Seritage Growth Properties
Form 10-K
March 11, 2016
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2015

Commission file number 001-37420

SERITAGE GROWTH PROPERTIES

(Exact name of registrant as specified in its charter)

Maryland	**38-3976287**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**

489 Fifth Avenue, 18th Floor, New York, New York	**10017**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code (212) 355-7800

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

Title of each class	Name of each exchange on which registered
Class A common shares of beneficial interest, par value $0.01 per share	**New York Stock Exchange**

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

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 x

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 x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted 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 and post such files). Yes x No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§232.405 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, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act (Check one):

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

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant as of July 6, 2015 was approximately $1,163,986,000 based upon the closing price of $37.10 of the registrant s common stock as reported on the New York Stock Exchange. The registrant has elected to use July 6, 2015 as the calculation date, which was the initial trading date of the registrant s common shares on the New York Stock Exchange, because as of the last business day of the registrant s most recently completed second fiscal quarter, the registrant was a privately held company.

As of March 4, 2016, the registrant had the following common shares outstanding:

Class	**Shares Outstanding**
Class A common shares of beneficial interest, par value $0.01 per share	25,261,542
Class B common shares of beneficial interest, par value $0.01 per share	1,589,020
Class C common shares of beneficial interest, par value $0.01 per share	6,329,485

DOCUMENTS INCORPORATED BY REFERENCE

Portions of Seritage Growth Properties Proxy Statement for its 2016 Annual Meeting of Shareholders, to be held May 3, 2016, are incorporated by reference into Part III of this Annual Report on Form 10-K.

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SERITAGE GROWTH PROPERTIES

ANNUAL REPORT ON FORM 10-K

PERIOD FROM JULY 7, 2015 (Date Operations Commenced) TO DECEMBER 31, 2015

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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K (the Annual Report) of Seritage Growth Properties contains statements that constitute forward-looking statements within the meaning of the federal securities laws. Any statements that do not relate to historical or current facts or matters are forward-looking statements. You can identify forward-looking statements by the use of forward-looking terminology such as believes, expects, may, will, should, seeks, approximately, intends, plans, pro forma, estimates or anticipates or the opposite of these words and phrases words or phrases which are predictions of or indicate future events or trends and which do not relate solely to historical matters. Statements concerning current conditions may also be forward-looking if they imply a continuation of current conditions. You can also identify forward-looking statements by discussions of strategy, plans or intentions.

Forward-looking statements involve numerous risks and uncertainties and you should not rely on them as predictions of future events. Forward-looking statements depend on assumptions, data or methods which may be incorrect or imprecise and we may not be able to realize them. The following factors, among others, could cause actual results and future events to differ materially from those set forth or contemplated in the forward-looking statements:

- Declines in retail, real estate and general economic conditions;
- Our current dependence on Sears Holdings Corporation for a substantial majority of our revenue;
- Sears Holdings Corporation s termination and other rights under its master lease with us;
- Risks relating to our recapture and redevelopment activities and potential acquisition or disposition of properties;
- Our limited operating history as an independent public company;
- The terms of our indebtedness;
- Tax, environmental, health, safety and land use laws and regulations; and
- Restrictions with which we are required to comply in order to maintain REIT status.

While forward-looking statements reflect our good faith beliefs, they are not guarantees of future performance. Except as required by law, we disclaim any obligation to publicly update or revise any forward-looking statement to reflect changes in underlying assumptions or factors of new information, data or methods, future events or other changes. For a further discussion of these and other factors that could impact our future results, performance or transactions, see Item 1A. Risk Factors.

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PART I

ITEM 1. BUSINESS

Seritage Growth Properties (Seritage) (NYSE: SRG), a Maryland real estate investment trust formed on June 3, 2015, is a fully-integrated, self-administered and self-managed real estate investment trust (REIT) as defined under Section 856(c) of the Internal Revenue Code (the Code). Seritage s assets are held by and its operations are primarily conducted through, directly or indirectly, Seritage Growth Properties, L.P., a Delaware limited partnership (the Operating Partnership). Under the partnership agreement of the Operating Partnership, Seritage, as the sole general partner, has exclusive responsibility and discretion in the management and control of the Operating Partnership. Unless otherwise expressly stated or the context otherwise requires, the Company , we, us, and our as used herein re to Seritage, the Operating Partnership and its owned and controlled subsidiaries.

Seritage is principally engaged in the acquisition, ownership, development, redevelopment, management and leasing of diversified retail real estate throughout the United States. As of December 31, 2015, our portfolio included approximately 42.4 million square feet of gross leasable area (GLA), consisting of 235 wholly owned properties totaling over 37.0 million square feet of GLA across 49 states and Puerto Rico, and interests in 31 joint venture properties totaling over 5.4 million square feet of GLA across 17 states.

On June 11, 2015 Sears Holdings Corporation (Sears Holdings) effected a rights offering (the Rights Offering) to Sears Holdings stockholders to purchase common shares of Seritage in order to fund, in part, the $2.7 billion acquisition of 234 of Sears Holdings owned properties and one of its ground leased properties (the Wholly Owned Properties), and its 50% interests in three joint ventures (the JV Interests) that collectively own 28 properties, ground lease one property and lease two properties (collectively, the JV Properties) (collectively, the Transaction). The Rights Offering ended on July 2, 2015, and the Company s Class A common shares were listed on the New York Stock Exchange on July 6, 2015.

On July 7, 2015, the Company completed the Transaction with Sears Holdings and commenced operations. The Company s only operations prior to the completion of the Rights Offering and Transaction were those incidental to the completion of such activities.

