



**Aloft**  
A DIVISION OF W HOTELS



**CONDOR**

HOSPITALITY TRUST

2016 ANNUAL REPORT



## CONDOR HOSPITALITY TRUST

Condor Hospitality Trust, Inc. (NASDAQ: CDOR), is a self-administered real estate investment trust that specializes in the investment and ownership of upper midscale and upscale, premium-branded select-service, extended stay, and limited-service hotels. The Company currently owns 19 hotels in 10 states, including nine high-quality select-service hotels that represent the new strategic direction of the portfolio. The Company's hotels are franchised under premium brands such as Hilton, Marriott, IHG, Choice and Wyndham, and operated by third party management companies.



## TO OUR SHAREHOLDERS:

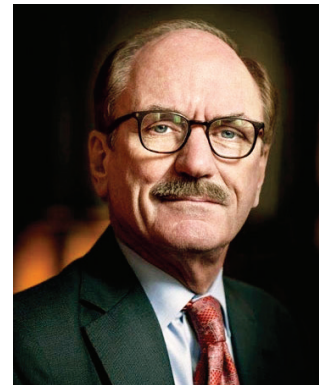
Condor has completed a remarkable year in 2016 as the transformation plan for the Company, that began under my leadership in March 2015, accelerated and was then substantially completed subsequent to year end with the closing of several significant transactions. During the first quarter of 2016, we closed a \$30 million private placement creating a new class of mandatorily convertible preferred stock, Series D, and utilized a significant portion of the net proceeds to redeem at par all of the outstanding Series A and Series B preferred stock, including all of the accrued unpaid preferred dividends since 2012, and to fully pay the accrued and unpaid dividends on the Series C preferred stock. Simultaneous with the closing of the private placement, the Series C preferred stock converted into the newly created mandatorily convertible Series D preferred shares. These actions left Condor with just one class of preferred stock that would mandatorily convert to our common stock upon the occurrence of a subsequent qualified equity offering of at least \$50 million. Additionally, these actions resulted in the payment of all arrears dividends. Importantly, this then allowed the Company to commence paying dividends on our common stock, which we declared for the second quarter in 2016 after they had been suspended for over seven years. All of the aforementioned successes set the stage for the future conversion of over \$60 million of the Series D preferred stock into our common stock, thereby dramatically increasing the market capitalization of Condor.

During the year, we moved forward two initiatives that are extremely important to the future of Condor: (i) the disposition of legacy hotels from the former investment strategy of the Company in order to recycle the sales proceeds into hotels that are consistent with our new investment strategy, and (ii) the identifying and acquiring of high-quality select-service hotels that are consistent with our new investment strategy. Our objective was to maximize sale proceeds from the dispositions and, when sufficient proceeds were then available, reinvest the sales

proceeds into the new investment strategy hotels. This was a difficult balancing act but we were successful and accomplished a dramatic transformation of the portfolio. Specifically, we closed on the sale of 25 Legacy Hotels during 2016, ending the year with just 13 legacy hotels, allowing us to close on the \$66 million acquisition of two hotels in the third and fourth

quarters and sign a purchase contract to acquire for approximately \$74 million four additional hotels, three of which we closed subsequent to year end. Not only was it significant that we closed or placed under contract for almost \$185 million nine high quality hotels consistent with our new investment strategy without raising additional equity capital, but also importantly, the Company on a prospective basis is now generating a majority of its revenues and EBITDA from the new investment strategy hotels. The result is that the market now views Condor as a transformed lodging REIT. It is extremely noteworthy to mention that the 7.6% REVPAR growth in 2016 achieved by our new investment strategy hotels was more than double what the industry as a whole achieved for the same period. We have plans to sell seven additional legacy hotels during 2017, three of which have already closed. We expect to end the year with just six of the legacy hotels. These 6 legacy hotels are being held to once again maximize the sales proceeds given recent disruptions from renovations and market conditions.

The financial condition and balance sheet of the Company continued to strengthen during the year. We finished 2016 with more than \$8 million of cash, after the closing of an acquisition of one hotel in early December, and before taking into consideration



J. William Blackham  
President and Chief Executive Officer





over \$5 million in reserves and restricted cash, a significant portion of which became unrestricted with transactions completed subsequent to year end. We signed a loan commitment led by KeyBanc Capital Markets Inc. and The Huntington National Bank for a \$90 million secured line of credit facility that included an expansion feature of up to \$400 million. We closed this loan facility in the first quarter of 2017, and, as a result, the Company has no loan maturities in 2017 and will enjoy a lower weighted average interest cost projected to be below 5% for the upcoming year. A significant portion of the warrants that existed previously were exchanged in January 2017 giving rise to less volatility of our earnings in the future due to the elimination of the volatility caused by derivative based accounting procedures.

We prepared the Company to be ready to launch an equity offering as soon as market conditions appeared to provide the greatest probability of success. Subsequent to the end of the year, we engaged KeyBanc to partner with the Company to complete a \$50 million equity offering. Prior to launching the offering, we completed the voluntary conversion of the Series D preferred stock to common stock, and announced a 6.5 to 1 reverse stock split. We believe the resulting double-digit share price enabled the Company to access a wider investor base. We completed the equity offering in the amount of \$50.1 million on March 29, 2017. With these actions the equity market capitalization of the Company now exceeds \$100 million. Subject to successful syndication, the limit on the line of credit is expected to increase to \$150 million thereby giving Condor in excess of \$100 million of additional acquisition capability, when coupled with an appropriate cash equity component. The debt and equity structure of the Company is now well positioned to enable us to acquire new investment strategy hotels in our pursuit of growing the Company with the goal of increasing shareholder value.

While I believe that it is not particularly useful to focus in detail on 2016 operating results for the hotel portfolio, since: (i) the majority of our 2016 revenues and earnings were still generated from legacy hotels, (ii) two new investment strategy hotels were acquired during the second half of 2016, and (iii) 25

legacy hotels were sold; it is important to note that the three new investment strategy hotels that we acquired in the fourth quarter of 2015, and thus owned for the entire year 2016, had operating results that exceeded our underwriting for those hotels at the time we were evaluating the acquisition of the hotels. In fact, the EBITDA yield in 2016 exceeded 10% on our total purchase price, a very attractive result for the Company.

Looking back at 2016, I am extremely pleased with what has been accomplished. Subsequent to year end we completed several remaining transactions that were initiated in 2016 that fully position the Company to now move forward with growth through accretive acquisitions. We will remain highly disciplined in evaluating prospective acquisition hotels and will only elect to proceed with acquisitions that meet our age, quality, markets, and brand criteria. We are unique compared to our public peer group and projections from industry analysts would support our expectation that our target markets should outperform the industry in the upcoming year. Our team is very capable and can accommodate the expected growth without the need to expand in the near term. Importantly, we now have access to capital when it is beneficial and advisable to gain access, and the Company has become very respected in the marketplace and, as a result, has advantages in the acquisition of new hotels.

It has been a pleasure to lead this transformative process for the benefit of all shareholders and a pleasure to further align myself with our shareholders with my purchase of additional common stock in our recent public offering, a \$750,000 increase in my share holdings. I wish to thank each of you for your confidence in the Condor team and for allowing me the privilege and pleasure to lead this Company.

J. William Blackham  
President & C.E.O.

## OUR MISSION

**Provide to our shareholders attractive total returns for the lodging sector, through disciplined investment in high-quality select-service, limited-service, extended stay and compact full-service hotels, and intensive asset management to achieve enhanced results.**



CONDOR HOSPITALITY TRUST

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## OUR BUSINESS AND PROPERTIES

References to “we,” “our,” “us,” and the “Company” refer to Condor Hospitality Trust, Inc., including, as the context requires, its direct and indirect subsidiaries. On March 15, 2017, we effected a 1-for-6.5 reverse stock split of our common stock. Except where otherwise indicated, all share and per share data in this Annual Report reflect this reverse stock split. This 2016 Annual Report does not reflect events occurring after December 31, 2016, except as specifically referenced herein.

### Forward-Looking Statements

Certain information included in this Annual Report may contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and as such may involve known and unknown risks, uncertainties, and other factors which may cause our actual results, performance, or achievements to be materially different from future results, performance, or achievements expressed or implied by such forward-looking statements. These forward-looking statements are based on assumptions that management has made in light of experience in the business in which we operate, as well as management’s perceptions of historical trends, current conditions, expected future developments, and other factors believed to be appropriate under the circumstances. These statements are not guarantees of performance or results. They involve risks, uncertainties (some of which are beyond our control), and assumptions. Management believes that these forward-looking statements are based on reasonable assumptions.

Forward-looking statements, which are based on certain assumptions and describe our future plans, strategies, and expectations are generally identifiable by use of the words “may,” “will,” “should,” “expect,” “anticipate,” “estimate,” “believe,” “intend,” or “project” or the negative thereof or other variations thereon or comparable terminology. Factors which could have a material adverse effect on our operations and future prospects include, but are not limited to, changes in economic conditions generally and the real estate market specifically, legislative/regulatory changes (including changes to laws governing the taxation of real estate investment trusts), availability of capital, risks associated with debt financing, interest rates, competition, supply and demand for hotel rooms in our current and proposed market areas, policies and guidelines applicable to real estate investment trusts, and other risks and uncertainties described in our filings with the Securities and Exchange Commission (“SEC”) from time to time. These risks and uncertainties should be considered in evaluating any forward-looking statements contained herein. We caution readers not to place undue reliance on any forward-looking statements included in this report which speak only as of the date of this Annual Report.

### Overview

The Company, which until July 15, 2015 was formerly named Supertel Hospitality, Inc., was incorporated in Virginia on August 23, 1994 and was reincorporated in Maryland on November 19, 2014. Our common stock began to trade on the Nasdaq Stock Market on October 30, 1996 and trades under the symbol “CDOR”. Our principal executive offices are located at 4800 Montgomery Lane, Suite 200, Bethesda, MD 20814 and we also maintain offices in Omaha, NE and Norfolk, NE.

The Company is a self-administered hotel investment company that specializes in the investment and ownership of premium-branded upper mid-scale and upscale select-service hotels. As of December 31, 2016, the Company owns 19 hotels in 12 states including one hotel owned through an 80% interest in a joint venture. The Company is organized and conducts its operations to qualify as a REIT for federal income tax purposes.

We conduct our business through a traditional UPREIT structure, in which our hotel properties are owned by our operating partnership, Condor Hospitality Limited Partnership (formerly named Supertel Limited Partnership) and its subsidiaries, for which we serve as general partner. As of December 31, 2016, we owned an approximate 97.8% ownership interest in Condor Hospitality Limited Partnership. In the future, Condor Hospitality Limited Partnership may issue limited partnership interests to third parties from time to time in connection with our acquisition of hotel properties or the raising of capital.

In order for the income from our hotel property investments to constitute “rents from real properties” for purposes of the gross income tests required for REIT qualification, the income we earn cannot be derived from the operation of any of our hotels. Therefore, Condor Hospitality Limited Partnership and its subsidiaries lease our hotel properties to our wholly-owned taxable REIT subsidiary, TRS Leasing, Inc., or TRS, or one of its wholly-owned subsidiaries. We refer to our TRS and its wholly-owned subsidiaries as our TRS Lessee. The TRS Lessee in turn engages third-party eligible independent contractors to manage the hotels. Condor Hospitality Limited Partnership, and our TRS and their respective subsidiaries are consolidated into the Company’s financial statements.

We are engaged primarily in the business of owning equity interests in hotel properties and therefore our business is disclosed as one reportable segment. See the consolidated financial statements and notes thereto included in this Annual Report for certain financial information.

## **Core Strategies**

### *Acquisition Strategy*

The objective of our acquisition strategy is to enable us to acquire assets that meet our target property characteristics and investment criteria at attractive valuations. We believe that our existing relationships with owners, operators, and developers of premium-branded upper-midscale and upscale select-service hotels will provide us with access to certain off-market acquisition opportunities before they become known to other real estate investors. We believe, off-market transactions lead to more attractive valuation outcomes. Our organizational documents do not limit the types of investments we can make; however, our intent is to execute the acquisition strategy as detailed herein.

We believe our target property characteristics and investment criteria, coupled with our ability to source off-market transactions, differentiates us from our peers and will enable us to achieve our mission of attractive returns to our shareholders.

### *Target Property Characteristics*

Our target properties are premium-branded upper-midscale and upscale select-service hotels located in the top 100 metropolitan statistical areas, or MSAs, with a primary focus on major secondary markets ranked 21 through 60. A typical acquisition hotel will have 80 to 150 rooms and will have been constructed within the last 10 years or significantly renovated since 2012. Hotels subject to ground leases, exterior corridor properties, and hotels in single demand generator markets generally will not be considered. Portfolio transactions generally will only be considered if all of the hotels in the portfolio meet our investment criteria.

### *Investment Criteria*

We perform thorough due diligence and utilize extensive research to evaluate any target market or property. This due diligence and research may include, but is not limited to, analyzing the long-term economic outlook of an MSA, reviewing trends in local lodging demand and supply, assessing property condition and required capital investment, and understanding historical property financial performance. Specific investment criteria for hotels we are looking to acquire may include but are not limited to hotels that:

- operate under leading premium franchise brands and possess key attributes such as building design and décor that is consistent with current generation brand standards;
- are located within the top 100 MSAs, with a primary focus on major secondary markets ranked 21 through 60 in close proximity to multiple demand drivers, including large corporations, regional hospitals, regional business hubs, recreational travel destinations, significant retail centers, and military installations, among others;
- are located within markets that have favorable economic, job growth, and demographic factors;



- have illustrated an ability to generate stabilized and dependable revenue and net operating income;
- were constructed or underwent major renovations less than ten years prior to our acquisition and have significant time (generally ten or more years) remaining on the existing franchise license;
- have some value-added growth potential through operating efficiencies, institutional asset management, repositioning, renovations, or rebranding;
- can be acquired at a discount to replacement cost; and/or
- can be acquired in off-market transactions.

### ***Disposition Strategy***

Currently, we are nearing completion of a nine year process of transitioning our portfolio from economy hotels to premium-branded upper-midscale and upscale select-service hotels. In order to achieve this objective, we have focused on disposing the portion of our portfolio that do not meet the property characteristics and investment criteria of our current business strategy. From January 1, 2009 to December 31, 2016, we have sold 110 midscale and economy hotels that no longer fit our investment strategy for combined sales prices of approximately \$226.5 million. The capital unlocked from asset sales has been and will continue to be redeployed into newer, higher-quality assets meeting the acquisition strategy discussed above. Just as we carefully evaluate the hotels we plan to acquire, our asset management team has evaluated the timing and composition of the portfolio of hotels we intend to sell. We are committed to a disciplined but timely monetization of our portfolio of hotels held for sale in order to achieve the strategic repositioning of the portfolio. In 2017, we will continue to dispose of assets that do not fit the new strategic vision of our portfolio with the goal of ending the first half of 2017 having substantially disposed of all our retained portfolio of hotels held for sale.

Additionally, from time to time, we may undertake the sale of one or more hotels that meet the property characteristics and investment criteria discussed above. These disposition decisions will be the result of a thorough analysis and typically in response to changes in market conditions, our current or projected return on our investment in the hotel, or other factors which we deem relevant to the disposition decision.

### ***Asset Management Strategy***

In order to qualify as a REIT under the Code, we cannot operate our hotels. Therefore, we lease our hotels to taxable REIT subsidiaries, which in turn engage independent hotel management companies to manage and operate the hotels. Our independent management companies are not affiliated with us or our management. See “Hotel Management Company Partners” below.

Through collaboration with our independent management companies, we seek to maximize value to our shareholders through improvements to our existing hotels’ operating results. We achieve this result by constantly monitoring the performance of each individual hotel and identifying opportunities for value-enhancement through intensive asset management strategies. We will make recommendations to our independent management companies in all aspects of our hotels operations, including revenue management, physical design, guest experience, market positioning, and overall property strategy. Fundamentally, all strategies are focused on growing the revenue of a hotel, controlling expenses, and maximizing the guest experience to drive returns.

We work with our independent management companies to develop short- and long-term capital investment plans that are focused on generating positive returns for our shareholders. The capital improvements may involve investments in expansions, additions, renovations, technology upgrades, and energy efficiency improvements.

Additionally, from time to time, we may come to the conclusion that a particular property may provide greater returns to our shareholders after an extensive repositioning of the property in the market. In these instances, capital investment in a greater amount than typical for a property may be required to achieve the

desired repositioning. These decisions are made after a thorough analysis of the property, market conditions, and the potential for a positive return on investment that exceeds our investment hurdle rates.

### ***Financing Strategy***

Our financing strategy is to minimize the cost of our capital in order to maximize the returns generated for our shareholders. We intend to finance our long-term growth with common and preferred equity issuances and debt financings that have staggered maturities. We intend to adhere to our long-term strategy to maintain our total net debt to total hotel investment to less than 40%. Recently, we entered into a new \$90.0 million secured revolving credit facility recourse line of credit secured by a first mortgage on certain hotels. Historically, we have obtained mortgage loans secured by first liens on the mortgaged property.

Since we are structured as an UPREIT, when acquiring hotel assets, we may seek to issue operating common units as full or partial consideration to sellers who may desire to take advantage of tax deferral on the sale of a hotel or participate in the income, and potential value appreciation, of our common stock.

### **Business Partners**

#### ***Franchise Partners***

We believe that in order to achieve our mission we must partner with the right franchisors of quality brands in our target segments. To this end, we have built strong relationships with many of the leading franchisors of the strongest brands in the segments we target, including Hilton, Marriott/Starwood, IHG, Choice, and Hyatt. The franchisors provide a variety of benefits and value which include national advertising, marketing programs to increase brand awareness, personnel training, and centralized reservation systems. We are constantly monitoring and evaluating the performance of these franchisors and their respective brands so that, when necessary, we can adapt our franchise partner strategy to maximize returns to our shareholders.

Under our franchise agreements, we are required to pay franchise fees generally between 3.3% and 5.5% of room revenue, plus additional fees for marketing, central reservation systems, and other franchisor programs and services that amount to between 2.5% and 6.0% of room revenue. The franchise agreements typically have 10 to 25 year terms although certain agreements may be terminated by either party on certain anniversary dates specified in the agreements. Further, each agreement provides for early termination fees in the event the agreement is terminated before the stated term.

Our 19 hotels owned at December 31, 2016 operate under the following national and independent brands. Pursuant to our previously discussed strategy, we envision the composition of this brand portfolio to change dramatically as we continue to transition the portfolio.

Franchise Brand	Number of Hotels	Number of Rooms
<b>Acquired In or Since 2012:</b>		
Courtyard by Marriott <sup>(1)</sup> . . . . .	1	120
Hilton Garden Inn <sup>(2)</sup> . . . . .	1	100
Hotel Indigo <sup>(3)</sup> . . . . .	1	142
Springhill Suites <sup>(1)</sup> . . . . .	1	116
Aloft <sup>(4)</sup> . . . . .	2	410
<b>Retained Portfolio of Hotels Acquired Prior to 2012:</b>		
Super 8 <sup>(5)</sup> . . . . .	2	227
Comfort Inn/Comfort Suites <sup>(6)</sup> . . . . .	6	535
Quality Inn <sup>(6)</sup> . . . . .	2	140
Days Inn <sup>(5)</sup> . . . . .	1	176
Key West Inn <sup>(7)</sup> . . . . .	1	40
Supertel Inn <sup>(8)*</sup> . . . . .	<u>1</u>	<u>41</u>
Total . . . . .	<u>19</u>	<u>2,047</u>

- (1) Courtyard by Marriott<sup>®</sup> and Springhill Suites<sup>®</sup> are a registered trademarks of Marriott International.
  - (2) Hilton Garden Inn<sup>®</sup> is a registered trademark of Hilton Hotels Corporation
  - (3) Hotel Indigo<sup>®</sup> is a registered trademark of InterContinental Hotels Group (IHG)
  - (4) Aloft<sup>®</sup> is a registered trademark of Hotels & Resorts Worldwide, Inc.; one of the hotels is owned by a joint venture which is 80% owned by the Company
  - (5) Super 8<sup>®</sup> and Days Inn<sup>®</sup> are registered trademarks of Wyndham Worldwide
  - (6) Comfort Inn<sup>®</sup>, Comfort Suites<sup>®</sup>, and Quality Inn<sup>®</sup> are registered trademarks of Choice Hotels International, Inc.
  - (7) Key West Inn<sup>®</sup> is a registered trademark of Key West Inns.
  - (8) Supertel Inn<sup>®</sup> is a registered trademark of Condor Hospitality Trust, Inc.
- \* Independent hotel brand unassociated with a national franchise brand

**Hotel Management Company Partners**

As a REIT, we cannot directly operate any of our hotels. We partner closely with some of who we believe are the leading hotel management companies in order to operate our hotels with the ultimate objective of improving same-store hotel performance throughout our portfolio. Each management agreement provides for a set term and is subject to early termination upon the occurrence of defaults and certain other events. As required under the REIT qualification rules, each of our management companies must qualify as an “eligible independent contractor”.

Each of the management companies receives a base monthly management fee of 3.0% to 3.5% of gross hotel revenue, with incentives for performance which increase such fee to a maximum of 5.0% of gross hotel revenues. The management agreements generally have initial terms of one to three years and renew for additional terms of one year unless either party to the agreement gives the other party written notice of termination at least 90 days before the end of a term. We may terminate a management agreement, subject to cure rights, if certain performance metrics tied to both individual hotel and total managed portfolio performance are not met. We may also terminate a management agreement with respect to a hotel at any time without reason upon payment of a termination fee. The management agreements terminate with respect to a hotel upon sale of the hotel, subject to certain notice requirements and, in some instances, payment of a termination fee.

Our 19 hotels owned at December 31, 2016 are operated by the following third-party management companies:

<u>Management Company</u>	<u>Number of Hotels</u>	<u>Number of Rooms</u>
Boast Hotel Management Company LLC .....	1	254
K Partners Hospitality Group LP .....	2	160
Kineth Hotel Corporation .....	3	268
Hospitality Management Advisors, Inc. ....	7	672
Peachtree Hospitality Management, LLC .....	3	378
Cherry Cove Hospitality Management, LLC .....	2	159
Presidian Hotels .....	<u>1</u>	<u>156</u>
Total .....	<u>19</u>	<u>2,047</u>

***Joint Venture***

We entered into a joint venture with Three Wall Capital LLC, or TWC, which acquired the 254-room Aloft hotel in downtown Atlanta, Georgia on August 22, 2016 for \$43.55 million. The name of the joint venture is Spring Street Hotel Property II LLC, or Spring Street JV. We own 80% of Spring Street JV, and TWC owns the remaining 20% of Spring Street JV. The hotel is leased to a TRS joint venture owned 80% by us and 20% by TWC and managed by Boast Hotel Management Company LLC, an affiliate of TWC.

The purchase price for the hotel was paid with \$9.80 million in cash (\$7.84 million contributed by us and \$1.96 million contributed by TWC) and \$33.75 million of proceeds from a term loan, secured by the hotel.

The limited liability company agreement, or JV Agreement, for Spring Street JV provides that, in exchange for our initial capital contributions, we received 80% and TWC received 20% of the equity interests in Spring Street JV. Any additional capital contributions to Spring Street JV generally will be made 80% by us and 20% by TWC.

## Hotel Property Portfolio

The following table sets forth certain information with respect to the hotels owned by us as of December 31, 2016 and under contract to be acquired by us as of January 23, 2017:

Brand	City	State	Rooms
<b><i>High Quality Select-Service Hotels</i></b>			
Hilton Garden Inn	Dowell	Maryland	100
Hotel Indigo	Atlanta (Airport)	Georgia	142
SpringHill Suites	San Antonio (Downtown)	Texas	116
Courtyard by Marriott	Jacksonville	Florida	120
Aloft	Leawood-Overland Park	Kansas	156
Aloft	Atlanta (Downtown)	Georgia	254
Home2 Suites <sup>(1)</sup>	Southaven	Mississippi	105
Home2 Suites <sup>(1)</sup>	Round Rock	Texas	91
Home2 Suites <sup>(1)</sup>	Lexington	Kentucky	103
Home2 Suites <sup>(1)</sup>	Tallahassee	Florida	132
			<b>1,319</b>
 Legacy Hotels Held for Use			
Comfort Suites	South Bend	Indiana	135
Comfort Suites	Fort Wayne	Indiana	127
Comfort Inn & Suites	Warsaw	Indiana	71
Quality Inn	Solomons	Maryland	59
Super 8	Creston	Iowa	121
Supertel Inn	Creston	Iowa	41
			<b>554</b>
 Legacy Hotels Held for Sale			
Comfort Suites	Lafayette	Indiana	62
Comfort Inn <sup>(2)</sup>	New Castle	Pennsylvania	79
Comfort Inn <sup>(2)</sup>	Harlan	Kentucky	61
Quality Inn	Morgantown	West Virginia	81
Days Inn	Bossier City	Louisiana	176
Super 8 <sup>(2)</sup>	Billings	Montana	106
Key West Inn	Key Largo	Florida	40
			<b>605</b>
			<b>2,478</b>

(1) This property is under contract to be acquired.

(2) This property is under contract to be sold.

## Seasonality of Hotel Business

Historically, as a result of the geographic areas in which we operate, the operations of our hotels have been seasonal in nature. Generally, occupancy rates, revenue, and operating income have been greater in the second and third quarters of the calendar year than in the first and fourth quarters, with the exception of our hotels located in Florida, which experience peak demand in the first and fourth quarters of the year. The results of recently acquired premium-branded, select-service hotels, because of their locations and chain scale, are expected to be less seasonal in nature than our retained portfolio of hotels.

## **Competition**

The hotel industry is highly competitive. Each of our hotels is located in a developed area that includes other hotel properties. The number of competitive hotel properties in a particular area could have a material adverse effect on revenue, occupancy, and the average daily room rate of our hotels or of hotel properties acquired in the future, and thus our financial results.

We may compete for investment opportunities with entities that have substantially greater financial resources than us. These entities generally may be able to accept more risk than we can prudently manage. Competition in general may reduce the number of suitable investment opportunities for us and increase the bargaining power of property owners seeking to sell.

## **Renovations, Capital Improvements and Replacements**

Our hotels have an ongoing need for renovations and other capital improvements, including replacements, from time to time, of furniture, fixtures and equipment. The franchisors of our hotels also require periodic capital improvements as a condition of keeping the franchise licenses. We generally budget 4.0% - 5.0% of annual revenue towards such renovations, capital improvements and replacements at our legacy hotels and 2.0% of annual revenue at our recently acquired hotels. Hotels that we plan to acquire may also have property improvement requirements imposed by the franchisors as a condition to our acquisition of the hotel. For example, we estimate that we will have to make \$1.8 million of capital improvements in connection with our acquisition of the Aloft hotel in Leawood, Kansas. We generally fund these costs with available cash or finance them with our credit facilities or loans.

## **Insurance**

We maintain comprehensive insurance on each of our hotel properties, including liability, fire, and extended coverage, of the type and amount we believe are customarily obtained for or by hotel owners. However, various types of catastrophic losses, like earthquakes and floods, or losses from foreign or domestic terrorist activities, may not be insurable or may not be economically insurable. For example, initially, we do not expect to obtain terrorism insurance on our hotel properties because it is costly. In the opinion of our management, our hotel properties are adequately covered by insurance.

## **Tax Status**

The Company qualifies and intends to continue to qualify as a REIT under the applicable provisions of the Code. In general, under such Code provisions, a trust which has made the required election and, in the taxable year, meets certain requirements and distributes to its shareholders at least 90% of its REIT taxable income, will not be subject to federal income tax to the extent of the income currently distributed to 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 income tax rates and generally will be unable to re-elect REIT status until the fifth calendar year after the year in which we failed to qualify as a REIT, unless we satisfy certain relief provisions. Even if the Company qualifies for taxation as a REIT, the Company may be subject to certain state and local taxes on its income and property, and to federal income and excise taxes on its undistributed taxable income. Taxable income from non-REIT activities managed through the TRS, which is taxed as a C corporation, is subject to federal, state, and local income taxes.

## **Employees**

As of December 31, 2016, we had 14 employees. The staff at our hotels are employed by our third-party hotel management companies.

**Available Information**

Our executive offices are located at 4800 Montgomery Lane, Suite 220, Bethesda, Maryland 20814, our telephone number is (301) 861-3305, and we maintain an Internet website located at [www.condorhospitality.com](http://www.condorhospitality.com). Our annual reports on Form 10-K and quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to these reports are available free of charge on our website as soon as reasonably practicable after they are filed with the SEC. We also make available the charters of our board committees and our Code of Business Conduct and Ethics on our website. Copies of these documents are available in print to any shareholder who requests them. Requests should be sent to Condor Hospitality Trust, Inc., 4800 Montgomery Lane, Suite 220, Bethesda, MD 20814, Attn: Corporate Secretary.

