operating Partnership's option) at a Base Rate or an Adjusted LIBOR plus an applicable margin based upon our then existing leverage. As of December 31, 2018, the interest rate was 4.28%. The applicable margin for Adjusted LIBOR borrowings ranged from 1.40% to 1.95% for the Revolver and 1.35% to 2.25% for the Term Loans. Base Rate means the higher of: (a) the Agent’s prime commercial rate, (b) the sum of (i) the average rate quoted by the Agent by two or more federal funds brokers selected by the Agent for sale to the Agent at face value of federal funds in the secondary market in an amount equal or comparable to the principal amount for which such rate is being determined, plus (ii) 1/2 of 1.00%, and (c) the LIBOR rate for such day plus 1.00%. Adjusted LIBOR means LIBOR divided by one minus the Eurodollar Reserve Percentage. The Eurodollar Reserve Percentage means the maximum reserve percentage at which reserves are imposed by the Board of Governors of the Federal Reserve System on eurocurrency liabilities.

We served as the guarantor for funds borrowed by the Operating Partnership under the 2018 Facility. The 2018 Facility contained customary terms and conditions, including, without limitation, affirmative and negative covenants such as information reporting requirements, maximum secured indebtedness to total asset value, minimum EBITDA (earnings before interest, taxes, depreciation, amortization or extraordinary items) to fixed charges, and maintenance of a minimum net worth. The 2018 Facility also contained customary events of default with customary notice and cure, including, without limitation, nonpayment, breach of covenant, misrepresentation of representations and warranties in a material respect, cross-default to other major indebtedness, change of control, bankruptcy and loss of REIT tax status.

The 2018 Facility includes an accordion feature that will allowed the Operating Partnership to increase the borrowing capacity to \$700 million, upon the satisfaction of certain conditions. As of December 31, 2018, \$441.2 million was drawn on the 2018 Facility and our unused borrowing capacity was \$58.8 million, assuming that we used the proceeds of the 2018 Facility to acquire properties, or to repay debt on properties, that are eligible to be included in the unsecured borrowing base. Proceeds from the 2018 Facility were used for general corporate purposes, including property acquisitions, debt repayment, capital expenditures, expansion, redevelopment and re-tenanting of properties in our portfolio and working capital.

On December 8, 2016, in connection with the Contribution, the Operating Partnership entered into the Second Amendment to the 2018 Facility and Reaffirmation of Guaranties (the “Second Amendment”) with Pillarstone OP, the Company and the other Guarantors party thereto, the lenders party thereto and the Agent. Pursuant to the Second Amendment, following the Contribution, Whitestone Offices, LLC and Whitestone CP Woodland Ph. 2, LLC were permitted to remain Material Subsidiaries (as defined in the 2018 Facility) and Guarantors under the 2018 Facility and their respective Pillarstone Properties were each permitted to remain an Eligible Property (as defined in the 2018 Facility) and be included in the Borrowing Base (as defined in the Facility) under the 2018 Facility. In addition, on December 8, 2016, Pillarstone OP entered into the Limited Guarantee (the “Limited Guarantee”) with the Agent, pursuant to which Pillarstone OP agreed to be joined as a party to the Facility to provide a limited guarantee up to the amount of availability generated by the Pillarstone Properties owned by Whitestone Offices, LLC and Whitestone CP Woodland Ph. 2, LLC. As of December 31, 2018, Pillarstone accounted for approximately \$5.7 million of the total amount drawn on the 2018 Facility.

As of December 31, 2018, our \$178.2 million in secured debt was collateralized by nine properties with a carrying value of \$279.1 million. Our loans contain restrictions that would require the payment of prepayment penalties for the acceleration of outstanding debt and are secured by deeds of trust on certain of our properties and by assignment of the rents and leases associated with those properties. In 2018, we were not in compliance with respect to the tangible Net Worth covenant (as defined in the 2018 Facility) and had received two waivers as of December 31, 2018. Had we been unable to obtain a waiver or other suitable relief from the lenders under the 2018 Facility, an Event of Default (as defined in the 2018 Facility) would have occurred, permitting the lenders holding a majority of the commitments under the 2018 Facility to, among other things, accelerate the outstanding indebtedness, which would make it immediately due and payable. The 2019 Facility contains a similar tangible Net Worth covenant that resets at a new threshold and changes the definition of Net Worth to add back accumulated depreciation. However, we can make no assurances that we will be in compliance with this covenant or other covenants under the 2019 Facility in future periods or, if we are not in compliance, that we will be able to obtain a waiver.

Scheduled maturities of our outstanding debt as of December 31, 2018 were as follows (in thousands):

Year	Amount Due (in thousands)
2019	\$ 248,199
2020	60,801
2021	51,611
2022	101,683
2023	20,720
Thereafter	136,430
Total	\$ 619,444

Capital Expenditures

We continually evaluate our properties' performance and value. We may determine it is in our shareholders' best interest to invest capital in properties we believe have potential for increasing value. We also may have unexpected capital expenditures or improvements for our existing assets. Additionally, we intend to continue investing in similar properties outside of Texas and Arizona in cities with exceptional demographics to diversify market risk, and we may incur significant capital expenditures or make improvements in connection with any properties we may acquire.

Contractual Obligations

As of December 31, 2018, we had the following contractual obligations (see Note 9 of our accompanying consolidated financial statements for further discussion regarding the specific terms of our debt):

	Total	Payment due by period (in thousands)			
		Less than 1 year (2019)	1 - 3 years (2020 - 2021)	3 - 5 years (2022 - 2023)	More than 5 years (after 2023)
Consolidated Contractual Obligations					
Long-Term Debt - Principal	\$619,444	\$248,199	\$112,412	\$122,403	\$136,430
Long-Term Debt - Fixed Interest	60,492	13,131	22,772	12,689	11,900
Long-Term Debt - Variable Interest ⁽¹⁾	6,633	6,633	—	—	—
Unsecured Credit Facility - Unused commitment fee ⁽²⁾	98	98	—	—	—
Operating Lease Obligations	185	85	100	—	—
Related Party Rent Lease Obligations	\$963	\$441	\$522	\$—	\$—
Total	\$687,815	\$268,587	\$135,806	\$135,092	\$148,330

As of December 31, 2018, we had one loan totaling \$241.2 million which bore interest at a floating rate. The ⁽¹⁾variable interest rate payments are based on LIBOR plus 1.40% to LIBOR plus 1.95%, which reflects our new interest rates under our 2014 Facility. The information in the table above reflects our projected interest rate obligations for the floating rate payments based on one-month LIBOR as of December 31, 2018, of 2.35%.

The unused commitment fees on our unsecured credit facility, payable quarterly, are based on the average daily ⁽²⁾unused amount of our unsecured credit facility. The fees are 0.20% for facility usage greater than 50% or 0.25% for facility usage less than 50%. The information in the table above reflects our projected obligations for our unsecured credit facility based on our December 31, 2018 balance of \$441.2 million.