As of December 31, 2015, we leased a substantial majority of the space in our portfolio at all but 11 of the Wholly Owned Properties (such 11 properties, the Third-Party Properties) to Sears Holdings under a master lease agreement (the Master Lease), with the remainder of such space leased to third-party tenants. The Third-Party Properties, which do not contain a Sears Holdings store or have any space leased to Sears Holdings, are leased solely to third-party tenants. A substantial majority of the space at the JV Properties is also leased to Sears Holdings by, as applicable, GS Portfolio Holdings LLC (the GGP JV), a joint venture between a subsidiary of the Operating Partnership and a subsidiary of General Growth Properties, Inc. (together with its other subsidiaries, GGP), SPS Portfolio Holdings LLC (the Simon JV), a joint venture between a subsidiary of the Operating Partnership and a subsidiary of Simon Property Group, Inc. (together with its other subsidiaries, Simon), or MS Portfolio LLC (the Macerich JV and, together with the GGP JV and the Simon JV, each, a JV and collectively, the JVs), a joint venture between a subsidiary of the Operating Partnership and a subsidiary of The Macerich Company (together with its subsidiaries, Macerich), in each case under a separate master lease with each JV (the JV Master Leases).

The Master Lease and the JV Master Leases provide the Company and the JVs with the right to recapture certain space from Sears Holdings at each property for retenanting or redevelopment purposes.

Business Strategies

Our primary objective is to create value for our shareholders through the re-leasing and redevelopment of the majority of our Wholly Owned Properties and JV Properties. In doing so, we expect to meaningfully grow net operating income (NOI) by re-leasing space to third-party retailers at materially higher rents while also substantially diversifying our tenant base. In order to achieve our objective, we intend to execute the following strategies:

Convert single-tenant buildings into multi-tenant properties at meaningfully higher rents. We intend to increase NOI and diversify our portfolio by actively recapturing space at our properties and re-leasing such space to third-party retailers for higher rents than are payable under the Master Lease by Sears Holdings.

We seek to optimize the mix of tenants at, and maximize the value of, our properties by focusing on growing national retailers and taking into account customer demographics and the competitive environment of each property s market area. We believe that the superior real estate locations, diversity of property types and national footprint that characterize our portfolio, combined with the unique recapture features of the Master Lease, make us well-positioned to meet the store growth needs of retailers across a variety of sectors and concepts. As we lease space to such retailers, we aim to create multi-tenant shopping centers that command superior rents and valuations due to their prime locations, synergies with adjoining retailers and proximity to productive malls and shopping centers.

Maximize value of vast land holdings through retail and mixed-use densification. Our portfolio includes over 3,000 acres of land, or approximately 13 acres per site for our Wholly Owned Properties, and our most significant geographic concentrations are in higher growth markets in California, Florida, Texas and the Northeast. We believe these land holdings will provide meaningful opportunities for additional retail and mixed-use development.

In addition to the right to recapture up to approximately 50% of the space occupied by Sears Holdings at substantially all of our Wholly Owned Properties, the Master Lease provides us with the right to recapture (i) 100% of the stores located at 21 identified properties; (ii) all of any automotive care centers which are free-standing or attached as appendages to the stores; and (iii) outparcels or outlots, as well as certain portions of parking areas and common areas.

The 21 identified properties for which we have 100% recapture rights include over 3.9 million square feet of entitled commercial space on over 350 acres of land and our portfolio of automotive care centers encompasses approximately 3.5 million square feet of scarce real estate typically located on the most visible and highly-trafficked site at a property. Given our fee ownership of these properties and control over parking lots and outparcels, we believe that many of these sites, as well as others throughout the portfolio, will provide attractive and value-enhancing development, redevelopment and densification opportunities.

Leverage existing and future joint venture relationships with leading real estate and financial partners. We currently own 50% interests in 31 JV Properties with leading regional mall REITs each of which, we believe, is focused on driving value creation at the JV Properties through recapturing and re-leasing space pursuant to the JV Master Leases.

We participate in 50% of all net value created at the JV Properties and expect to benefit from the leasing and redevelopment platforms of our JV partners, as well as stores that are, generally, located at high-productivity malls within their respective portfolios.

We may participate in future joint ventures to leverage our human and capital resources and pursue additional value-creating projects. We will generally seek partners that provide incremental expertise or, as a result of circumstances, allow us to create more value together than we believe we could create on our own.

Maintain a flexible capital structure to support value creation activities. The capital structure resulting from the Transaction provides us with sufficient financial flexibility and capacity to fund our current capital needs and redevelopment opportunities. We believe we have access to multiple forms of capital, including internally generated cash from operations, that can provide us with additional funding to invest in value-creating projects.

Significant Tenants

Substantially all of the Company s real estate properties are leased to Sears Holdings, and the majority of our rental revenues are derived from the Master Lease.

The Master Lease provides Seritage the right to recapture up to approximately 50% of the space occupied by Sears Holdings at each of the Wholly Owned Properties included in the Master Lease (subject to certain exceptions). In addition, Seritage has the right to recapture any automotive care centers which are freestanding or attached as appendages to the stores, and all outparcels or outlots, as well as certain portions of parking areas and common areas. We also have the right to recapture 100% of the space occupied by Sears Holdings at each of 21 identified Wholly Owned Properties by making a specified lease termination payment to Sears Holdings. While we will be permitted to exercise our recapture rights all at once or in stages as to any particular property, we will not be permitted to recapture all or substantially all of the space subject to the recapture right at more than 50 Wholly Owned Properties during any lease year.

The Master Lease also provides for certain rights to Sears Holdings to terminate the Master Lease with respect to Wholly Owned Properties that cease to be profitable for operation by Sears Holdings. In order to terminate the Master Lease with respect to a certain property, Sears Holdings must make a payment to us of an amount equal to one year of rent (together with taxes and other expenses) with respect to such property. Such termination right, however, will be limited so that it will not have the effect of reducing the fixed rent under the Master Lease by more than 20% per annum. Further, no such termination rights can be exercised prior to August 1, 2016.

A substantial majority of the space at the JV Properties is leased to Sears Holdings under the JV Master Leases which include recapture rights and termination rights with similar terms as the Master Lease.

Sears Holdings is a publicly traded company and is subject to the informational filing requirements of the Securities Exchange Act of 1934, as amended, and is required to file periodic reports on Form 10-K and Form 10-Q with the Securities and Exchange Commission (SEC); refer to www.sec.gov for Sears Holdings Corporation s publicly available financial information. We make no representation as to the accuracy or completeness of the information regarding Sears Holdings that is available through the SEC s website or otherwise made available by Sears Holdings or any third party, and none of such information is incorporated by reference herein.