## MARKET AND MARKET PRICE OF COMMON STOCK

Our common stock trades on the Nasdaq Stock Market under the symbol “CDOR.” The closing sales price for our common stock on April 4, 2017 was \$10.78 per share. The table below sets forth the high and low sales prices per share for our common stock reported on the Nasdaq Stock Market for the periods indicated (adjusted to reflect the 1-for-6.5 reverse stock split effective March 15, 2017).

	<b>Condor Hospitality Trust, Inc.</b>	
	<b>Common Stock</b>	
	<u>High</u>	<u>Low</u>
<b>Fiscal year ended December 31, 2016</b>		
Fourth Quarter	\$14.235	\$ 9.945
Third Quarter	\$ 20.41	\$ 11.05
Second Quarter	\$ 16.90	\$ 9.815
First Quarter	\$ 14.56	\$ 4.55
<b>Fiscal year ended December 31, 2015</b>		
Fourth Quarter	\$10.335	\$ 6.50
Third Quarter	\$ 17.81	\$ 5.20
Second Quarter	\$ 24.05	\$10.465
First Quarter	\$14.755	\$ 9.23

In August 2016, we paid a dividend to the holders of our common stock of \$0.065 per share for the second quarter of 2016. In September 2016, our board of directors declared a cash dividend for the third quarter of 2016 of \$0.195 per share on our common stock, paid on October 12, 2016 to holders of record on September 29, 2016. In December 2016, our board of directors declared a cash dividend for the fourth quarter of 2016 of \$0.195 per share on our common stock, paid on January 5, 2017 to holders of record on December 20, 2016. In March 2017, our board of directors declared a cash dividend for the first quarter of \$0.195 per share on our common stock outstanding, to be paid on April 7, 2017 to holders of record on March 31, 2017. No dividends on our common stock were paid in the other periods presented above. The actual amount of future dividends will be determined by the board of directors based on the actual results of operations, economic conditions, capital expenditure requirements and other factors that the board of directors deems relevant.

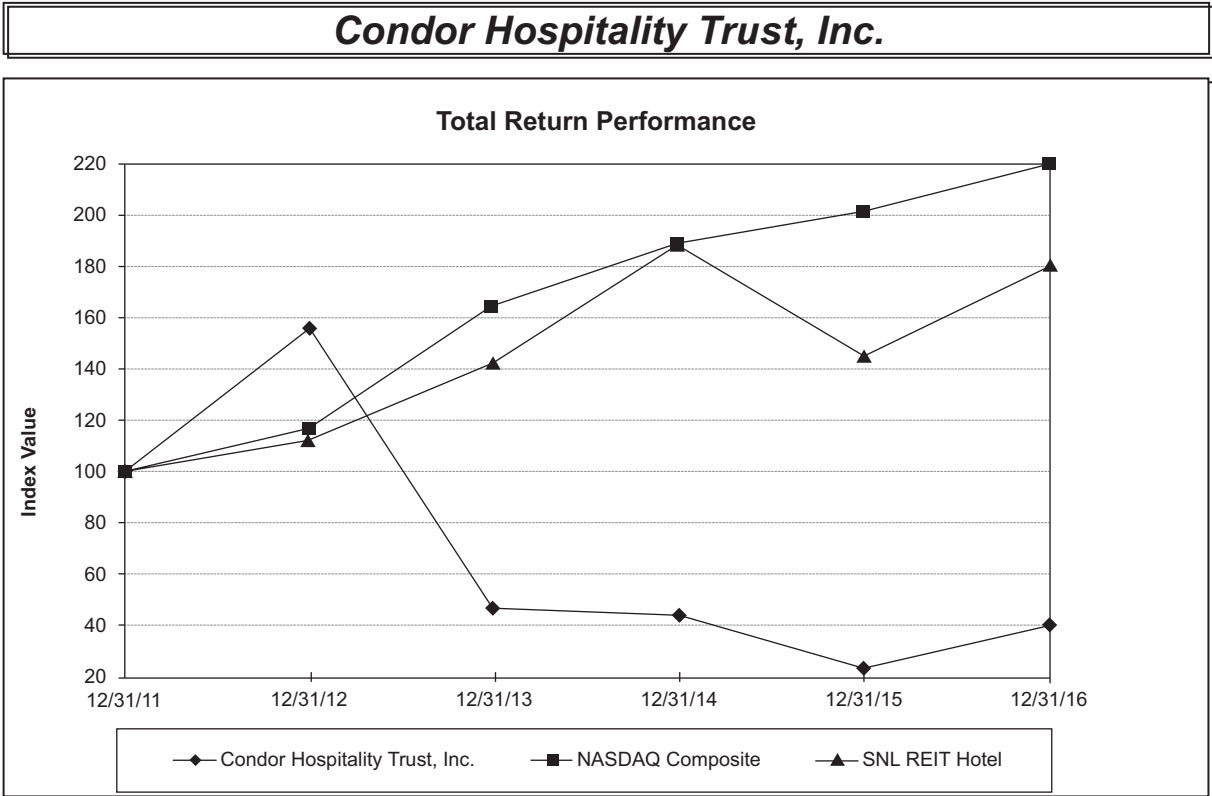
As of April 4, 2017, there were 51 holders of record of our common stock. However, because the vast majority of our common shares are held by brokers and other institutions on behalf of shareholders, we believe that there are considerably more beneficial holders of our common shares than record holders.

Information with respect to beneficial ownership of our common stock is set forth under “Securities Ownership of Certain Beneficial Owners and Management” in our Proxy Statement for the 2017 Annual Meeting of Stockholders and is incorporated herein by this reference.



## SHARE PERFORMANCE

The following graph compares the yearly percentage change in the cumulative total shareholder return on our common stock for the period December 31, 2011 through December 31, 2016, with the cumulative total return on the SNL Securities Hotel REIT Index (“Hotel REITs Index”) and the Nasdaq Composite (“Nasdaq—Total US Index”) for the same period. The Hotel REIT Index is comprised of publicly traded REITs that focus on investments in hotel properties. The Nasdaq Composite is comprised of all United States common shares traded on the Nasdaq Stock Market. The comparison assumes a starting investment of \$100 on December 31, 2011 in our common stock and in each of the indices shown and assumes that all dividends are reinvested. The performance graph is not necessarily indicative of future investment performance.



<i>Index</i>	<i>Period Ending</i>					
	<u>12/31/11</u>	<u>12/31/12</u>	<u>12/31/13</u>	<u>12/31/14</u>	<u>12/31/15</u>	<u>12/31/16</u>
Condor Hospitality Trust, Inc. . . . .	100.00	155.68	46.55	44.07	23.85	40.32
NASDAQ Composite . . . . .	100.00	117.45	164.57	188.84	201.98	219.89
SNL REIT Hotel . . . . .	100.00	112.80	142.50	188.10	145.51	180.34

## SELECTED FINANCIAL DATA

The following sets forth selected financial and operating data on a historical consolidated basis. The following information 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 related notes thereto, appearing in this Annual Report.

<b>In thousands, except share and per share data</b>	<b>As of and for the years ended December 31,</b>				
	<b>2016</b>	<b>2015</b>	<b>2014</b>	<b>2013</b>	<b>2012</b>
<b>Revenue</b>					
Room rentals and other hotel services	\$ 50,647	\$ 58,714	\$ 58,799	\$ 55,027	\$ 56,990
<b>Operating expense</b>					
Hotel and property operations	37,092	43,367	44,391	43,033	42,056
Depreciation and amortization	5,190	5,400	6,437	6,300	6,393
General and administrative	5,792	5,493	4,192	3,923	3,908
Acquisitions and terminated transactions	550	684	—	713	240
Terminated equity transactions	—	246	76	1,050	—
Total operating expenses	48,624	55,190	55,096	55,019	52,597
<b>Operating income</b>	2,023	3,524	3,703	8	4,393
Net gain (loss) on disposition of assets	23,132	4,798	(1)	(47)	(9)
Equity in loss of joint venture	(244)	—	—	—	—
Unrealized derivative gain (loss)	6,377	11,578	(14,430)	10,028	(247)
Other income	55	114	116	34	103
Interest expense	(4,710)	(5,522)	(7,116)	(5,620)	(5,283)
Loss on debt extinguishment	(2,187)	(213)	(158)	(458)	(138)
Impairment loss	(1,477)	(3,829)	(1,269)	(2,438)	(97)
Earnings (loss) from continuing operations before income taxes	22,969	10,450	(19,155)	1,507	(1,278)
Income tax (expense) benefit	(125)	—	—	—	6,588
Earnings (loss) from continuing operations	22,844	10,450	(19,155)	1,507	(7,866)
Gain (loss) from discontinued operations, net of tax	678	3,872	2,896	(2,860)	(2,354)
<b>Net earnings (loss)</b>	23,522	14,322	(16,259)	(1,353)	(10,220)
(Earnings) loss attributable to noncontrolling interest	(727)	(1,197)	23	2	10
Net earnings (loss) attributable to controlling interests	22,795	13,125	(16,236)	(1,351)	(10,210)
Dividends declared and undeclared and in kind dividends deemed on preferred stock	(20,748)	(3,632)	(3,452)	(3,349)	(3,169)
<b>Net earnings (loss) attributable to common shareholders</b>	<b>\$ 2,047</b>	<b>\$ 9,493</b>	<b>\$ (19,688)</b>	<b>\$ (4,700)</b>	<b>\$ (13,379)</b>
Weighted average number of common shares—basic	761	752	600	445	444
Weighted average number of common shares—diluted	5,536	3,575	600	445	444
<b>Basic</b>					
Basic EPS from continuing operations	\$ 1.82	\$ 8.06	\$ (37.64)	\$ (4.16)	\$ (24.83)
Basic EPS from discontinued operations	0.85	4.55	4.81	(6.44)	(5.27)
Total EPS Basic	\$ 2.67	\$ 12.61	\$ (32.83)	\$ (10.60)	\$ (30.10)
<b>Diluted</b>					
Diluted EPS from continuing operations	\$ 0.78	\$ (0.98)	\$ (37.64)	\$ (4.16)	\$ (24.83)
Diluted EPS from discontinued operations	0.13	0.98	4.81	(6.44)	(5.27)
Total EPS Diluted	\$ 0.91	\$ —	\$ (32.83)	\$ (10.60)	\$ (30.10)
<b>Balance sheet data</b>					
Total investment in hotel properties, net	\$114,871	\$130,699	\$139,182	\$164,356	\$191,091
Cash and cash equivalents	\$ 8,326	\$ 4,870	\$ 173	\$ 45	\$ 891
Total assets	\$140,665	\$142,346	\$144,820	\$169,500	\$199,223
Total debt, net of deferred financing costs, including convertible debt at fair value	\$ 64,035	\$ 86,011	\$ 91,063	\$115,460	\$130,197
Total equity	\$ 70,799	\$ 34,495	\$ 19,092	\$ 32,726	\$ 36,651

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The discussion that follows is based primarily on our consolidated financial statements as of December 31, 2016 and 2015, and for the years ended December 31, 2016, 2015 and 2014, and should be read along with the consolidated financial statements and related notes contained elsewhere in this Annual Report.

### Overview

The Company is a self-administered REIT for federal income tax purposes that specializes in the investment and ownership of high-quality select-service, limited-service, extended stay, and compact full-service hotels. Substantially all of our operations are conducted through Condor Hospitality Limited Partnership, our operating partnership, of which the Company is the sole general partner. As of December 31, 2016, the Company owned 19 hotels, representing 2,047 rooms, in 12 states, including one hotel owned through an 80% interest in an unconsolidated joint venture.

The Company experienced another year of positive transition in 2016 with significant enhancements to its portfolio composition, equity structure, debt profile, and brand. The Company's new strategy enabled the Company to announce its first common dividend since 2009. The Company declared and paid three consecutive quarterly dividends commencing in the second quarter of 2016. Significant accomplishments for 2016 are summarized as follows:

**Portfolio Composition:** In 2016, the Company sold 25 legacy hotels generating \$61.4 million of gross proceeds. These legacy asset sales were completed in individual transactions at valuations management believes were attractive. The net proceeds were recycled into two acquisitions. In August 2016, the Company closed on a joint venture to acquire the Aloft Atlanta for \$43.6 million. In December 2016, the Company acquired the Aloft hotel in Leawood, Kansas for \$22.5 million. Both of these assets are representative of the Company's new investment strategy to acquire high-quality, premium-branded, select-service assets. Subsequent to the close of the year, on January 23, 2017, the Company announced that it had executed an agreement to purchase a portfolio of four Home2 Suites hotels for \$73.8 million. The transaction is expected to close in the first quarter of 2017, subject to customary closing conditions.

**Equity Structure:** On March 16, 2016, the Company closed on a \$30.0 million private placement of Series D Preferred Stock, enabling the full redemption, including accrued dividends, of the 8% Series A Cumulative Preferred Stock, or Series A Preferred Stock, and 10% Series B Cumulative Preferred Stock, or Series B Preferred Stock. Simultaneously with the sale and issuance of the 6.25% Series D Cumulative Convertible Preferred Stock, or Series D Preferred Stock, in the \$30.0 million private placement, the Company exchanged all of the outstanding 6.25% Series C Cumulative Convertible Preferred Stock, or Series C Preferred Stock, for the new Series D Preferred Stock. Subsequent to December 31, 2016, on February 28, 2017, the holders of all of the outstanding Series D Preferred Stock voluntarily converted to an aggregate of 6,004,957 shares of common stock. At the time of conversion, the Series D holders were granted \$9.25 million of newly created 6.25% Series E Cumulative Convertible Preferred Stock, or Series E Preferred Stock.

**Debt Profile:** Subsequent to December 31, 2016, on March 1, 2017, the Company closed a new \$90.0 million secured revolving credit facility. KeyBank N.A. and The Huntington National Bank serve as the lenders for the revolving credit facility. The new credit facility significantly reduced the Company's weighted average cost of debt and enabled the refinancing of the substantial majority of 2017 and 2018 maturities. The credit facility also enables the Company to accelerate the closing of acquisitions. Management believes the new facility is a strong indicator of Condor's credit-worthiness and the confidence of the Company's banks in the Company's new strategic direction.

**Rebranding:** The Company completed a comprehensive rebranding in 2016. The Company launched a new website in March 2016 and revised all reporting materials to reflect the new strategic direction of the Company.

With the aforementioned successes serving as a foundation for future growth, the Company's management is excited about 2017 and is confident in its ability to achieve the mission of providing attractive total returns in the lodging sector to the Company's shareholders.

We remain cautiously optimistic on the outlook of the hospitality sector in 2017. The hospitality sector experienced its seventh straight year of positive RevPAR growth in 2016. The expected decline in the pace of RevPAR growth materialized in 2016 and is expected to continue into 2017. Most industry forecasts estimate that U.S. RevPAR will grow at a slower pace in 2017, generally between 2.0%—3.0%. The slower pace of RevPAR growth we believe is primarily driven by concerns on new supply and concerns on slowing economic growth. The Company management believes the sectors and segments it targets will see growth in excess of these estimates. While many primary markets have a large influx of new supply, the markets the Company targets are experiencing less aggressive supply growth. Additionally, the markets the Company targets are less affected, we believe, by alternative lodging platforms like Airbnb than many larger markets. We believe these supply factors, combined with the possibility of continued positive economic growth, should enable our hotels to experience growth in RevPAR in 2017.

We believe that the performance of the hotel industry is strongly correlated with the performance of the macro-economy. The equity markets have so far reacted favorably following the U.S. Presidential election. However, it is unknown if the new administration's policies will have a positive or negative impact on the economy. Additionally, the continued threat of terrorism and economic and geopolitical turbulence abroad could derail the macro-economy. Barring any major disruption to the U.S. economy, we expect a continued improvement in lodging fundamentals, with a more tepid improvement in lodging fundamentals in 2017 than in 2016. The manner in which the economy continues to grow, if at all, is not predictable and outside of our control. As a result, there can be no assurances that we will be able to grow our hotel revenue, ADR, occupancy, or RevPAR. The Company's management continually monitors the economic environment and works to adjust its strategy to seek to maximize value and returns to shareholders.

## Hotel Property Portfolio Activity

### Acquisitions

On August 1, 2016, the Company entered into a joint venture, the Atlanta JV, with Three Wall Capital, or TWC, to acquire a 254-room Aloft hotel in downtown Atlanta, Georgia. The Company accounts for the Atlanta JV under the equity method. The Company owns 80% of the Atlanta JV with TWC owning the remaining 20%. The Atlanta JV is comprised of two companies: Spring Street Hotel Property II LLC, of which Condor Hospitality Limited Partnership indirectly owns an 80% equity interest, and Spring Street Hotel OpCo II LLC, of which our TRS indirectly owns an 80% equity interest. TWC owns the remaining 20% equity interest in these two companies.

On August 22, 2016, the Atlanta JV closed on the acquisition of the Atlanta Aloft hotel for a purchase price of \$43.6 million, before working capital and similar adjustments. A summary of this acquisition and its funding as completed by the Atlanta JV is as follows (in thousands):

<u>Hotel</u>	<u>Land</u>	<u>Buildings, improvements, and vehicles</u>	<u>Furniture and equipment</u>	<u>Land option (1)</u>	<u>Total purchase price</u>	<u>Debt originated at acquisition</u>	<u>Net cash</u>
Aloft Atlanta, GA	\$13,025	\$34,048	\$2,667	\$(6,190)	\$43,550	\$33,750	\$9,800

(1) The purchase agreement includes a provision which permits the seller to purchase the surface parking lot north of the hotel exercisable for ten years at less than market price.

The purchase price for the Atlanta Aloft was paid by the Atlanta JV with \$9.8 million in cash, of which \$7.8 million was contributed by the Company and \$2.0 million was contributed by TWC, and \$33.8 million of proceeds from a term loan secured by the property. Condor additionally contributed \$1.4 million and TWC additionally contributed \$0.4 million to the Atlanta JV to cover acquisition costs and to provide working capital to the entity.

On December 14, 2016, we also acquired one wholly-owned hotel, the 156-room Aloft in Leawood, Kansas, or Aloft Leawood, through a single-purpose bankruptcy remote entity 100% owned by Condor Hospitality Limited Partnership. A summary of this acquisition and its funding is as follows (in thousands):

<u>Hotel</u>	<u>Land</u>	<u>Buildings, improvements, and vehicles</u>	<u>Furniture and equipment</u>	<u>Total purchase price</u>	<u>Debt originated at acquisition</u>	<u>Issuance of Condor Hospitality Limited Partnership common units</u>	<u>Net cash</u>
Aloft Leawood, KS	\$3,339	\$18,046	\$1,115	\$22,500	\$15,925	\$50	\$6,525

The \$22.5 million purchase price was funded with the proceeds of two mortgage loans provided by Great Western Bank totaling \$15.9 million, approximately \$6.5 million in cash, and the issuance of 213,904 common units in Condor Hospitality Limited Partnership with a value of \$50,000.

During 2015, we acquired three wholly-owned premium select-service hotel properties through three single-purpose bankruptcy remote entities 100% owned by Condor Hospitality Limited Partnership from affiliates of Peachtree Hotel Group II, LLC. A summary of these acquisitions and their funding is as follows (in thousands):

<u>Hotel</u>	<u>Acquisition date</u>	<u>Land</u>	<u>Building, improvements, and vehicles</u>	<u>Furniture and equipment</u>	<u>Total purchase price</u>	<u>Assumption of debt</u>	<u>Debt originated at acquisition</u>	<u>Issuance of Condor Hospitality Limited Partnership common units</u>	<u>Net cash</u>
Hotel Indigo									
Atlanta, GA	10/2/2015	\$ 800	\$ 8,700	\$1,500	\$11,000	\$ —	\$ 5,000	\$150	\$ 5,850
Marriott Courtyard									
Jacksonville, FL	10/2/2015	2,100	11,050	850	14,000	—	10,100	150	3,750
SpringHill Suites									
San Antonio, TX	10/1/2015	<u>1,597</u>	<u>14,353</u>	<u>1,550</u>	<u>17,500</u>	<u>11,220</u>	<u>—</u>	<u>150</u>	<u>6,130</u>
Total		<u>\$4,497</u>	<u>\$34,103</u>	<u>\$3,900</u>	<u>\$42,500</u>	<u>\$11,220</u>	<u>\$15,100</u>	<u>\$450</u>	<u>\$15,730</u>

The \$42.5 million purchase price was funded with the assumption of one loan with an aggregate outstanding principal balance of \$11.2 million and two newly originated GE Capital loans (sold to Western Alliance Bank, or WAB, in April 2016) totaling \$15.1 million. The remaining \$16.2 million was funded with \$14.9 million in cash, approximately \$0.8 million of borrowings from the Company's existing credit facility with Great Western Bank, and the issuance of operating units from Condor Hospitality Limited Partnership representing limited partnership interest in that entity. A total of 2,298,879 common units in Condor Hospitality Limited Partnership were issued with a value of \$450,000.

There were no hotel acquisitions in 2014.

Additionally, as discussed further in the Subsequent Events footnote to our consolidated financial statements appearing elsewhere in this Annual Report, on January 23, 2017, the Company executed an agreement to purchase a portfolio of four Home2 Suites hotels for \$73.8 million. The portfolio includes the Home2 Suites Memphis / Southaven, the Home2 Suites Austin / Round Rock, the Home2 Suites Lexington University / Medical Center (Kentucky), and the Home2 Suites Tallahassee State Capitol. The closing of these acquisitions is anticipated to occur in the first and second quarters of 2017, but is subject to customary closing conditions including accuracy of representations and warranties and compliance with covenants and obligations.

## Dispositions

Pursuant to our disposition strategy, the following hotel sales were executed in 2016:

<u>Date of sale</u>	<u>Location</u>	<u>Brand</u>	<u>Condor lender</u>	<u>Number of rooms</u>	<u>Gross proceeds (in thousands)</u>
01/04/16	Kirkville, MO	Super 8	Great Western	61	\$ 1,525
01/07/16	Lincoln, NE	Super 8	Great Western	133	2,800
01/08/16	Greenville, SC	Savannah Suites	Western Alliance Bank	170	2,700
03/30/16	Portage, WI	Super 8	Morgan Stanley	61	2,375
04/25/16	O'Neill, NE	Super 8	Morgan Stanley	72	1,725
05/10/16	Culpeper, VA	Quality Inn	Morgan Stanley	49	2,200
05/19/16	Storm Lake, IA	Super 8	Morgan Stanley	59	2,800
05/24/16	Cleveland, TN	Clarion	Morgan Stanley	59	2,231
05/26/16	Coralville, IA	Super 8	Morgan Stanley	84	3,375
05/27/16	Keokuk, IA	Super 8	Morgan Stanley	61	2,153
06/06/16	Chambersburg, PA	Comfort Inn	Morgan Stanley	63	2,150
08/08/16	Pittsburg, KS	Super 8	Morgan Stanley	64	1,620
09/09/16	Mt. Pleasant, IA	Super 8	Morgan Stanley	54	1,850
09/19/16	Danville, KY	Quality Inn	Morgan Stanley	63	2,288
09/26/16	Menomonie, WI	Super 8	Morgan Stanley	81	3,000
10/14/16	Glasgow, KY	Comfort Inn	Western Alliance Bank	60	2,400
11/04/16	Sioux Falls, SD	Days Inn	Western Alliance Bank	86	2,095
11/07/16	Shelby, NC	Comfort Inn	Morgan Stanley	76	4,090
11/17/16	Rocky Mount, VA	Comfort Inn	Morgan Stanley	61	2,160
11/17/16	Farmville, VA	Days Inn	Morgan Stanley	59	2,390
11/18/16	Marion, IN	Comfort Suites	Huntington	62	2,992
11/30/16	Farmville, VA	Comfort Inn	Morgan Stanley	50	2,573
12/05/16	Princeton, WV	Quality Inn	Morgan Stanley	50	2,150
12/21/16	Burlington, IA	Super 8	Morgan Stanley	62	2,860
12/22/16	Atlanta, GA	Savannah Suites	Western Alliance Bank	164	2,925
			<b>Total</b>	<u>1,864</u>	<u>\$61,427</u>

Net proceeds, after expenses and debt repayment, totaled \$19.2 million in 2016. In 2015, 17 hotels with 1,673 rooms were sold for gross proceeds of \$54.7 million, and net proceeds, after expenses and debt repayment, of \$25.3 million. In 2014, 13 hotels with 1,265 rooms were sold for gross proceeds of \$22.3 million, and net proceeds, after expenses and debt repayment, of \$2.6 million.

Based on the criteria discussed in the footnotes to the consolidated financial statements appearing elsewhere in this Annual Report, as of December 31, 2016, the Company had seven hotels classified as held for sale. At the beginning of 2016, the Company had 16 hotels held for sale and during the year classified an additional 16 hotels as held for sale. Twenty-five of these hotels were sold during 2016. If a hotel is considered held for sale as of the most recent balance sheet date presented or was sold in any period presented, the hotel property and the debt it collateralizes are shown as held for sale in all periods presented.

As discussed in the footnotes to our consolidated financial statements appearing elsewhere in this Annual Report, as of October 1, 2014 we adopted ASU 2014-08 which changes the criteria for reporting a discontinued operation such that only disposals representing a strategic shift in operations should be presented as discontinued operations subsequent to adoption. As a result of this adoption, only the operations of hotels meeting the criteria to be considered held for sale prior to October 1, 2014 (excluding those subsequently reclassified as held for use), none of which remain unsold at December 31, 2016, are included in discontinued operations for all periods presented as no individual hotel disposition represents a strategic shift that has (or will have) a major effect on our operations or financial results.

## Operating Performance Metrics

The following table presents our RevPAR, ADR, and occupancy for our same store operations. The comparisons for same store operations include all of our hotels owned as of December 31, 2016 which were owned throughout the periods presented and exclude the three hotels we acquired in October 2015, the hotel acquired through our Atlanta JV in August 2016, and the hotel acquired in December 2016 (14 hotels included in same store results, seven of which are considered held for use, or HFU, and seven of which are considered held for sale, or HFS). All hotels included in same store operations were owned throughout each of the periods presented. The performance metrics for the five hotels acquired in 2015 and 2016, one of which is owned by a joint venture which is 80% owned by the Company, represent post-acquisition operations only and are separately presented. Performance metrics presented for the hotel owned through our Atlanta JV reflect 100% of the operating results of the property including our interest and the interest of our joint venture partner.

	Year ended December 31,								
	2016			2015			2014		
	Occupancy	ADR	RevPAR	Occupancy	ADR	RevPAR	Occupancy	ADR	RevPAR
Same store HFU	65.52%	\$ 83.96	\$55.00	67.71%	\$ 82.33	\$55.75	67.83%	\$76.15	\$51.65
Same store HFS	56.93%	70.43	40.10	60.45%	67.84	41.01	68.84%	63.12	43.45
Total same store	61.41%	\$ 77.96	\$47.87	64.22%	\$ 75.79	\$48.67	68.31%	\$69.85	\$47.72
October 2015									
Acquisitions	72.92%	\$113.39	\$82.68	65.22%	\$116.48	\$75.97	—	\$ —	\$ —
Aloft Atlanta JV	69.87%	\$136.97	\$95.70	—	\$ —	\$ —	—	\$ —	\$ —
Aloft Leawood	68.20%	\$102.76	\$70.08	—	\$ —	\$ —	—	\$ —	\$ —

In the same store HFU portfolio of hotels, 2016 RevPAR decreased 1.3%, driven by a decrease of 3.2% in occupancy partially offset by an increase of 2.0% in ADR. This decrease in occupancy was driven by market challenges facing these hotels as a result of declines in the oil and gas, rail, and fracking industries as well as renovation interruption at three of these hotels during the 2016. Despite the decrease in occupancy, the Company was able to increase ADR due to continued improvement in the economy and, to a lesser extent, decreases in inventory as a result of the ongoing renovations at certain hotels.

In the same store HFU portfolio of hotels, 2015 RevPAR increased 7.9% from 2014, driven by an increase in ADR of 8.1%. In 2015, the Company focused on increasing ADR in light of an improving economy and increasing leisure and transient travel.