Distributions

During 2018, we paid distributions to our common shareholders and OP unit holders of \$46.1 million, compared to \$41.7 million in 2017. Common shareholders and OP unit holders receive monthly distributions. Payments of distributions are declared quarterly and paid monthly. The distributions paid to common shareholders and OP unit holders were as follows (in thousands, except per share data) for the years ended December 31, 2018 and 2017:

Quarter Paid	Common Shares		Noncontrolling OP Unit Holders		Total
	Distributions Per Common Share	Total Amount Paid	Distributions Per OP Unit	Total Amount Paid	Total Amount Paid
2018					
Fourth Quarter	\$0.2850	\$ 11,302	\$0.2850	\$ 265	\$ 11,567
Third Quarter	0.2850	11,294	0.2850	286	11,580
Second Quarter	0.2850	11,203	0.2850	295	11,498
First Quarter	0.2850	11,145	0.2850	309	11,454
Total	\$1.1400	\$44,944	\$1.1400	\$ 1,155	\$46,099
2017					
Fourth Quarter	\$0.2850	\$ 11,002	\$0.2850	\$ 309	\$ 11,311
Third Quarter	0.2850	10,948	0.2850	309	11,257
Second Quarter	0.2850	10,093	0.2850	310	10,403
First Quarter	0.2850	8,429	0.2850	313	8,742
Total	\$1.1400	\$40,472	\$1.1400	\$ 1,241	\$41,713

Results of Operations

Year Ended December 31, 2018 Compared to Year Ended December 31, 2017

The following table provides a general comparison of our results of operations for the years ended December 31, 2018 and 2017 (dollars in thousands, except per share data):

	Year Ended December			
	31,			
	2018	2017		
Number of properties owned and operated	57	59		
Aggregate GLA (sq. ft.) ⁽¹⁾	4,841,660	5,023,215		
Ending occupancy rate - operating portfolio ⁽¹⁾	90	% 91	%	
Ending occupancy rate	90	% 90	%	
Number of properties managed	11	14		
Aggregate GLA (sq. ft.)	1,307,930	1,531,737		
Ending occupancy rate - managed operating portfolio	80	% 81	%	
Total property revenues	\$119,863	\$125,959		
Total property expenses	37,431	42,110		
Total other expenses	64,651	74,430		
Provision for income taxes	347	386		
Gain on sale of properties	(4,629)	(16)		
Profit sharing expense	—	278		
Loss on disposal of assets	82	183		
Income from continuing operations	21,981	8,588		
Income from discontinued operations	—	—		
Net income	21,981	8,588		
Less: Net income attributable to noncontrolling interests	550	254		
Net income attributable to Whitestone REIT	\$21,431	\$8,334		
Funds from operations ⁽²⁾	\$39,398	\$35,045		
Funds from operations core ⁽³⁾	48,778	47,096		
Property net operating income ⁽⁴⁾	89,949	83,849		
Distributions paid on common shares and OP units	46,099	41,713		
Distributions per common share and OP unit	\$1.1400	\$1.1400		
Distributions paid as a percentage of funds from operations core	95	% 89	%	

(1) Excludes (i) new acquisitions, through the earlier of attainment of 90% occupancy or 18 months of ownership, and (ii) properties that are undergoing significant redevelopment or re-tenanting.

(2) For an explanation and reconciliation of funds from operations and funds from operations core to net income, see “Funds From Operations” below.

(3) For a reconciliation of funds from operations core to net income, see “FFO Core” below.

(4) For an explanation and reconciliation of property net operating income to net income, see “Property Net Operating Income” below.

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Property revenues. We had rental income and tenant reimbursements of approximately \$119,863,000 for the year ended December 31, 2018 as compared to \$125,959,000 for the year ended December 31, 2017, a decrease of \$6,096,000, or 5%. The year ended December 31, 2018 included \$6,486,000 in increased revenues from Non-Same Store operations and \$15,441,000 in decreased revenues from the derecognition of Pillarstone Properties as a result of the adoption of Topic 606 and ASC 610. We define “Non-Same Stores” as properties acquired since the beginning of the period being compared and properties that have been sold, but not classified as discontinued operations. During the twelve months ended December 31, 2018, Same Store revenues increased \$2,859,000. We define “Same Stores” as properties owned during the entire period being compared. For purposes of comparing the year ended December 31, 2018 to the year ended December 31, 2017, Same Stores include properties owned from January 1, 2017 to December 31, 2018. Same Store average occupied square feet increased from 3,959,354 for the year ended December 31, 2017 to 3,967,881 for the year ended December 31, 2018, increasing Same Store revenue by \$201,000. Same Store revenue rate per average leased square foot increased \$0.67 for the year ended December 31, 2018 to \$25.10 per average leased square foot as compared to the year ended December 31, 2017 revenue rate per average leased square foot of \$24.43, increasing Same Store revenue by \$2,658,480. The revenue rate per average leased square foot is calculated by dividing the total revenue by the average square feet leased during the period.

Property expenses. Our property expenses were \$37,431,000 for the year ended December 31, 2018, as compared to \$42,110,000 for the year ended December 31, 2017, a decrease of \$4,679,000, or 11%. Property expenses for the year ended December 31, 2018 included Same Store and Non-Same Store amounts of \$30,794,000 and \$6,637,000, respectively. Property expenses for the year ended December 31, 2017 included Same Store and Non-Same Store amounts of \$30,833,000 and \$4,102,000, respectively. The primary components of total property expenses, Same Store property expenses and Non-Same Store property expenses are detailed in the tables below (in thousands):

	Year Ended December 31,		Increase	% Increase	
	2018	2017	(Decrease)	(Decrease)	
Overall Property Expenses	\$37,431	\$42,110	\$ (4,679)	(11)	%
Real estate taxes	\$16,362	\$17,897	\$ (1,535)	(9)	%
Utilities	4,470	5,514	(1,044)	(19)	%
Contract services	7,017	7,186	(169)	(2)	%
Repairs and maintenance	3,900	5,052	(1,152)	(23)	%
Bad debt	1,391	2,356	(965)	(41)	%
Labor and other	4,291	4,105	186	5	%
Total	\$37,431	\$42,110	\$ (4,679)	(11)	%
	Year Ended December 31,		Increase	% Increase	
	2018	2017	(Decrease)	(Decrease)	
Same Store Property Expenses	\$13,253	\$13,032	\$ 221	2	%
Real estate taxes	\$13,253	\$13,032	\$ 221	2	%
Utilities	3,816	3,935	(119)	(3)	%
Contract services	5,602	5,278	324	6	%
Repairs and maintenance	3,571	3,830	(259)	(7)	%
Bad debt	1,361	1,867	(506)	(27)	%
Labor and other	3,191	2,891	300	10	%
Total	\$30,794	\$30,833	\$ (39)	—	%
	Year Ended December 31,		Increase	% Increase	
	2018	2017	(Decrease)	(Decrease)	
Non-Same Store Property Expenses	\$3,109	\$2,273	\$ 836	37	%
Real estate taxes	\$3,109	\$2,273	\$ 836	37	%
Utilities	654	417	237	57	%
Contract services	1,415	764	651	85	%
Repairs and maintenance	329	309	20	6	%

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Bad debt	30	100	(70)	(70)%
Labor and other	1,100	239	861		360	%
Total	\$6,637	\$4,102	\$ 2,535		62	%

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Real estate taxes. Real estate taxes decreased \$1,535,000, or 9%, during the year ended December 31, 2018 as compared to 2017. The \$1,535,000 decrease was comprised of increases of \$836,000 in Non-Same Store expense, \$221,000 in Same Store expense and offset by decrease of \$2,592,000 from the derecognition of Pillarstone Properties as a result of the adoption of Topic 606 and ASC 610. We actively work to keep our valuations and resulting taxes low because a majority of these taxes are charged to our tenants through triple net leases, and we strive to keep these charges to our tenants as low as possible.

Utilities. Utilities decreased \$1,044,000, or 19%, during the year ended December 31, 2018 as compared to 2017. The \$1,044,000 decrease was comprised of increases of \$237,000 in Non-Same Store expense and offset by decreases of \$119,000 in our Same Store properties and \$1,162,000 from the derecognition of Pillarstone Properties as a result of the adoption of Topic 606 and ASC 610.

Contract services. Contract services decreased \$169,000, or 2%, during the year ended December 31, 2018 as compared to 2017. The \$169,000 decrease was comprised of increases of \$324,000 in Same Store expense and \$651,000 in Non-Same Store expense, offset by a decrease of \$1,144,000 from the derecognition of Pillarstone Properties as a result of the adoption of Topic 606 and ASC 610.

Repairs and maintenance. Repairs and maintenance decreased \$1,152,000, or 23%, during the year ended December 31, 2018 as compared to 2017. The \$1,152,000 decrease was comprised of decreases of \$259,000 in Same Store expense and \$913,000 from the derecognition of Pillarstone Properties as a result of the adoption of Topic 606 and ASC 610, partially offset by an increase of \$20,000 in our Non-Same Store properties.