Competition

We compete for investment opportunities and prospective tenants with other REITs, real estate partnerships or other real estate companies, private individuals, investment companies, private equity and hedge fund investors, sovereign funds, pension funds, insurance companies, lenders and other investors. In addition, revenues from our properties are dependent on the ability of our tenants and operators to compete with other retail operators.

Some of our competitors are significantly larger and have greater financial resources and lower costs of capital than we have. Increased competition will make it more challenging to identify and successfully capitalize on investment opportunities that meet our objectives. Our ability to compete is also impacted by national and local economic trends, availability of investment alternatives, availability and cost of capital, construction and renovation costs, existing laws and regulations, new legislation and population trends.

As a landlord, we compete in the real estate market with numerous developers and owners of properties, including the shopping centers in which our properties are located. Some of our competitors have greater economies of scale, relationships with national tenants at multiple properties which are owned or operated by such competitors, access to more resources and greater name recognition than we do. If our competitors offer space at rental rates below the current market rates or below the rentals we currently charge, or on terms and conditions which include locations at multiple properties, we may lose our existing and/or potential tenants and we may be pressured to reduce our rental rates or to offer substantial rent abatements, tenant improvement allowances, early termination rights or below-market renewal options in order to win new tenants and retain tenants when our leases expire.

Environmental Matters

Our properties are subject to environmental laws regulating, among other things, air emissions, wastewater discharges and the handling and disposal of wastes. Certain of the properties were built during the time that asbestos-containing building materials were routinely installed in residential and commercial structures. In addition, a substantial portion of the properties we acquired from Sears Holdings currently include, or previously included, automotive care center facilities and retail fueling facilities, and are or were subject to laws and regulations governing the handling, storage and disposal of hazardous substances contained in some of the products or materials used or sold in the automotive care center facilities (such as motor oil, fluid in hydraulic lifts, antifreeze and solvents and lubricants), the recycling/disposal of batteries and tires, air emissions, wastewater discharges and waste management. In addition to these products or materials, the equipment in use or previously used at such properties, such as service equipment, car lifts, oil/water separators, and storage tanks, has been subject to increasing environmental regulation relating to, among other things, the storage, handling, use, disposal, and transportation of hazardous materials. The Master Lease obligates Sears Holdings to comply with applicable environmental laws and to indemnify us if their noncompliance results in losses or claims against us, and to remove all automotive care center equipment and facilities upon the expiration or sooner termination of the Master Lease. We expect that any future leases will include similar provisions for other operators of their respective spaces with respect to environmental matters first arising during their occupancy. An operator s failure to comply could result in fines and penalties or the requirement to undertake corrective actions which may result in significant costs to the operator and thus adversely affect their ability to meet their obligations to us.

Pursuant to U.S. federal, state and local environmental laws and regulations, a current or previous owner or operator of real property may be required to investigate, remove and/or remediate a release of hazardous substances or other regulated materials at, or emanating from, such property. Further, under certain circumstances, such owners or operators of real property may be held liable for property damage, personal injury and/or natural resource damage resulting from or arising in connection with such releases. Certain of these laws have been interpreted to be joint and several unless the harm is divisible and there is a reasonable basis for allocation of responsibility. We also may be liable under certain of these laws for damage that occurred prior to our ownership of a property or at a site where we sent wastes for disposal. The failure to properly remediate a property may also adversely affect our ability to lease, sell or rent the property or to borrow funds using the property as collateral.

Under the Master Lease, Sears Holdings is required to indemnify us from certain environmental liabilities at the Wholly Owned Properties before or during the period in which each Wholly Owned Property is leased to Sears Holdings, including removal and remediation of all affected facilities and equipment constituting the automotive care center facilities (and each JV Master Lease includes a similar requirement of Sears Holdings). In addition, pursuant to the terms our debt financing agreements, an escrow account for environment remediation was funded at the closing of the Transaction in the amount of approximately $12.0 million.

In connection with the ownership of our current or past properties and any properties that we may acquire in the future, we could be legally responsible for environmental liabilities or costs relating to a release of hazardous substances or other regulated materials at or emanating from such property. We are not aware of any environmental issues that are expected to have a material impact on the operations of our properties.

Insurance

We have comprehensive liability, property and rental loss insurance with respect to our portfolio of properties. We believe that such insurance provides adequate coverage.

REIT Qualification

We plan to elect to be treated as a REIT for U.S. federal income tax purposes commencing with our initial taxable year ended December 31, 2015 and expect to continue to operate so as to qualify as a REIT. So long as we qualify as a REIT, we generally will not be subject to U.S. federal income tax on net taxable income that we distribute annually to our shareholders. In order to qualify as a REIT for U.S. federal income tax purposes, we must continually satisfy tests concerning, including, but not limited to, the real estate qualification of sources of our income, the composition and values of our assets, the amounts we distribute to our shareholders and the diversity of ownership of our stock. In order to comply with REIT requirements, we may need to forego otherwise attractive opportunities and limit our expansion opportunities and the manner in which we conduct our operations. See Risk Factors Risks Related to Status as a REIT.

Financial Information about Industry Segments

We currently operate in a single reportable segment, which includes the acquisition, ownership, development, redevelopment, management and leasing of retail properties. We review operating and financial information for each property on an individual basis and therefore, each property represents an individual operating segment. We do not distinguish or group our consolidated operations based on geography, size, or type. We aggregate all of our properties into one reportable segment due to their similarities with regard to the nature and economics of the properties, tenants and operational process.

Employees

As of March 4, 2016, we had 21 full-time employees. Our employees are not covered by a collective bargaining agreement, and we consider our employee relations to be satisfactory.