## Results of Operations

*Comparison of the year ended December 31, 2016 to the year ended December 31, 2015 (in thousands, except per share amounts)*

	Year ended December 31,						Continuing operations variance
	2016			2015			
	Continuing operations	Discontinued operations	Total	Continuing operations	Discontinued operations	Total	
Revenue	\$ 50,647	\$ 6	\$ 50,653	\$ 58,714	\$ 2,923	\$ 61,637	\$ (8,067)
Hotel and property operations expense	(37,092)	(4)	(37,096)	(43,367)	(1,946)	(45,313)	6,275
Depreciation and amortization expense	(5,190)	—	(5,190)	(5,400)	—	(5,400)	210
General and administrative expense	(5,792)	—	(5,792)	(5,493)	—	(5,493)	(299)
Acquisition and terminated transactions expense	(550)	—	(550)	(684)	—	(684)	134
Terminated equity transactions	—	—	—	(246)	—	(246)	246
Net gain (loss) on disposition of assets	23,132	681	23,813	4,798	2,997	7,795	18,334
Equity in loss of joint venture	(244)	—	(244)	—	—	—	(244)
Net gain on derivatives and convertible debt	6,377	—	6,377	11,578	—	11,578	(5,201)
Other income (expense)	55	—	55	114	—	114	(59)
Interest expense	(4,710)	(5)	(4,715)	(5,522)	(223)	(5,745)	812
Loss on extinguishment of debt	(2,187)	—	(2,187)	(213)	—	(213)	(1,974)
Impairment (loss) recovery	(1,477)	—	(1,477)	(3,829)	121	(3,708)	2,352
Income tax expense	(125)	—	(125)	—	—	—	(125)
<b>Net earnings</b>	<u>\$ 22,844</u>	<u>\$678</u>	<u>\$ 23,522</u>	<u>\$ 10,450</u>	<u>\$ 3,872</u>	<u>\$ 14,322</u>	<u>\$12,394</u>

### Revenue

During 2016, revenue from continuing operations decreased by \$8,067 between the periods. Revenue from properties acquired in and subsequent to the fourth quarter of 2015 increased \$10,175 and revenue from our other held for use assets remained consistent, decreasing by \$129. Revenue from held for sale and sold properties decreased by \$18,113 driven by property sales during the periods presented.

### Expenses

Hotel and property operations expense from continuing operations decreased by \$6,275, driven by declines resulting from sold hotels partially offset by increases related to newly acquired properties. In totality, hotel and operations expenses from continuing operations decreased as a percentage of revenue by 0.6% because of increases in ADR and because the legacy hotels that remain in our portfolio and our recent acquisitions have higher operating margins than the hotels that were sold during the period.

Interest expense and depreciation expense from continuing operations decreased by \$812 and \$210, respectively, between the periods as a result of a net decrease in the size of the Company's hotel portfolio and thus its debt levels. Additionally, interest expense was favorably impacted by a decrease in the weighted average interest rate on total debt outstanding between the periods, from 5.31% at December 31, 2015 to 4.86% at December 31, 2016, as a result of debt repaid upon the sale of properties and the lower than average interest rate obtained on the Great Western Bank debt obtained as part of the Leawood Aloft acquisition in December 2016.



The \$299 increase in general and administrative expense was driven by increased compensation expense resulting from compensation arrangements put into place with the new management team in 2015 as well as increased professional fees associated with increased business activity in 2016. These increases were partially offset by decreased directors' and officers' insurance premiums and decreased employee recruiting costs following significant executive recruiting in 2015.

Acquisition and terminated transaction costs will fluctuate period to period based on our acquisition activities. Acquisition costs typically consist of transfer taxes, legal fees, and other costs associated with acquiring a hotel property as well as transactions that were terminated during the year.

The \$246 of terminated equity transactions expense in 2015 consists of charges incurred in the preparation of an exchange offer commenced on August 6, 2015. This offer was withdrawn on September 17, 2015.

#### *Impairment Losses*

In 2016, we incurred \$1,477 of impairment losses, all of which was included in continuing operations. In 2015, we incurred \$3,708 of impairment losses, all of which was included in continuing operations with the exception of net recovery of \$121 included in discontinued operations. All impairments recognized in both years related either to hotels held for sale at some point or sold during the year.

#### *Dispositions*

In 2016, twenty-four hotels were sold with gains totaling \$24,256 and one hotel was sold with no gain as it had been previously impaired. In 2015, eight hotels were sold with gains totaling \$7,759 and nine hotels were sold with no gain as they had been previously impaired.

#### *Net Gain on Derivatives and Convertible Debt*

The change in net gain on derivatives and convertible debt was driven by the change in fair value of the derivative liabilities for the current year compared to the year ended December 31, 2015. The fair value of the derivative liabilities decreased by an aggregate of \$6,680 during 2016 and \$11,578 during 2015. The decreases in fair value in both periods was primarily a result of a decrease in the Company's stock price during the periods, which in turn decreases the value assigned to the conversion feature of the Series C Preferred Stock and the outstanding common stock warrants throughout 2015 and while being marked to market in the first quarter of 2016.

### Income Tax Expense

As of both December 31, 2016 and 2015, a full valuation allowance continued to be recorded against the net deferred tax asset due to the uncertainty of realization because of historical operating losses. As such, no income tax expense or benefit was recorded during either year with the exception of amounts totaling \$125 for alternative minimum tax recorded in 2016 related to the use of net operating losses during the period. Management believes the combined federal and state income tax rate for the TRS will be approximately 38% and income tax benefit or expense will vary based on the taxable earnings or loss of the TRS.

### Comparison of the year ended December 31, 2015 to the year ended December 31, 2014 (in thousands, except per share amounts)

	Year ended December 31,						Continuing operations variance
	2015			2014			
	Continuing operations	Discontinued operations	Total	Continuing operations	Discontinued operations	Total	
Revenue	\$ 58,714	\$ 2,923	\$ 61,637	\$ 58,799	\$ 13,579	\$ 72,378	\$ (85)
Hotel and property operations expense	(43,367)	(1,946)	(45,313)	(44,391)	(10,410)	(54,801)	1,024
Depreciation and amortization expense	(5,400)	—	(5,400)	(6,437)	(112)	(6,549)	1,037
General and administrative expense	(5,493)	—	(5,493)	(4,192)	—	(4,192)	(1,301)
Acquisition and terminated transactions expense	(684)	—	(684)	—	—	—	(684)
Terminated equity transactions	(246)	—	(246)	(76)	—	(76)	(170)
Net gain on disposition of assets	4,798	2,997	7,795	(1)	2,751	2,750	4,799
Equity in loss of joint venture	—	—	—	—	—	—	—
Net gain on derivatives and convertible debt	11,578	—	11,578	(14,430)	—	(14,430)	26,008
Other income	114	—	114	116	—	116	(2)
Interest expense	(5,522)	(223)	(5,745)	(7,116)	(1,140)	(8,256)	1,594
Loss on extinguishment of debt	(213)	—	(213)	(158)	(120)	(278)	(55)
Impairment (loss) recovery	(3,829)	121	(3,708)	(1,269)	(1,652)	(2,921)	(2,560)
Income tax expense	—	—	—	—	—	—	—
<b>Net earnings</b>	<u>\$ 10,450</u>	<u>\$ 3,872</u>	<u>\$ 14,322</u>	<u>\$(19,155)</u>	<u>\$ 2,896</u>	<u>\$(16,259)</u>	<u>\$29,605</u>

### Revenue

During 2015, revenue from continuing operations remained stable, decreasing by \$85 between the periods. Revenue from properties acquired in the fourth quarter of 2015 totaled \$2,611 and revenue from our other held for use assets increased \$1,117, largely driven by an improving economy and a mild winter in early 2015 which increased construction and special projects business at our properties. Revenue from held for sale and sold properties included in continuing operations decreased by \$3,813 driven by property sales during the periods presented.

### *Expenses*

Hotel and property operations expense from continuing operations decreased by \$1,024, driven by declines resulting from sold hotels. The decrease in these expenses outpaced the decrease in revenue because of increases in ADR as discussed above and because the legacy hotels that remained in our portfolio in 2015 and our 2015 acquisitions have higher operating margins than the hotels that were sold during the period.

Interest expense from continuing operations and depreciation expense from continuing operations decreased by \$1,594 and \$1,037, respectively, between the periods as a result of a net decrease in the size of the Company's hotel portfolio and thus its debt levels. Additionally, interest expense was favorably impacted by a decrease in the weighted average interest rate on total debt outstanding between the periods, from 6.48% at December 31, 2014 to 5.31% at December 31, 2015, as a result of debt repaid upon the sale of properties and debt refinancings during 2015.

The \$1,301 increase in general and administrative expense was driven by increased compensation expense resulting from compensation arrangements put into place with the new management team in 2015 and severance accrued for management who left the Company during the year, as well as recruiting expenses incurred in relation to those transitions. Increased director and officer insurance premiums, increased travel, legal, and professional fees expense resulting from our name change, increased transactional activity during the year, and increased directors' fees resulting from the increased size of our Board of Directors also contributed to this change.

Acquisition and terminated transaction costs will fluctuate period to period based on our acquisition activities. Acquisition costs typically consist of transfer taxes, legal fees, and other costs associated with acquiring a hotel property as well as expenses incurred related to transactions that were terminated during the year. The increase in these expenses in 2015 was a result of the three acquisitions consummated during the year as well as increased activity by management to review potential future transactions.

The \$246 of terminated equity transactions expense in 2015 consists of charges incurred in the preparation of an exchange offer commenced on August 6, 2015. This offer was withdrawn on September 17, 2015.

### *Impairment (Loss) Recovery*

In 2015, we incurred \$3,708 of impairment losses, all of which were included in continuing operations with the exception of net recovery of \$121 included in discontinued operations. In 2014, we incurred impairment losses totaling \$2,921, of which \$1,269 was in continuing operations and \$1,652 was in discontinued operations. All impairments recognized in both years related either to hotels held for sale at some point or sold during the year.

### *Dispositions*

In 2015, eight hotels were sold with gains totaling \$7,759 and nine hotels were sold that had been previously impaired and as such had no gains. In 2014, five hotels were sold with gains totaling \$2,749 and eight hotels were sold that had been previously impaired and as such had no gains.

### *Net Gain (Loss) on Derivatives and Convertible Debt*

The change in net gain (loss) on derivatives and convertible debt was driven by the relative changes in derivative value between the years ended December 31, 2015 and 2014. The fair value of the derivative liabilities decreased by an aggregate of \$11,578 during 2015 and increased by \$14,430 during 2014. The decrease in fair value in 2015 was primarily a result of a decrease in the Company's stock price in 2015, which in turn decreases the value assigned to the conversion feature of the Series C Preferred Stock and the outstanding common stock

warrants. The increase in fair value in 2014 was primarily due to the change in exercise price of the related warrants adjusted downward from \$62.40 to \$12.48, and to a change in the conversion price of the Series C Preferred Stock from \$52.00 to \$10.40, the public offering price of the common stock in the Company's subscription rights offering concluded on June 6, 2014.

#### *Income Tax Expense*

As of December 31, 2015 and 2014, a full valuation allowance continued to be recorded against the net deferred tax asset due to the uncertainty of realization because of historical operating losses. As such, no income tax expense or benefit was recorded for the years ended December 31, 2015 or 2014. Management believes the combined federal and state income tax rate for the TRS will be approximately 38% and income tax benefit or expense will vary based on the taxable earnings or loss of the TRS.

#### **Non-GAAP Financial Measures**

Non-GAAP financial measures are measures of our historical financial performance that are different from measures calculated and presented in accordance with accounting principles generally accepted in the United States of America, or GAAP. We report Funds from Operations, or FFO, Adjusted FFO, or AFFO, Earnings Before Interest, Taxes, Depreciation, and Amortization, or EBITDA, Adjusted EBITDA, and Hotel EBITDA as non-GAAP measures that we believe are useful to investors as key measures of our operating results and which management uses to facilitate a periodic evaluation of our operating results relative to those of our peers. Our non-GAAP measures should not be considered as an alternative to U.S. GAAP net earnings as an indication of financial performance or to U.S. GAAP cash flows from operating activities as a measure of liquidity. Additionally, these measures are not indicative of funds available to fund cash needs or our ability to make cash distributions as they have not been adjusted to consider cash requirements for capital expenditures, property acquisitions, debt service obligations, or other commitments.

#### ***Funds from Operations ("FFO") & Adjusted FFO ("AFFO")***

We calculate FFO in accordance with the standards established by the National Association of Real Estate Investment Trusts ("NAREIT"), which defines FFO as net earnings computed in accordance with GAAP, excluding gains or losses from sales of real estate assets, impairment, and the depreciation and amortization of real estate assets. FFO is calculated both for the Company in total and as FFO attributable to common shares and common units, which is FFO excluding preferred stock dividends. AFFO is FFO attributable to common shares and common units adjusted to exclude items we do not believe are representative of the results from our core operations, such as non-cash gains or losses on derivative liabilities and convertible debt and cash charges for acquisition or equity raising costs. All REITs do not calculate FFO and AFFO in the same manner; therefore, our calculation may not be the same as the calculation of FFO and AFFO for similar REITs.

We consider FFO and AFFO to be useful additional measures of performance for an equity REIT because they facilitate an understanding of the operating performance of our properties without giving effect to real estate depreciation and amortization, which assumes that the value of real estate assets diminishes predictably over time. Since real estate values have historically risen or fallen with market conditions, we believe that FFO and AFFO provide a meaningful indication of our performance.

The following table reconciles net earnings (loss) to FFO and AFFO for the years ended December 31 (in thousands). All amounts presented include both continuing and discontinued operations as well as our portion of the results of our unconsolidated Atlanta JV.

<b>Reconciliation of Net earnings (loss) to FFO and AFFO</b>	<b>Year ended December 31,</b>		
	<b>2016</b>	<b>2015</b>	<b>2014</b>
Net earnings (loss)	\$ 23,522	\$ 14,322	\$(16,259)
Depreciation and amortization expense	5,190	5,400	6,549
Depreciation and amortization expense from Atlanta JV	377	—	—
Net gain on disposition of assets	(23,813)	(7,795)	(2,750)
Net loss on disposition of assets from Atlanta JV	2	—	—
Impairment loss	1,477	3,708	2,921
<b>FFO</b>	<b>6,755</b>	<b>15,635</b>	<b>(9,539)</b>
Dividends declared and undeclared and in kind dividends deemed on preferred stock	(20,748)	(3,632)	(3,452)
<b>FFO attributable to common shares and common units</b>	<b>\$(13,993)</b>	<b>\$ 12,003</b>	<b>\$(12,991)</b>
Net (gain) loss on derivatives and convertible debt	(6,377)	(11,578)	14,430
Net loss on derivatives from Atlanta JV	5	—	—
Acquisitions and terminated transactions expense	550	684	—
Acquisition expense from Atlanta JV	239	—	—
Gain on debt conversion	—	—	(88)
Terminated equity transactions expense	—	246	76
<b>AFFO attributable to common shares and common units</b>	<b>\$(19,576)</b>	<b>\$ 1,355</b>	<b>\$ 1,427</b>

***Earnings Before Interest, Taxes, Depreciation, and Amortization (“EBITDA”), Adjusted EBITDA, and Hotel EBITDA***

We calculate EBITDA and Adjusted EBITDA by adding back to net earnings certain non-operating expenses and certain non-cash charges which are based on historical cost accounting that we believe may be of limited significance in evaluating current performance. We believe these adjustments can help eliminate the accounting effects of depreciation and amortization and financing decisions and facilitate comparisons of core operating profitability between periods. In calculating EBITDA, we add back to net earnings interest expense, loss on debt extinguishment, income tax expense, and depreciation and amortization expense. In calculating Adjusted EBITDA, we adjust EBITDA to add back net gain/loss on disposition of assets, acquisition and terminated transactions expense, and terminated equity transactions expense, which are cash charges. We also add back impairment and gain or loss on derivatives and convertible debt, which are non-cash charges. EBITDA and Adjusted EBITDA, as presented, may not be comparable to similarly titled measures of other companies.

We believe EBITDA and Adjusted EBITDA to be useful additional measures of our operating performance, excluding the impact of our capital structure (primarily interest expense), our asset base (primarily depreciation and amortization expense), and other items we do not believe are representative of the results from our core operations.

The Company further excludes general and administrative expenses, other non-operating income or expense, and certain hotel and property operations expenses that are not allocated to individual properties in assessing hotel performance (primarily certain general liability and other insurance costs, land lease costs, and office and banking fees) from Adjusted EBITDA to calculate Hotel EBITDA. Hotel EBITDA is similar to the non-GAAP measure of Property Operating Income, or POI, presented in filings prior to the September 30, 2016 Form 10-Q except that Hotel EBITDA also excludes the unallocated hotel and property operations expenses previously included in POI. Hotel EBITDA, as presented, may not be comparable to similarly titled measures of other companies.

Hotel EBITDA is intended to isolate property level operational performance over which the Company's hotel operators have direct control. We believe Hotel EBITDA is helpful to investors as it better communicates the comparability of our hotels' operating results for all of the Company's hotel properties and is used by management to measure the performance of the Company's hotels and the effectiveness of the operators of the hotels.

The following table reconciles net earnings (loss) to EBITDA, Adjusted EBITDA, and Hotel EBITDA for the years ended December 31 (in thousands). All amounts presented include both continuing and discontinued operations as well as our portion of the results of our unconsolidated Atlanta JV.

<b>Reconciliation of Net earnings (loss) to EBITDA, Adjusted EBITDA, and Hotel EBITDA</b>	<b>Year ended December 31,</b>		
	<b>2016</b>	<b>2015</b>	<b>2014</b>
Net earnings (loss)	\$ 23,522	\$ 14,322	\$(16,259)
Interest expense	4,715	5,745	8,256
Interest expense from Atlanta JV	618	—	—
Loss on debt extinguishment	2,187	213	278
Income tax expense	125	—	—
Depreciation and amortization expense	5,190	5,400	6,549
Depreciation and amortization expense from Atlanta JV	377	—	—
<b>EBITDA</b>	<b>36,734</b>	<b>25,680</b>	<b>(1,176)</b>
Net gain on disposition of assets	(23,813)	(7,795)	(2,750)
Net loss on disposition of assets from Atlanta JV	2	—	—
Impairment loss	1,477	3,708	2,921
Net (gain) loss on derivatives and convertible debt	(6,377)	(11,578)	14,430
Net loss on derivatives from Atlanta JV	5	—	—
Acquisitions and terminated transactions expense	550	684	—
Acquisition expense from Atlanta JV	239	—	—
Gain on debt conversion	—	—	(88)
Terminated equity transactions expense	—	246	76
<b>Adjusted EBITDA</b>	<b>8,817</b>	<b>10,945</b>	<b>13,413</b>
General and administrative expense	5,792	5,493	4,192
Other income	(55)	(114)	(28)
Unallocated hotel and property operations expense	467	495	319
<b>Hotel EBITDA</b>	<b>\$ 15,021</b>	<b>\$ 16,819</b>	<b>\$ 17,896</b>
Revenue	\$ 50,653	\$ 61,637	\$ 72,378
JV revenue	2,962	—	—
Condor and Atlanta JV revenue	\$ 53,615	\$ 61,637	\$ 72,378
Hotel EBITDA as a percentage of revenue	28%	27%	25%

## **Liquidity and Capital Resources**

### ***Liquidity Requirements***

We expect to meet our short-term liquidity requirements through net cash provided by operations, existing cash balances and working capital, short-term borrowings under our revolving credit agreement, and the release of restricted cash upon the satisfaction of usage requirements. At December 31, 2016, the Company had \$8.3 million of cash and cash equivalents on hand and \$1.2 million of unused availability under its revolving credit agreement. Subsequent to December 31, 2016, on March 1, 2017, we closed on a new \$90.0 million secured revolving credit facility and drew approximately \$34.25 million under this new credit facility, of which \$1.55 million was used to pay a portion of the reserves and costs related entering into this credit facility, and \$32.7

million was used to repay outstanding borrowings with Great Western Bank, Western Alliance Bank, Morgan Stanley Mortgage Capital Holdings, Cantor Commercial Real Estate Lending and the Huntington National Bank.

Our short-term liquidity requirements consist primarily of operating expenses and other expenditures directly associated with our hotel properties, recurring maintenance and capital expenditures necessary to maintain our hotels in accordance with brand standards, interest expense and scheduled principal payments on outstanding indebtedness, restricted cash funding obligations, and the payment of dividends in accordance with the REIT requirements of the Code and as required in connection with our Series E Preferred Stock. We presently expect to invest approximately \$4.0 million to \$5.0 million in capital expenditures related to hotel properties we currently own through March 31, 2018.

To maintain our REIT tax status, we generally must distribute at least 90% of our taxable income to our shareholders annually. In addition, we are subject to a 4% non-deductible excise tax if the actual amount distributed to shareholders in a calendar year is less than a minimum amount specified under the federal income tax laws. We have a general dividend policy of paying out approximately 100% of annual REIT taxable income. The actual amount of any future dividends will be determined by the Board of Directors based on our actual results of operations, economic conditions, capital expenditure requirements, and other factors that the Board of Directors deems relevant.

Our longer-term liquidity requirements consist primarily of the cost of acquiring additional hotel properties, renovations and other capital expenditures that periodically are made related to our hotel properties, and scheduled debt payments, including maturing loans. Possible sources of liquidity to fund debt maturities and acquisitions and to meet other obligations include additional secured or unsecured debt financings, asset sales and proceeds from public or private issuances of debt or equity securities.

Prior to the consideration of any asset sales or our new \$90.0 million debt facility obtained subsequent to December 31, 2016, contractual principal payments on our debt outstanding, including normal amortization, totaled \$15.8 million through March 31, 2018, including the February 1, 2017 maturity of one of our WAB loans with a balance at December 31, 2016 of \$4.8 million, the November 6, 2017 maturity of our Cantor loan with a balance at December 31, 2016 of \$5.7 million, the December 1, 2017 maturity of our Morgan Stanley loan with a balance at December 31, 2016 of \$0.9 million, and the February 1, 2018 maturity of one of our WAB loans with a balance at December 31, 2016 of \$2.8 million. As discussed further in the Subsequent Events footnote of the consolidated financial statements, on January 27, 2017, the WAB loan due February 1, 2017 was extended to February 1, 2018. Subsequently, on March 1, 2017, each of these loans was repaid in full from borrowings under our new \$90.0 million secured credit facility that matures on March 1, 2019. Following this refinancing, contractual principal payments on our debt outstanding at December 31, 2016 through March 31, 2018 totaled \$1.1 million.

### ***Sources and Uses of Cash***

*Cash provided by Operating Activities.* Our cash provided by operations was \$2.7 million, \$5.0 million, and \$5.5 million for the years ended December 31, 2016, 2015, and 2014, respectively. These changes in operating cash flows were driven by changes in net income, after adjusting for non-cash items, which decreased by \$2.0 million in 2016 from 2015 and decreased by \$0.9 million in 2015 from 2014. Other changes in operating cash flows between the periods were due to miscellaneous changes in property tax and insurance escrow balances and accounts receivable.

*Cash provided by Investing Activities.* Our cash provided by investing activities was \$21.9 million, \$5.4 million, and \$17.9 million for the years ended December 31, 2016, 2015, and 2014, respectively. The lower cash flows in 2015 from the other periods presented was primarily a result of differences in the net cash spent on acquisitions and investment in joint venture less cash received from asset sales which, net, totaled \$26.9 million in 2016, \$10.7 million in 2015, and \$21.3 million in 2014.

*Cash used in Financing Activities.* Our cash used by financing activities was \$21.2 million, \$5.7 million, and \$23.3 million for the years ended December 31, 2016, 2015, and 2014, respectively. This increase in cash flows in 2016 was primarily related to cash received in the first quarter of 2016 related to the Series D Preferred Stock issuance less cash used to redeem the Series A and B Preferred Stock and cash dividends paid on the Series C and Series D Preferred Stock, which together had a net impact to financing cash flows of \$5.1 million, as well as decreased net principal payments on long-term and revolving debt of \$19.0 million as a result of decreased net revolver activity as well as decreased debt repayments required upon the sale of hotel properties. These increases were partially offset with prepayment penalties of \$1.8 million paid in 2016 upon the sale of properties encumbered by certain of the Company's debt. From 2014 to 2015, debt repayments increased due to increased property sales. However, this increase in debt repayments was offset by increased cash inflows for new debt obtained, including the debt obtained in connection with the 2015 acquisitions which totaled \$15.1 million excluding debt assumed.

### **Outstanding Indebtedness**

At December 31, 2016, we had long-term debt of \$57.4 million associated with assets held for use with a weighted average term to maturity of 2.9 years and a weighted average interest rate of 4.89%. Of this total, at December 31, 2016, \$26.1 million is fixed rate debt with a weighted average term to maturity of 2.8 years and a weighted average interest rate of 4.78% and \$31.3 million is variable rate debt with a weighted average term to maturity of 2.9 years and a weighted average interest rate of 4.98%. At December 31, 2015, we had long-term debt of \$45.5 million associated with assets held for use with a weighted average term to maturity of 3.3 years and a weighted average interest rate of 4.98%. Of this total, at December 31, 2015, \$12.5 million is fixed rate debt with a weighted average term to maturity of 1.6 years and a weighted average interest rate of 5.63% and \$33.0 million is variable rate debt with a weighted average term to maturity of 3.9 years and a weighted average interest rate of 4.74%.

Debt is classified as held for sale if the properties collateralizing it are held for sale. Debt associated with assets held for sale is classified in the table below based on its contractual maturity although the balances are expected to be repaid within one year upon the sale of the related hotel properties. Aggregate annual principal payments on debt for the next five years and thereafter are as follows (in thousands):

	<u>Held for sale</u>	<u>Held for use</u>	<u>Total</u>
2017	\$1,574	\$11,333	\$12,907
2018	2,603	12,065	14,668
2019	52	1,120	1,172
2020	1,771	19,199	20,970
2021	—	13,672	13,672
Total	<u>\$6,000</u>	<u>\$57,389</u>	<u>\$63,389</u>

### **Financial Covenants**

The Company's debt agreements contain requirements as to the maintenance of minimum levels of debt service and fixed charge coverage and required loan-to-value and leverage ratios, and place certain restrictions on dividends. As of December 31, 2016, we were in compliance with our financial covenants.

If we fail to pay our indebtedness when due, fail to comply with covenants or otherwise default on our loans, unless waived, we could incur higher interest rates during the period of such loan defaults, be required to immediately pay our indebtedness, and ultimately lose our hotels through lender foreclosure if we are unable to obtain alternative sources of financing with acceptable terms. Our new \$90.0 million secured credit facility contains cross-default provisions which would allow the lender to declare a default and accelerate our indebtedness to them if we default on our other loans and such default would permit that lender to accelerate our indebtedness under any such loan. As of December 31, 2016, we are not in default of any of our loans.



### **Significant Debt Transactions**

During 2016, the Company sold 25 hotel properties for combined gross sales proceeds of \$61.4 million. Net proceeds were used to pay off the associated loans totaling \$37.6 million, to fund acquisitions, to reduce the balance of the revolving credit facility with Great Western Bank, and for general corporate purposes. These dispositions, as well as adjustments required to remain in compliance with the required debt service ratio, decreased the total availability under the Great Western Bank revolver from \$5.7 million at December 31, 2015 to \$1.2 million at December 31, 2016.

On December 14, 2016, the purchase of the Aloft Leawood was financed, in part, with the proceeds of mortgage loans provided by Great Western Bank in an aggregate principal amount of \$15.9 million. The loans require monthly principal and interest payments based on a 25-year amortization (in the case of the \$14.3 million loan) and 7-year amortization (in the case of the \$1.6 million loan), with the principal balances due and payable on December 1, 2021. The term of the loans may be extended for an additional two years subject to interest rate adjustments. The loans bear interest at a fixed rate of 4.33% per annum and are non-recourse, as long as a certain pre-dividend debt service coverage ratio is met and with the exception of losses resulting from fraud, theft, and involuntary bankruptcy.

Additionally, as discussed further in the Subsequent Events footnote to the consolidated financial statements appearing elsewhere in this Annual Report, two significant debt events occurred in early 2017. On January 27, 2017, the WAB loan with a balance of \$4.8 million at December 31, 2016 due February 1, 2017 was extended to February 1, 2018. On March 1, 2017, a significant portion of the Company's debt (including all debt outstanding at December 31, 2016 with the exception of the two variable rate WAB loans and the two fixed rate Great Western Bank loans) was refinanced with borrowings under our new \$90.0 million secured credit facility that matures on March 1, 2019. Following this refinancing, contractual debt maturities related to the debt outstanding at December 31, 2016 were as follows:

	<u>Held for sale</u>	<u>Held for use</u>	<u>Total</u>
2017	\$ —	\$ 916	\$ 916
2018	—	930	930
2019	6,000	27,691	33,691
2020	—	14,180	14,180
2021	—	13,672	13,672
Total	<u>\$6,000</u>	<u>\$57,389</u>	<u>\$63,389</u>

The new credit agreement provides for a \$90.0 million senior secured credit facility and includes an accordion feature that would allow the facility to be increased to \$400.0 million with additional lender commitments. Availability under the facility is based on a borrowing base formula for the pool of hotel properties securing the facility. As of March 1, 2017, the collateral pool consisted of 14 hotel properties and the availability under the facility is \$41.05 million. The facility is guaranteed by the Company and its material subsidiaries that do not have stand-alone financing. Prior to the occurrence of specific capital achievements, borrowings under the facility accrue interest, at the Company's option, at either LIBOR plus 3.95% or a base rate plus 2.95%. Thereafter, borrowings bear interest based on a leverage-based pricing grid, at the Company's option, at either LIBOR plus a spread ranging from 2.25% to 3.00% (depending on leverage) or a base rate plus a spread ranging from 1.25% to 2.00% (depending on leverage). The facility matures in two years and has an automatic one-year extension upon the completion of specific capital achievements, subject to certain conditions. The facility has two additional one-year extension options following additional capital achievements, subject to certain conditions. The facility contains customary representations and warranties, covenants and events of default.