Bad debt. Bad debt for the year ended December 31, 2018 decreased \$965,000, or 41%, as compared to 2017. The \$965,000 decrease was comprised of decreases of \$506,000 in Same Store expense, \$70,000 in our Non-Same Store properties, and \$389,000 from the derecognition of Pillarstone Properties as a result of the adoption of Topic 606 and ASC 610.

Labor and other. Labor and other expenses increased \$186,000, or 5%, for year ended December 31, 2018 as compared to 2017. The \$186,000 increase was comprised of increases of \$861,000 in Non-Same Store expense and \$300,000 in Same Store expense, offset by a decrease of \$975,000 from the derecognition of Pillarstone Properties as a result of the adoption of Topic 606 and ASC 610.

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Same Store and Non-Same Store net operating income. The components of Same Store, Non-Same Store net operating income, real estate partnership, and net income are detailed in the table below (in thousands):

	Year Ended		Increase (Decrease)	% Increase (Decrease)	
	December 31, 2018	2017			
Same Store (49 properties excluding development land)					
Property revenues					
Rental revenues	\$72,454	\$71,987	\$467	1	%
Other revenues	27,138	24,746	2,392	10	%
Total property revenues	99,592	96,733	2,859	3	%
Property expenses					
Property operation and maintenance	17,541	17,801	(260)	(1))%
Real estate taxes	13,253	13,032	221	2	%
Total property expenses	30,794	30,833	(39)	—	%
Total same store net operating income	68,798	65,900	2,898	4	%
Non-Same Store (4 properties excluding development land)					
Property revenues					
Rental revenues	14,190	9,679	4,511	47	%
Other revenues	6,081	4,106	1,975	48	%
Total property revenues	20,271	13,785	6,486	47	%
Property expenses					
Property operation and maintenance	3,528	1,829	1,699	93	%
Real estate taxes	3,109	2,273	836	37	%
Total property expenses	6,637	4,102	2,535	62	%
Total Non-Same Store net operating income	13,634	9,683	3,951	41	%
Pillarstone OP properties net operating income	—	8,266	(8,266)	(100))%
Pro rata share of real estate partnership	7,725	—	7,725	Not meaningful	
Total property net operating income	90,157	83,849	6,308	8	%
Less total other expenses, excluding pro rata share of real estate partnership net operating income, provision for income taxes, gain on sale of properties and gain (loss) on disposal of assets	68,176	75,261	(7,085)	(9))%
Net income	\$21,981	\$8,588	\$13,393	156	%

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Other expenses. Our other expenses were \$64,651,000 for the year ended December 31, 2018, as compared to \$74,430,000 for the year ended December 31, 2017, a decrease of \$9,779,000, or 13%. The primary components of other expenses, net are detailed in the table below (in thousands):

	Year Ended		Increase	% Increase	
	December 31, 2018	December 31, 2017			
General and administrative	\$23,281	\$23,949	\$ (668)	(3)%
Depreciation and amortization	25,679	27,240	(1,561)	(6)%
Equity in earnings of real estate partnership	(8,431)	—	(8,431)	Not Meaningful	
Interest expense	25,177	23,651	1,526	6	%
Interest, dividend and other investment income	(1,055)	(410)	(645)	157	%
Total other expenses	\$64,651	\$74,430	\$ (9,779)	(13)%

General and administrative. General and administrative expenses decreased approximately \$668,000 for the year ended December 31, 2018 as compared to 2017. The decrease in general and administrative expenses included decreased share-based compensation expense costs of \$3,668,000, decreased acquisition costs of \$832,000, and decreased other expenses of \$407,000, offset by increased professional fees primarily resulting from a proxy contest at our 2018 annual meeting of shareholders of \$2,099,000, increased salaries and benefits, net of allocated costs of \$2,080,000, and increased marketing costs of \$60,000

Equity in earnings of real estate partnership. Equity in earnings of real estate partnership increased \$8,431,000 for the year ended December 31, 2018 as compared to 2017 from the derecognition of Pillarstone Properties as a result of the adoption of Topic 606 and ASC 610.

Depreciation and amortization. Depreciation and amortization decreased \$1,561,000, or 6%, for the year ended December 31, 2018 as compared to 2017. Non-Same Store depreciation increased \$1,166,000. Same Store depreciation increased \$1,142,000. The increase in Same Store depreciation is attributable to redevelopment and re-tenanting investments. Depreciation for Pillarstone OP properties decreased by \$3,933,000 from the derecognition of Pillarstone Properties as a result of the adoption of Topic 606 and ASC 610. Depreciation on corporate assets and amortization of commission costs increased \$64,000.

Interest expense. Interest expense increased \$1,526,000, or 6%, for the year ended December 31, 2018 as compared to 2017 from the derecognition of Pillarstone Properties as a result of the adoption of Topic 606 and ASC 610. A decrease in our average outstanding notes payable balance of \$262,000 accounted for \$9,000 in decreased interest expense, and an increase in our effective interest rate to 3.89% for the year ended December 31, 2018 as compared to 3.62% for the year ended December 31, 2017, resulting in a \$1,726,000 increase in interest expense. Amortization of loan fees decreased interest expense by \$191,000 for the year ended December 31, 2018 as compared to the year ended December 31, 2017.

Interest, dividend and other investment income. Interest, dividend and other investment income increased \$645,000, or 157%, for the year ended December 31, 2018 as compared to 2017. During the year ended December 31, 2018, our interest income decreased \$69,000, interest from real estate partnership increased \$583,000, amortization of guaranty of real estate partnership income increased \$72,000, our gain on sales of investments in available-for-sale securities increased \$71,000 and our dividend income decreased \$12,000 as compared to the amounts realized during the year ended December 31, 2017.

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Year Ended December 31, 2017 Compared to Year Ended December 31, 2016

The following table provides a general comparison of our results of operations for the years ended December 31, 2017 and 2016 (dollars in thousands, except per share data):

	Year Ended December			
	31,			
	2017	2016		
Number of properties wholly-owned and operated	59	55		
Aggregate GLA (sq. ft.) ⁽¹⁾	5,023,215	4,557,425		
Ending occupancy rate - wholly-owned operating portfolio ⁽¹⁾	91	% 90	%	
Ending occupancy rate - all wholly-owned properties	90	% 89	%	
Number of properties managed	14	14		
Aggregate GLA (sq. ft.)	1,531,737	1,531,737		
Ending occupancy rate - managed operating portfolio	81	% 81	%	
Total property revenues	\$125,959	\$104,437		
Total property expenses	42,110	34,092		
Total other expenses	74,430	65,189		
Provision for income taxes	386	289		
Gain on sale of properties	(16)	(3,357)		
Profit sharing expense	278	15		
Loss on disposal of assets	183	96		
Net income	8,588	8,113		
Less: Net income attributable to noncontrolling interests	254	182		
Net income attributable to Whitestone REIT	\$8,334	\$7,931		
Funds from operations ⁽²⁾	\$35,045	\$27,031		
Funds from operations core ⁽³⁾	47,096	39,379		
Property net operating income ⁽⁴⁾	83,849	70,345		
Distributions paid on common shares and OP units	41,713	32,640		
Distributions per common share and OP unit	\$1.1400	\$1.1400		
Distributions paid as a percentage of funds from operations core	89	% 83	%	

(1) Excludes (i) new acquisitions, through the earlier of attainment of 90% occupancy or 18 months of ownership, and (ii) properties that are undergoing significant redevelopment or re-tenanting.

(2) For an explanation and reconciliation of funds from operations and funds from operations core to net income, see “Funds From Operations” below.

(3) For a reconciliation of funds from operations core to net income, see “FFO Core” below.

(4) For an explanation and reconciliation of property net operating income to net income, see “Property Net Operating Income” below.