Available Information

Our principal offices are located at 489 Fifth Avenue, New York, New York 10017 and our telephone number is (212) 355-7800. Our website address is www.seritage.com. Our reports electronically filed with or furnished to the SEC pursuant to Section 13(a) or 15(d) of the Securities Exchange Act can be accessed through this site, free of charge, as soon as reasonably practicable after we electronically file or furnish such reports. These filings are also available on the SEC s website at www.sec.gov. Our website also contains copies of our corporate governance guidelines and code of business conduct and ethics as well as the charters of our audit, compensation and nominating and corporate governance committees. The information on our website is not part of this or any other report we file with or furnish to the SEC.

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ITEM 1A. RISK FACTORS

Certain factors may have a material adverse effect on our business, financial condition and results of operations. You should consider carefully the risks and uncertainties described below, in addition to other information contained in this Annual Report, including our consolidated financial statements and related notes. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties that we are unaware of, or that we currently believe are not material, may also become important factors that adversely affect our business. If any of the following risks actually occurs, our business, financial condition, results of operations, and future prospects could be materially and adversely affected. In that event, the trading price of our common shares of beneficial interest could decline, and you could lose part or all of your investment.

Risks Related to Our Business and Operations

We will be substantially dependent on Sears Holdings, as a tenant, until we diversify the tenancy of our portfolio, and an event that has a material adverse effect on Sears Holdings business, financial condition or results of operations could have a material adverse effect on our business, financial condition or results of operations.

Sears Holdings is the lessee of a substantial majority of our properties and accounts for a substantial majority of our revenues. Under the Master Lease, Sears Holdings is required to pay all insurance, taxes, utilities and maintenance and repair expenses in connection with these leased properties and to indemnify, defend and hold us harmless from and against various claims, litigation and liabilities arising in connection with its business, subject to proportionate sharing of certain of these expenses with occupants of the remainder of the space not leased to Sears Holdings. We also rely on Sears Holdings for certain support services, pursuant to a transition services agreement that we have entered into with a subsidiary of Sears Holdings (the Transition Services Agreement). Sears Holdings may not in the future have sufficient assets, income and access to financing to enable it to satisfy its payment obligations under the Master Lease. In addition, Sears Holdings has disclosed that its domestic pension and postretirement benefit plan obligations are currently underfunded. Sears Holdings may have to make significant cash payments to some or all of its pension and postretirement benefit plans, which would reduce the cash available for its businesses, potentially including its rent obligations under the Master Lease. The inability or unwillingness of Sears Holdings to meet its rent obligations and other obligations under the Master Lease could materially adversely affect our business, financial condition or results of operations, including our ability to pay the interest, principal and other costs and expenses under our financings, or to pay dividends to Seritage shareholders as required to maintain our status as a REIT. For these reasons, if Sears Holdings were to experience a material adverse effect on its business, financial condition or results of operations, our business, financial condition or results of operations could also be materially adversely affected.

Our dependence on rental payments from Sears Holdings as our main source of revenues may limit our ability to enforce our rights under the Master Lease. In addition, we may be limited in our ability to enforce our rights under the Master Lease because it is a unitary lease and does not provide for termination with respect to individual properties by reason of the default of the tenant. Failure by Sears Holdings to comply with the terms of the Master Lease or to comply with the regulations to which the leased properties are subject could require us to find another master lessee for all such leased property and there could be a decrease or cessation of rental payments by Sears Holdings. In such event, we may be unable to locate a suitable master lessee or a lessee for individual properties at similar rental rates and other obligations and in a timely manner or at all, which would have the effect of reducing our rental revenues. In addition, each JV is subject to similar limitations on enforcements of remedies and risks under its respective JV Master Lease, which could reduce the value of our investment in, or distributions to us by, one or more of the JVs.

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

A tenant bankruptcy or insolvency could diminish the rental revenue we receive from that property or could force us to take back tenant space as a result of a default or a rejection of the lease by a tenant in bankruptcy. In particular, a bankruptcy or insolvency of Sears Holdings, which is our primary tenant, could result in a loss of a substantial portion of our rental revenue and materially and adversely affect us. Any claims against bankrupt tenants for unpaid future rent would be subject to statutory limitations that would likely result in our receipt of rental revenues that are substantially less than the contractually specified rent we are owed under their leases or no payments at all. In addition, any claim we have for unpaid past rent will likely not be paid in full. If a tenant becomes bankrupt or insolvent, federal law may prohibit us from evicting such tenant based solely upon such bankruptcy or insolvency. We may also be unable to re-lease a terminated or rejected space or re-lease it on comparable or more favorable terms. If we do re-lease rejected space, we may incur costs for brokerage, marketing and tenant expenses.

Sears Holdings leases a substantial majority of our properties. Bankruptcy laws afford certain protections to tenants that may also affect the Master Lease or JV Master Leases. Subject to certain restrictions, a tenant under a master lease generally is required to assume or reject the master lease as a whole, rather than making the decision on a property-by-property basis. This prevents the tenant from assuming only the better performing properties and terminating the master lease with respect to the poorer performing properties. Whether or not a bankruptcy court will require that a master lease be assumed or rejected as a whole depends upon a facts and circumstances analysis considering a number of factors, including the parties intent, the nature and purpose of the relevant documents, whether there was separate and distinct consideration for each property included in the master lease, the provisions contained in the relevant documents and applicable state law. If a bankruptcy court in a Sears Holdings bankruptcy were to allow the Master Lease or a JV Master Lease to be rejected in part, certain underperforming leases related to properties we or the applicable JV as landlord under a JV Master Lease, respectively, own could be rejected by the tenant in bankruptcy while tenant-favorable leases are allowed to remain in place, thereby adversely affecting payments to us derived from the properties. For this and other reasons, a Sears Holdings bankruptcy could materially and adversely affect us.

In addition, although we believe that the Master Lease is a true lease for purposes of bankruptcy law, it is possible that a bankruptcy court could re-characterize the lease transaction set forth in the Master Lease as a secured lending transaction. If the Master Lease were judicially recharacterized as a secured lending transaction, we would not be treated as the owner of the property and could lose certain rights as the owner in the bankruptcy proceeding. In addition, each JV is subject to this risk with respect to its JV Master Lease, which could reduce the value of our investment in, or distribution to us by, one or more of the JVs.