On March 1, 2017, the Company borrowed \$34.3 million under the new credit facility to repay existing indebtedness and pay reserves costs related to the closing of the facility. The Company anticipates using borrowings under the facility, to fund a portion of the purchase price for three out of the four Home2 Suites hotels currently under contract to be acquired, which will be added to the collateral pool for the facility. Borrowings under the facility can also be used for future acquisitions and general corporate purposes.

## Significant Equity Transactions

On March 16, 2016, the Company entered into a series of agreements providing for:

- the issuance and sale of 3,000,000 shares of Series D Cumulative Preferred Stock in a private transaction to SREP for an aggregate purchase price of \$30 million;
- the exchange of all of the outstanding Series C Preferred Stock plus cumulative accrued and unpaid dividends for 3,245,156 shares of Series D Preferred Stock plus cash dividends of \$1.484 million and 6.25% convertible debt of \$1.012 million; and
- the cash redemption of all of the outstanding Series A Preferred Stock and Series B Preferred Stock plus cumulative accrued and unpaid dividends, which was completed on April 15, 2016 for a total redemption price, including related expenses, of \$20.167 million.

In connection with these transactions, the Company and SREP entered into a Stock Purchase Agreement, or Stock Purchase Agreement, dated March 16, 2016 pursuant to which Condor issued and sold 3,000,000 shares of Series D Preferred Stock to SREP on March 16, 2016 for an aggregate purchase price of \$30.0 million. The Stock Purchase Agreement required that \$20.2 million of the purchase price be deposited into an escrow account for the purpose of effecting the redemption of the Series A Preferred Stock and Series B Preferred Stock and that the remaining amount of the purchase price be delivered to Condor.

Simultaneously, the Company entered into an agreement, or Exchange Agreement, with RES pursuant to which all 3,000,000 outstanding shares of Series C Preferred Stock were exchanged for 3,000,000 shares of Series D Preferred Stock. Under the Exchange Agreement, in lieu of payment of accrued and unpaid dividends in the amount of \$4.9 million on the Series C Preferred Stock, Condor (a) paid to RES an amount of cash equal to \$1.5 million, (b) issued to RES 245,156 shares of Series D Preferred Stock and (c) issued to RES a convertible promissory note, bearing interest at 6.25% per annum, in the principal amount of \$1.012 million (such that RES, IRSA, and their affiliates do not beneficially own in excess of 49% of the voting stock of Condor).

Pursuant to the Stock Purchase Agreement, on April 15, 2016, Condor redeemed all of the outstanding Series A and Series B Preferred Stock, in accordance with redemption notices issued on March 16, 2016, as follows:

- all 803,270 outstanding shares of the Series A Preferred Stock at the redemption price of \$10.00 per share plus \$2.084940 per share in accrued and unpaid dividends (plus compounded interest) through the redemption date for a total redemption price of \$9.7 million; and
- all 332,500 outstanding shares of the Series B Preferred Stock at the redemption price of \$25.00 per share plus \$6.354167 per share in accrued and unpaid dividends through the redemption date for a total redemption price of \$10.5 million.

The terms of the convertible promissory note issued to RES provide that RES at its option may at any time elect to convert the note, in whole or part, by notice delivered to the Company, into a number of shares of common stock determined by dividing the principal amount of the note to be converted by \$10.40. Any time the Series E Preferred Stock is required by its terms to be converted into common stock of the Company, the note will be automatically converted into the number of shares of common stock determined by dividing the principal amount of the note to be converted by \$10.40. Any such conversion shall be reduced such that RES, together with its affiliates, does not beneficially own more than 49% of the voting stock of the Company and shall reduce the principal amount of the note proportionally.

The terms of the convertible promissory note and the Series D Preferred Stock are discussed in Note 7, *Convertible Debt at Fair Value*, and Note 10, *Preferred Stock*, to our consolidated financial statements appearing elsewhere in this Annual Report.

Additionally, on January 24, 2017, the Company exchanged 23,160 new warrants, or New Warrants, to purchase common stock of the Company for 576,923 warrants (or Old Warrants, see further discussion in Note 10, *Preferred Stock*, to our consolidated financial statements appearing elsewhere in this Annual Report) held by RES. The number of New Warrants issued in exchange for the Old Warrants equals the number of shares of common stock issuable upon exercise of the Old Warrants pursuant to a cashless exercise provisions of the Old Warrants. The New Warrants are exercisable for 23,160 shares of common stock, have an exercise price of \$.0065 for each common share and expire on January 24, 2019.

As discussed further in the Subsequent Events footnote of the consolidated financial statements appearing elsewhere in this Annual Report, on February 28, 2017, the holders of the Series D Preferred Stock voluntarily converted all of their shares of Series D Preferred Stock into an aggregate of 6,004,957 shares of common stock at a conversion price of \$10.40 per common share pursuant to the terms of the preferred stock. The terms of the Series D Preferred Stock provided for automatic conversion following certain future common stock offerings, and also provided for potential additional payments to the holders depending on the sales price of common stock in the offerings. As a result of the voluntary conversion, the holders are no longer entitled to the potential payments. To induce the holders of the Series D Preferred Stock to voluntarily convert their shares, the Company issued the holders \$9.25 million of a new series of preferred stock, the Series E Preferred Stock.

To maintain our REIT tax status, we generally must distribute at least 90% of our taxable income to our shareholders annually. In addition, we are subject to a 4% non-deductible excise tax if the actual amount distributed to shareholders in a calendar year is less than a minimum amount specified under the federal income tax laws. We have a general dividend policy of paying out approximately 100% of annual REIT taxable income. The actual amount of any future dividends will be determined by the board of directors based on our actual results of operations, economic conditions, capital expenditure requirements, and other factors that the Board of Directors deems relevant.

### Contractual Obligations

Below is a summary of certain contractual obligations as of December 31, 2016 (in thousands):

<u>Contractual obligations</u>	<u>Total</u>	<u>Payments due by period</u>			
		<u>2017</u>	<u>2018-2019</u>	<u>2020-2021</u>	<u>After 2021</u>
Long-term debt including interest (1)	\$64,905	\$13,788	\$16,378	\$34,739	\$—
Corporate office leases	561	156	297	108	—
Total contractual obligations	<u>\$65,466</u>	<u>\$13,944</u>	<u>\$16,675</u>	<u>\$34,847</u>	<u>\$—</u>

- (1) Interest rate payments on our variable rate debt have been estimated using interest rates in effect at December 31, 2016

Long-term debt and lease payments above include only amounts related to properties classified as held for use. Future debt payments, including interest, related to the seven held for sale properties that are expected to be sold within the next 12 months totaling \$6.4 million and future obligations on one land lease related to a held for sale property totaling \$1.8 million are not included in the table above.

We have various standing or renewable contracts with vendors. These contracts are all cancelable with immaterial or no cancellation penalties. Contract terms are generally one year or less. We also have management agreements in place for the management and operation of our hotel properties which requires us to pay management fees to our hotel management companies. See “Our Business and Properties—Business Partners.”

### Inflation

We rely on the performance of our hotels to increase revenues to keep pace with inflation. Generally, our hotel operators possess the ability to adjust room rates daily to reflect the effects of inflation. However, competitive pressures may limit the ability of our management companies to raise room rates.

## **Off Balance Sheet Financing Transactions**

We have not entered into any off balance sheet financing transactions.

## **Critical Accounting Policies**

Our consolidated financial statements have been prepared in conformity with U.S. GAAP, which requires management to make estimates and assumptions that effect the reported amount of assets and liabilities at the date of our financial statements and the reported amounts of revenues and expenses during the reporting period. While we do not believe the reported amounts would be materially different, application of these policies involves the exercise of judgment and the use of assumptions as to future uncertainties and, as a result, actual results could differ from these estimates. We evaluate our estimates and judgments on an ongoing basis. We base our estimates on experience and on various other assumptions that are believed to be reasonable under the circumstances.

Critical accounting policies are those that are both important to the presentation of our financial condition and results of operations and require management's most difficult, complex, or subjective judgments. We have identified the following principal accounting policies that have a material effect on our consolidated financial statements.

### ***Investment in Hotel Properties***

At the time of acquisition, the Company allocates the purchase price of assets to asset classes based on the fair value of the acquired real estate, furniture, fixtures and equipment, and intangible assets, if any, and the fair value of liabilities assumed, including debt. Acquisition date fair values are determined based on replacement costs, appraised values, and estimated fair values using methods similar to those used by independent appraisers including discounted cash flows and capitalization rates. Acquisition costs are expensed as incurred.

The Company's investments in hotel properties are recorded at cost and are depreciated using the straight-line method over an estimated useful life of 15 to 40 years for buildings and improvements and 3 to 12 years for furniture, fixtures, and equipment.

Development and construction costs of properties in development are capitalized including, where applicable, direct and indirect costs, including real estate taxes and interest costs. Development and construction costs and costs of significant improvements, replacements, or renovations are capitalized while costs of maintenance and repairs are expensed as incurred.

On a quarterly basis, the Company reviews the carrying value of each held for use hotel to determine if certain circumstances, known as triggering events, exist indicating impairment to the carrying value of the hotel or that depreciation periods should be modified. These triggering events include a significant change in the cash flows of or a significant adverse change in the business climate for a hotel. If facts or circumstances support the possibility of impairment, the Company will prepare an estimate of the undiscounted future cash flows, without interest charges, of the specific hotel and determine if the investment in such hotel is recoverable based on these undiscounted future cash flows. If the investment is not recoverable based on this analysis, an impairment charge will be taken, if necessary, to reduce the carrying value of the hotel to the hotel's fair value.

### ***Investment in Joint Venture***

If it is determined that we do not have a controlling interest in a joint venture, either through our financial interest in a variable interest entity, or VIE, or through our voting interest in a voting interest entity, or VOE, and we have the ability to provide significant influence, the equity method of accounting is used. Under this method, the investment, originally recorded at cost, is adjusted to recognize our share of net earnings or losses of the

affiliate as they occur, with losses limited to the extent of our investment in, advances to, and commitments to the investee. Pursuant to our Atlanta JV agreement, allocations of profits and losses of our Atlanta JV may be allocated disproportionately to nominal ownership percentages due to specified preferred return rate thresholds.

On an annual basis or at interim periods if events and circumstances indicate that the investment may be impaired, the Company reviews the carrying value of its investment in unconsolidated joint venture to determine if circumstances indicate impairment to the carrying value of the investment that is other than temporary. The investment is considered impaired if its estimated fair value is less than the carrying amount of the investment and that impairment is other than temporary.

### ***Assets Held for Sale and Discontinued Operations***

A hotel is considered held for sale (a) when a contract for sale is entered into, a substantial, nonrefundable deposit has been committed by the purchaser, and sale is expected to occur within one year, or (b) if management has committed to and is actively engaged in a plan sell the property, the property is available for sale in its current condition, and it is probable the sale will be completed within one year. If a hotel is considered held for sale as of the most recent balance sheet presented or was sold in any period presented, the hotel property and the debt it collateralizes are shown as held for sale in all periods presented.

Depreciation of our hotels is discontinued at the time they are considered held for sale. If the fair value of the held for sale property less costs to sell is lower than the carrying value of the hotel, the Company will record an impairment loss. Impairment losses on held for sale properties may be subsequently recovered up to the amount of the cumulative impairment losses taken while the property is held for sale should future revisions to fair value estimates be required. If active marketing ceases or the property no longer meets the criteria to be classified as held for sale, the property is reclassified to held for use and measured at the lower of its (a) carrying amount before the property was classified as held for sale, adjusted for any depreciation expense that would have been recognized had the property been continuously classified as held for use, or (b) its fair value at the date of the subsequent decision not to sell.

Historically, we have presented the results of operations of hotel properties that have been sold or considered held for sale as discontinued operations. In April 2014, the Financial Accounting Standards Board, or FASB, issued Accounting Standards Update (“ASU”) 2014-08, *Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*. The amendments in ASU 2014-08 change the criteria for reporting a discontinued operation and require new disclosures of both discontinued operations and certain other significant disposals that do not meet the definition of a discontinued operation. Only disposals representing a strategic shift in operations that have a major effect on an entity’s operations and financial results should be presented as discontinued operations subsequent to adoption. The Company adopted the pronouncement on October 1, 2014. As a result of this early adoption, only the operations of hotels meeting the criteria to be considered held for sale prior to October 1, 2014 are included in discontinued operations for all periods presented as no individual hotel disposition represents a strategic shift in operations or has a major effect on our operations or financial results.

Gains on the sale of real estate are recognized when a property is sold, provided that the profit is determinable, meaning that collectability of the sales price is reasonably assured or can be estimated, and that the earnings process is complete, meaning that the seller is not obligated to perform significant activities after the sale in order to earn the profit. If these criteria are not met, the timing of the sale is determined based on various criteria related to the terms of the transaction and any continuing involvement in the form of management or financial assistance associated with the property. If the sales criteria are not met, the gain is deferred and the finance, installment, or cost recovery method, as appropriate, is applied until the sales criteria are met. To the extent we sell a property and retain a partial ownership interest in the property, we generally recognize a gain to the extent of the third party ownership interest.

### ***Income Taxes***

The Company qualifies and intends to continue to qualify as a REIT under applicable provisions of the Code. In general, under such Code provisions, a trust which has made the required election and, in the taxable year, meets certain requirements and distributes to its shareholders at least 90% of its REIT taxable income, will not be subject to federal income tax to the extent of the income currently distributed to 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 income tax rates and generally will be unable to re-elect REIT status until the fifth calendar year after the year in which we failed to qualify as a REIT, unless we satisfy certain relief provisions. Even if the Company qualifies for taxation as a REIT, the Company may be subject to certain state and local taxes on its income and property, and to federal income and excise taxes on its undistributed taxable income. Except with respect to the TRS, the Company does not believe that it will be liable for significant federal or state income taxes in future years.

A REIT will incur a 100% tax on the net gain derived from any sale or other disposition of property that the REIT holds primarily for sale to customers in the ordinary course of a trade or business. We do not believe any of our hotels were held primarily for sale in the ordinary course of our trade or business. However, if the Internal Revenue Service, or IRS, were to successfully assert that we held such hotels primarily for sale in the ordinary course of our business, the gain from such sales could be subject to a 100% prohibited transaction tax.

Taxable income from non-REIT activities managed through the TRS, which is taxed as a C-corporation, is subject to federal, state, and local income taxes. We account for the federal income taxes of our TRS using the asset and liability method. Under this method, deferred income taxes are recognized for temporary differences between the financial reporting bases of assets and liabilities of the TRS and their respective tax bases and for operating loss and tax credit carryforwards based on enacted tax rates expected to be in effect when such amounts are realized or settled. However, deferred tax assets are recognized only to the extent that it is more likely than not that they will be realized based on consideration of available evidence, including tax planning strategies and projections for future taxable income over the periods in which the remaining deferred tax assets are deductible. In assessing the realizability of deferred tax assets, the Company considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income.

The Company may recognize a tax benefit from an uncertain tax position when it is more-likely-than-not (defined as a likelihood of more than 50%) that the position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on its technical merits. If a tax position does not meet the more-likely-than-not recognition threshold, despite the Company's belief that its filing position is supportable, the benefit of that tax position is not recognized in the statement of operations. The Company recognizes interest and penalties, as applicable, related to unrecognized tax benefits as a component of income tax expense. The Company recognizes unrecognized tax benefits in the period that the uncertainty is eliminated by either affirmative agreement to the uncertain tax position by the applicable taxing authority or by expiration of the applicable statute of limitations.

### ***New Accounting Pronouncements***

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers*, which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The original updated accounting guidance was effective for annual and interim reporting periods in fiscal years beginning after December 15, 2016, however, in July 2015, the FASB approved a one year delay of the effective date to fiscal years beginning after December 15, 2017. As such, the standard will be effective for the Company on January 1, 2018. The standard permits the use of either the retrospective or cumulative effect transition method. The Company has begun to evaluate each of its revenue streams under the

new model. Based on preliminary assessments, the Company does not expect the adoption of this guidance to materially affect the amount or timing of revenue recognition for revenues from room, food and beverage, and other hotel level sales. Furthermore, for real estate sales to third parties, primarily a result of disposition of real estate in exchange for cash with few contingencies, we do not expect the standard to significantly impact the recognition of or accounting for these sales.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*, which supersedes most existing lease guidance in U.S. GAAP when it becomes effective. ASU 2016-02 requires, among other changes to the lease accounting guidance, lessees to recognize most leases on-balance sheet via a right of use asset and lease liability and additional qualitative and quantitative disclosures. ASU 2016-02 is effective for the Company for annual periods in fiscal years beginning after December 15, 2019, permits early adoption, and mandates a modified retrospective transition method. The Company is required to adopt ASU 2016-02 on January 1, 2020. The Company is evaluating the effect that ASU 2016-02 will have on its consolidated financial statements and related disclosures.

In January 2017, the FASB issued ASU 2017-01, *Business Combinations (Topic 805): Clarifying the Definition of a Business*, which clarifies the definition of a business to assist entities with evaluating whether transactions should be accounted for as acquisitions of assets or business combinations. This standard will be effective for annual periods beginning after December 15, 2017, although early adoption is permitted. We are evaluating the effect of ASU 2017-01 on our consolidated financial statements and related disclosures.

## Quantitative And Qualitative Disclosures About Market Risk

Market risk includes risks that arise from changes in interest rates, foreign currency exchange rates, commodity prices, equity prices, and other market changes that effect market-sensitive instruments. At December 31, 2016, our market risk arises primarily from interest rate risk relating to variable rate borrowings and the market risk related to our convertible debt that fair value will fluctuate following changes in the Company's common stock price or changes in interest rates.

### Interest Rate Sensitivity

We seek to limit the impact of interest rate changes on earnings and cash flows and to lower our overall borrowing costs by closely monitoring our variable rate debt and converting such debt to fixed rates when we deem such conversion advantageous. From time to time, we may enter into interest rate swap agreements or other interest rate hedging agreements. At December 31, 2016, we have an interest rate swap in place which effectively locks the variable interest rate on our Huntington Bank debt (balance of \$7.4 million) at 4.13% and an interest rate cap in place which caps the 30-day LIBOR interest rate on our Latitude debt (December 31, 2016 balance of \$11.1 million) at 1.0%. We do not intend to enter into derivative or interest rate transactions for speculative purposes.

The table below provides information about financial instruments that are sensitive to changes in interest rates. The table presents scheduled maturities, including the amortization of principal and related weighted-average interest rates for the debt maturing in each specified period, excluding \$6.0 million of debt related to hotel properties held for sale (dollars in thousands):

	<u>2017</u>	<u>2018</u>	<u>2019</u>	<u>2020</u>	<u>2021</u>	<u>Total</u>
Fixed rate debt	\$10,700	\$ 545	\$ 569	\$ 593	\$13,672	\$26,079
Average fixed interest rate	5.44%	4.33%	4.33%	4.33%	4.33%	4.78%
Variable rate debt	\$ 633	\$11,520	\$ 551	\$18,606	\$ —	\$31,310
Average variable interest rate	4.53%	6.86%	3.87%	3.87%	— %	4.98%
Total debt	\$11,333	\$12,065	\$1,120	\$19,199	\$13,672	\$57,389
Total average interest rate	5.39%	6.74%	4.10%	3.88%	4.33%	4.89%

At December 31, 2016, approximately 54.9% of our outstanding debt, excluding debt related to hotel properties held for sale, is subject to fixed interest rates or effectively locked with an interest rate swap, while 45.1% of our debt is subject to floating rates. Assuming no increase in the level of our variable debt outstanding at December 31, 2016 and after giving effect to our interest rate swap, if interest rates increased by 1.0% our cash flow related to hotel properties held for use would decrease by approximately \$0.3 million per year.



**AUDITED CONSOLIDATED FINANCIAL STATEMENTS**

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## **Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders  
Condor Hospitality Trust, Inc.:

We have audited the accompanying consolidated balance sheets of Condor Hospitality Trust, Inc. and subsidiaries (the Company) as of December 31, 2016 and 2015, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2016. In connection with our audits of the consolidated financial statements, we have also audited the related financial statement schedule, Schedule III- Real Estate and Accumulated Depreciation. These consolidated financial statements and the financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Condor Hospitality Trust, Inc. and subsidiaries as of December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2016, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

As discussed in note 1 to the consolidated financial statements, the Company has changed its method of accounting for discontinued operations as of October 1, 2014 on a prospective basis due to the adoption of Accounting Standards Update 2014-08.

(signed) KPMG LLP

McLean, Virginia

March 1, 2017, except for note 17, as to which the date is March 16, 2017

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Consolidated Balance Sheet

(In thousands, except share and per share data)

	<u>As of December 31,</u>	
	<u>2016</u>	<u>2015</u>
<b>Assets</b>		
Investment in hotel properties, net	\$ 96,158	\$ 75,899
Investment in unconsolidated joint venture	9,036	—
Cash and cash equivalents	8,326	4,870
Restricted cash, property escrows	5,350	3,776
Accounts receivable, net of allowance for doubtful accounts of \$21 and \$10	1,416	1,169
Prepaid expenses and other assets	1,666	1,832
Investment in hotel properties held for sale, net	18,713	54,800
<b>Total Assets</b>	<u>\$ 140,665</u>	<u>\$ 142,346</u>
<b>Liabilities and Equity</b>		
<b>Liabilities</b>		
Accounts payable, accrued expenses, and other liabilities	\$ 5,823	\$ 5,419
Derivative liabilities, at fair value	8	8,759
Convertible debt, at fair value	1,315	—
Long-term debt, net of deferred financing costs	56,775	44,667
Long-term debt related to hotel properties held for sale, net of deferred financing costs	5,945	41,344
<b>Total Liabilities</b>	69,866	100,189
Redeemable preferred stock:		
10% Series B, 800,000 shares authorized; \$.01 par value, 332,500 shares outstanding, liquidation preference of \$10,182 at December 31, 2015	—	7,662
<b>Equity</b>		
<b>Shareholders' Equity</b>		
Preferred stock, 40,000,000 shares authorized:		
8% Series A, 2,500,000 shares authorized, \$.01 par value, 803,270 shares outstanding, liquidation preference of \$9,485 at December 31, 2015	—	8
6.25% Series C, 3,000,000 shares authorized, \$.01 par value, 3,000,000 shares outstanding, liquidation preference of \$34,492 at December 31, 2015	—	30
6.25% Series D, 6,700,000 shares authorized, \$.01 par value, 6,245,156 shares outstanding, liquidation preference of \$63,427 at December 31, 2016	61,333	—
Common stock, \$.01 par value, 200,000,000 shares authorized; 762,590 and 760,288 shares outstanding	8	8
Additional paid-in capital	118,655	138,428
Accumulated deficit	(112,024)	(105,858)
<b>Total Shareholders' Equity</b>	67,972	32,616
Noncontrolling interest in consolidated partnership (Condor Hospitality Limited Partnership), redemption value of \$2,008 and \$1,197	2,827	1,879
<b>Total Equity</b>	<u>70,799</u>	<u>34,495</u>
<b>Total Liabilities and Equity</b>	<u>\$ 140,665</u>	<u>\$ 142,346</u>

See accompanying notes to consolidated financial statements.

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Consolidated Statement of Operations

(In thousands, except per share data)

	Year ended December 31,		
	2016	2015	2014
<b>Revenue</b>			
Room rentals and other hotel services	\$ 50,647	\$58,714	\$ 58,799
<b>Operating expenses</b>			
Hotel and property operations	37,092	43,367	44,391
Depreciation and amortization	5,190	5,400	6,437
General and administrative	5,792	5,493	4,192
Acquisition and terminated transactions	550	684	—
Terminated equity transactions	—	246	76
Total operating expenses	<u>48,624</u>	<u>55,190</u>	<u>55,096</u>
<b>Operating income</b>	2,023	3,524	3,703
Net gain (loss) on disposition of assets	23,132	4,798	(1)
Equity in loss of joint venture	(244)	—	—
Net gain (loss) on derivatives and convertible debt	6,377	11,578	(14,430)
Other income	55	114	116
Interest expense	(4,710)	(5,522)	(7,116)
Loss on debt extinguishment	(2,187)	(213)	(158)
Impairment loss	(1,477)	(3,829)	(1,269)
Earnings (loss) from continuing operations before income taxes	22,969	10,450	(19,155)
Income tax expense	(125)	—	—
Earnings (loss) from continuing operations	22,844	10,450	(19,155)
Gain from discontinued operations, net of tax	678	3,872	2,896
<b>Net earnings (loss)</b>	23,522	14,322	(16,259)
(Earnings) loss attributable to noncontrolling interest	(727)	(1,197)	23
<b>Net earnings (loss) attributable to controlling interests</b>	22,795	13,125	(16,236)
Dividends declared and undeclared and in kind dividends deemed on preferred stock	(20,748)	(3,632)	(3,452)
<b>Net earnings (loss) attributable to common shareholders</b>	<u>\$ 2,047</u>	<u>\$ 9,493</u>	<u>\$(19,688)</u>
<b>Earnings per Share</b>			
Continuing operations—Basic	\$ 1.82	\$ 8.06	\$ (37.64)
Discontinued operations—Basic	0.85	4.55	4.81
Total—Basic Earnings per Share	<u>\$ 2.67</u>	<u>\$ 12.61</u>	<u>\$ (32.83)</u>
Continuing operations—Diluted	\$ 0.78	\$ (0.98)	\$ (37.64)
Discontinued operations—Diluted	0.13	0.98	4.81
Total—Diluted Earnings per Share	<u>\$ 0.91</u>	<u>\$ —</u>	<u>\$ (32.83)</u>

See accompanying notes to consolidated financial statements.

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Consolidated Statement of Equity

(In thousands)

	Years ended December 31, 2016, 2015, and 2014								
	Shares of preferred stock	Preferred stock	Shares of common Stock	Common stock	Additional paid-in capital	Accumulated Deficit	Total shareholders' equity	Noncontrolling interest	Total equity
<b>Balance at December 31, 2013</b>	<u>3,803</u>	<u>\$ 38</u>	<u>446</u>	<u>\$ 4</u>	<u>\$135,318</u>	<u>\$(102,747)</u>	<u>\$ 32,613</u>	<u>\$ 113</u>	<u>\$ 32,726</u>
Stock-based compensation	—	—	1	—	34	—	34	—	34
Rights offering	—	—	275	3	2,588	—	2,591	—	2,591
Net loss	—	—	—	—	—	(16,236)	(16,236)	(23)	(16,259)
<b>Balance at December 31, 2014</b>	<u>3,803</u>	<u>\$ 38</u>	<u>722</u>	<u>\$ 7</u>	<u>\$137,940</u>	<u>\$(118,983)</u>	<u>\$ 19,002</u>	<u>\$ 90</u>	<u>\$ 19,092</u>
Stock-based compensation	—	—	3	—	143	—	143	—	143
Long-term incentive plan	—	—	—	—	—	—	—	142	142
Issuance of common stock	—	—	35	1	345	—	346	—	346
Issuance of common units	—	—	—	—	—	—	—	450	450
Net income	—	—	—	—	—	13,125	13,125	1,197	14,322
<b>Balance at December 31, 2015</b>	<u>3,803</u>	<u>\$ 38</u>	<u>760</u>	<u>\$ 8</u>	<u>\$138,428</u>	<u>\$(105,858)</u>	<u>\$ 32,616</u>	<u>\$1,879</u>	<u>\$ 34,495</u>
Stock-based compensation	—	—	3	—	134	—	134	—	134
Long-term incentive plan	—	—	—	—	—	—	—	171	171
Issuance of common units	—	—	—	—	—	—	—	50	50
Common dividends declared (\$0.455 per share)	—	—	—	—	—	(347)	(347)	—	(347)
Series D Preferred Stock dividends declared	—	—	—	—	—	(3,090)	(3,090)	—	(3,090)
Redemption of Series A and B Preferred Stock	(803)	(8)	—	—	(7,390)	(5,107)	(12,505)	—	(12,505)
Exchange of Series C and issuance of Series D Preferred Stock	3,245	61,303	—	—	(12,517)	(20,417)	28,369	—	28,369
Net income	—	—	—	—	—	22,795	22,795	727	23,522
<b>Balance at December 31, 2016</b>	<u>6,245</u>	<u>\$61,333</u>	<u>763</u>	<u>\$ 8</u>	<u>\$118,655</u>	<u>\$(112,024)</u>	<u>\$ 67,972</u>	<u>\$2,827</u>	<u>\$ 70,799</u>

See accompanying notes to consolidated financial statements.