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Property revenues. We had rental income and tenant reimbursements of approximately \$125,959,000 for the year ended December 31, 2017 as compared to \$104,437,000 for the year ended December 31, 2016, an increase of \$21,522,000, or 21%. The year ended December 31, 2017 included \$17,057,000 in increased revenues from Non-Same Store operations and \$181,000 in increased revenues from Pillarstone OP. We define “Non-Same Stores” as properties acquired since the beginning of the period being compared and properties that have been sold, but not classified as discontinued operations. During the twelve months ended December 31, 2017, Same Store revenues increased \$4,284,000. We define “Same Stores” as properties owned during the entire period being compared. For purposes of comparing the year ended December 31, 2017 to the year ended December 31, 2016, Same Stores include properties owned from January 1, 2016 to December 31, 2017. Same Store average occupancy increased from 89.0% for the year ended December 31, 2016 to 89.5% for the year ended December 31, 2017. Same Store revenue rate per average leased square foot increased \$0.81 for the year ended December 31, 2017 to \$23.49 per average leased square foot as compared to the year ended December 31, 2016 revenue rate per average leased square foot of \$22.68, increasing Same Store revenue by \$3,143,000. The revenue rate per average leased square feet is calculated by dividing the total revenue by the average square feet leased during the period.

Property expenses. Our property expenses were \$42,110,000 for the year ended December 31, 2017, as compared to \$34,092,000 for the year ended December 31, 2016, an increase of \$8,018,000, or 24%. Property expenses for the year ended December 31, 2017 included Same Store, Non-Same Store and Pillarstone OP amounts of \$29,809,000, \$5,126,000 and \$7,175,000, respectively. Property expenses for the year ended December 31, 2016 included Same Store, Non-Same Store and Pillarstone OP amounts of \$27,078,000, \$607,000 and \$6,407,000, respectively. The primary components of total property expenses, Same Store property expenses and Non-Same Store property expenses are detailed in the tables below (in thousands):

	Year Ended December 31,		Increase	% Increase	
	2017	2016			
Overall Property Expenses					
Real estate taxes	\$17,897	\$14,383	\$3,514	24	%
Utilities	5,514	4,868	646	13	%
Contract services	7,186	5,941	1,245	21	%
Repairs and maintenance	5,052	3,802	1,250	33	%
Bad debt	2,356	1,589	767	48	%
Labor and other	4,105	3,509	596	17	%
Total	\$42,110	\$34,092	\$8,018	24	%
	Year Ended December 31,			% Increase	
	2017	2016	Increase		
Same Store Property Expenses					
Real estate taxes	\$12,883	\$11,873	\$1,010	9	%
Utilities	3,738	3,423	315	9	%
Contract services	4,988	4,865	123	3	%
Repairs and maintenance	3,733	2,921	812	28	%
Bad debt	1,742	1,367	375	27	%
Labor and other	2,725	2,629	96	4	%
Total	\$29,809	\$27,078	\$2,731	10	%
	Year Ended December 31,		Increase	% Increase	
	2017	2016	(Decrease)	(Decrease)	
Non-Same Store Property Expenses					
Real estate taxes	\$2,422	\$190	\$2,232	1,175	%

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Utilities	614	101	513	508	%
Contract services	1,054	84	970	1,155	%
Repairs and maintenance	406	77	329	427	%
Bad debt	225	17	208	1,224	%
Labor and other	405	138	267	193	%
Total	\$5,126	\$607	\$ 4,519	744	%

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Real estate taxes. Real estate taxes increased \$3,514,000, or 24%, during the year ended December 31, 2017 as compared to 2016. The \$3,514,000 increase was comprised of increases of \$2,232,000 in Non-Same Store expense, \$1,010,000 in Same Store expense and \$272,000 in Pillarstone OP properties. We actively work to keep our valuations and resulting taxes low because a majority of these taxes are charged to our tenants through triple net leases, and we strive to keep these charges to our tenants as low as possible.

Utilities. Utilities increased \$646,000, or 13%, during the year ended December 31, 2017 as compared to 2016. The \$646,000 increase was comprised of increases of \$513,000 in Non-Same Store expense and \$315,000 in Same Store expenses, offset by a decrease of \$182,000 in Pillarstone OP properties.

Contract services. Contract services increased \$1,245,000, or 21%, during the year ended December 31, 2017 as compared to 2016. The \$1,245,000 increase was comprised of increases of \$970,000 in Non-Same Store expense, \$123,000 in Same Store expense and \$152,000 in Pillarstone OP properties.

Repairs and maintenance. Repairs and maintenance increased \$1,250,000, or 33%, during the year ended December 31, 2017 as compared to 2016. The \$1,250,000 increase was comprised of increases of \$329,000 in Non-Same Store expense, \$812,000 in Same Store expense and \$109,000 in Pillarstone OP properties.

Bad debt. Bad debt for the year ended December 31, 2017 increased \$767,000, or 48%, as compared to 2016. The \$767,000 increase was comprised of increases of \$208,000 in Non-Same Store expense, \$375,000 in Same Store expense and \$184,000 in Pillarstone OP properties.

Labor and other. Labor and other expenses increased \$596,000, or 17%, for year ended December 31, 2017 as compared to 2016. The \$596,000 increase was comprised of increases of \$267,000 in Non-Same Store expense, \$96,000 in Same Store expense and \$233,000 in Pillarstone OP properties.

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Same Store, Non-Same Store and Pillarstone OP net operating income. The components of Same Store, Non-Same Store and Pillarstone OP property net operating income and net income are detailed in the table below (in thousands):

	Year Ended December 31,		Increase	%	
	2017	2016	(Decrease)	Increase	(Decrease)
Same Store (49 properties excluding development land)					
Property revenues					
Rental revenues	\$67,706	\$65,340	\$ 2,366	4	%
Other revenues	23,456	21,538	1,918	9	%
Total property revenues	91,162	86,878	4,284	5	%
Property expenses					
Property operation and maintenance	16,926	15,205	1,721	11	%
Real estate taxes	12,883	11,873	1,010	9	%
Total property expenses	29,809	27,078	2,731	10	%
Total same store net operating income	61,353	59,800	1,553	3	%
Non-Same Store (4 properties excluding development land)					
Property revenues					
Rental revenues	13,960	1,796	12,164	677	%
Other revenues	5,396	503	4,893	973	%
Total property revenues	19,356	2,299	17,057	742	%
Property expenses					
Property operation and maintenance	2,704	417	2,287	548	%
Real estate taxes	2,422	190	2,232	1,175	%
Total property expenses	5,126	607	4,519	744	%
Total Non-Same Store net operating income	14,230	1,692	12,538	741	%
Pillarstone OP properties (14 properties)					
Property revenues					
Rental revenues	12,902	12,932	(30)	0	%
Other revenues	2,539	2,328	211	9	%
Total property revenues	15,441	15,260	181	1	%
Property expenses					
Property operation and maintenance	4,583	4,087	496	12	%
Real estate taxes	2,592	2,320	272	12	%
Total property expenses	7,175	6,407	768	12	%
Total Pillarstone OP properties net operating income	8,266	8,853	(587)	(7))%
Total property net operating income	83,849	70,345	13,504	19	%
Less total other expenses, provision for income taxes and loss on disposal of assets	75,261	62,232	13,029	21	%

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Net income	\$8,588	\$8,113	\$ 475	6	%
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Other expenses. Our other expenses were \$74,430,000 for the year ended December 31, 2017, as compared to \$65,189,000 for the year ended December 31, 2016, an increase of \$9,241,000, or 14%. The primary components of other expenses, net are detailed in the table below (in thousands):

	Year Ended		Increase (Decrease)	% Increase (Decrease)
	December 31, 2017	2016		
General and administrative	\$23,949	\$23,922	\$ 27	— %
Depreciation and amortization	27,240	22,457	4,783	21 %
Interest expense	23,651	19,239	4,412	23 %
Interest, dividend and other investment income	(410)	(429)	19	(4)%
Total other expenses	\$74,430	\$65,189	\$ 9,241	14 %

General and administrative. General and administrative expenses increased approximately \$27,000 for the year ended December 31, 2017 as compared to 2016. The increase in general and administrative expenses included increased salaries and benefits costs of \$282,000, increased share-based compensation of \$179,000 and increased professional fees of \$133,000, offset by decreased acquisition expenses and other expenses of \$541,000 and \$26,000, respectively.