Sears Holdings right to terminate the Master Lease with respect to a portion of our properties could negatively impact our business, results of operations and financial condition.

Under the terms of the Master Lease, in each year after the first lease year, Sears Holdings will have the right to terminate the Master Lease with respect to properties representing up to 20% of the aggregate annual rent payment under the Master Lease with respect to all properties, if, with respect to a property leased under the Master Lease, the EBITDAR for the 12-month period ending as of the most recent fiscal quarter end produced by the Sears Holdings store operated there is less than the rent allocated to such property payable during that year. While Sears Holdings must pay a termination fee equal to one year of rent (together with taxes and other expenses) with respect to such property, the value of some of the properties could be materially adversely affected if we are not able to re-lease such properties at the same rates which Sears Holdings was paying in a timely manner or at all, and this may negatively impact our business, results of operations and financial condition. In addition, Sears Holdings will have the right to terminate a portion of the JV Master Lease with the GGP JV with respect to up to four JV Properties in any lease year, the JV Master Lease with the Simon JV with respect to up to three JV Properties in any lease year and the JV Master Lease with the Macerich JV with respect to up to three JV Properties in any lease year, in each case if, with respect to a JV Property owned by the applicable JV, the same EBITDAR condition is satisfied, which could reduce the value of our investment in, or distributions to us by, one or more of the JVs.

We may not be able to renew leases or re-lease space at our properties, or lease space in newly recaptured properties, and property vacancies could result in significant capital expenditures.

When leases for our properties expire, the premises may not be re-released in a timely manner or at all, or the terms of re-releasing, including the cost of allowances and concessions to tenants, may be less favorable than the current lease terms. The loss of a tenant through lease expiration or other circumstances may require us to spend (in addition to other re-letting expenses) significant amounts of capital to renovate the property before it is suitable for a new tenant and cause us to incur significant costs in the form of ongoing expenses for property maintenance, taxes, insurance and other expenses. Many of the leases we will enter into or acquire may be for properties that are especially suited to the particular business of the tenants operating on those properties. Because these properties have been designed or physically modified for a particular tenant, if the current lease is terminated or not renewed, we may be required to renovate the property at substantial costs, decrease the rent we charge or provide other concessions to re-lease the property. In addition, if we are required or otherwise determine to sell the property, we may have difficulty selling it to a party other than the tenant due to the special purpose for which the property may have been designed or modified. This potential illiquidity may limit our ability to quickly modify our portfolio in response to changes in economic or other conditions, including tenant demand. Also, we may not be able to lease new properties to an appropriate mix of tenants or for rents that are consistent with our expectations. To the extent that our leasing plans are not achieved or we incur significant capital expenditures as a result of property vacancies, our business, results of operations and financial condition could be materially adversely affected.

Real estate investments are relatively illiquid.

Our properties represent a substantial portion of our total consolidated assets, and these investments are relatively illiquid. Significant expenditures associated with each equity investment, such as mortgage payments, real estate taxes, insurance, and repair and maintenance costs, are generally not reduced when circumstances cause a reduction in income from the investment. If income from a property declines while the related expenses do not decline, our income and cash available to us would be adversely affected. If it becomes necessary or desirable for us to dispose of one or more of our mortgaged properties, we might not be able to obtain a release of the lien on the mortgaged property without payment of the associated debt or other costs and expenses. As a result, our ability to sell one or more of our properties or investments in real estate in response to any changes in economic or other conditions may be limited. If we want to sell a property, we may not be able to dispose of it in the desired time period or at a sale price that would exceed the cost of our investment in that property.

The number of potential buyers for certain properties that we may seek to sell may be limited by the presence of such properties in retail or mall complexes owned or managed by other property owners. In addition, our ability to sell or dispose of certain properties may be hindered by the fact that such properties are subject to the Master Lease or a JV Master Lease, as the terms of the Master Lease and the JV Master Leases or the fact that Sears Holdings is the lessee may make such properties less attractive to a potential buyer than alternative properties that may be for sale. Furthermore, if we decide to sell any of our properties, we may provide financing to purchasers and bear the risk that the purchasers may default, which may delay or prevent our use of the proceeds of the sales for other purposes or the distribution of such proceeds to our shareholders.

Both we and our tenants face a wide range of competition that could affect our ability to operate profitably.

The presence of competitive alternatives, both to our properties and the businesses that lease our properties, affects our ability to lease space and the level of rents we can obtain. Our properties operate in locations that compete with other retail properties and also compete with other forms of retailing, such as catalogs and e-commerce websites. Competition may also come from strip centers, outlet centers, lifestyle centers and malls, and both existing and future development projects. New construction, renovations and expansions at competing sites could also negatively affect our properties. In addition, we compete with other retail property companies for tenants and qualified management. These other retail property companies may have relationships with tenants that we do not have since we have a limited operating history, including with respect to national chains that may be desirable tenants. If we are unable to successfully compete, our business, results of operations and financial condition could be materially adversely affected.

In addition, the retail business is highly competitive and if our tenants fail to differentiate their shopping experiences, create an attractive value proposition or execute their business strategies, they may terminate, default on, or fail to renew their leases with us, and our results of operations and financial condition could be materially adversely affected. Furthermore, we believe that the increase in digital and mobile technology usage has increased the speed of the transition from shopping at physical locations to web-based purchases and that our tenants, including Sears Holdings, may be negatively affected by these changing consumer spending habits. If our tenants are unsuccessful in adapting their businesses, and, as a result terminate, default on, or fail to renew their leases with us, our results of operations and financial condition could be materially adversely affected.

Our pursuit of investments in and redevelopment of properties, and investments in and acquisitions or development of additional properties, may be unsuccessful or fail to meet our expectations.