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Consolidated Statement of Cash Flows

(In thousands, except share and per share data)

	Year ended December 31,		
	2016	2015	2014
<b>Cash flows from operating activities:</b>			
Net earnings (loss)	\$ 23,522	\$ 14,322	\$(16,259)
Adjustments to reconcile net earnings (loss) to net cash provided by operating activities:			
Depreciation and amortization expense	5,190	5,400	6,549
Net gain on disposition of assets	(23,813)	(7,794)	(2,750)
Net (gain) loss on derivatives and convertible debt	(6,377)	(11,578)	14,430
Equity in loss of joint venture	244	—	—
Amortization of deferred financing costs	597	714	1,292
Amortization of debt discount	—	—	38
Loss on extinguishment of debt	2,187	213	278
Gain on debt conversion	—	—	(88)
Impairment loss	1,477	3,708	2,921
Stock-based compensation and long term incentive plan expense	305	285	34
Amortization of warrant issuance cost	12	58	58
Changes in operating assets and liabilities:			
(Increase) decrease in assets	(244)	442	(63)
Decrease in liabilities	(432)	(800)	(933)
Net cash provided by operating activities	<u>2,668</u>	<u>4,970</u>	<u>5,507</u>
<b>Cash flows from investing activities:</b>			
Additions to hotel properties	(3,446)	(3,853)	(3,034)
Investment in joint venture	(9,280)	—	—
Acquisitions of hotel properties	(22,450)	(42,592)	—
Proceeds from sale of hotel assets	58,593	53,306	21,316
Net changes in capital expenditure escrows	(1,475)	(1,463)	(340)
Net cash provided by investing activities	<u>21,942</u>	<u>5,398</u>	<u>17,942</u>
<b>Cash flows from financing activities:</b>			
Deferred financing costs	(136)	(865)	(485)
Principal payments on long-term debt	(39,965)	(51,868)	(22,207)
Proceeds from long-term debt	15,925	44,620	—
Payments on revolving debt	(10,305)	(39,056)	(30,843)
Proceeds from revolving debt	10,198	41,152	29,692
Debt early extinguishment penalties	(1,752)	—	(120)
Series D Preferred Stock issuance	28,881	—	—
Series A and B Preferred Stock redemption, including accumulated dividends	(20,167)	—	—
Cash dividends paid to common shareholders	(198)	—	—
Cash dividends paid to Series C and D Preferred shareholders	(3,598)	—	—
Proceeds from common stock issued in rights offering	—	346	860
Rights offering issuance costs	—	—	(218)
Other items	(37)	—	—
Net cash used in financing activities	<u>(21,154)</u>	<u>(5,671)</u>	<u>(23,321)</u>

See accompanying notes to consolidated financial statements.

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Consolidated Statements of Cash Flows (continued)

(In thousands, except share and per share data)

	Year ended December 31,		
	2016	2015	2014
Increase in cash and cash equivalents	\$ 3,456	\$ 4,697	\$ 128
Cash and cash equivalents, beginning of year	4,870	173	45
Cash and cash equivalents, end of year	<u>\$ 8,326</u>	<u>\$ 4,870</u>	<u>\$ 173</u>
Supplemental cash flow information			
Interest paid, net of amounts capitalized	\$ 4,229	\$ 5,085	\$ 7,119
Income taxes paid	\$ 37	\$ —	\$ —
<b>Schedule of noncash investing and financing activities:</b>			
Unamortized debt discount	\$ —	\$ —	\$ 113
Convertible loan embedded derivative	\$ —	\$ —	\$ (151)
Debt converted to common stock	\$ —	\$ —	\$(2,000)
Common stock issued on conversion of debt	\$ —	\$ —	\$ 1,950
Debt assumed in acquisitions	\$ —	\$11,220	\$ —
Fair Value of CHLP common units issued in acquisitions	\$ 50	\$ 450	\$ —
In kind dividends deemed on preferred stock	\$20,218	\$ —	\$ —

See accompanying notes to consolidated financial statements.

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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**NOTE 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

***Description of Business***

Condor Hospitality Trust, Inc. (“CDOR,” “Condor,” or the “Company”), which until July 15, 2015 was formerly named Supertel Hospitality, Inc., was incorporated in Virginia on August 23, 1994 and was reincorporated in Maryland on November 19, 2014. CDOR is a self-administered real estate investment trust (“REIT”) for federal income tax purposes that specializes in the investment and ownership of high-quality select-service, limited-service, extended stay, and compact full-service hotels. As of December 31, 2016, the Company owned 19 hotels in 12 states, including one hotel owned through an 80% interest in an unconsolidated joint venture (the “Atlanta JV”).

CDOR, through its wholly owned subsidiary, Condor Hospitality REIT Trust (formerly Supertel Hospitality REIT Trust), owns a controlling interests in Condor Hospitality Limited Partnership (“CHLP”) (formerly Supertel Limited Partnership), for which we serve as general partner. CHLP, including its various subsidiary partnerships, holds substantially all of the Company’s assets (with the exception of the furniture and equipment of 14 properties held by TRS Leasing, Inc.) and conducts all of its operations. At December 31, 2016, the Company owned 97.8% of the common operating units (“common units”) of CHLP with the remaining common units owned by other limited partners and long-term incentive plan unit holders (see Note 12). The Company’s 100% owned E&P Financing Limited Partnership no longer owns any assets or conducts any operations following the sale of its last remaining property in January 2016.

In order for the income from our hotel property investments to constitute “rents from real properties” for purposes of the gross income tests required by the Internal Revenue Service (“IRS”) for REIT qualification, the income we earn cannot be derived from the operation of any of our hotels. Therefore, CHLP and its subsidiaries lease our hotel properties to the Company’s wholly owned taxable REIT subsidiary, TRS Leasing, Inc., and its wholly owned subsidiaries (the “TRS”). The TRS in turn engages third-party eligible independent contractors to manage the hotels. CHLP, the TRS, and their respective subsidiaries are consolidated into the Company’s financial statements.

References to “we,” “our,” and “us” herein refer to Condor Hospitality Trust, Inc., including as the context requires, its direct and indirect subsidiaries.

Historically, as a result of the geographic areas in which we operate, the operations of our hotels have been seasonal in nature. Generally, occupancy rates, revenue, and operating income have been greater in the second and third quarters of the calendar year than in the first and fourth quarters, with the exception of our hotels located in Florida, which experience peak demand in the first and fourth quarters of the year. The results of the hotels acquired in 2015 and 2016 (see Note 3), because of their locations and chain scale, are expected to be less seasonal in nature than our legacy portfolio of assets.

***Basis of Presentation***

The consolidated financial statements have been prepared in accordance with U.S. general accepted accounting principles (“U.S. GAAP”) and include the accounts of the Company, as well as the accounts of CHLP and its subsidiaries and our wholly owned TRS and its subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.



**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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**NOTE 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

***Estimates, Risks, and Uncertainties***

The preparation of the consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that effect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements as well as revenue and expenses recognized during the reporting period. Actual results could differ from those estimates. Because the state of the economy and of the real estate market can significantly impact hotel operational performance and the estimated fair value of our assets, it is possible that the estimates and assumptions that have been utilized in the preparation of the consolidated financial statements could change.

***Investment in Hotel Properties***

At the time of acquisition, the Company allocates the purchase price of assets to asset classes based on the fair value of the acquired real estate, furniture, fixtures, and equipment, and intangible assets, if any, and the fair value of liabilities assumed, including debt. Acquisition date fair values are determined based on replacement costs, appraised values, and estimated fair values using methods similar to those used by independent appraisers including discounted cash flows and capitalization rates. Acquisition costs are expensed as incurred.

The Company's investments in hotel properties are recorded at cost and are depreciated using the straight-line method over an estimated useful life of 15 to 40 years for buildings and improvements and 3 to 12 years for furniture and equipment.

Renovations and/or replacements that improve or extend the life of the hotel properties are capitalized and depreciated over their useful lives. Repairs and maintenance are expensed as incurred.

On a quarterly basis, the Company reviews the carrying value of each held for use hotel to determine if certain circumstances, known as triggering events, exist indicating impairment to the carrying value of the hotel or that depreciation periods should be modified. These triggering events include a significant change in the cash flows of or a significant adverse change in the business climate for a hotel. If facts or circumstances support the possibility of impairment, the Company will prepare an estimate of the undiscounted future cash flows, without interest charges, of the specific hotel and determine if the investment in such hotel is recoverable based on these undiscounted future cash flows. If the investment is not recoverable based on this analysis, an impairment charge will be taken, if necessary, to reduce the carrying value of the hotel to the hotel's fair value.

***Investment in Joint Venture***

If it is determined that we do not have a controlling interest in a joint venture, either through our financial interest in a variable interest entity ("VIE") or through our voting interest in a voting interest entity ("VOE") and we have the ability to provide significant influence, the equity method of accounting is used. Under this method, the investment, originally recorded at cost, is adjusted to recognize our share of net earnings or losses of the affiliate as they occur, with losses limited to the extent of our investment in, advances to, and commitments to the investee. Pursuant to our Atlanta JV agreement, allocations of the profits and losses of our Atlanta JV may be allocated disproportionately to nominal ownership percentages due to specified preferred return rate thresholds.

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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**NOTE 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

Distributions received from a joint venture are classified in the statement of cash flows using the cumulative distributions approach. Distributions are classified as cash inflows from operating activities unless cumulative distributions, including those from prior periods not designated as a return of investment, exceed cumulative recognized equity in earnings of the joint venture. Excess distributions are classified as cash inflows from investing activities as a return of investment.

On an annual basis or at interim periods if events and circumstances indicate that the investment may be impaired, the Company reviews the carrying value of its investment in unconsolidated joint venture to determine if circumstances indicate impairment to the carrying value of the investment that is other than temporary. The investment is considered impaired if its estimated fair value is less than the carrying amount of the investment and that impairment is other than temporary.

***Assets Held for Sale and Discontinued Operations***

A hotel is considered held for sale (a) when a contract for sale is entered into, a substantial, nonrefundable deposit has been committed by the purchaser, and sale is expected to occur within one year, or (b) if management has committed to and is actively engaged in a plan sell the property, the property is available for sale in its current condition, and it is probable the sale will be completed within one year. If a hotel is considered held for sale as of the most recent balance sheet presented or was sold in any period presented, the hotel property and the debt it collateralizes are shown as held for sale in all periods presented.

Depreciation of our hotels is discontinued at the time they are considered held for sale. If the fair value of the held for sale property less costs to sell is lower than the carrying value of the hotel, the Company will record an impairment loss. Impairment losses on held for sale properties may be subsequently recovered up to the amount of the cumulative impairment losses taken while the property is held for sale should future revisions to fair value estimates be required. If active marketing ceases or the property no longer meets the criteria to be classified as held for sale, the property is reclassified to held for use and measured at the lower of its (a) carrying amount before the property was classified as held for sale, adjusted for any depreciation expense that would have been recognized had the property been continuously classified as held for use, or (b) its fair value at the date of the subsequent decision not to sell.

Historically, we have presented the results of operations of hotel properties that have been sold or considered held for sale as discontinued operations. In April 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-08, *Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*. The amendments in ASU 2014-08 change the criteria for reporting a discontinued operation and require new disclosures of both discontinued operations and certain other significant disposals that do not meet the definition of a discontinued operation. Only disposals representing a strategic shift in operations that have a major effect on an entity’s operations and financial results should be presented as discontinued operations subsequent to adoption. The Company adopted the pronouncement on October 1, 2014. As a result of this adoption, only the operations of hotels meeting the criteria to be considered held for sale prior to October 1, 2014 are included in discontinued operations for all periods presented as no individual hotel disposition represents a strategic shift in operations or has a major effect on our operations or financial results.

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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**NOTE 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

Gains on the sale of real estate are recognized when a property is sold, provided that the profit is determinable, meaning that collectability of the sales price is reasonably assured or can be estimated, and that the earnings process is complete, meaning that the seller is not obligated to perform significant activities after the sale in order to earn the profit. If these criteria are not met, the timing of the sale is determined based on various criteria related to the terms of the transaction and any continuing involvement in the form of management or financial assistance associated with the property. If the sales criteria are not met, the gain is deferred and the finance, installment, or cost recovery method, as appropriate, is applied until the sales criteria are met. To the extent we sell a property and retain a partial ownership interest in the property, we generally recognize a gain to the extent of the third party ownership interest.

***Cash and Cash Equivalents***

Cash and cash equivalents includes cash and highly liquid investments with original maturities of three months or less when acquired, and are carried at cost which approximates fair value. The Company maintained a major portion of its deposits with Great Western Bank, a Nebraska Corporation, at December 31, 2016 and with US Bank at December 31, 2015. The balances on deposit at Great Western Bank and US Bank may at times exceed the federal deposit insurance limit, however, management believes that no significant credit risk exists with respect to the uninsured portion of these cash balances.

***Restricted Cash***

Restricted cash consists of cash held in escrow for the replacement of furniture and fixtures or for real estate taxes and property insurance as required under certain loan agreements. For purposes of the statement of cash flows, changes in restricted cash caused by changes in required reserves for real estate taxes or property insurance are shown as operating activities. Changes in restricted cash caused by changes in required reserves for the replacement of furniture and fixtures are shown as investing activities.

***Deferred Financing Cost***

Direct costs incurred in financing transactions are capitalized as deferred financing costs and amortized to interest expense over the term of the related loan using the effective interest method. Deferred financing costs are presented on the balance sheet as a direct deduction from the associated debt liability.

***Derivative Liabilities***

In the normal course of business, the Company is exposed to the effects of interest rate changes, and the Company may enter into derivative instruments including interest rate swaps, caps, and collars to manage or economically hedge interest rate risk. Additionally, prior to the first quarter of 2016, the Company was required to include on the balance sheet certain bifurcated embedded derivative instruments such as conversion features in convertible instruments and certain common stock warrants.

All derivatives recognized by the Company are reported as derivative liabilities on the balance sheet and are adjusted to their fair value at each reporting date. Realized and unrealized gains and losses on derivative

## **Condor Hospitality Trust, Inc. and Subsidiaries**

### Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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#### **NOTE 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

instruments are included in net gain (loss) on derivatives and convertible debt with the exception of realized gains and losses related to interest rate instruments which are included in interest expense on the statement of operations.

#### ***Noncontrolling Interest***

Noncontrolling interest in CHLP represents the limited partners' proportionate share of the equity in the operating partnership and long-term incentive plan ("LTIP") units (see Note 12). Earnings and loss are allocated to noncontrolling interest in accordance with the weighted average percentage ownership of CHLP during the period.

#### ***Revenue Recognition***

Revenue consists of amounts derived from hotel operations, including the sale of rooms, food and beverage, and other ancillary amenities. Revenue from the operation of the hotel properties is recognized when rooms are occupied and services have been rendered. Sales, use, occupancy, and similar taxes collected from customers and remitted to governmental authorities are accounted for on a net basis and therefore are excluded from revenue in the statement of operations.

#### ***Income Taxes***

The Company qualifies and intends to continue to qualify as a REIT under applicable provisions of the Internal Revenue Code (the "Code"), as amended. In general, under such Code provisions, a trust which has made the required election and, in the taxable year, meets certain requirements and distributes to its shareholders at least 90% of its REIT taxable income, will not be subject to federal income tax to the extent of the income currently distributed to 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 income tax rates and generally will be unable to re-elect REIT status until the fifth calendar year after the year in which we failed to qualify as a REIT, unless we satisfy certain relief provisions. Even if the Company qualifies for taxation as a REIT, the Company may be subject to certain state and local taxes on its income and property, and to federal income and excise taxes on its undistributed taxable income. Except with respect to the TRS, the Company does not believe that it will be liable for significant federal or state income taxes in future years.

A REIT will incur a 100% tax on the net gain derived from any sale or other disposition of property that the REIT holds primarily for sale to customers in the ordinary course of a trade or business. We do not believe any of our hotels were held primarily for sale in the ordinary course of our trade or business. However, if the IRS would successfully assert that we held such hotels primarily for sale in the ordinary course of our business, the gain from such sales could be subject to a 100% prohibited transaction tax.

Taxable income from non-REIT activities managed through the TRS, which is taxed as a C-Corporation, is subject to federal, state, and local income taxes. We account for the federal income taxes of our TRS using the asset and liability method. Under this method, deferred income taxes are recognized for temporary differences

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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**NOTE 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

between the financial reporting bases of assets and liabilities of the TRS and their respective tax bases and for operating loss and tax credit carryforwards based on enacted tax rates expected to be in effect when such amounts are realized or settled. However, deferred tax assets are recognized only to the extent that it is more likely than not that they will be realized based on consideration of available evidence, including tax planning strategies and projections for future taxable income over the periods in which the remaining deferred tax assets are deductible. In assessing the realizability of deferred tax assets, the Company considers whether it is more likely than not (defined as a likelihood of more than 50%) that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income.

The Company may recognize a tax benefit from an uncertain tax position when it is more-likely-than-not (defined as a likelihood of more than 50%) that the position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on its technical merits. If a tax position does not meet the more-likely-than-not recognition threshold, despite the Company's belief that its filing position is supportable, the benefit of that tax position is not recognized in the statement of operations. The Company recognizes interest and penalties, as applicable, related to unrecognized tax benefits as a component of income tax expense. The Company recognizes unrecognized tax benefits in the period that the uncertainty is eliminated by either affirmative agreement to the uncertain tax position by the applicable taxing authority or by expiration of the applicable statute of limitations. For the years ended December 31, 2016, 2015, and 2014, the Company did not record any uncertain tax positions.

***Fair Value Measurements***

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements are utilized to determine the value of certain liabilities, to perform impairment assessments, to account for hotel acquisitions, and for disclosure purposes. Fair value measurements are classified into a three-tiered fair value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

Level 1: Inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Directly or indirectly observable inputs other than quoted prices included in Level 1. Level 2 inputs may include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, and model-derived valuations whose inputs are observable.

Level 3: Unobservable inputs for which there is little or no market data, which require a reporting entity to develop its own assumptions.

Our estimates of fair value were determined using available market information and appropriate valuation methods. Considerable judgment is necessary to interpret market data and develop estimated fair value. The use of different market assumptions or valuation techniques may have a material effect on estimated fair value measurements. We classify assets and liabilities in the fair value hierarchy based on the lowest level of input that is significant to the fair value measurement.

## Condor Hospitality Trust, Inc. and Subsidiaries

### Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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#### **NOTE 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

With the exception of fixed rate debt (see Note 8) and other financial instruments carried at fair value, the carrying amounts of the Company's financial instruments approximates their fair values due to their short-term nature or variable market-based interest rates.

##### ***Fair Value Option***

Under U.S. GAAP, the Company has the irrevocable option to report most financial assets and financial liabilities at fair value on an instrument by instrument basis, with changes in fair value reported in net earnings. This option was elected for the treatment of the Company's convertible debt entered into on March 16, 2016 (see Note 7).

##### ***Stock-Based Compensation***

Stock-based compensation for awards with a service condition only is measured based on the fair value of the award on the date of grant and recognized as compensation expense on a straight line basis over the service period. The compensation cost related to awards for which vesting is contingent upon achieving a market based criteria is measured at the fair value of the award on the date of grant, including consideration of the market criteria, and amortized on a straight line basis over the performance period. The fair value of the award at grant is measured using either the closing stock price on the date of grant (for vested and unvested share awards), the Black-Scholes model (for options and warrants), or a Monte Carlo simulation (for LTIP awards), as appropriate. Compensation cost is recognized as additional paid-in capital for awards of the Company's common stock and as noncontrolling interest for LTIP awards of CHLP common units.

##### ***Recently Adopted Accounting Standards***

In November 2014, the FASB issued ASU 2014-16, *Derivatives and Hedging (Topic 815): Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share is More Akin to Debt or to Equity*, which clarifies certain of the criteria for determining whether derivative features in a hybrid financial instrument should be separately recognized. ASU 2014-16 is effective for fiscal years beginning after December 15, 2015 and permits either a retrospective or cumulative effect transition method. ASU 2014-16 was adopted by the Company on January 1, 2016 and was utilized in determining the accounting for the 6.25% Series D Cumulative Convertible Preferred Stock ("Series D Preferred Stock") issued in March 2016 (see Note 10).

In February 2015, the FASB issued ASU No. 2015-02, *Consolidation—Amendments to the Consolidation Analysis*, which amends the current consolidation guidance effecting both the VIE and VOE consolidation models. The standard does not add or remove any of the characteristics in determining if an entity is a VIE or VOE, but rather enhances the way the Company assesses some of these characteristics. The Company adopted this standard on January 1, 2016 and concluded that CHLP now meets the criteria to be considered a VIE of which the Company is the primary beneficiary and, accordingly, the Company continues to consolidate CHLP. The Company's sole significant asset is its investment in CHLP, and consequently, substantially all of the Company's assets and liabilities represent those assets and liabilities of CHLP. All of the Company's debt is an obligation of CHLP. This ASU was also used in the determination of the accounting for the Atlanta JV entered into in August 2016 (see Note 5).

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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**NOTE 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

In April 2015, the FASB issued ASU 2015-03, *Simplifying the Presentation of Debt Issuance Costs*, which requires debt issuance costs to be presented in the balance sheet as a direct deduction from the associated debt liability. The Company adopted this standard on January 1, 2016 and presents all debt issuance costs, other than issuance costs related to its revolving credit facility, as a direct deduction from the carrying value of the debt liability. Adoption of this standard was applied retrospectively for all periods presented, effecting only the presentation of the balance sheet. The adoption of this standard did not have a material impact on the Company's financial position and had no impact on the results of operations or cash flows. For the amounts of the reclassification, see Note 6.

***Recently Issued Accounting Standards***

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers*, which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The original updated accounting guidance was effective for annual and interim reporting periods in fiscal years beginning after December 15, 2016, however, in July 2015, the FASB approved a one year delay of the effective date to fiscal years beginning after December 15, 2017. As such, the standard will be effective for the Company on January 1, 2018. The standard permits the use of either the retrospective or cumulative effect transition method. The Company has begun to evaluate each of its revenue streams under the new model. Based on preliminary assessments, the Company does not expect the adoption of this guidance to materially affect the amount or timing of revenue recognition for revenues from room, food and beverage, and other hotel level sales. Furthermore, for real estate sales to third parties, primarily a result of disposition of real estate in exchange for cash with few contingencies, we do not expect the standard to significantly impact the recognition of or accounting for these sales.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*, which supersedes most existing lease guidance in U.S. GAAP when it becomes effective. ASU 2016-02 requires, among other changes to the lease accounting guidance, lessees to recognize most leases on-balance sheet via a right of use asset and lease liability and additional qualitative and quantitative disclosures. ASU 2016-02 is effective for the Company for annual periods in fiscal years beginning after December 15, 2019, permits early adoption, and mandates a modified retrospective transition method. The Company is required to adopt ASU 2016-02 on January 1, 2020. The Company is evaluating the effect that ASU 2016-02 will have on its consolidated financial statements and related disclosures.

In January 2017, the FASB issued ASU 2017-01, *Business Combinations (Topic 805): Clarifying the Definition of a Business*, which clarifies the definition of a business to assist entities with evaluating whether transactions should be accounted for as acquisitions of assets or business combinations. This standard will be effective for annual periods beginning after December 15, 2017, although early adoption is permitted. The Company is evaluating the effect that ASU 2017-01 will have on its consolidated financial statements and related disclosures.

***Reclassifications***

Certain amounts in prior year financial statements have been reclassified to conform to current year presentation.

Beginning in the first quarter of 2016, we have revised the classification of cash payments for debt prepayment or extinguishment penalties in our statements of cash flows from where they were previously presented as

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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**NOTE 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

operating cash flows to financing cash flows. We have concluded that this classification is preferable as these payments are closely related to other financing cash flows, such as the repayment of debt, and reflect the impact of financing decisions made by management. This revised policy is also consistent with the ASU 2016-15, *Statement of Cash Flows*, which was issued in August 2016 and becomes effective for the Company on January 1, 2018. This revision in classification had the effect of increasing operating cash flows and decreasing financing cash flows by \$1,752, \$0, and \$120 during the years ended December 31, 2016, 2015, and 2014, respectively.

***Liquidity***

The following disclosure and analysis is pursuant to ASU 2014-15, *Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern*. ASU 2014-15 requires the Company to evaluate whether there are conditions and events, considered in the aggregate, that raise substantial doubt about its ability to continue as a going concern within one year after the date the financial statements are issued. To satisfy the requirements of this standard, the Company's evaluation considered a 15 month period beginning January 1, 2017.

We expect to meet our short-term liquidity requirements through net cash provided by operations, existing cash balances and working capital, short-term borrowings under our revolving credit agreement with Great Western Bank, and the release of restricted cash upon the satisfaction of usage requirements. At December 31, 2016, the Company had \$8,326 million of cash and cash equivalents on hand and \$1,234 of unused availability under its revolving credit agreement. Our short-term liquidity requirements consist primarily of operating expenses and other expenditures directly associated with our hotel properties, recurring maintenance and capital expenditures necessary to maintain our hotels in accordance with brand standards, interest expense and scheduled principal payments on outstanding indebtedness, restricted cash funding obligations, and the payment of dividends in accordance with the REIT requirements of the Internal Revenue Code and as required in connection with our Series D Preferred Stock (which, as discussed as a subsequent event (see Note 17), was converted to common stock with \$9,250 of a new class of stock, Series E Preferred Stock, issued on February 28, 2017). We presently expect to invest approximately \$4,000 to \$5,000 in capital expenditures related to hotel properties we currently own through March 31, 2018.

To maintain our REIT tax status, we generally must distribute at least 90% of our taxable income to our shareholders annually. In addition, we are subject to a 4% non-deductible excise tax if the actual amount distributed to shareholders in a calendar year is less than a minimum amount specified under the federal income tax laws. We have a general dividend policy of paying out approximately 100% of annual REIT taxable income. The actual amount of any future dividends will be determined by the Board of Directors based on our actual results of operations, economic conditions, capital expenditure requirements, and other factors that the Board of Directors deems relevant.

Our longer-term liquidity requirements consist primarily of the cost of acquiring additional hotel properties, renovations and other one-time capital expenditures that periodically are made related to our hotel properties, and scheduled debt payments, including maturing loans. Possible sources of liquidity to fund debt maturities and acquisitions and to meet other obligations include additional secured or unsecured debt financings and proceeds from public or private issuances of debt or equity securities.



## Condor Hospitality Trust, Inc. and Subsidiaries

### Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

#### NOTE 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Prior to the consideration of any asset sales or our ability to refinance debt subsequent to December 31, 2016, contractual principal payments on our debt outstanding, including normal amortization, total \$15,788 through March 31, 2018, including the February 1, 2017 maturity of one of our Western Alliance Bank (“WAB”) loans with a balance at December 31, 2016 of \$4,806, the November 6, 2017 maturity of our Cantor loan with a balance at December 31, 2016 of \$5,713, the December 1, 2017 maturity of our Morgan Stanley loan with a balance at December 31, 2016 of \$912, and the February 1, 2018 maturity of one of our WAB loans with a balance at December 31, 2016 of \$2,803. On January 27, 2017, the WAB loan due February 1, 2017 was extended to February 1, 2018. Subsequently, on March 1, 2017, each of these pieces of debt was refinanced with a \$90,000 secured credit facility that matures on March 1, 2019. Following this refinancing, contractual principal payments on our debt outstanding at December 31, 2016 through March 31, 2018 totaled approximately \$1,100.

#### NOTE 2. INVESTMENT IN HOTEL PROPERTIES

Investments in hotel properties consisted of the following at December 31:

	As of December 31,					
	2016			2015		
	Held for sale	Held for use	Total	Held for sale	Held for use	Total
Land	\$ 2,392	\$ 14,020	\$ 16,412	\$ 8,184	\$ 10,683	\$ 18,867
Acquired below market lease intangibles	—	—	—	883	—	883
Buildings, improvements, vehicles	23,118	85,565	108,683	70,932	67,174	138,106
Furniture and equipment	5,427	12,776	18,203	19,170	11,418	30,588
Construction-in-progress	23	63	86	322	133	455
Investment in hotel properties	30,960	112,424	143,384	99,491	89,408	188,899
Less accumulated depreciation	(12,247)	(16,266)	(28,513)	(44,691)	(13,509)	(58,200)
Investment in hotel properties, net	<u>\$ 18,713</u>	<u>\$ 96,158</u>	<u>\$114,871</u>	<u>\$ 54,800</u>	<u>\$ 75,899</u>	<u>\$130,699</u>

#### NOTE 3. ACQUISITION OF HOTEL PROPERTIES

On December 14, 2016, the Company acquired one wholly-owned hotel, the Aloft Leawood / Overland Park (Kansas City). The allocation of the purchase price based on fair value, which was determined using Level 3 fair value inputs, was as follows:

Hotel	Land	Buildings, improvements, and vehicles	Furniture and equipment	Total purchase price	Debt originated at acquisition	Issuance of CHLP common units	Net cash
Aloft Leawood, KS	\$3,339	\$18,046	\$1,115	\$22,500	\$15,925	\$50	\$6,525

The \$22,500 purchase price was funded with the proceeds of two mortgage loans provided by Great Western Bank totaling \$15,925, approximately \$6,525 in cash, and the issuance of 213,904 common units from CHLP with a value of \$50.