Depreciation and amortization. Depreciation and amortization increased \$4,783,000, or 21%, for the year ended December 31, 2017 as compared to 2016. Non-Same Store depreciation increased \$2,649,000, Pillarstone OP depreciation decreased \$264,000 and Same Store depreciation increased \$1,810,000. The increase in Same Store depreciation is attributable to redevelopment and re-tenanting investments. Depreciation on corporate assets and amortization of commission costs increased \$60,000.

Interest expense. Interest expense increased \$4,412,000, or 23%, for the year ended December 31, 2017 as compared to 2016. An increase in our average outstanding notes payable balance of \$97,534,000 accounted for \$3,366,000 in increased interest expense, and an increase in our effective interest rate to 3.62% for the year ended December 31, 2017 as compared to 3.45% for the year ended December 31, 2016, resulting in a \$1,016,000 increase in interest expense. Amortization of loan fees increased interest expense by \$30,000 for the year ended December 31, 2017 as compared to the year ended December 31, 2016.

Interest, dividend and other investment income. Interest, dividend and other investment income decreased \$19,000, or 4%, for the year ended December 31, 2017 as compared to 2016. During the year ended December 31, 2017, our interest income increased \$79,000, our gains on sales of investments in available-for-sale securities decreased \$91,000 and our dividend income decreased \$7,000 as compared to the amounts realized during the year ended December 31, 2016.

Quarterly Results of Operations

Comparison of the Three Months Ended March 31, 2018 and 2017

The following table provides a general comparison of our results of operations for the three months ended March 31, 2018 and 2017 after giving effect to the Quarterly Restatement - See Note 19 to our accompanying consolidated financial statements for further details - (dollars in thousands, except per share data):

	Three Months Ended March 31,				
	2018 (as Restated)	2017	Change	Change %	
Number of properties owned and operated	58	55	3	5	%
Aggregate GLA (sq. ft.) ⁽¹⁾	4,949,285	4,584,488	364,797	8	%
Ending occupancy rate - operating portfolio ⁽¹⁾	91	% 89	% 2	% 2	%
Ending occupancy rate	91	% 88	% 3	% 3	%
Number of properties managed	14	14	—	—	%
Aggregate GLA (sq. ft.)	1,531,737	1,531,737	—	—	%
Ending occupancy rate - managed operating portfolio	78	% 80	% (2))(3))%
Total property revenues	\$29,785	\$28,267	\$1,518	5	%
Total property expenses	8,832	9,414	(582)	(6))%
Total other expenses	17,643	17,192	451	3	%
Provision for income taxes	110	81	29	36	%
Gain on sale of properties	(249)	—	(249)	Not meaningful	
Profit sharing expense	—	64	(64)	(100))%
Loss on disposal of assets	180	23	157	683	%
Net income	3,269	1,493	1,776	119	%
Less: Net income attributable to noncontrolling interests	88	53	35	66	%
Net income attributable to Whitestone REIT	\$3,181	\$1,440	\$1,741	121	%

(1) Excludes (i) new acquisitions, through the earlier of attainment of 90% occupancy or 18 months of ownership, and (ii) properties that are undergoing significant redevelopment or re-tenanting.

Property revenues. We had rental income and tenant reimbursements of approximately \$29,785,000 for the three months ended March 31, 2018 as compared to \$28,267,000 for the three months ended March 31, 2017, an increase of \$1,518,000, or 5% as the result of an increase in the average leased square feet.

Property expenses. Our property expenses were \$8,832,000 for the three months ended March 31, 2018, as compared to \$9,414,000 for the three months ended March 31, 2017, a decrease of \$582,000, or 6%.

Other expenses. Our other expenses were \$17,643,000 for the three months ended March 31, 2018, as compared to \$17,192,000 for the three months ended March 31, 2017, an increase of \$451,000, or 3%.

Comparison of the Three Months Ended June 30, 2018 and 2017

The following table provides a general comparison of our results of operations for the three months ended June 30, 2018 and 2017 after giving effect to the Quarterly Restatement - See Note 19 to our accompanying consolidated financial statements for further details - (dollars in thousands, except per share data):

	Three Months Ended June 30,			
	2018 (as Restated)	2017	Change	Change %
Number of properties owned and operated	58	58	—	— %
Aggregate GLA (sq. ft.) ⁽¹⁾	4,949,285	5,023,009	(73,724)	(1) %
Ending occupancy rate - operating portfolio ⁽¹⁾	91 %	90 %	1 %	1 %
Ending occupancy rate	91 %	89 %	2 %	2 %
Number of properties managed	14	14	—	— %
Aggregate GLA (sq. ft.)	1,529,861	1,531,737	(1,876)	— %
Ending occupancy rate - managed operating portfolio	77 %	78 %	(1) %	(1) %
Total property revenues	\$29,473	\$30,208	\$(735)	(2) %
Total property expenses	8,922	9,862	(940)	(10) %
Total other expenses	18,414	18,057	357	2 %
Provision for income taxes	59	89	(30)	(34) %
Gain on sale of properties	—	(16)	16	(100) %
Profit sharing expense	—	101	(101)	(100) %
Loss on disposal of assets	73	72	1	1 %
Net income	2,005	2,043	(38)	(2) %
Less: Net income attributable to noncontrolling interests	51	60	(9)	(15) %
Net income attributable to Whitestone REIT	\$1,954	\$1,983	\$(29)	(1) %

(1) Excludes (i) new acquisitions, through the earlier of attainment of 90% occupancy or 18 months of ownership, and (ii) properties that are undergoing significant redevelopment or re-tenanting.

Property revenues. We had rental income and tenant reimbursements of approximately \$29,473,000 for the three months ended June 30, 2018 as compared to \$30,208,000 for the three months ended June 30, 2017, a decrease of \$735,000, or 2% as a result of the derecognition of Pillarstone Properties as a result of the adoption of Topic 606 and ASC 610.

Property expenses. Our property expenses were \$8,922,000 for the three months ended June 30, 2018, as compared to \$9,862,000 for the three months ended June 30, 2017, a decrease of \$940,000, or 10% as a result of the derecognition of Pillarstone Properties as a result of the adoption of Topic 606 and ASC 610.

Other expenses. Our other expenses were \$18,414,000 for the three months ended June 30, 2018, as compared to \$18,057,000 for the three months ended June 30, 2017, an increase of \$357,000, or 2%.

Comparison of the Three Months Ended September 30, 2018 and 2017

The following table provides a general comparison of our results of operations for the three months ended September 30, 2018 and 2017 after giving effect to the Quarterly Restatement - See Note 19 to our accompanying consolidated financial statements for further details - (dollars in thousands, except per share data):0

	Three Months Ended September 30,				
	2018 (as Restated)	2017	Change	Change %	
Number of properties owned and operated	57	58	(1)	(2)	%
Aggregate GLA (sq. ft.) ⁽¹⁾	4,843,519	5,023,215	(179,696)	(4)	%
Ending occupancy rate - operating portfolio ⁽¹⁾	92 %	90 %	2 %	2 %	%
Ending occupancy rate	92 %	90 %	2 %	2 %	%
Number of properties managed	14	14	—	—	%
Aggregate GLA (sq. ft.)	1,529,861	1,531,737	(1,876)	—	%
Ending occupancy rate - managed operating portfolio	80 %	80 %	— %	— %	%
Total property revenues	\$30,704	\$33,653	\$(2,949)	(9)	%
Total property expenses	9,831	11,285	(1,454)	(13)	%
Total other expenses	17,125	19,062	(1,937)	(10)	%
Provision for income taxes	92	126	(34)	(27)	%
Gain on sale of properties	(4,380)	—	(4,380)	Not meaningful	
Profit sharing expense	—	63	(63)	(100)	%
Loss on disposal of assets	3	40	(37)	(93)	%
Net income	8,033	3,077	4,956	161	%
Less: Net income attributable to noncontrolling interests	198	84	114	136	%
Net income attributable to Whitestone REIT	\$7,835	\$2,993	\$4,842	162	%

(1) Excludes (i) new acquisitions, through the earlier of attainment of 90% occupancy or 18 months of ownership, and (ii) properties that are undergoing significant redevelopment or re-tenanting.