We intend to grow our business through investments in, and acquisitions or development of, properties, including through the recapture and redevelopment of space at many of our properties. However, our industry is highly competitive, and we face competition from other REITs, investment companies, private equity and hedge fund investors, sovereign funds, lenders, and other investors, some of whom are significantly larger and have greater resources and lower costs of capital. This competition will make it more challenging to identify and successfully capitalize on acquisition and development opportunities that meet our investment objectives. If we are unable to finance acquisitions or other development opportunities on commercially favorable terms, our business, financial condition or results of operations could be materially adversely affected. Additionally, the fact that we must distribute 90% of our net taxable income in order to maintain our qualification as a REIT may limit our ability to rely upon rental payments from leased properties or subsequently acquired properties in order to finance acquisitions. As a result, if debt or equity financing is not available on acceptable terms, further acquisitions or other development opportunities might be limited or curtailed.

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Investments in, and acquisitions of, properties we might seek to acquire entail risks associated with real estate investments generally, including (but not limited to) the following risks and as noted elsewhere in this section:

- we may be unable to acquire a desired property because of competition;
- even if we are able to acquire a desired property, competition from other potential acquirers may significantly increase the purchase price;
- even if we enter into agreements for the acquisition of properties, these agreements are subject to customary conditions to closing, including completion of due diligence investigations to our satisfaction;
- we may incur significant costs and divert management attention in connection with evaluation and negotiation of potential acquisitions, including ones that we are subsequently unable to complete;
- we may acquire properties that are not initially accretive to our results upon acquisition, and we may not successfully manage and lease those properties to meet our expectations;
- we may be unable to finance the acquisition on favorable terms in the time period we desire, or at all;
- even if we are able to finance the acquisition, our cash flow may be insufficient to meet our required principal and interest payments;
- we may spend more than budgeted to make necessary improvements or renovations to acquired properties;
- we may be unable to quickly and efficiently integrate new acquisitions, particularly the acquisition of portfolios of properties, into our existing operations;
- market conditions may result in higher than expected vacancy rates and lower than expected rental rates; and
- we may acquire properties subject to liabilities and without any recourse, or with only limited recourse, with respect to unknown liabilities.

In addition, we intend to redevelop a significant portion of the properties purchased from Sears Holdings in order to make space available for lease to additional retail tenants and potentially other third-party lessees for other uses. The redevelopment of these properties involves the risks associated with real estate development activities generally. Our redevelopment strategies also involve additional risks, including that Sears Holdings may terminate or fail to renew leases with us for the applicable portion of the redeveloped space as a result of our redevelopment activities. If we are unable to successfully redevelop properties or to lease the redeveloped properties to third parties on acceptable terms, our business, results of operations and financial condition could be materially adversely affected.

Current and future redevelopment may not yield expected returns.

We expect to undertake redevelopment, expansion and reinvestment projects involving our properties as part of our long-term strategy. Likewise, each JV expects to undertake redevelopment, expansion and reinvestment projects involving its JV Properties, with respect to which we may be required to make additional capital contributions to the applicable JV under certain circumstances. These projects are subject to a number of risks, including (but not limited to):

- abandonment of redevelopment activities after expending resources to determine feasibility;
- loss of rental income, as well as payments of maintenance, repair, real estate taxes and other charges, from Sears Holdings related to space that is recaptured pursuant to the Master Lease (or the JV Master Leases) and which may not be re-leased to third parties;
- restrictions or obligations imposed pursuant to other agreements;
- construction and/or lease-up costs (including tenant improvements or allowances) and delays and cost overruns, including construction costs that exceed original estimates;
- failure to achieve expected occupancy and/or rent levels within the projected time frame or at all;

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- inability to operate successfully in new markets where new properties are located;
- inability to successfully integrate new or redeveloped properties into existing operations;
- difficulty obtaining financing on acceptable terms or paying operating expenses and debt service costs associated with redevelopment properties prior to sufficient occupancy and commencement of rental obligations under new leases;
- changes in zoning, building and land use laws, and conditions, restrictions or limitations of, and delays or failures to obtain, necessary zoning, building, occupancy, land use and other governmental permits;
- changes in local real estate market conditions, including an oversupply of, or a reduction in demand for, retail space or retail goods, and the availability and creditworthiness of current and prospective tenants;
- negative perceptions by retailers or shoppers of the safety, convenience and attractiveness of the property;
- exposure to fluctuations in the general economy due to the significant time lag between commencement and completion of redevelopment projects; and
- vacancies or ability to rent space on favorable terms, including possible market pressures to offer tenants rent abatements, tenant improvements, early termination rights or below-market renewal options.

If any of these events occur at any time during the process with respect to any project, overall project costs may significantly exceed initial cost estimates, which could result in reduced returns or losses from such investments. In addition, we may not have sufficient liquidity to fund such projects, and delays in the completion of a redevelopment project may provide various tenants the right to withdraw from a property.

Rising expenses could reduce cash flow and funds available for future development.

If any property is not fully occupied or becomes vacant in whole or in part, or if rents are being paid in an amount that is insufficient to cover operating costs and expenses, we could be required to expend funds with respect to that property for operating expenses. Our properties are subject to increases in tax rates and tax assessments, utility costs, insurance costs, repairs, maintenance and administrative expenses, and other operating expenses. We may also incur significant expenditures as a result of deferred maintenance for the properties we have already acquired (subject to reserved funds to cover certain of these costs) and other properties we may acquire in the future. While properties under the Master Lease and the JV Master Leases are generally leased on a triple-net basis (subject to proportionate sharing of operating expenses with respect to space not leased by Sears Holdings), renewals of leases or future leases may not be negotiated on that basis, in which event we may have to pay those costs. If we are unable to lease properties on a triple-net-lease basis or on a basis requiring the tenants to pay all or some of such expenses, or if tenants fail to pay required tax, utility and other impositions and other operating expenses, we could be required to pay those costs which could adversely affect funds available for future development or cash available for distributions.

Real estate related taxes may increase, and if these increases are not passed on to tenants, our income will be reduced.

Some local real property tax assessors may seek to reassess some of our properties as a result of our acquisitions of properties. Generally, from time to time, our property taxes increase as property values or assessment rates change or for other reasons deemed relevant by the assessors. An increase in the assessed valuation of a property for real estate tax purposes will result in an increase in the related real estate taxes on that property. Although the Master Lease and some third-party tenant leases may permit us to pass through such tax increases to the tenants for payment, there is no assurance that renewal leases or future leases will be negotiated on the same basis. Increases not passed through to tenants will reduce our income and the cash available for distributions to our shareholders.