## Condor Hospitality Trust, Inc. and Subsidiaries

### Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

#### NOTE 3. ACQUISITION OF HOTEL PROPERTIES (continued)

During 2015, the Company acquired three wholly-owned hotel properties. The allocation of the purchase price based on fair value, which was determined using Level 3 fair value inputs, was as follows:

<u>Hotel</u>	<u>Acquisition date</u>	<u>Land</u>	<u>Building, improvements, and vehicles</u>	<u>Furniture and equipment</u>	<u>Total purchase price</u>	<u>Assumption of debt</u>	<u>Debt originated at acquisition</u>	<u>Issuance of CHLP common units</u>	<u>Net cash</u>
Hotel Indigo									
Atlanta, GA	10/2/2015	\$ 800	\$ 8,700	\$1,500	\$11,000	\$ —	\$ 5,000	\$150	\$ 5,850
Marriott Courtyard									
Jacksonville, FL	10/2/2015	2,100	11,050	850	14,000	—	10,100	150	3,750
SpringHill Suites									
San Antonio, TX	10/1/2015	<u>1,597</u>	<u>14,353</u>	<u>1,550</u>	<u>17,500</u>	<u>11,220</u>	<u>—</u>	<u>150</u>	<u>6,130</u>
Total		<u>\$4,497</u>	<u>\$34,103</u>	<u>\$3,900</u>	<u>\$42,500</u>	<u>\$11,220</u>	<u>\$15,100</u>	<u>\$450</u>	<u>\$15,730</u>

The \$42,500 purchase price was funded with the assumption of one loan with an aggregate outstanding principal balance of \$11,220 and two newly originated GE Capital loans totaling \$15,100 (sold to WAB in April 2016). The remaining \$16,180 was funded with approximately \$14,900 in cash, approximately \$830 of borrowings from the Company's existing credit facility with Great Western Bank, and the issuance of common units from CHLP. A total of 2,298,879 common units were issued with a value of \$450.

There were no hotel acquisitions in 2014.

Included in the statement of operations for the year ended December 31, 2016 and 2015 is total revenue of \$12,786 and \$2,611 and total operating income of \$2,279 and \$356, respectively, which represent the results of operations for these four hotels since the date of acquisition.

#### *Pro Forma Results (Unaudited)*

The following condensed pro forma financial data is presented as if all acquisitions completed during the years ended December 31, 2016 and 2015 (including the Atlanta JV acquisition subsequently discussed (see Note 5)) had been completed on January 1, 2015 and 2014, respectively. The pro forma results below exclude acquisition costs of \$550 and \$684 incurred during the years ended December 31, 2016 and 2015, respectively. The condensed pro forma financial data is not necessarily indicative of what actual results of operations of the Company would have been assuming the acquisitions had been consummated on January 1, 2015 and 2014, nor do they purport to represent the results of operations for future periods.

	<u>Years ended December 31,</u>	
	<u>2016</u>	<u>2015</u>
Total revenue	\$56,741	\$73,281
Operating income	\$ 3,970	\$ 6,774
Net Income attributable to common shareholders	\$ 3,755	\$10,816
Net Income per share available to common shareholders-basic	\$ 4.94	\$ 14.36
Net Income per share available to common shareholders-diluted	\$ 1.23	\$ 0.32

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

**NOTE 4: DISPOSITION OF HOTEL PROPERTIES AND DISCONTINUED OPERATIONS**

As of December 31, 2016, the Company had seven hotels classified as held for sale. At the beginning of 2016, the Company had 16 hotels held for sale and during the year classified an additional 16 hotels as held for sale. Twenty-five of these hotels were sold during 2016. None of the hotels reclassified as held for sale since the Company's adoption of ASU 2014-08 on October 1, 2014 represent a strategic shift that has (or will have) a major effect on the entity's operations and financial results. As a result, only hotels classified as held for sale prior to October 1, 2014 (excluding those subsequent reclassified as held for use), none of which remain unsold at December 31, 2016, are included in discontinued operations with all other hotels, including those subsequently sold or classified as held for sale, reported in continuing operations.

In 2016, 2015, and 2014, the Company sold 25 hotels, 17 hotels, and 13 hotels, respectively, resulting in total gains of \$24,256, \$7,759, and \$2,749, respectively, of which \$23,575, \$4,996, and \$0, respectively, was included in continuing operations.

Included in these 2015 sales were two hotels in Alexandria, Virginia that were sold on July 13, 2015 for a combined gross sales price of \$19,000. These hotels represent a significant disposition, and as such, their operating results are disclosed. The Alexandria Comfort Inn and Days Inn hotels had combined net earnings (loss) of (\$665) and \$761 for the years ended December 31, 2015 and 2014, respectively. Net earnings for the year ended December 31, 2015 includes impairment expense of \$1,020 which was recognized following the hotels classification as held for sale. Earnings attributable to noncontrolling interest related to these properties for the years ended December 31, 2015 and 2014 were \$3 and \$1, respectively.

The Company allocates interest expense to discontinued operations for debt that is to be assumed or that is required to be repaid as a result of the disposal transaction. The following table sets forth the components of discontinued operations for the years ended December 31, 2016, 2015 and 2014:

	<u>Year ended December 31,</u>		
	<u>2016</u>	<u>2015</u>	<u>2014</u>
Revenue	\$ 6	\$ 2,923	\$ 13,579
Hotel and property operations expense	(4)	(1,946)	(10,410)
Depreciation and amortization expense	—	—	(112)
General and administrative expense	—	—	—
Net gain on dispositions of assets	681	2,997	2,751
Interest expense	(5)	(223)	(1,140)
Loss on extinguishment of debt	—	—	(120)
Impairment recovery (loss)	—	121	(1,652)
	<u>\$678</u>	<u>\$ 3,872</u>	<u>\$ 2,896</u>
Capital expenditures	<u>\$—</u>	<u>\$ 90</u>	<u>\$ 338</u>

## Condor Hospitality Trust, Inc. and Subsidiaries

### Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

#### NOTE 5. INVESTMENT IN UNCONSOLIDATED JOINT VENTURE

On August 1, 2016, the Company entered into a joint venture with Three Wall Capital LLC and certain of its affiliates (“TWC”) to acquire a 254-room Aloft hotel in downtown Atlanta, Georgia. The Company accounts for the Atlanta JV under the equity method. Condor owns 80% of the Atlanta JV with TWC owning the remaining 20%. The Atlanta JV is comprised of two companies: Spring Street Hotel Property II LLC, of which CHLP indirectly owns an 80% equity interest, and Spring Street Hotel OpCo II LLC, of which our TRS indirectly owns an 80% equity interest. TWC owns the remaining 20% equity interest in these two companies.

On August 22, 2016, the Atlanta JV closed on the acquisition of the Atlanta Aloft for a purchase price of \$43,550, subject to working capital and similar adjustments. The purchase price was allocated by the Atlanta JV based on fair value, which was determined using Level 3 fair value inputs, as documented in the table below:

<u>Hotel</u>	<u>Land</u>	<u>Buildings, improvements, and vehicles</u>	<u>Furniture and equipment</u>	<u>Land option (1)</u>	<u>Total purchase price</u>	<u>Debt originated at acquisition</u>	<u>Net cash</u>
Aloft Atlanta, GA	\$13,025	\$34,048	\$2,667	\$(6,190)	\$43,550	\$33,750	\$9,800

- (1) The purchase agreement includes a provision which permits the seller to purchase the surface parking lot north of the hotel exercisable for ten years at less than market rates

The purchase price for the Atlanta Aloft was paid with \$9,800 in cash, of which \$7,840 was contributed by Condor and \$1,960 was contributed by TWC, and \$33,750 of proceeds from a term loan secured by the property. Condor additionally contributed \$1,440 and TWC additionally contributed \$360 to the Atlanta JV to cover acquisition costs and to provide working capital to the entity. The term loan, obtained from LoanCore Capital Credit REIT LLC, has an initial term of 24 months with three 12-month extension periods which may be exercised at the Atlanta JV’s option subject to certain conditions and fees. The interest rate is a floating rate calculated on the one-month LIBOR plus 5.0%, and as a condition to closing, the Atlanta JV purchased a LIBOR cap of 3.0%. The current interest rate on the loan is 5.75%. The loan is non-recourse to the Atlanta JV, subject to specified exceptions. The loan is also non-recourse to Condor, except for certain customary carve-outs which are guaranteed by the Company.

Under the Atlanta JV agreement, the Atlanta JV is managed by TWC in accordance with business plans and budgets approved by both partners. Major decisions as detailed in the agreement also require joint approval. Condor may remove TWC as manager of the Atlanta JV and appoint a new manager only upon the occurrence of certain events. The Atlanta Aloft hotel is managed by Boast Hotel Management Company LLC (“Boast”), an affiliate of TWC. The Atlanta JV paid to Boast total management fees of \$110 during the year ended December 31, 2016.

Net cash flow and profits from the Atlanta JV will be distributed each fiscal year first with a 10% preferred return on capital contributions to Condor, second with a 10% preferred return on capital contributions to TWC, and third with any remainder distributed to the partners based on their pro-rata equity ownership. Losses are allocated based on pro-rata equity ownership. The Atlanta JV agreement also includes buy-sell rights for both members (generally after three years of hotel ownership for Condor and after five years for TWC) and Condor has a purchase option for TWC’s Atlanta JV ownership interest exercisable between the third and fifth anniversary of the hotel closing.

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

**NOTE 5. INVESTMENT IN UNCONSOLIDATED JOINT VENTURE (continued)**

The following tables represent the total assets, liabilities, equity, and components of net income (loss), including the Company's share, of the Atlanta JV as of and for the year ended December 31, 2016:

	<u>As of December 31, 2016</u>
Investment in hotel properties, net	\$49,305
Cash and cash equivalents	1,184
Restricted cash, property escrows	464
Accounts receivable, prepaid expenses, and other assets	<u>320</u>
<b>Total Assets</b>	<u><u>\$51,273</u></u>
Accounts payable, accrued expenses, and other liabilities	\$ 633
Land option liability	6,190
Long-term debt, net of deferred financing costs	<u>33,155</u>
<b>Total Liabilities</b>	39,978
Condor equity	9,036
TWC equity	<u>2,259</u>
<b>Total Equity</b>	<u>11,295</u>
<b>Total Liabilities and Equity</b>	<u><u>\$51,273</u></u>
	<u>Year ended December 31, 2016</u>
<b>Revenue</b>	
Room rentals and other hotel services	\$3,703
<b>Operating Expenses</b>	
Hotel and property operations	2,457
Depreciation and amortization	471
Acquisition	<u>299</u>
Total operating expenses	<u>3,227</u>
<b>Operating income</b>	476
Net loss on disposition of assets	(2)
Net loss on derivative	(6)
Interest expense	<u>(773)</u>
<b>Net loss</b>	<u><u>\$ (305)</u></u>
Condor allocated loss	\$ (244)
TWC allocated loss	<u>(61)</u>
<b>Net loss</b>	<u><u>\$ (305)</u></u>

## Condor Hospitality Trust, Inc. and Subsidiaries

### Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

#### NOTE 6. LONG-TERM DEBT

Long-term debt, including debt related to hotel properties held for sale, consisted of the following loans payable at December 31:

Lender	Balance at December 31, 2016	Interest rate at December 31, 2016	Maturity	Amortization provision	Properties encumbered at December 31, 2016	Balance at December 31, 2015
<b>Fixed rate debt</b>						
Western Alliance Bank	\$ 4,806	7.17%	02/2017	15 years	2	\$ 10,819
Western Alliance Bank	2,803	4.75%	02/2018	15 years	2	3,864
Cantor Commercial Real Estate Lending	5,713	4.25%	11/2017	30 years	1	5,826
Morgan Stanley Mortgage Capital Holdings, LLC	912	5.83%	12/2017	25 years	4	27,542
Great Western Bank (7)	14,326	4.33%	12/2021	25 years	1	—
Great Western Bank (7)	1,599	4.33%	12/2021	7 years	—	—
Total fixed rate debt	30,159					48,051
<b>Variable rate debt</b>						
Great Western Bank (6)	—	4.75% (1)	06/2018	Interest only	2	3,215
Western Alliance Bank	4,882	4.18% (2)	11/2020	25 years	1	4,990
Western Alliance Bank	9,863	4.18% (2)	11/2020	25 years	1	10,079
The Huntington National Bank LMREC 2015—CREI, Inc. (Latitude)	7,361	2.87% (3)	11/2020	25 years	3	9,981
	11,124	7.00% (4)	05/2018	\$12 monthly (5)	1	11,220
Total variable rate debt	33,230				18	39,485
Total long-term debt	\$63,389					\$ 87,536
Less: Deferred financing costs	(669)					(1,525)
Total long-term debt, net of deferred financing costs	62,720					86,011
Less: Long-term debt related to hotel properties held for sale, net of deferred financing costs of \$55 and \$736	(5,945)					(41,344)
Long-term debt related to hotel properties held for use, net of deferred financing costs of \$614 and \$789	\$56,775					\$ 44,667

(1) Prime rate plus 1%; was fixed rate debt at 4.5% prior to amendment on June 5, 2015

(2) 90-day LIBOR plus 3.25%

(3) 30-day LIBOR plus 2.25%, fixed at 4.13% after giving effect to interest rate swap

(4) 30-day LIBOR plus 6.25% 30-day LIBOR capped at 1.0% after giving effect to market rate cap (see Note 8)

(5) \$12 monthly payment began May 2016

(6) Total availability under this revolving credit facility was \$1,234 at December 31, 2015; commitment fee on unused facility is 0.25%

(7) Both loans are collateralized by Aloft Leawood

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

**NOTE 6. LONG-TERM DEBT (continued)**

At December 31, 2016, we had long-term debt of \$57,389 associated with assets held for use with a weighted average term to maturity of 2.9 years and a weighted average interest rate of 4.89%. Of this total, at December 31, 2016, \$26,079 is fixed rate debt with a weighted average term to maturity of 2.8 years and a weighted average interest rate of 4.78% and \$31,310 is variable rate debt with a weighted average term to maturity of 2.9 years and a weighted average interest rate of 4.98%. At December 31, 2015, we had long-term debt of \$45,455 associated with assets held for use with a weighted average term to maturity of 3.3 years and a weighted average interest rate of 4.98%. Of this total, at December 31, 2015, \$12,439 is fixed rate debt with a weighted average term to maturity of 1.6 years and a weighted average interest rate of 5.63% and \$33,016 is variable rate debt with a weighted average term to maturity of 3.9 years and a weighted average interest rate of 4.74%.

Debt is classified as held for sale if the properties collateralizing it are held for sale. Debt associated with assets held for sale is classified in the table below based on its contractual maturity although the balances are expected to be repaid within one year upon the sale of the related hotel properties. Aggregate annual principal payments on debt for the next five years and thereafter are as follows:

	<u>Held for sale</u>	<u>Held for use</u>	<u>Total</u>
2017	\$1,574	\$11,333	\$12,907
2018	2,603	12,065	14,668
2019	52	1,120	1,172
2020	1,771	19,199	20,970
2021	—	13,672	13,672
Total	<u>\$6,000</u>	<u>\$57,389</u>	<u>\$63,389</u>

As discussed further in the Subsequent Events footnote (see Note 17), on January 27, 2017, the WAB loan with a balance of \$4,806 at December 31, 2016 due February 1, 2017 was extended to February 1, 2018. On March 1, 2017 a significant portion of the Company's debt (including all debt outstanding at December 31, 2016 with the exception of the two variable rate WAB loans and the two fixed rate Great Western Bank loans) was refinanced with a \$90,000 secured credit facility that matures on March 1, 2019.

***Financial Covenants***

The Company's debt agreements contain requirements as to the maintenance of minimum levels of debt service and fixed charge coverage and required loan-to-value and leverage ratios, and place certain restrictions on dividends. As of December 31, 2016, we were in compliance with our financial covenants.

If we fail to pay our indebtedness when due, fail to comply with covenants or otherwise default on our loans, unless waived, we could incur higher interest rates during the period of such loan defaults, be required to immediately pay our indebtedness, and ultimately lose our hotels through lender foreclosure if we are unable to obtain alternative sources of financing with acceptable terms. Our Great Western Bank and certain of our WAB facilities contain cross-default provisions which would allow Great Western Bank and WAB to declare a default

## Condor Hospitality Trust, Inc. and Subsidiaries

### Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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#### **NOTE 6. LONG-TERM DEBT (continued)**

and accelerate our indebtedness to them if we default on our other loans and such default would permit that lender to accelerate our indebtedness under any such loan. As of December 31, 2016, we are not in default of any of our loans.

##### ***2014 Convertible Loan***

On January 9, 2014, we entered into an unsecured convertible loan agreement with Real Estate Strategies, L.P. (“RES”), for a revolving line of credit of up to \$2,000 with an annual interest rate equal to LIBOR plus 7%. During the first quarter of 2014, the Company borrowed the full amount of \$2,000 available under the loan agreement.

Upon issuance, it was determined that the conversion feature should be bifurcated from its host instrument and accounted for as a freestanding derivative liability as there was no explicit limit to the number of shares to be delivered upon settlement of the conversion option. The initial fair value of the conversion feature was determined to be \$151 and was recorded as a derivative liability with the offset recorded as a debt discount against the convertible loan.

RES applied the amount owed to it under the loan to purchase 192,307 shares of newly issued common stock. On June 11, 2014, the effective purchase date, \$1,950, the fair value of the shares issued, was recorded in equity, and a gain of \$88 was recorded in other income to reflect the change in fair value from March 31, 2014 to the date of conversion of the convertible loan, amortized debt discount, and the separately accounted for embedded derivative.

#### **NOTE 7: CONVERTIBLE DEBT AT FAIR VALUE**

As part of an agreement entered into on March 16, 2016 (the “Exchange Agreement”) with RES (see Note 10), the Company issued to RES a Convertible Promissory Note (the “Note”), bearing interest at 6.25% per annum, in the principal amount of \$1,012. If the Series D Preferred Stock is outstanding, RES at its option may at any time elect to convert the Note, in whole or part, by notice delivered to the Company, into a number of shares of Series D Preferred Stock determined by dividing the principal amount of the Note to be converted by \$10.00. Any time the Series D Preferred Stock is required by its terms to be converted into common stock of the Company (see Note 10), the Note will be automatically converted into the number of shares of common stock that RES would have received had RES converted this Note into Series D Preferred Stock immediately prior to the conversion of the Series D Preferred Stock. Any such conversion shall be reduced such that RES, together with its affiliates, does not beneficially own more than 49% of the voting stock of the Company and shall reduce the principal amount of the Note proportionally.

The Company has made an irrevocable election to record this Note in its entirety at fair value utilizing the fair value option available under U.S. GAAP in order to more accurately reflect the economic value of this Note. As such, gains and losses on the Note are included in net gain (loss) on derivatives and convertible debt within net earnings each reporting period. Losses related to this Note were recognized totaling \$303 during the year ended December 31, 2016. The fair value of the Note is determined using a Monte Carlo simulation model. The Monte Carlo simulation method is a generally accepted statistical method used to generate a defined number of stock price paths in order to develop a reasonable estimate of the range of future expected stock prices of the Company



**Condor Hospitality Trust, Inc. and Subsidiaries**  
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(In thousands, except share and per share data)

**NOTE 7: CONVERTIBLE DEBT AT FAIR VALUE (continued)**

and its peer group and minimize standard error. The fair value of the Note on the date of issuance was determined to be equal to its principal amount. Interest expense related to this Note is recorded separately from other changes in its fair value within interest expense each period.

The following table represents the difference between the fair value and the unpaid principal balance of the Note as of December 31, 2016:

	Fair value as of December 31, 2016	Unpaid principal balance as of December 31, 2016	Fair value carrying amount over/(under) unpaid principal
6.25% Convertible Debt	\$1,315	\$1,012	\$303

**NOTE 8: FAIR VALUE MEASUREMENTS AND DERIVATIVE INSTRUMENTS**

Our determination of fair value measurements is based on the assumptions that market participants would use in pricing the asset or liability. At December 31, 2016, the Company's convertible debt (see Note 7) and certain derivative instruments were the only financial instruments measured in the financial statements at fair value on a recurring basis. Nonrecurring fair value measurements were utilized in the determination of the fair value of acquired hotel properties and related assumed debt in 2016 and 2015 (see Note 3), the acquisition accounting performed by the Atlanta JV in 2016 (see Note 5), the accounting for the equity transactions that occurred in March 2016 (see Note 10), and in the valuation of impaired hotels during the years ended December 31, 2016, 2015, and 2014.

***Derivative Instruments***

Currently, the Company uses derivatives, such as interest rate swaps and caps, to manage its interest rate risk. The fair value of interest rate positions is determined using the standard market methodology of netting the discounted expected future cash receipts and payments. Variable interest rates used in the calculation of projected receipts and payments on the positions are based on an expectation of future interest rates derived from observable market interest rate curves and volatilities. Derivatives expose the Company to credit risk in the event of non-performance by the counterparties under the terms of the agreements. The Company believes it minimizes this credit risk by transacting with major creditworthy financial institutions. These interest rate positions at December 31, 2016 and 2015 are as follows:

Associated debt	Type	Terms	Effective Date	Maturity Date	Notional amount at December 31, 2016	Notional amount at December 31, 2015
Huntington	Swap	Swaps 30-day LIBOR + 2.25% for fixed rate of 4.13 %; cancellable at Company's option anytime after 11/01/2018 without penalty	11/2015	11/2020	\$ 7,361 (1)	\$ 9,981 (1)
Latitude	Cap	Caps 30-day LIBOR at 1.0%	03/2016	06/2017	\$ 11,124 (1)	\$ —
Latitude	Cap	Caps 30-day LIBOR at 2.5%	10/2015	05/2016	\$ —	\$ 11,220 (1)

(1) Notional amounts amortize consistently with the principal amortization of the associated loans

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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**NOTE 8: FAIR VALUE MEASUREMENTS AND DERIVATIVE INSTRUMENTS (continued)**

Additionally, prior to the execution of the Exchange Agreement (see Note 10) on March 16, 2016 which extinguished the instrument, the Company was required to bifurcate and include on the balance sheet at fair value the embedded conversion option in the 6.25% Series C Cumulative Convertible Preferred Stock (“Series C Preferred Stock”) due to the presence of an antidilution provision that required an adjustment in the common stock conversion ratio should subsequent issuances of the Company’s common stock be issued below the instrument’s original conversion price of \$52.00 per share. As a result of a subscription rights offering by the Company which concluded on June 6, 2014 (see Note 9), the conversion price of the Series C Preferred Stock, pursuant to its terms, was adjusted to \$10.40, the exercise price of the subscription rights for a share of common stock, where the conversion price remained until the instrument’s extinguishment.

Similarly, prior to the execution of the Exchange Agreement, the terms of the common stock warrants issued to the holders of the Series C Preferred Stock (see Note 10) also included an antidilution provision that required a reduction in the warrant’s exercise price of \$62.40 should the conversion ratio of the Series C Preferred Stock be adjusted due to antidilution provisions. Accordingly, the warrants did not qualify for equity classification, and, as a result, the fair value of the derivative was shown as a derivative liability on the balance sheet. As a result of a subscription rights offering by the Company which concluded on June 6, 2014 (see Note 9), the exercise price of the warrants for a share of common stock was adjusted to \$12.48, equal to 120% of the adjusted conversion price of the Series C Preferred Stock. With the execution of the Exchange Agreement, this provision of these warrants was effectively eliminated and the conversion price was locked permanently at \$12.48. Following this modification of terms, the warrants qualify for equity classification and were reclassified to additional paid-in capital at their fair value of \$611 on the date of the modification.

The fair value of the derivative liabilities recognized in connection with the Series C Preferred Stock was determined using the Monte Carlo simulation method.

All derivatives recognized by the Company are reported as derivative liabilities on the balance sheet and are adjusted to their fair value at each reporting date. All gains and losses on derivative instruments are included in net gain (loss) on derivatives and convertible debt and with the exception of realized gains and losses related to the interest rate instruments, which are included in interest expense on the statements of operations. Net gains (losses) of \$6,680, \$11,578, and (\$14,430) were recognized related to derivative instruments for the years ended December, 2016, 2015, and 2014, respectively.

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

**NOTE 8: FAIR VALUE MEASUREMENTS AND DERIVATIVE INSTRUMENTS (continued)**

***Recurring Fair Value Measurements***

The following tables provide the fair value of the Company's financial liabilities carried at fair value and measured on a recurring basis:

There were no transfers between levels during the years ended December 31, 2016, 2015, or 2014.

	<u>Fair value at December 31, 2016</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Interest rate derivative	\$ 8	\$—	\$ 8	\$ —
Convertible debt	1,315	—	—	1,315
	<u>\$1,323</u>	<u>\$—</u>	<u>\$ 8</u>	<u>\$1,315</u>
	<u>Fair value at December 31, 2015</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Series C preferred embedded derivative	\$6,271	\$—	\$—	\$6,271
Warrant derivative	2,411	—	—	2,411
Interest rate derivatives	77	—	77	—
	<u>\$8,759</u>	<u>\$—</u>	<u>\$ 77</u>	<u>\$8,682</u>

The following table presents a reconciliation of the beginning and ending balances of items measured at fair value on a recurring basis that use significant unobservable inputs (Level 3) and the related gains and losses recorded in the statement of operations during the periods:

	<u>Year ended December 31,</u>						
	<u>2016</u>				<u>2015</u>		
	<u>Series C Preferred embedded derivative</u>	<u>RES warrant derivative</u>	<u>Convertible debt</u>	<u>Total</u>	<u>Series C Preferred embedded derivative</u>	<u>RES warrant derivative</u>	<u>Total</u>
Fair value, beginning of period	\$ 6,271	\$ 2,411	\$ —	\$ 8,682	\$13,804	\$ 6,533	\$ 20,337
Net (gains) losses recognized in earnings	(4,848)	(1,800)	303	(6,345)	(7,533)	(4,122)	(11,655)
Purchase and issuances	—	—	1,012	1,012	—	—	—
Sales and settlements	(1,423)	—	—	(1,423)	—	—	—
Gross transfers into Level 3	—	—	—	—	—	—	—
Gross transfers out of Level 3 (1)	—	(611)	—	(611)	—	—	—
Fair value, end of period	<u>\$ —</u>	<u>\$ —</u>	<u>\$1,315</u>	<u>\$ 1,315</u>	<u>\$ 6,271</u>	<u>\$ 2,411</u>	<u>\$ 8,682</u>
Total unrealized (gains) losses during the period included in earnings related to instruments held at end of period	\$ —	\$ —	\$ 303	\$ 303	\$ (7,533)	\$ (4,122)	\$ (11,655)

(1) RES warrants were permanently reclassified to additional paid-in capital as discussed above

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(In thousands, except share and per share data)

**NOTE 8: FAIR VALUE MEASUREMENTS AND DERIVATIVE INSTRUMENTS (continued)**

***Fair Value of Debt***

The Company estimates the fair value of its fixed rate debt by discounting the future cash flows of each instrument at estimated market rates or credit spreads consistent with the maturity of debt obligations with similar credit policies. Credit spreads take into consideration general market conditions and maturity. The inputs utilized in estimating the fair value of debt are classified in Level 2 of the fair value hierarchy. The carrying value, net of deferred financing costs, and estimated fair value of the Company's debt, excluding convertible debt, which is presented in the balance sheet at fair value, is presented in the table below:

	Carrying value at December 31,		Estimated fair value at December 31,	
	2016	2015	2016	2015
Held for use	\$56,775	\$44,667	\$57,456	\$45,771
Held for sale	5,945	41,344	6,433	43,508
Total	<u>\$62,720</u>	<u>\$86,011</u>	<u>\$63,889</u>	<u>\$89,279</u>

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**NOTE 8: FAIR VALUE MEASUREMENTS AND DERIVATIVE INSTRUMENTS (continued)**

***Impaired Hotel Properties***

In the performance of impairment analysis for both held for sale and held for use properties, fair value is determined with the assistance of independent real estate brokers and through the use of revenue multiples based on the Company's experience with hotel sales as well as available industry information. For held for sale properties, estimated selling costs are based on our experience with similar asset sales. These are considered Level 3 inputs. All impairment in the table below related to held for use properties relates to impairments taken when those properties were previously held for sale or upon their reclassification to held for use. The amount of impairment and recovery of previously recorded impairment recognized in the years ended December 31, 2016, 2015, and 2014 is shown in the table below:

	2016		Year ended December 31, 2015		2014	
	Number of hotels	Impairment (loss) recovery	Number of hotels	Impairment (loss) recovery	Number of hotels	Impairment (loss) recovery
<b>Continuing Operations:</b>						
<b>Held for sale hotels:</b>						
Impairment loss	4	\$(1,273)	—	\$ —	—	\$ —
<b>Sold hotels:</b>						
Impairment loss	1	(204)	6	(3,914)	2	(1,388)
Recovery of impairment	—	—	1	85	1	119
Net impairment loss reported in continuing operations	<u>5</u>	<u>\$(1,477)</u>	<u>7</u>	<u>\$(3,829)</u>	<u>3</u>	<u>\$(1,269)</u>
<b>Discontinued Operations:</b>						
<b>Sold hotels:</b>						
Impairment loss	—	\$ —	1	\$ (117)	8	\$(2,450)
Recovery of impairment	—	—	3	238	5	798
Net impairment loss reported in discontinued operations	<u>—</u>	<u>\$ —</u>	<u>4</u>	<u>\$ 121</u>	<u>13</u>	<u>\$(1,652)</u>
Total net impairment:	<u>5</u>	<u>\$(1,477)</u>	<u>11</u>	<u>\$(3,708)</u>	<u>16</u>	<u>\$(2,921)</u>

**NOTE 9. COMMON STOCK**

The Company's common stock is duly authorized, full paid, and non-assessable.