Property revenues. We had rental income and tenant reimbursements of approximately \$30,704,000 for the three months ended September 30, 2018 as compared to \$33,653,000 for the three months ended September 30, 2017, a decrease of \$2,949,000, or 9% as a result of the derecognition of Pillarstone Properties as a result of the adoption of Topic 606 and ASC 610.

Property expenses. Our property expenses were \$9,831,000 for the three months ended September 30, 2018, as compared to \$11,285,000 for the three months ended September 30, 2017, a decrease of \$1,454,000, or 13% as a result of the derecognition of Pillarstone Properties as a result of the adoption of Topic 606 and ASC 610.

Other expenses. Our other expenses were \$17,125,000 for the three months ended September 30, 2018, as compared to \$19,062,000 for the three months ended September 30, 2017, a decrease of \$1,937,000, or 10% as a result of the derecognition of Pillarstone Properties as a result of the adoption of Topic 606 and ASC 610.

Reconciliation of Non-GAAP Financial Measures

Funds From Operations (“FFO”)

The National Association of Real Estate Investment Trusts (“NAREIT”) defines FFO as net income (loss) available to common shareholders computed in accordance with GAAP, excluding gains or losses from sales of operating real estate assets or assets of equity method investments, impairment charges on properties held for investment and extraordinary items, plus depreciation and amortization of operating properties, including our share of equity method investments. We calculate FFO in a manner consistent with the NAREIT definition.

Management uses FFO as a supplemental measure to conduct and evaluate our business because there are certain limitations associated with using GAAP net income (loss) alone as the primary measure of our operating performance.

Historical cost accounting for real estate assets in accordance with GAAP implicitly assumes that the value of real estate assets diminishes predictably over time. Because real estate values instead have historically risen or fallen with market conditions, management believes that the presentation of operating results for real estate companies that use historical cost accounting is insufficient by itself. In addition, securities analysts, investors and other interested parties use FFO as the primary metric for comparing the relative performance of equity REITs.

FFO should not be considered as an alternative to net income or other measurements under GAAP, as an indicator of our operating performance or to cash flows from operating, investing or financing activities as a measure of liquidity. FFO does not reflect working capital changes, cash expenditures for capital improvements or principal payments on indebtedness. Although our calculation of FFO is consistent with that of NAREIT, there can be no assurance that FFO presented by us is comparable to similarly titled measures of other REITs.

FFO Core

Management believes that the computation of FFO in accordance with NAREIT’s definition includes certain items that are not indicative of the results provided by our operating portfolio and affect the comparability of our period-over-period performance. These items include, but are not limited to, legal settlements, proxy contest fees, debt extension costs, non-cash share-based compensation expense, rent support agreement payments received from sellers on acquired assets, management fees from Pillarstone and acquisition costs. Therefore, in addition to FFO, management uses FFO Core, which we define to exclude such items. Management believes that these adjustments are appropriate in determining FFO Core as they are not indicative of the operating performance of our assets. In addition, we believe that FFO Core is a useful supplemental measure for the investing community to use in comparing us to other REITs as many REITs provide some form of adjusted or modified FFO. However, there can be no assurance that FFO Core presented by us is comparable to the adjusted or modified FFO of other REITs.

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Below are the calculations of FFO and FFO Core and the reconciliations to net income, which we believe is the most comparable GAAP financial measure (in thousands):

	Year Ended December 31,		
	2018	2017	2016
FFO AND FFO CORE			
Net income attributable to Whitestone REIT	\$21,431	\$8,334	\$7,931
Adjustments to reconcile to FFO: ⁽¹⁾			
Depreciation and amortization of real estate assets	25,401	26,290	22,179
Depreciation and amortization of real estate assets of real estate partnership (pro rata) ⁽²⁾	2,903	—	—
(Gain) loss on sale or disposal of assets and properties, net	(4,547)	167	(3,261)
Gain on sale or disposal of properties or assets of real estate partnership (pro rata) ⁽²⁾	(6,340)	—	—
Net income attributable to noncontrolling interests	550	254	182
FFO	\$39,398	\$35,045	\$27,031
Share-based compensation expense	\$6,758	\$10,426	\$10,247
Proxy contest professional fees	2,534	—	—
Early debt extinguishment costs of real estate partnership	88	—	—
Acquisition costs	—	1,625	2,101
FFO Core	\$48,778	\$47,096	\$39,379

⁽¹⁾ Includes pro-rata share attributable to real estate partnership.

⁽²⁾ Included in equity in earnings of real estate partnership on the consolidated statements of operations and comprehensive income.

Property Net Operating Income (“NOI”)

Management believes that NOI is a useful measure of our property operating performance. We define NOI as operating revenues (rental and other revenues) less property and related expenses (property operation and maintenance and real estate taxes). Other REITs may use different methodologies for calculating NOI and, accordingly, our NOI may not be comparable to other REITs. Because NOI excludes general and administrative expenses, depreciation and amortization, involuntary conversion, interest expense, interest income, provision for income taxes, gain or loss on sale or disposition of assets, and our pro rata share of NOI of equity method investments, it provides a performance measure that, when compared year over year, reflects the revenues and expenses directly associated with owning and operating commercial real estate properties and the impact to operations from trends in occupancy rates, rental rates and operating costs, providing perspective not immediately apparent from net income. We use NOI to evaluate our operating performance since NOI allows us to evaluate the impact that factors such as occupancy levels, lease structure, lease rates and tenant base have on our results, margins and returns. In addition, management believes that NOI provides useful information to the investment community about our property and operating performance when compared to other REITs since NOI is generally recognized as a standard measure of property performance in the real estate industry. However, NOI should not be viewed as a measure of our overall financial performance since it does not reflect general and administrative expenses, depreciation and amortization, involuntary conversion, interest expense, interest income, provision for income taxes and gain or loss on sale or disposition of assets, the level of capital expenditures and leasing costs necessary to maintain the operating performance of our properties.

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Below is the calculation of NOI and the reconciliation to net income, which we believe is the most comparable GAAP financial measure (in thousands):

	Year Ended December 31,		
PROPERTY NET OPERATING INCOME (“NOI”)	2018	2017	2016
Net income attributable to Whitestone REIT	\$21,431	\$8,334	\$7,931
General and administrative expenses	23,281	23,949	23,922
Depreciation and amortization	25,679	27,240	22,457
Equity in earnings of real estate partnership	(8,431)	—	—
Interest expense	25,177	23,651	19,239
Interest, dividend and other investment income	(1,055)	(410)	(429)
Provision for income taxes	347	386	289
Gain on sale of properties	(4,629)	(16)	(3,357)
Management fee, net of related expenses	(208)	—	—
Profit sharing expense	—	278	15
Loss on sale or disposal of assets	82	183	96
NOI of real estate partnership (pro rata)	7,725	—	—
Net income attributable to noncontrolling interests	550	254	182
NOI	\$89,949	\$83,849	\$70,345

Taxes

We elected to be taxed as a REIT under the Code beginning with our taxable year ended December 31, 1999. As a REIT, we generally are not subject to federal income tax on income that we distribute to our shareholders. If we fail to qualify as a REIT in any taxable year, we will be subject to federal income tax on our taxable income at regular corporate rates. We believe that we are organized and operate in a manner to qualify and be taxed as a REIT, and we intend to operate so as to remain qualified as a REIT for federal income tax purposes.