Changes in building and/or zoning laws may require us to update a property in the event of recapture or prevent us from fully restoring a property in the event of a substantial casualty loss and/or require us to meet additional or more stringent construction requirements.

Due to changes, among other things, in applicable building and zoning laws, ordinances and codes that may affect certain of our properties that have come into effect after the initial construction of the properties, certain properties may not comply fully with current building and/or zoning laws, including electrical, fire, health and safety codes and regulations, use, lot coverage, parking and setback requirements, but may qualify as permitted non-conforming uses. Such changes in building and zoning laws may require updating various existing physical conditions of buildings in connection with our recapture, renovation, and/or redevelopment of properties. In addition, such changes in building and zoning laws may limit our or our tenants ability to restore the premises of a property to its previous condition in the event of a substantial casualty loss with respect to the property or the ability to refurbish, expand or renovate such property to remain compliant, or increase the cost of construction in order to comply with changes in building or zoning codes and regulations. If we are unable to restore a property to its prior use after a substantial casualty loss or are required to comply with more stringent building or zoning codes and regulations, we may be unable to re-lease the space at a comparable effective rent or sell the property at an acceptable price, which may materially and adversely affect us.

Our real estate assets may be subject to impairment charges.

On a periodic basis, we must assess whether there are any indicators that the value of our real estate assets and other investments may be impaired. If an impairment indicator is identified, a property s value is considered to be impaired only if management s estimate of current and projected operating cash flows (undiscounted and unlevered), taking into account the anticipated and probability weighted holdings periods, are less than the carrying value of the property. In our estimate of cash flows model, we consider factors such as expected future operating income, trends and prospects, the effects of demand, competition and other factors. If we are evaluating the potential sale of an asset or development alternatives, the undiscounted future cash flows considers the most likely course of action at the balance sheet date based on current plans, intended holding periods and available market information. We are required to make subjective assessments as to whether there are impairments in the value of our real estate assets and other investments. These assessments may have a direct impact on our earnings because recording an impairment charge results in an immediate negative adjustment to earnings. We may take impairment charges in the future related to the impairment of our assets, and any future impairment could have a material adverse effect on our results of operations in the period in which the impairment charge is taken.

Properties in our portfolio may be subject to ground leases; if we are found to be in breach of these ground leases or are unable to renew them, we could be materially and adversely affected.

We currently have one property in our portfolio that is on land subject to a ground lease. Accordingly, we only own a long-term leasehold in the land underlying this property, and we own the improvements thereon only during the term of the ground lease. In the future, our portfolio may include additional properties subject to ground leases or similar interests. If we are found to be in breach of a ground lease, we could lose the right to use the property and could also be liable to the ground lessor for damages. In addition, unless we can purchase a fee interest in the underlying land or extend the terms of these leases before their expiration, which we may be unable to do, we will lose our right to operate these properties and our interest in the improvements upon expiration of the leases. Our ability to exercise options to extend the term of our ground lease is subject to the condition that we are not in default under the terms of the ground lease at the time that we exercise such options, and we may not be able to exercise our options at such time. In addition, three JV Properties are currently ground leased or leased and, therefore, subject to similar risks. Furthermore, we may not be able to renew our ground lease or future ground leases upon their expiration (after the exercise of all renewal options). If we were to lose the right to use a property due to a breach or non-renewal or final expiration of the ground lease, we would be unable to derive income from such property, which could materially and adversely affect our business, financial conditions or results of operations.

Certain properties within our portfolio are subject to restrictions pursuant to reciprocal easement agreements, operating agreements, or similar agreements, some of which contain a purchase option or right of first refusal or right of first offer in favor of a third party.

Many of the properties in our portfolio are, and properties that we acquire in the future may be, subject to use restrictions and/or operational requirements imposed pursuant to ground leases, restrictive covenants or conditions, reciprocal easement agreements or operating agreements (collectively, Property Restrictions) that could adversely affect our ability to redevelop the properties or lease space to third parties. Such Property Restrictions could include, for example, limitations on alterations, changes, expansions, or reconfiguration of properties; limitations on use of properties, including for retail uses only; limitations affecting parking requirements; restrictions on exterior or interior signage or facades; or access to an adjoining mall, among other things. In certain cases, consent of the other party or parties to such agreements may be required when altering, reconfiguring, expanding, redeveloping or re-leasing properties. Failure to secure such consents when necessary may harm our ability to execute leasing, redevelopment or expansion strategies, which could adversely affect our business, financial condition or results of operations. In certain cases, a third party may have a purchase option or right of first refusal or right of first offer that is activated by a sale or transfer of the property, or a change in use or operations, including a closing of the Sears Holdings operation or cessation of business operations, on the encumbered property.

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Economic conditions may affect the cost of borrowing, which could materially adversely affect our business.

Our business is affected by a number of factors that are largely beyond our control but may nevertheless have a significant negative impact on us. These factors include, but are not limited to:

- interest rates and credit spreads;
- the availability of credit, including the price, terms and conditions under which it can be obtained;
- a decrease in consumer spending or sentiment, including as a result of increases in savings rates and tax increases, and any effect that this may have on retail activity;
- the actual and perceived state of the real estate market, market for dividend-paying stocks and public capital markets in general; and
- unemployment rates, both nationwide and within the primary markets in which we operate.

In addition, economic conditions such as inflation or deflation could materially adversely affect our business, financial condition and results of operations. Deflation may have an impact on our ability to repay our debt. Deflation may delay consumption and thus weaken tenant sales, which may reduce our tenants ability to pay rents. Deflationary pressure on retailers may diminish their ability to rent our space and decrease our ability to re-lease the space on favorable terms to us. In an inflationary economic environment, increased inflation may have a pronounced negative impact on the interest expense we pay in connection with our indebtedness and our general and administrative expenses, as these costs could increase at a rate higher than rents we collect. Also, inflation may adversely affect tenant leases with stated rent increases, which could be lower than the increase in inflation at any given time. Inflation could also have an adverse effect on consumer spending, which could impact our tenants sales and, in turn, our own results of operations. Restricted lending practices may impact our ability to obtain financing for our properties and may also negatively impact our tenants ability to obtain credit. Decreases in consumer demand can have a direct impact on our tenants and the rents we receive.