On March 11, 2015, an executive officer exercised a warrant to purchase 35,060 shares at the price of \$9.88 per share (see Note 12).

The Company concluded a subscription rights offering on June 6, 2014. Each subscription right entitled its holder to purchase one share of common stock of the Company for \$10.40 per share. Subscription rights to purchase 274,954 shares of common stock were exercised for \$2,860, of which \$2,000 was paid by the conversion of a loan owed by the Company to RES (see Note 6). The Company incurred issuance costs of \$218.

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

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**NOTE 10. PREFERRED STOCK**

On March 16, 2016, the Company entered into a series of agreements providing for:

- the issuance and sale of Condor's Series D Preferred Stock under a private transaction to SREP III Flight-Investco, L.P. ("SREP"), an affiliate of StepStone Group LP;
- the exchange of all of Condor's outstanding Series C Preferred Stock for Series D Preferred Stock; and
- the cash redemption of all of Condor's outstanding 8% Series A Cumulative Preferred Stock ("Series A Preferred Stock") and 10% Series B Cumulative Preferred Stock ("Series B Preferred Stock").

In connection with these transactions, the Company and SREP entered into a Stock Purchase Agreement (the "Stock Purchase Agreement") dated March 16, 2016 pursuant to which Condor issued and sold 3,000,000 shares of Series D Preferred Stock to SREP on the March 16, 2016 for an aggregate purchase price of \$30,000. The Stock Purchase Agreement required that \$20,147 of the purchase price be deposited into an escrow account for the purpose of effecting the redemption of the Series A and Series B Preferred Stock and that the remaining amount of the purchase price be delivered to Condor.

Simultaneously, the Company entered into the Exchange Agreement with RES pursuant to which all 3,000,000 outstanding shares of Series C Preferred Stock were exchanged for 3,000,000 shares of Series D Preferred Stock. Under the Exchange Agreement, in lieu of payment of accrued and unpaid dividends in the amount of \$4,947 on the Series C Preferred Stock, Condor (a) paid to RES an amount of cash equal to \$1,484, (b) issued to RES 245,156 shares of Series D Preferred Stock (such that RES, IRSA Inversiones y Representaciones Sociedad Anónima ("IRSA"), and their affiliates do not beneficially own in excess of 49% of the voting stock of Condor) and (c) issued to RES a convertible promissory note, bearing interest at 6.25% per annum, in the principal amount of \$1,012 (see Note 7).

Pursuant to the Stock Purchase Agreement, on April 15, 2016, Condor redeemed all of the outstanding Series A and Series B Preferred Stock, in accordance with redemption notices issued on March 16, 2016, as follows:

- all 803,270 outstanding shares of the Series A Preferred Stock at the redemption price of \$10.00 per share plus \$2.084940 per share in accrued and unpaid dividends (plus compounded interest) through the redemption date for a total redemption price of \$9,707; and
- all 332,500 outstanding shares of the Series B Preferred Stock at the redemption price of \$25.00 per share plus \$6.354167 per share in accrued and unpaid dividends through the redemption date for a total redemption price of \$10,425.

The effect of these transactions on the Company's preferred stock and the key terms of the remaining series of the Company's preferred stock are discussed individually below.

***Series A Preferred Stock***

On December 30, 2005, the Company offered and sold 1,521,258 shares of Series A Preferred Stock. At December 31, 2015, 803,270 shares of Series A Preferred Stock remained outstanding until the completion of the redemption on April 15, 2016.

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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**NOTE 10. PREFERRED STOCK (continued)**

Dividends on the Series A Preferred Stock were cumulative and payable monthly in arrears on the last day of each month, at the annual rate of 8% of the \$10.00 liquidation preference per share, equivalent to a fixed annual amount of \$.80 per share. The Company was able to redeem the Series A Preferred Stock, in whole or in part, at any time or from time to time for cash at a redemption price of \$10.00 per share, plus all accrued and unpaid dividends. Commencing with dividends due on December 31, 2013, the Company suspended payment of dividends on its Series A Preferred Stock to preserve capital and improve liquidity. Unpaid dividends accumulated and bore additional dividends at 8%, compounded monthly. Accumulated but unpaid dividends were \$1,452, or \$1.807 per share, as of December 31, 2015. These dividends were not reflected as an obligation on the balance sheet.

Holders of the Series A Preferred Stock generally had no voting rights. However, if dividends on the Series A Preferred Stock were in arrears for six consecutive months or nine months (whether or not consecutive) in any twelve-month period, holders of the Series A Preferred Stock, voting together as a single class with all series of preferred stock for which like voting rights are exercisable, were entitled to elect two directors. At the Company's annual meeting on June 10, 2015, holders of the Series A Preferred Stock and Series B Preferred Stock, voting as one class, elected two directors. With the issuance of the redemption notices on March 16, 2016 and the redemption funds deposited in escrow, all rights of the holders of the Series A Preferred Stock were terminated with the exception of the right to receive the redemption price, including the right to board representation.

The difference between the recorded value of the Series A Preferred Stock prior to the issuance of the redemption notice and the redemption value of the Series A Preferred Stock plus related expenses, a total of \$2,326, was recorded as a reduction of accumulated deficit during the year ended December 31, 2016 as the amount is considered a deemed dividend on the Series A Preferred Stock. Of this amount, \$874 was recorded as a reduction of net earnings attributable to common shareholders as the portion of this deemed dividends that was in excess of preferred dividends deducted to arrive at net earnings attributable to common shareholders in previous periods.

***Series B Preferred Stock***

At December 31, 2015, there were 332,500 shares of Series B Preferred Stock outstanding, originally sold on June 3, 2008, which remained outstanding until the completion of the redemption on April 15, 2016.

Dividends on the Series B Preferred Stock were cumulative and are payable quarterly in arrears on each March 31, June 30, September 30, and December 31, or, if not a business day, the next succeeding business day, at the annual rate of 10.0% of the \$25.00 liquidation preference per share, equivalent to a fixed annual amount of \$2.50 per share. The Company was able to redeem the Series B Preferred Stock, in whole or in part, at any time or from time to time for cash at a redemption price of \$25.00 per share, plus all accrued and unpaid dividends. Also, upon a change of control, each outstanding share of the Company's Series B Preferred Stock would be redeemed for cash at a redemption price of \$25.00 per share, plus all accrued and unpaid dividends. Commencing with dividends due on December 31, 2013, the Company suspended payment of dividends on its Series B Preferred Stock to preserve capital and improve liquidity. Unpaid dividends on the Series B Preferred Stock did not bear interest. Unpaid dividends were \$1,870 or \$5.625 per share, as of December 31, 2015. These dividends were not reflected as an obligation on the balance sheet.

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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**NOTE 10. PREFERRED STOCK (continued)**

Holders of the Series B Preferred stock generally had no voting rights. However, if the dividends on the Series B Preferred Stock were in arrears for six or more quarterly periods (whether or not consecutive), holders of the Series B Preferred Stock, voting together as a single class with all series of preferred stock for which like voting rights are exercisable, would be entitled to elect two directors. At the Company's annual meeting on June 10, 2015, holders of Series A Preferred Stock and Series B Preferred Stock, voting as one class, elected two directors. With the issuance of the redemption notices on March 16, 2016 and the redemption funds deposited in escrow, all rights of the holders of the Series B Preferred Stock were terminated with the exception of the right to receive the redemption price, including the right to board representation.

The difference between the recorded value of the Series B Preferred Stock prior to the issuance of the redemption notice and the redemption value of the Series B Preferred Stock, a total \$2,781, was recorded as a reduction of accumulated deficit during the year ended December 31, 2016 as the amount is considered a deemed dividend on the Series B Preferred Stock. Of this amount, \$911 was recorded as a reduction of net earnings attributable to common shareholders as the portion of this deemed dividend that was in excess of preferred dividends deducted to arrive at net earnings attributable to common shareholders in previous periods.

***Series C Preferred Stock and RES Warrants***

The Company entered into a Purchase Agreement dated November 16, 2011 for the issuance and sale of Series C Preferred Stock and warrants under a private transaction with RES. In two closings on February 1, 2012 and February 15, 2012, the Company completed the sale to RES of 3,000,000 shares of Series C Preferred Stock and 576,923 warrants to purchase shares of common stock. All of the Series C Preferred Stock remained outstanding prior to the execution of the Exchange Agreement on March 16, 2016. The 576,923 warrants remained outstanding at December 31, 2016 with a current exercise price of \$12.48 per share (see Note 8) and an expiration date of January 31, 2017. As discussed further in Subsequent Events (see Note 17), these warrants were exchanged for newly issued warrants in January 2017.

Each of the 3,000,000 shares of Series C Preferred Stock was convertible, in whole or in part, at RES's option, at any time, but subject to RES's beneficial ownership limitation, into the number of shares of common stock equal to the \$10.00 per share liquidation preference, divided by the conversion price then in effect, which is equal to the rate of 0.9615385 shares of common stock for each share of Series C Preferred Stock. As a result of the subscription rights offering concluded on June 6, 2014 (see Note 9), the conversion price was adjusted downward from \$52.00 to \$10.40, equal to the public offering price of our common stock in the subscription rights offering, where the conversion price remained until the instrument's extinguishment. A holder of Series C Preferred Stock would not have conversion rights to the extent the conversion would cause the holder and its affiliates to beneficially own more than 34% of voting stock (the "Beneficial Ownership Limitation"). "Voting stock" means capital stock having the power to vote generally for the election of directors of the Company. A holder of warrants would similarly not have exercise rights to the extent the exercise of a warrant would cause the holder and its affiliates to own capital stock in an amount exceeding the Beneficial Ownership Limitation.

Each share of Series C Preferred Stock was entitled to a dividend of \$0.625 per year payable in equal quarterly dividends. Commencing with dividends due on December 31, 2013, the Company suspended payment of



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**NOTE 10. PREFERRED STOCK (continued)**

dividends on its Series C Preferred Stock to preserve capital and improve liquidity. Unpaid dividends accumulated and bore additional dividends at 6.25%, compounded quarterly. Accumulated but unpaid dividends were \$4,492, or \$1.497 per share, as of December 31, 2015. These dividends are not reflected as an obligation on the balance sheet.

The Series C Preferred Stock voted with the common stock as one class, subject to certain voting limitations. For any vote, the voting power of the Series C Preferred Stock was equal to the lesser of: (a) 0.12096 vote per share or (b) an amount of votes per share such that the vote of all shares of Series C Preferred Stock in the aggregate equal 34% of the combined voting power of all the Company voting stock, minus an amount equal to the number of votes represented by the other shares of voting stock beneficially owned by RES and its affiliates.

On March 16, 2016, the Series C Preferred Stock was extinguished under the Exchange Agreement discussed above. Upon this extinguishment, the difference between the recorded value of the Series C Preferred Stock prior to the exchange and the fair value of the consideration received in the exchange, a total of \$20,366, was recorded as a reduction of accumulated deficit as the amount is considered a deemed dividend on the Series C Preferred Stock. Of this amount, \$15,874 was recorded as a reduction of net earnings attributable to common shareholders as the portion of this deemed dividend that was in excess of preferred dividends deducted to arrive at net earnings attributable to common shareholders in previous periods.

***Series D Preferred Stock***

Following the execution of the Stock Purchase Agreement and Exchange Agreement on March 16, 2016, there were 6,245,156 shares of Series D Preferred Stock outstanding.

The Series D Preferred stockholders rank senior to the Company's common stock and any other preferred stock issuances and receive preferential cumulative cash dividends at a rate of 6.25% per annum, payable quarterly in arrears on each March 31, June 30, September 30, and December 31, or, if not a business day, the next succeeding business day, of the \$10.00 face value per share. Dividends on the Series D Preferred Stock accrue whether or not the Company has earnings, whether or not there are funds legally available for the payment of such dividends, whether or not such dividends are declared, and whether or not such dividends are prohibited by agreement. Whenever the dividends on the Series D Preferred Stock are in arrears for four consecutive quarters, then upon notice by holders of in the aggregate not less than 40% of the outstanding Series D Preferred Stock, the Company will (a) take all appropriate action reasonably within its means to maximize the assets legally available for paying such dividends and to monetize such assets (for example, but without limiting the generality of the foregoing, by selling or liquidating all of some of the Company's assets or by selling the Company as a going concern), (b) pay out of all such assets legally available (including any proceeds from any sale or liquidation of such assets) the maximum possible amount of such unpaid dividends, and (c) thereafter, at any time and from time to time when additional assets of the Company (including any proceeds from any sale or liquidation of such assets) become legally available to pay such unpaid dividends, pay such remaining unpaid dividends until all dividends accumulated on the Series D Preferred Stock have been fully paid. Dividends on the Series D Preferred Stock were paid on June 30, 2016, September 30, 2016, and January 3, 2017 which included all amounts due through those dates.

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Notes To Consolidated Financial Statements

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**NOTE 10. PREFERRED STOCK (continued)**

Each share of Series D Preferred Stock is convertible, at the option of the holder, at any time into a number of shares of common stock determined by dividing the conversion price of \$10.40 into an amount equal to the \$10.00 face value per share plus accrued and unpaid dividends, if any. The conversion price is subject to anti-dilution adjustments upon the occurrence of stock splits and stock dividends. Each outstanding share of Series D Preferred Stock will be converted into a number of shares of common stock determined by dividing the conversion price of \$10.40 into the \$10.00 face value per share, which is equal to a rate of 0.9615385 shares of common stock for each share of Series D Preferred Stock, automatically upon closing of a Qualified Offering (defined as a single offering of common stock of at least \$50,000 or up to three offerings in the aggregate of at least \$75,000, all with certain minimum prices per share and a potential make whole payment required in certain scenarios) without any further action by the holders of such shares or the Company.

The Series D Preferred Stock is redeemable by the Company at any time subject to certain restrictions, in whole or in a partial redemption of up to \$30,000, at \$12.00 per share on or before March 16, 2019, \$13.00 per share from March 16, 2019 to March 16, 2020, and \$14.00 per share on or after March 16, 2020, plus all accrued and unpaid dividends. If a Qualified Offering has not occurred on or before September 30, 2021, holders that hold in the aggregate not less than 40% of the outstanding shares of the Series D Preferred Stock have the right to elect to have the Company fully liquidate in a commercially reasonable manner as determined by the Board of Directors of the Company to provide for liquidation distributions to the holders of the Series D Preferred Stock in an amount per share equal to \$14.00 in cash plus accrued and unpaid dividends. Once this right has been exercised and the Company has been notified, the dividend rate on the Series D Preferred Stock after September 30, 2021 will increase from 6.25% per annum to 12.5% per annum. The holders of Series D Preferred Stock vote their Series D Preferred Stock as a single class with the holders of the common stock on all matters submitted to such holders for vote or consent. For each such vote or consent, each share of Series D Preferred Stock entitles the holder to cast one vote for each whole vote (rounded to the nearest whole number) that such holder would be entitled to cast had such holder converted its Series D Preferred Stock into shares of common stock as of the date immediately prior to the record date for determining the shareholders of the Company eligible to vote on any such matter.

The fair value of the Series D Preferred Stock was determined to be equal to its face value on the date of issuance.

As discussed further as a subsequent event (see Note 17), on February 28, 2017, the holders of the Series D Preferred Stock voluntarily converted to common stock. At the time of conversion, the Series D holders were granted \$9,250 of newly created Series E Preferred Stock.

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### Notes To Consolidated Financial Statements

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#### NOTE 10. PREFERRED STOCK (continued)

##### *Impact of Preferred Stock on Net Earnings (Loss) Attributable to Common Shareholders*

The components of dividends declared and undeclared and in kind dividends deemed on preferred stock are as follows:

	Year ended December 31,		
	2016	2015	2014
Preferred A dividends accrued at stated rate	\$ 222	\$ 727	\$ 671
Preferred A additional deemed dividends upon redemption	652	—	—
Preferred B dividends accrued at stated rate	243	831	831
Preferred B additional deemed dividends upon redemption	668	—	—
Preferred C dividends accrued at stated rate	455	2,074	1,950
Preferred C additional deemed dividends at exchange	15,418	—	—
Preferred D dividends accrued at stated rate	3,090	—	—
Dividends declared and undeclared and in kind dividends deemed on preferred stock	<u>\$20,748</u>	<u>\$3,632</u>	<u>\$3,452</u>

#### NOTE 11. NONCONTROLLING INTEREST OF COMMON UNITS IN CHLP

At December 31, 2016 and 2015, 7,872,943 and 7,659,039 of CHLP's common units were outstanding, respectively. These amounts include 2,609,791 and 2,395,887 common units held by limited partners at December 31, 2016 and 2015, respectively, and 5,263,152 LTIP units outstanding at December 31, 2016 and 2015 which were not yet earned at those dates (see Note 12). The combined redemption value for the common units and LTIP units was \$2,008 and \$1,197 at December 31, 2016 and 2015, respectively.

Our ownership interest in CHLP as of December 31, 2016, 2015, and 2014 was 97.8%, 90.1%, and 99.9%, respectively, which includes consideration of the common units of the limited partners as well as the LTIP units. The Company's increased ownership interest in CHLP during 2016 was primarily the result of the contribution to CHLP of the proceeds from the Series D Preferred Stock issuance during the first quarter of 2016 which was partially offset by the proceeds used to redeem the Series A and B Preferred Stock, which were withdrawn from CHLP, in the second quarter of 2016 (see Note 10). The Company's decreased ownership in CHLP during 2015 was a result of two events. On March 2, 2015, the Company granted an equity award of 5,263,152 LTIP units to an executive officer representing profit interests in the Company's operating partnership (see Note 12). On October 1 and 2, 2015, as partial consideration for the purchase of hotels (see Note 3), 2,298,879 common units in CHLP were issued.

Each limited partner of CHLP may, subject to certain limitations, require that CHLP redeem all or a portion of his or her common units at any time after a specified period following the date the units were acquired, by delivering a redemption notice to CHLP. When a limited partner tenders common units for redemption, the Company can, at its sole discretion, choose to purchase the units for either (1) a number of shares of Company common stock at a rate of one share of common stock for each 52 common units redeemed or (2) cash in an

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**NOTE 11. NONCONTROLLING INTEREST OF COMMON UNITS IN CHLP (continued)**

amount equal to the market value of the number of shares of Company common stock the limited partner would have received if the Company chose to purchase the units for common stock. No common units were redeemed in 2016, 2015, or 2014.

**NOTE 12. STOCK-BASED COMPENSATION**

The Company previously had a 2006 Stock Plan which had been approved by the Company's shareholders. The 2006 Stock Plan authorized the grant of stock options, stock appreciation rights, restricted stock, and stock bonuses for up to 9,615 shares of common stock. The 2006 Stock Plan expired on December 31, 2015.

As a replacement for the 2006 Stock Plan, the Board of Directors adopted the Condor 2016 Stock Plan, which was approved by the Company's shareholders at the annual shareholders meeting on June 15, 2016. The 2016 Stock Plan authorizes the issuance of stock options, stock appreciation rights, restricted stock, restricted stock units, performance shares, deferred stock units, and other forms of stock-based compensation. The maximum number of shares of the Company's common stock that may be issued under the 2016 Stock Plan is 461,538, provided, however, that awards under this plan may not exceed 38,461 shares of common stock prior to the conversion into common stock of all shares of Series D Preferred Stock (see Note 10).

***Options and Unvested Share Awards***

At December 31, 2016, the Company had a total of 865 vested stock options outstanding with a weighted average exercise price of \$48.945 per share and no unvested stock options or unvested share awards outstanding.

***Warrants***

On March 2, 2015, the Company granted a warrant to an executive officer of the Company outside of the 2006 Stock Plan as an inducement material to the executive's acceptance of employment. The warrant entitles the executive to purchase a total of 101,213 authorized but previously unissued shares of the Company's common stock with a grant date price at (i) \$9.88 per share (the adjusted closing bid price of the common stock on Nasdaq on March 2, 2015) if at least one-third but not more than one-half of the shares were purchased on or prior to March 17, 2015, and (ii) \$12.48 per share for shares purchased after. The warrant has a three-year term. The executive officer exercised the warrant in part to purchase 35,060 shares on March 11, 2015 at the price of \$9.88 per share. The warrant remains exercisable for 66,153 shares at an exercise price of \$12.48 per share. As of December 31, 2016, the total unrecognized compensation cost related to the warrants was approximately \$115, which is expected to be recognized over the next 14 months.

The Company records compensation expense for warrants based on the estimated fair value of the warrants on the date of grant determined using the Black-Scholes option-pricing model. The Company uses historical data among other factors to estimate expected price volatility, expected warrant life, dividend rate, and expected forfeiture rate. The risk-free rate is based on the U.S. Treasury yield in effect at the time of grant for the

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

**NOTE 12. STOCK-BASED COMPENSATION (continued)**

estimated life of the warrants. The following table summarizes the estimates used in the Black-Scholes option-pricing model related to the warrants granted in 2015:

	<u>\$9.88 Grant March 2, 2015</u>	<u>\$12.48 Grant March 2, 2015</u>
Volatility	53.10%	78.60%
Expected forfeitures	0.00%	0.00%
Expected term	15 days	3.00 years
Risk free interest rate	0.02%	1.06%

***LTIP Awards***

On March 2, 2015, the Company granted an equity award of 5,263,152 LTIP units, representing profit interests in CHLP, to an executive officer of the company. The LTIP units are earned in one-third increments upon the Company's common stock achieving price per share milestones of \$22.75, \$29.25, and \$35.75 respectively. Earned LTIP units vest in March 2018, or earlier upon a change in control of the Company, and can be redeemed at the rate of one share of common stock for each 52 earned LTIP units for up to 101,213 common shares. As of December 31, 2016, the total unrecognized compensation cost related to the LTIP units was \$199, which is expected to be recognized over the next 14 months.

The Company records compensation expense for the LTIP units based on the estimated fair value of the units on the date of grant determined using the Monte Carlo simulation model. The Company uses historical data among other factors to estimate expected price volatility, expected LTIP life, volume weighted average price, and expected forfeiture rate. The risk-free rate is based on the U.S. Treasury yield in effect at the time of grant for the estimated life of the LTIP. The following table summarizes the estimates used in the Monte Carlo option-pricing model related to the LTIP grant in 2015:

	<u>Grant Date March 2, 2015</u>
Volatility	75.5%
Expected forfeitures	0.00%
Weighted average price	\$9.945
Expected term	3.00 years
Risk free interest rate	1.06%

***Investment Committee Share Compensation***

Independent directors serving as members of the Investment Committee of the Board of Directors receive their monthly Investment Committee fees in the form of shares of the Company's common stock issued under the available stock plan, priced as the average of the closing price of the stock for the first 20 trading days of the calendar year. The shares issued to the independent directors of the Investment Committee for the year ended December 31, 2016 under the 2016 Stock Plan totaled 2,361. The shares issued for the years ended December 31, 2015 and 2014 under the 2006 Stock Plan totaled 3,295 and 1,494, respectively.

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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**NOTE 12. STOCK-BASED COMPENSATION (continued)**

*Stock-Based Compensation Expense*

The expense recognized in the financial statements for stock-based compensation, including the LTIP, related to employees and directors for the years ended December 31, 2016, 2015, and 2014 was \$305, \$285, and \$34, respectively, all of which is included in general and administrative expense.

**NOTE 13. INCOME TAXES**

The Company has recognized no current or deferred income tax expense or benefit from continuing operations or related to discontinued operations for the years ended December 31, 2016, 2015, and 2014 with the exception of Alternative Minimum Tax (“AMT”) recognized at both the REIT and the TRS during the year ended December 31, 2016. Income tax expense related to AMT totaled \$35 for the REIT and \$90 for the TRS and was the result of the application of limits on the use of net operating loss carryovers to offset AMT income.

Actual income tax expense of the TRS for the years ended December 31, 2016, 2015, and 2014 differs from the “expected” income tax expense (benefit) (computed by applying the appropriate U.S. federal income tax rate of 34% to earnings before income taxes) as a result of the following:

	Year ended December 31,		
	2016	2015	2014
Computed “expected” income tax (benefit) expense	\$ 993	\$ 684	\$(118)
State income taxes, net of federal income tax (benefit) expense	139	82	(14)
(Decrease) increase in valuation allowance	(1,082)	(722)	132
Other	(50)	(44)	—
Alternative minimum tax	90	—	—
Total income tax expense	<u>\$ 90</u>	<u>\$ —</u>	<u>\$ —</u>

**Condor Hospitality Trust, Inc. and Subsidiaries**

## Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

**NOTE 13. INCOME TAXES (continued)**

The tax effects of temporary differences that give rise to significant portions of deferred tax assets and deferred tax liabilities at December 31, 2016 and 2015 are as follows:

	<u>As of December 31,</u>	
	<u>2016</u>	<u>2015</u>
<b><u>Deferred Tax Assets</u></b>		
Expenses accrued for consolidated financial statement purposes, nondeductible for tax return purposes	\$ 99	\$ 113
Net operating losses carried forward for federal income tax purposes	1,477	6,902
Book depreciation in excess of tax depreciation	38	—
Subtotal deferred tax assets	1,614	7,015
Valuation allowance	(1,551)	(6,923)
Total deferred tax assets	63	92
<b><u>Deferred Liabilities</u></b>		
Tax depreciation in excess of book depreciation	—	92
JV basis difference	63	—
Total deferred tax liabilities	63	92
Net deferred tax assets	\$ —	\$ —

In assessing the realizability of deferred tax assets, the Company considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The Company considers projected reversals of deferred income tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Management uses historical experience and short and long-range business forecasts to develop such estimates. Further, we employ various prudent and feasible tax planning strategies to facilitate the recoverability of future deductions. A cumulative loss in recent years is a significant piece of evidence with respect to realizability that outweighs the other evidence, and the TRS incurred net losses in 2014 and had taxable income in 2016 and 2015 primarily due to taxable income generated from property sales during the year. As a result of this analysis, the Company believes that a full valuation allowance against the net deferred tax asset position is necessary at December 31, 2016 and 2015. The valuation of deferred tax assets requires judgment in assessing the likely future tax consequences of events that have been recognized in our financial statements or tax returns and future profitability. Our accounting for deferred taxes represents our best estimate of those future events. Changes in our current estimates, due to unanticipated events or otherwise, could have a material impact on our financial condition and results of operations.

After consideration of limitations related to a change in control as defined under Internal Revenue Code Section 382 following the Company's 2012 transactions with RES (see Note 10), the TRS's net operating loss carryforward at December 31, 2016 as determined for federal income tax purposes was \$3,810. The availability of the loss carryforwards will expire in 2022 through 2035.

**Condor Hospitality Trust, Inc. and Subsidiaries**

## Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

**NOTE 13. INCOME TAXES (continued)**

As of December 31, 2016, the tax years that remain subject to examination by major tax jurisdictions generally include 2013 through 2016.

Distributions to the extent of our current and accumulated earnings and profits for federal income tax purposes generally will be taxable to a shareholder as ordinary income. Distributions in excess of current and accumulated earnings and profits generally will be treated as a nontaxable reduction of the shareholder's basis in such shareholder's shares, to the extent thereof, and thereafter as taxable capital gain. Distributions that are treated as a reduction of the shareholder's basis in its shares will have the effect of increasing the amount of gain, or reducing the amount of loss, recognized upon the sale of the shareholder's shares.

For income tax purposes, distributions paid per share in 2016 were characterized as follows:

	<b>For the year ended December 31, 2016</b>	
	<b>Amount</b>	<b>%</b>
<b>Common Shares:</b>		
Ordinary income	\$0.455000	100%
Capital gain	—	—
Return of capital	—	—
Total	<u>\$0.455000</u>	<u>100%</u>
<b>Series C Preferred Stock:</b>		
Ordinary income	\$1.649124	100%
Capital gain	—	—
Return of capital	—	—
Total	<u>\$1.649124</u>	<u>100%</u>
<b>Series D Preferred Stock:</b>		
Ordinary income	\$0.494792	100%
Capital gain	—	—
Return of capital	—	—
Total	<u>\$0.494792</u>	<u>100%</u>

The common and preferred share distributions declared on December 6, 2016 and paid on January 5, 2017 and January 3, 2017, respectively, were treated as 2016 distributions for tax purposes.