Inflation

We anticipate that the majority of our leases will continue to be triple-net leases or otherwise provide that tenants pay for increases in operating expenses and will contain provisions that we believe will mitigate the effect of inflation. In addition, many of our leases are for terms of less than five years, which allows us to adjust rental rates to reflect inflation and other changing market conditions when the leases expire. Consequently, increases due to inflation, as well as ad valorem tax rate increases, generally do not have a significant adverse effect upon our operating results.

Off-Balance Sheet Arrangements

Guarantees We may guarantee the debt of a real estate partnership primarily because it allows the real estate partnership to obtain funding at a lower cost than could be obtained otherwise. This results in a higher return for the real estate partnership on its investment, and a higher return on our investment in the real estate partnership. We may receive a fee from the real estate partnership for providing the guarantee. Additionally, when we issue a guarantee, the terms of the real estate partnership’s partnership agreement typically provide that we may receive indemnification from the real estate partnership or have the ability to increase our ownership interest. See Note 5 and Note 19 to the accompanying consolidated financial statements for information related to our guarantees of our real estate partnership’s debt as of December 31, 2018 and 2017.

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Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

Our future income, cash flows and fair value relevant to our financial instruments depend upon prevailing market interest rates. Market risk refers to the risk of loss from adverse changes in market prices and interest rates. Based upon the nature of our operations, we are not subject to foreign exchange rate or commodity price risk. The principal market risk to which we are exposed is the risk related to interest rate fluctuations. Many factors, including governmental monetary and tax policies, domestic and international economic and political considerations, and other factors that are beyond our control contribute to interest rate risk. Our interest rate risk objective is to limit the impact of interest rate fluctuations on earnings and cash flows and to lower our overall borrowing costs. To achieve this objective, we manage our exposure to fluctuations in market interest rates for our borrowings through the use of fixed rate debt instruments to the extent that reasonably favorable rates are obtainable.

All of our financial instruments were entered into for other than trading purposes.

Fixed Interest Rate Debt

As of December 31, 2018, \$378.2 million, or approximately 61%, of our outstanding debt was subject to fixed interest rates, which limit the risk of fluctuating interest rates. Though a change in the market interest rates affects the fair market value, it does not impact net income to shareholders or cash flows. Our total outstanding fixed interest rate debt has an average effective interest rate as of December 31, 2018 of approximately 3.92% per annum with expirations ranging from 2019 to 2027 (see Note 9 to our accompanying consolidated financial statements for further detail). Holding other variables constant, a 1% increase or decrease in interest rates would cause a \$13.1 million decline or increase, respectively, in the fair value for our fixed rate debt.

Variable Interest Rate Debt

As of December 31, 2018, \$241.2 million, or approximately 39%, of our outstanding debt was subject to floating interest rates of LIBOR plus 1.40% to 1.95% and not currently subject to a hedge. The impact of a 1% increase or decrease in interest rates on our floating rate debt would result in a decrease or increase, respectively, of annual net income of approximately \$2.4 million.

Item 8. Financial Statements and Supplementary Data.

The information required by this Item 8 is incorporated by reference to our accompanying consolidated financial statements beginning on page F-1 of this Annual Report on Form 10-K.

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

None.

Item 9A. Controls and Procedures.

Overview

As previously announced on February 26, 2019, the Audit Committee of the Board of Trustees (the “Audit Committee”) of the Company, after consultation with members of senior management of the Company, concluded that the Company’s unaudited consolidated financial statements as of and for the periods ended March 31, 2018, June 30, 2018 and September 30, 2018 (collectively, the “2018 Quarterly Financial Statements”) included in the Company’s Quarterly Reports on Form 10-Q for the quarterly periods ended March 31, 2018, June 30, 2018 and September 30, 2018, respectively, should be restated to correct an accounting error. Please refer to “Part II - Item 7 - Management’s

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Discussion and Analysis of Financial Condition and Results of Operations” and Note 19 (Selected Quarterly Financial Data), included in “Part II - Item 8 - Consolidated Financial Statements and Supplementary Data” for a more detailed description of the Quarterly Restatement.

Notwithstanding the existence of the material weakness described below, we believe that the consolidated financial statements in this Annual Report on Form 10-K fairly present, in all material respects, our financial position, results of operations and cash flows as of the dates, and for the periods presented, in conformity with GAAP.

Evaluation of Disclosure Controls and Procedures

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We maintain disclosure controls and procedures that are designed to provide a reasonable assurance that information required to be disclosed in our reports filed or submitted under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure.

Our management, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, has carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of December 31, 2018. Based upon that evaluation, and in light of the material weakness in the design and operation of our internal control over financial reporting disclosed below, our Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this report, our disclosure controls and procedures were not effective at the reasonable assurance level referenced above. In designing and evaluating disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. Management is required to apply judgment in evaluating the cost benefit relationship of possible controls and procedures.

Management's Report on Internal Control Over Financial Reporting

Management, under the supervision of our Chief Executive Officer and Chief Financial Officer, is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rules 13a-15(e) under the Exchange Act). Internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external reporting purposes in accordance with GAAP, and includes those policies and procedures that:

pertain to the maintenance of records that in reasonable detail accurately and fairly reflect our transactions and dispositions of our assets;

provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and

provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on our financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis.

Our management conducted a process to assess the effectiveness of our internal control over financial reporting as of December 31, 2018, based on the criteria established in Internal Control – Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission, or COSO. This framework highlights that the control environment sets the tone of the organization, influences the control consciousness of its people, and is the foundation for all other components of internal control over financial reporting.

During the assessment process, we identified the following material weakness as of December 31, 2018 in the Company's internal controls over financial reporting and disclosure controls and procedures.

- Application of New Accounting Pronouncements, including proper assessment of judgment items in complex accounting transactions - The Company did not have effective controls to ensure the proper application of new accounting pronouncements in its financial statements. After its review of the error and its internal controls over financial reporting and disclosure controls and procedures, the Company determined that it did not appropriately weigh its legal rights in its assessment of the transfer of control criteria under Topic 606 as it pertained to the Contribution.

The material weakness described above contributed to accounting errors that required the restatement of our consolidated financial statements for the first three quarterly periods of the year ended December 31, 2018. As a result of the material weakness described above, management has concluded that, as of December 31, 2018, our internal control over financial reporting was not effective.

The Company's independent registered public accounting firm has issued a report on the effectiveness of the Company's internal control over financial reporting, which appears on page F-3 of this Annual Report on Form 10-K.

Remediation of Material Weakness in Internal Control over Financial Reporting

Our management, under the supervision of our Chief Executive Officer and Chief Financial Officer, and with the oversight of the Audit Committee, has undertaken a plan to remediate the material weakness identified above. The remediation efforts summarized below, which are either implemented or in the process of being implemented, are intended to address the identified material weakness.

- Enhancements to internal controls regarding the adoption of new accounting pronouncements including:
 - Enhanced documentation of the details of new accounting pronouncements;
 - Enhanced documentation of areas in new accounting pronouncements that require the exercise of management's judgment; and
 - Enhanced documentation of the applicability of new accounting pronouncements to the Company's business.
- Engagement of outside technical experts to assist the Company in the application and adoption of new accounting pronouncements.
- Ensure key accounting personnel have appropriate training.
- Additional accounting staff with appropriate experience, certification, education and training.
- Implementation of a disclosure review committee, including outside technical advisors, the Chief Financial Officer, accounting staff, and other members of management. The committee will meet quarterly, at a minimum, to provide guidance and oversight to ensure the proper implementation of the enhanced internal controls regarding the adoption of new accounting pronouncements.
- Quarterly review with the Audit Committee of new accounting pronouncements, including a discussion of key judgment areas.

Changes in Internal Control Over Financial Reporting

Other than those described in "Remediation of Material Weakness in Internal Control over Financial Reporting" above, there have been no changes during the Company's quarter ended December 31, 2018, in the Company's internal controls over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Item 9B. Other Information.

None.

PART III

Item 10. Trustees, Executive Officers and Corporate Governance.

The information required by Item 10 of Form 10-K is incorporated herein by reference to such information as set forth in the definitive proxy statement for our 2019 Annual Meeting of Shareholders.