Compliance with the Americans with Disabilities Act may require us to make expenditures that adversely affect our cash flows.

The Americans with Disabilities Act (the ADA) has separate compliance requirements for public accommodations and commercial facilities, but generally requires that buildings be made accessible to people with disabilities. Compliance with the ADA requirements could require removal of access barriers, and non-compliance could result in imposition of fines by the United States government or an award of damages to private litigants, or both. While the tenants to whom our properties are leased are generally obligated by law or lease to comply with the ADA provisions applicable to the property being leased to them, if required changes involve other property not being leased to such tenants, if the required changes include greater expenditures than anticipated, or if the changes must be made on a more accelerated basis than anticipated, the ability of these tenants to cover costs could be adversely affected. Moreover, certain third-party leases may require the landlord to comply with the ADA with respect to the building as a whole and/or the tenant s space. As a result of any of the foregoing circumstances, we could be required to expend funds to comply with the provisions of the ADA, which could adversely affect our results of operations and financial condition.

Environmental, health, safety and land use laws and regulations may limit or restrict some of our operations.

As the owner or operator of various real properties and facilities, we must comply with various federal, state and local environmental, health, safety and land use laws and regulations. We and our properties are subject to such laws and regulations relating to the use, storage, disposal, emission and release of hazardous and non-hazardous substances and employee health and safety, as well as zoning restrictions. Historically, Sears Holdings has not incurred significant expenditures to comply with these laws with respect to the substantial majority of the space at the properties. However, a substantial portion of our properties that have resulted in certain remediation activities currently include, or previously included, automotive care center facilities and retail fueling facilities, and/or above-ground or underground storage tanks, and are or were subject to laws and regulations governing the handling, storage and disposal of hazardous substances contained in some of the products or materials used or sold in the automotive care center facilities (such as gasoline, motor oil, fluid in hydraulic lifts, antifreeze, solvents and lubricants), the recycling/disposal of batteries and tires, air emissions, wastewater discharges and waste management. In addition to these products, the equipment in use or previously used at such properties, such as service equipment, car lifts, oil/water separators, and storage tanks, has been subject to increasing environmental regulation relating to, among other things, the storage, handling, use, disposal and transportation of hazardous materials. There are also federal, state and local laws, regulations and ordinances that govern the use, removal and/or replacement of underground storage tanks in the event of a release on, or an upgrade or redevelopment of, certain properties. Such laws, as well as common-law standards, may impose liability for any releases of hazardous substances associated with the underground storage tanks and may provide for third parties to seek recovery from owners or operators of such properties for damages associated with such releases. If hazardous substances are released from any underground storage tanks on any of our properties, we may be materially and adversely affected. In a few states, transfers of some types of sites are conditioned upon clean-up of contamination prior to transfer. If any of our properties are subject to such contamination, we may be subject to substantial clean-up costs before we are able to sell or otherwise transfer the property.

Under the Master Lease, Sears Holdings is required to indemnify us from certain environmental liabilities at the properties purchased from Sears Holdings before or during the period in which each property is leased to Sears Holdings, including removal and remediation of all affected facilities and equipment constituting the automotive care center facilities (and each JV Master Lease includes a similar requirement of Sears Holdings). Although existing and future third-party leases are expected to require tenants generally to indemnify us for such tenants non-compliance with environmental laws as a result of their occupancy, such tenants typically will not be required to indemnify us for environmental non-compliance arising prior to their occupancy. In such cases, we may incur costs and expenses under such leases or as a matter of law. The amount of any environmental liabilities could exceed the amounts for which Sears Holdings or other third parties are required to indemnify us (or the applicable JV) or their financial ability to do so. In addition, under the terms of the agreements governing our indebtedness, we have deposited funds in a reserve account that will be used to fund costs incurred in correcting certain environmental and other conditions. The amount of such funds may not be sufficient to correct the environmental and other conditions to which they are expected to be applied.

In addition, additional laws which may be passed in the future, or a finding of a violation of or liability under existing laws, could require us and/or one or more of the JVs to make significant expenditures and otherwise limit or restrict some of our or its or their operations, which could have an adverse effect on our business, financial condition and results of operations.

Environmental compliance costs and liabilities associated with real estate properties owned by us may materially and adversely affect us.

Our properties may be subject to known and unknown environmental liabilities under various federal, state and local laws and regulations relating to human health and the environment. Certain of these laws and regulations may impose joint and several liability on certain statutory classes of persons, including owners or operators, for the costs of investigation or remediation of contaminated properties. These laws and regulations apply to past and present business operations on the properties, and the use, storage, handling and recycling or disposal of hazardous substances or wastes. We may face liability regardless of our knowledge of the contamination, the timing of the contamination, the cause of the contamination or the party responsible for the contamination of the property.

We may be held primarily or jointly and severally liable for costs relating to the investigation and clean-up of any of our properties from which there has been a release or threatened release of a regulated material as well as other affected properties, regardless of whether we knew of or caused the release.

As the owner or operator of real property, we may also incur liability based on various building conditions. For example, buildings and other structures on properties that we currently own or operate or those we acquire or operate in the future contain, may contain, or may have contained, asbestos-containing material (or ACM). Environmental, health and safety laws require that ACM be properly managed and maintained and may impose fines or penalties on owners, operators or employers for non-compliance with those requirements. These requirements include special precautions, such as removal, abatement or air monitoring, if ACM would be disturbed during maintenance, renovation or demolition of a building, potentially resulting in substantial costs. In addition, we may be subject to liability for personal injury or property damage sustained as a result of exposure to ACM or releases of ACM into the environment. In addition, the presence of significant mold or other airborne contaminants at any of our properties could require us to undertake a costly remediation program to contain or remove the mold