Item 11. Executive Compensation.

The information required by Item 11 of Form 10-K is incorporated herein by reference to such information as set forth in the definitive proxy statement for our 2019 Annual Meeting of Shareholders.

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

The following table provides information regarding our equity compensation plans as of December 31, 2018:

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
	(a)	(b)	(c)
Equity compensation plans approved by security holders	—	(1) \$	— 3,172,158 (2)
Equity compensation plans not approved by security holders	—	—	— (3)
Total	—	\$	— 3,172,158

(1) Excludes 3,119,221 common shares subject to outstanding restricted common share units granted pursuant to our 2008 Long-Term Equity Incentive Ownership Plan, as amended (the “2008 Plan”).

At our annual meeting of shareholders on May 11, 2017, our shareholders voted to approve the 2018 Long-Term Equity Incentive Ownership Plan (the “2018 Plan”). The 2018 Plan provides for the issuance of up to 3,433,831 common shares and OP units pursuant to awards under the 2018 Plan. The 2018 Plan became effective on July 30,

(2) 2018, which is the day after the 2008 Plan expired. Pursuant to the 2008 Plan, the maximum aggregate number of common shares that were issuable under the 2008 Plan was increased upon each issuance of common shares by the Company so that at any time the maximum number of shares that were issuable under the 2008 Plan equaled 12.5% of the aggregate number of common shares of the Company and OP units issued and outstanding (other than units issued to or held by the Company).

(3) Excludes 8,333 restricted common shares issued to trustees outside the 2008 Plan.

The remaining information required by Item 12 of Form 10-K is incorporated by reference to such information as set forth in the definitive proxy statement for our 2019 Annual Meeting of Shareholders.

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

The information required by Item 13 of Form 10-K is incorporated herein by reference to such information as set forth in the definitive proxy statement for our 2019 Annual Meeting of Shareholders.

Item 14. Principal Accountant Fees and Services.

The information required by Item 14 of Form 10-K is incorporated herein by reference to such information as set forth in the definitive proxy statement for our 2019 Annual Meeting of Shareholders.

PART IV

Item 15. Exhibits and Financial Statement Schedules.

1. Financial Statements. The list of our financial statements filed as part of this Annual Report on Form 10-K is set forth on page F-1 herein.

2. Financial Statement Schedules.

a. Schedule II - Valuation and Qualifying Accounts

b. Schedule III - Real Estate and Accumulated Depreciation

All other financial statement schedules have been omitted because the required information of such schedules is not present, is not present in amounts sufficient to require a schedule or is included in the consolidated financial statements.

3. Exhibits. The list of exhibits filed as part of this Annual Report on Form 10-K in response to Item 601 of Regulation S-K is submitted on the Exhibit Index attached hereto and incorporated herein by reference.

Item 16. Form 10-K Summary.

None.

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Exhibit No. Description

- 3.1.1 Articles of Amendment and Restatement of Whitestone REIT (previously filed as and incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K, filed on July 31, 2008)
- 3.1.2 Articles Supplementary (previously filed as and incorporated by reference to Exhibit 3(i).1 to the Registrant's Current Report on Form 8-K, filed December 6, 2006)
- 3.1.3 Articles of Amendment (previously filed and incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K, filed on August 24, 2010)
- 3.1.4 Articles of Amendment (previously filed and incorporated by reference to Exhibit 3.2 to the Registrant's Current Report on Form 8-K, filed on August 24, 2010)
- 3.1.5 Articles Supplementary (previously filed and incorporated by reference to Exhibit 3.3 to the Registrant's Current Report on Form 8-K, filed on August 24, 2010)
- 3.1.6 Articles of Amendment (previously filed as and incorporated by reference to Exhibit 3.1.1 to the Registrant's Current Report on Form 8-K, filed June 27, 2012)
- 3.1.7 Articles of Amendment (previously filed as and incorporated by reference to Exhibit 3.1.2 to the Registrant's Current Report on Form 8-K, filed June 27, 2012)
- 3.2 Amended and Restated Bylaws of Whitestone REIT (previously filed as and incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K, filed October 9, 2008)
- 10.1 Agreement of Limited Partnership of Whitestone REIT Operating Partnership, L.P. (previously filed as and incorporated by reference to Exhibit 10.1 to the Registrant's General Form for Registration of Securities on Form 10, filed on April 30, 2003)
- 10.2 Certificate of Formation of Whitestone REIT Operating Partnership II GP, LLC (previously filed as and incorporated by reference to Exhibit 10.3 to the Registrant's General Form for Registration of Securities on Form 10, filed on April 30, 2003)
- 10.3 Limited Liability Company Agreement of Whitestone REIT Operating Partnership II GP, LLC (previously filed as and incorporated by reference to Exhibit 10.4 to the Registrant's General Form for Registration of Securities on Form 10, filed on April 30, 2003)
- 10.4 Agreement of Limited Partnership of Whitestone REIT Operating Partnership II, L.P. (previously filed as and incorporated by reference to Exhibit 10.6 to the Registrant's General Form for Registration of Securities on Form 10, filed on April 30, 2003)
- 10.5 Amendment to the Agreement of Limited Partnership of Whitestone REIT Operating Partnership, L.P. (previously filed in and incorporated by reference to Exhibit 10.1 to the Registrant's Registration Statement on Form S-11, Commission File No. 333-111674, filed on December 31, 2003)
- 10.6 Promissory Note between HCP REIT Operating Company IV LLC and MidFirst Bank, dated March 1, 2007 (previously filed and incorporated by reference to Exhibit 10.25 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2006, filed on March 30, 2007)
- 10.7 Term Loan Agreement among Whitestone REIT Operating Partnership, L.P., Whitestone Pima Norte LLC, Whitestone REIT Operating Partnership III LP, Hartman REIT Operating Partnership III LP LTD, Whitestone REIT Operating Partnership III GP LLC and KeyBank National Association, dated January 25, 2008 (previously filed as and incorporated by reference to Exhibit 10.29 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2007, filed on March 31, 2008)

Exhibit No. Description

- 10.8+ Whitestone REIT 2008 Long-Term Equity Incentive Ownership Plan (previously filed and incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K, filed July 31, 2008)
- 10.9 Promissory Note among Whitestone Corporate Park West, LLC and MidFirst Bank dated August 5, 2008 (previously filed and incorporated by reference to Exhibit 99.1 to the Registrant's Current Report on Form 8-K, filed August 8, 2008)
- 10.10 Promissory Note among Whitestone Centers LLC and Sun Life Assurance Company of Canada dated October 1, 2008 (previously filed and incorporated by reference to Exhibit 99.1 to the Registrant's Current Report on Form

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8-K, filed October 7, 2008)

10.11 Promissory Note among Whitestone Centers LLC and Sun Life Assurance Company of Canada dated October 1, 2008 (previously filed and incorporated by reference to Exhibit 99.2 to the Registrant's Current Report on Form 8-K, filed October 7, 2008)

10.12 Promissory Note among Whitestone Centers LLC and Sun Life Assurance Company of Canada dated October 1, 2008 (previously filed and incorporated by reference to Exhibit 99.3 to the Registrant's Current Report on Form 8-K, filed October 7, 2008)

10.13 Promissory Note among Whitestone Centers LLC and Sun Life Assurance Company of Canada dated October 1, 2008 (previously filed and incorporated by reference to Exhibit 99.4 to the Registrant's Current Report on Form 8-K, filed October 7, 2008)

10.14 Promissory Note among Whitestone Centers LLC and Sun Life Assurance Company of Canada dated October 1, 2008 (previously filed and incorporated by reference to Exhibit 99.5 to the Registrant's Current Report on Form 8-K, filed October 7, 2008)

10.15 Note among Whitestone Offices LLC and Nationwide Life Insurance Company dated October 1, 2008 (previously filed and incorporated by reference to Exhibit 99.6 to the Registrant's Current Report on Form 8-K, filed October 7, 2008)

10.16 Floating Rate Pr