A portion of the redemption price of the Series A and B Preferred Stock that was redeemed for cash on April 15, 2016 included amounts equal to the accrued and unpaid dividends on such stock. However, the entire redemption price, inclusive of amounts equal to accrued and unpaid dividends, was treated as payment in exchange for the redeemed stock and none of the redemption price is treated as a distribution of dividends under the Code for federal income tax purposes.

No dividends on common stock or preferred stock were paid in or declared related to 2015 or 2014.



## Condor Hospitality Trust, Inc. and Subsidiaries

### Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

#### NOTE 14. EARNINGS PER SHARE

Basic earnings per share (“EPS”) is computed by dividing net earnings (loss) attributable to common shareholders by the weighted average number of common shares outstanding. Diluted EPS is computed after adjusting the numerator and denominator of the basic EPS computation for the effects of any dilutive potential common shares outstanding during the period. These effects include adjustments to the numerator for any change in fair value included in net earnings (loss) attributed to the certain derivative liabilities (related to the Series C Preferred Stock and warrants) during the period the convertible securities are dilutive. The computation of basic and diluted EPS is presented below:

	Year ended December 31,		
	2016	2015	2014
<b>Numerator: Basic(1)</b>			
Net earnings (loss) attributable to common shareholders			
Continuing operations—Basic	\$ 1,390	\$ 6,055	\$ (22,581)
Discontinued operations—Basic	657	3,438	2,893
Total Basic	<u>\$ 2,047</u>	<u>\$ 9,493</u>	<u>\$ (19,688)</u>
<b>Numerator: Diluted(1)</b>			
Net earnings (loss) attributable to common shareholders from continuing operations	\$ 1,390	\$ 6,055	\$ (22,581)
Dividends on Series C Preferred Stock	—	2,074	—
Dividends on Series D Preferred Stock	3,090	—	—
Unrealized gain on warrant derivative	—	(4,122)	—
Unrealized gain on Series C Preferred Embedded Derivative	—	(7,533)	—
Continuing operations—Diluted	4,480	(3,526)	(22,581)
Discontinued operations—Diluted	657	3,438	2,893
Total Diluted	<u>\$ 5,137</u>	<u>\$ (88)</u>	<u>\$ (19,688)</u>
<b>Denominator</b>			
Weighted average number of common shares—Basic	761,112	751,634	599,552
Unvested stock	—	619	—
Series C Preferred Stock	—	2,884,615	—
Series D Preferred Stock	4,774,433	—	—
Warrants—Employees	—	106	—
Warrants—RES	—	(61,504)	—
Weighted average number of common shares—Diluted	<u>5,535,545</u>	<u>3,575,470</u>	<u>599,552</u>
<b>Earnings Per Share</b>			
Continuing operations—Basic	\$ 1.82	\$ 8.06	\$ (37.64)
Discontinued operations—Basic	0.85	4.55	4.81
Total—Basic Earnings Per Share	<u>\$ 2.67</u>	<u>\$ 12.61</u>	<u>\$ (32.83)</u>
Continuing operations—Diluted	\$ 0.78	\$ (0.98)	\$ (37.64)
Discontinued operations—Diluted	0.13	0.98	4.81
Total—Diluted Earnings Per Share	<u>\$ 0.91</u>	<u>\$ —</u>	<u>\$ (32.83)</u>

- (1) The loss (earnings) attributable to noncontrolling interest is allocated between continuing and discontinued operations for the purpose of the EPS calculation

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

**NOTE 14. EARNINGS PER SHARE (continued)**

Potentially dilutive common shares, if any, have been excluded from the denominator if they are antidilutive to net earnings (loss) attributable to common shareholders. The following table summarizes the weighted average number of potentially dilutive securities that have been excluded from the denominator for the purpose of computing diluted EPS:

	Year ended December 31,		
	2016	2015	2014
Outstanding stock options	865	865	1,346
Unvested stock awards outstanding	—	—	237
Warrants—RES	576,923	—	576,923
Warrants—Employees	66,153	55,249	—
Series C preferred Stock	598,991	—	2,884,615
LTIP common units(1)	101,213	84,576	—
Convertible debt	77,336	—	84,826
CHLP common units(1)	46,265	13,008	1,865
Total potentially dilutive securities excluded from the denominator	<u>1,467,746</u>	<u>153,698</u>	<u>3,549,812</u>

- (1) LTIP and common units of CHLP have been omitted from the denominator for the purpose of computing diluted EPS since the effect of including these amounts in the numerator and denominator would have no impact on calculated EPS

**NOTE 15. COMMITMENTS AND CONTINGENCIES**

***Management Agreements***

Our TRS engages eligible independent contractors as property managers for each of our hotels in accordance with the requirements for qualification as a REIT. The hotel management agreements provide that the management companies have control of all operational aspects of the hotels, including employee-related matters. The management companies must generally maintain each hotel under their management in good repair and condition and perform routine maintenance, repairs, and minor alterations. Additionally, the management companies must operate the hotels in accordance with the national franchise agreements that cover the hotels, which includes, as applicable, using franchisor sales and reservation systems and abiding by franchisors' marketing standards. The management agreements generally require the TRS to fund debt service, working capital needs, and capital expenditures and to fund the management companies' third-party operating expenses, except those expenses not related to the operation of hotels. The TRS also is responsible for obtaining and maintaining certain insurance policies with respect to the hotels.

Each of the management companies employed by the TRS at December 31, 2016 receive a base monthly management fee of 3.0% to 3.5% of gross hotel revenue, with incentives for performance which increase such fee to a maximum of 5.0%. For the years ended December 31, 2016, 2015, and 2014, base management fees

## Condor Hospitality Trust, Inc. and Subsidiaries

### Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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#### **NOTE 15. COMMITMENTS AND CONTINGENCIES (continued)**

incurred totaled \$1,619, \$2,466, and \$3,101, respectively, of which \$1,619, \$2,348, and \$2,521, respectively, was included in continuing operations as hotel and property operations expense. For the years ended December 31, 2016 and 2015, incentive management fees, included in continuing operations in their entirety, totaled \$190 and \$158, respectively.

The management agreements generally have initial terms of one to three years and renew for additional terms of one year unless either party to the agreement gives the other party written notice of termination at least 90 days before the end of a term. The Company may terminate a management agreement, subject to cure rights, if certain performance metrics tied to both individual hotel and total managed portfolio performance are not met. The Company may also terminate a management agreement with respect to a hotel at any time without reason upon payment of a termination fee. The management agreements terminate with respect to a hotel upon sale of the hotel, subject to certain notice requirements.

#### ***Franchise Agreements***

As of December 31, 2016, 17 of our 18 wholly owned properties operate under franchise licenses from national hotel companies. Under our franchise agreements, we are required to pay franchise fees generally between 3.3% and 5.5% of room revenue, plus additional fees for marketing, central reservation systems, and other franchisor programs and services that amount to between 2.5% and 6.0% of room revenue. The franchise agreements typically have 10 to 25 year terms although certain agreements may be terminated by either party on certain anniversary dates specified in the agreements. Further, each agreement provides for early termination fees in the event the agreement is terminated before the stated term. Franchise fee expense totaled \$3,123, \$3,883, and \$4,691, for the years ended December 31, 2016, 2015, and 2014, respectively, of which \$3,123, \$3,853, and \$4,051, respectively, was included in continuing operations as hotel and property operations expense. The initial fees incurred to enter into the franchise agreements are capitalized and amortized over the life of the franchise agreements.

#### ***Leases***

The Company assumed a land lease agreement at the time of purchase related to one hotel owned at December 31, 2016. The lease requires monthly payments of the greater of \$2 or 5% of room revenue and is associated with a property held for sale at December 31, 2016. Land lease expense totaled \$105, \$105, and \$102 for the years ended December 31, 2016, 2015, and 2014, respectively, all of which is included in continuing operations as hotel and property operations expense.

The Company entered into three new office lease agreements in 2016, replacing all existing office lease agreements which expired in 2016. These leases expire in 2019 through 2021 and have combined rent expense of approximately \$132 annually. Office lease expense totaled \$199, \$163, and \$162 in the years ended December 31, 2016, 2015, and 2014, respectively, and is included in general and administrative expense.

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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**NOTE 15. COMMITMENTS AND CONTINGENCIES (continued)**

As of December 31, 2016, the future minimum lease payments applicable to non-cancellable operating leases, excluding leases associated with properties held for sale at December 31, 2016, are as follows:

	<u>Lease rents</u>
2017	\$156
2018	159
2019	138
2020	61
2021	47
	<u>\$561</u>

As of December 31, 2016, the Company had agreements with two restaurants and a cell tower operator for leased space at our hotel locations. Lease income totaled \$86, \$198, and \$309 for the years ended December 31, 2016, 2015, and 2014, respectively, of which \$86, \$177, and \$292, respectively, was included in continuing operations in room rentals and other hotel services revenue.

***Obligation to RES***

The Company had an obligation to RES to use \$25,000 of the proceeds from its capital infusion in 2012 to pursue hotel acquisitions (see Note 10). There were no contractual restrictions or penalties related to the use of these funds for purposes other than acquisitions, but the Company was obligated to replace these funds promptly as it had the ability to do so. Following the completion of the hotel acquisitions in 2015 and 2016 (see Note 3) and the acquisition made through the Atlanta JV in August 2016 (see Note 5), the Company has satisfied this obligation.

***Benefit Plans***

The Company has a qualified contributory retirement plan under Section 401(k) of the Code (the “401(k) Plan”) which covers all employees who meet certain eligibility requirements. Voluntary contributions may be made to the 401(k) Plan by employees. The 401(k) Plan is a Safe Harbor Plan and requires a mandatory employer contribution. The employer contribution expense for the years ended December 31, 2016, 2015, and 2014 was \$73, \$66, and \$59, respectively, and is included in general and administrative expenses.

***Litigation***

Various claims and legal proceedings arise in the ordinary course of business and may be pending against the Company and its properties. We are not currently involved in any material litigation, nor, to our knowledge, is any material litigation threatened against us. The Company has insurance to cover potential material losses and we believe it is not reasonably possible that such matters will have a material impact on our financial condition or results of operations.

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**NOTE 16. QUARTERLY OPERATING RESULTS (UNAUDITED)**

	Quarters ended (unaudited)				
	March 31, 2016	June 30, 2016	September 30, 2016	December 31, 2016	Total 2016
<b>Revenue</b>	\$ 12,503	\$14,155	\$13,519	\$10,470	\$ 50,647
Operating expenses	12,662	12,508	12,445	11,009	48,624
<b>Operating income (loss)</b>	(159)	1,647	1,074	(539)	2,023
Net gain on dispositions of assets	3,367	8,856	3,591	7,318	23,132
Equity in loss of joint venture	—	—	(54)	(190)	(244)
Net gain on derivatives and convertible debt	6,117	162	26	72	6,377
Other income (expense)	(21)	23	85	(32)	55
Interest expense	(1,329)	(1,248)	(1,127)	(1,006)	(4,710)
Loss on debt extinguishment	(173)	(976)	(399)	(639)	(2,187)
Impairment loss	(793)	(121)	(343)	(220)	(1,477)
Earnings from continuing operations before income tax expense	7,009	8,343	2,853	4,764	22,969
Income tax expense	—	—	—	(125)	(125)
Earnings (loss) from continuing operations	7,009	8,343	2,853	4,639	22,844
Gain from discontinued operations, net of tax	678	—	—	—	678
<b>Net earnings</b>	7,687	8,343	2,853	4,639	23,522
Earnings attributable to noncontrolling interest	(389)	(178)	(61)	(99)	(727)
<b>Earnings attributable to controlling interests</b>	7,298	8,165	2,792	4,540	22,795
Dividends declared and undeclared and in kind dividends deemed on preferred stock	(17,740)	(1,057)	(976)	(975)	(20,748)
<b>Net earnings (loss) attributable to common shareholders</b>	<u>\$(10,442)</u>	<u>\$ 7,108</u>	<u>\$ 1,816</u>	<u>\$ 3,565</u>	<u>\$ 2,047</u>
<b>Basic Earnings Per Share(1)</b>					
Basic EPS from continuing operations	\$ (14.63)	\$ 9.36	\$ 2.41	\$ 4.68	\$ 1.82
Basic EPS from discontinued operations	0.91	—	—	—	0.85
Total EPS Basic	<u>\$ (13.72)</u>	<u>\$ 9.36</u>	<u>\$ 2.41</u>	<u>\$ 4.68</u>	<u>\$ 2.67</u>
<b>Diluted Earnings Per Share(1)</b>					
Diluted EPS from continuing operations	\$ (14.63)	\$ 1.17	\$ 0.39	\$ 0.65	\$ 0.78
Diluted EPS from discontinued operations	0.91	—	—	—	0.13
Total EPS Diluted	<u>\$ (13.72)</u>	<u>\$ 1.17</u>	<u>\$ 0.39</u>	<u>\$ 0.65</u>	<u>\$ 0.91</u>

- (1) Quarterly and total annual EPS are based on the weighted average number of shares outstanding during each quarter and the annual period. Due to rounding and differences in earnings and losses between the quarterly and annual periods, the sum of the quarterly EPS amounts may not equal the reported amounts for the year.

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**NOTE 16. QUARTERLY OPERATING RESULTS (UNAUDITED) (continued)**

	Quarters ended (unaudited)				
	March 31, 2015	June 30, 2015	September 30, 2015	December 31, 2015	Total 2015
<b>Revenue</b>	\$12,692	\$16,733	\$15,895	\$13,394	\$58,714
Operating expenses	13,134	14,247	13,983	13,826	55,190
<b>Operating income (loss)</b>	(442)	2,486	1,912	(432)	3,524
Net gain (loss) on dispositions of assets	11	(137)	2,927	1,997	4,798
Net gain (loss) on derivatives and convertible debt	4,823	(4,710)	7,895	3,570	11,578
Other income (expense)	95	31	(4)	(8)	114
Interest expense	(1,547)	(1,510)	(1,137)	(1,328)	(5,522)
Loss on debt extinguishment	(7)	—	(104)	(102)	(213)
Impairment recovery (loss)	(777)	(3,053)	313	(312)	(3,829)
Earnings (loss) from continuing operations before income tax expense	2,156	(6,893)	11,802	3,385	10,450
Income tax expense	—	—	—	—	—
Earnings (loss) from continuing operations	2,156	(6,893)	11,802	3,385	10,450
Gain from discontinued operations, net of tax	1,294	994	152	1,432	3,872
<b>Net earnings (loss)</b>	3,450	(5,899)	11,954	4,817	14,322
(Earnings) loss attributable to noncontrolling interest	(281)	284	(724)	(476)	(1,197)
<b>Earnings (loss) attributable to controlling interests</b>	3,169	(5,615)	11,230	4,341	13,125
Dividends declared and undeclared and in kind dividends deemed on preferred stock	(891)	(902)	(914)	(925)	(3,632)
<b>Net earnings (loss) attributable to common shareholders</b>	<u>\$ 2,278</u>	<u>\$ (6,517)</u>	<u>\$10,316</u>	<u>\$ 3,416</u>	<u>\$ 9,493</u>
<b>Basic Earnings Per Share(1)</b>					
Basic EPS from continuing operations	\$ 1.56	\$ (9.88)	\$ 13.39	\$ 2.85	\$ 8.06
Basic EPS from discontinued operations	1.56	1.30	0.20	1.63	4.55
Total EPS Basic	<u>\$ 3.12</u>	<u>\$ (8.58)</u>	<u>\$ 13.59</u>	<u>\$ 4.48</u>	<u>\$ 12.61</u>
<b>Diluted Earnings Per Share(1)</b>					
Diluted EPS from continuing operations	\$ (0.91)	\$ (9.88)	\$ 0.78	\$ (0.26)	\$ (0.98)
Diluted EPS from discontinued operations	0.33	1.30	0.07	0.33	0.98
Total EPS Diluted	<u>\$ (0.58)</u>	<u>\$ (8.58)</u>	<u>\$ 0.85</u>	<u>\$ 0.07</u>	<u>\$ —</u>

- (1) Quarterly and total annual EPS are based on the weighted average number of shares outstanding during each quarter and the annual period. Due to rounding and differences in earnings and losses between the quarterly and annual periods, the sum of the quarterly EPS amounts may not equal the reported amounts for the year.

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#### NOTE 17. SUBSEQUENT EVENTS

##### *Subsequent Property Activity*

On January 23, 2017 the Company executed an agreement to purchase a portfolio of four Home2 Suites hotels for \$73,750. The portfolio includes the Home2 Suites Memphis / Southaven, the Home2 Suites Austin / Round Rock, the Home2 Suites Lexington University / Medical Center (Kentucky), and the Home2 Suites Tallahassee State Capitol. The closing of these acquisitions is anticipated to occur in the first quarter of 2017, but is subject to customary closing conditions including accuracy of representations and warrants and compliance with covenants and obligations.

##### *Subsequent Debt Transactions*

On January 27, 2017, the Company extended the maturity date on the WAB loan with a principal balance of \$4,806 on December 31, 2016 from February 1, 2017 to February 1, 2018. This loan was subsequently repaid in full with the refinancing discussed below.

On March 1, 2017, a significant portion of the Company's debt (including all debt outstanding at December 31, 2016 with the exception of the two variable rate WAB loans and the two fixed rate Great Western Bank loans) was refinanced with a secured credit facility that matures on March 1, 2019. Following this refinancing, contractual debt maturities on debt outstanding at December 31, 2016 were as follows:

	<u>Held for sale</u>	<u>Held for use</u>	<u>Total</u>
2017	\$ —	\$ 916	\$ 916
2018	—	930	930
2019	6,000	27,691	33,691
2020	—	14,180	14,180
2021	—	13,672	13,672
Total	<u>\$6,000</u>	<u>\$57,389</u>	<u>\$63,389</u>

The credit agreement provides for a \$90,000 senior secured credit facility and includes an accordion feature that would allow the facility to be increased to \$400,000 with additional lender commitments. Availability under the facility is based on a borrowing base formula for the pool of hotel properties securing the facility. As of the closing date, the collateral pool consisted of 14 hotel properties. As of the closing date, four hotels were excluded from the borrowing base until certain conditions are satisfied and the availability under the facility was \$34,250. Those four hotels are expected to be added to the borrowing base within days after the closing and the availability under the facility is expected to increase to \$41,050. The facility is guaranteed by the Company and its material subsidiaries that do not have stand-alone financing. Prior to the occurrence of specific capital achievements, borrowings under the facility accrue interest, at the Company's option, at either LIBOR plus 3.95% or a base rate plus 2.95%. Thereafter, borrowings bear interest based on a leverage-based pricing grid, at the Company's option, at either LIBOR plus a spread ranging from 2.25% to 3.00% (depending on leverage) or a base rate plus a spread ranging from 1.25% to 2.00% (depending on leverage). The facility matures in two years and has an automatic one-year extension upon the completion of specific capital achievements. The facility has two additional one-year extension options following additional capital achievements. The facility contains customary representations and warranties, covenants and events of default.

**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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**NOTE 17. SUBSEQUENT EVENTS (continued)**

On March 1, 2017, the Company borrowed \$34,250 under the facility to repay existing indebtedness and pay reserves costs related to closing of the facility. The Company anticipates using borrowings under the facility to acquire three out of the four Home2 Suites hotels currently under contract to be acquired, which will be added to the collateral pool for the facility. Borrowings under the facility can also be used for future acquisitions and general corporate purposes.

***Subsequent Equity Transactions***

On January 24, 2017, the Company exchanged 23,160 new warrants (the “New Warrants”) to purchase common stock of the Company for 576,923 warrants (the “Old Warrants”, see Note 10) held by RES. The number of New Warrants issued in exchange for the Old Warrants equals the number of shares of common stock issuable upon exercise of the Old Warrants pursuant to a cashless exercise provisions of the Old Warrants. The New Warrants are exercisable for 23,160 shares of common stock, have an exercise price of \$0.0065 for each common share and expire on January 24, 2019.

On February 28, 2017, the holders of the Series D Preferred Stock voluntarily converted their shares into 6,004,957 shares of common stock at \$10.40 per share pursuant to the terms of the preferred stock. The terms of the Series D Preferred Stock provided for automatic conversion following certain future common stock offerings, and also provided for potential additional payments to the holders depending on the sales price of common stock in the offerings. As a result of the voluntary conversion, the holders are no longer entitled to the potential payments. To induce the holders of the Series D Preferred Stock to voluntarily convert their shares, the Company issued the holders \$9,250 of a new series of preferred stock, the Series E Preferred Stock.

The Series E Preferred Stock ranks senior to the Company’s common stock and any other preferred stock issuances and receives preferential cumulative cash dividends at a rate of 6.25% per annum, payable quarterly of the \$10.00 face value per share. If the Company fails to pay a dividend then during the period that dividends are not paid, the dividend rate increases to 12.5%, if specific equity offering or offerings have not occurred, and increases 9.50% per annum if such equity or equity offerings have occurred. Dividends on the Series E Preferred Stock accrue whether or not the Company has earnings, whether or not there are funds legally available for the payment of such dividends, whether or not such dividends are declared, and whether or not such dividends are prohibited by agreement. Subject to certain shareholder approvals, required under Nasdaq Marketplace Rules, which Condor will seek and expects to obtain at the next annual shareholders meeting, each share of Series E Preferred Stock is convertible, at the option of the holder, at any time on or after February 28, 2019, into a number of shares of common stock determined by dividing the conversion price of \$13.845 into an amount equal to the \$10.00 face value per share plus accrued and unpaid dividends, if any. Upon liquidation, each share of Series E Preferred Stock is entitled to \$10.00 per share, accrued and unpaid dividends, and an additional amount based on liquidation preference that the holders may have foregone by converting their Series D Preferred Stock into common stock, as adjusted for stock appreciation and dividends paid on the common stock. The conversion price is subject to anti-dilution adjustments upon the occurrence of stock splits and stock dividends. Following a specific equity offering or offerings, from time to time a number of shares of Series E Preferred Stock automatically converts into common stock if the common stock trades at 120% of the conversion price for 60 trading days, and the number of shares converted will be determined by certain trading volumes measures. The



**Condor Hospitality Trust, Inc. and Subsidiaries**  
Notes To Consolidated Financial Statements

(In thousands, except share and per share data)

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**NOTE 17. SUBSEQUENT EVENTS (continued)**

Company has rights, following a specific equity offering or offerings, to redeem up to 490,250 shares of the Series E Preferred Stock at prices from 110% to 130% of its liquidation value, and the holders have put rights commencing March 16, 2021 to put the Series E Preferred Stock to the Company at 130% of its liquidation preference, which the Company can satisfy with cash or common stock. The Series E Preferred Stock votes as a class on matters generally affecting the Series E Preferred Stock, and as long as 434,750 shares of Series E Preferred Stock (47% of the originally issued shares of Series E Preferred Stock) remain outstanding, then 75% approval of the Series E Preferred Stock will be required to approve merger, consolidation, liquidation or winding up of Condor, related party transactions exceeding \$120, payment of dividends on common stock except from funds from operations or to maintain REIT status, the grant of exemptions from Condor's charter limitation on ownership of 9.9% of any class or series of its securities (exclusive of persons currently holding exemptions), issuance of preferred stock or commitment or agreement to do any of the foregoing.

Effective on March 15, 2017, the Company effected a reverse stock split of its common stock at a ratio of 1-for-6.5. No fractional shares of common stock were issued as fractional shares were settled in cash. Unless otherwise noted, impacted amounts and share information included in the financial statements and notes thereto have been retroactively adjusted for the stock split as if such stock split occurred on the first day of the first period presented. Certain amounts in the notes to the financial statements may be slightly different than previously reported due to rounding of fractional shares as a result of the reverse stock split.

**Condor Hospitality Trust, Inc. and Subsidiaries**  
**Schedule III Real Estate and Accumulated Depreciation**  
**As of December 31, 2016**  
**(In thousands)**

Brand	Location	Acquisition date	Encumbrance	Initial cost			Additions, (dispositions), (impairments) Subsequent to acquisition			Gross amount at December 31, 2016				Net book value
				Land	Buildings & improvements	Furniture & equipment	Land	Buildings & improvements	Furniture & equipment	Land	Buildings & improvements	Furniture & equipment	Accumulated depreciation	
Super 8	Creston, Iowa	09/19/1978	GWBR	\$ 56	\$ 765	\$ 76	\$ 90	\$ 1,574	\$ 892	\$ 146	\$ 2,339	\$ 968	\$ (2,213)	\$ 1,240
Quality Inn	Solomons, Maryland	06/01/1986	WAB	2,304	2,719	269	—	1,514	436	2,304	4,233	705	(3,220)	4,022
Comfort Inn	New Castle, Pennsylvania	07/01/1987	MS	57	3,732	369	(1)	344	426	56	4,076	795	(2,550)	2,377
Key West Inn	Key Largo, Florida	08/01/1987	MS	339	2,947	292	—	1,186	342	339	4,133	634	(2,553)	2,553
Comfort Inn	Harlan, Kentucky	07/01/1993	WAB	—	2,684	265	—	(1,265)	512	—	1,419	777	(532)	1,664
Quality Inn	Morgantown, West Virginia	10/01/1996	MS	398	3,749	347	—	633	704	398	4,382	1,051	(2,732)	3,099
Comfort Suites	Ft. Wayne, Indiana	11/07/2005	HUNT	1,200	3,964	840	—	1,037	591	1,200	5,001	1,431	(2,555)	5,077
Comfort Suites	Lafayette, Indiana	11/07/2005	HUNT	850	3,054	420	—	375	301	850	3,429	721	(1,561)	3,439
Comfort Inn & Suites	Warsaw, Indiana	11/07/2005	HUNT	650	2,121	380	—	380	438	650	2,501	818	(1,330)	2,639
Comfort Suites	South Bend, Indiana	11/30/2005	WAB	500	10,602	910	(250)	(4,264)	1,392	250	6,338	2,302	(1,691)	7,199
Supertel Inn	Creston, Iowa	06/30/2006	MS	235	2,364	344	—	(16)	65	235	2,348	409	(1,012)	1,980
Super 8	Billings, Montana	01/05/2007	WAB	518	4,648	159	(27)	(12)	259	491	4,636	418	(1,507)	4,038
Days Inn	Bossier City, Louisiana	04/04/2007	GWBR	1,025	5,031	87	(768)	(3,792)	750	257	1,239	837	(813)	1,520
Hilton Garden Inn	Dowell, Maryland	05/25/2012	CANTOR	1,400	9,492	323	—	621	348	1,400	10,113	671	(1,644)	10,540
SpringHill Suites	San Antonio, Texas	10/01/2015	LAT	1,597	14,353	1,550	—	114	20	1,597	14,467	1,570	(786)	16,848
Courtyard by Marriott	Jacksonville, Florida	10/02/2015	WABJ	2,100	11,050	850	—	152	3	2,100	11,202	853	(710)	13,445
Hotel Indigo	Atlanta, Georgia	10/02/2015	WABA	800	8,700	1,500	—	86	141	800	8,786	1,641	(729)	10,498
Aloft	Leawood, Kansas	12/14/2016	GWB	3,339	18,046	1,115	—	(5)	—	3,339	18,041	1,115	(57)	22,438
Subtotal Hotel Properties				17,368	110,021	10,096	(956)	(1,338)	7,620	16,412	108,683	17,716	(28,195)	114,616
Construction in progress				—	—	—	—	82	4	—	82	4	—	86
Office building				69	1,517	—	(69)	(1,517)	487	—	—	487	(318)	169
<b>Total</b>				<u>\$17,437</u>	<u>\$111,538</u>	<u>\$10,096</u>	<u>\$(1,025)</u>	<u>\$(2,773)</u>	<u>\$8,111</u>	<u>\$16,412</u>	<u>\$108,765</u>	<u>\$18,207</u>	<u>\$(28,513)</u>	<u>\$114,871</u>

**Condor Hospitality Trust, Inc. and Subsidiaries**  
**Notes to Schedule III Real Estate and Accumulated Depreciation**  
**As of December 31, 2016**  
**(In thousands)**

Encumbrance codes refer to the following lenders:

MS	Morgan Stanley	WAB	Western Alliance Bank Fixed Rate Debt
GWBR	Great Western Bank Revolving Credit Facility	HUNT	Huntington
LAT	Latitude	CANTOR	Cantor
WABA	Western Alliance Bank Variable Rate Debt—\$4.9m	WABJ	Western Alliance Bank Variable Rate Debt—\$9.9m
GWB	Great Western Bank Fixed Rate Debt		

See Accompanying Report of Independent Registered Public Accounting Firm

**Condor Hospitality Trust, Inc. and Subsidiaries**  
**Notes to Schedule III Real Estate and Accumulated Depreciation**  
**As of December 31, 2016**  
(In thousands)

<u>ASSET BASIS</u>	<u>Total</u>
(a) <b>Balance at January 1, 2014</b>	\$248,468
Additions	3,058
Disposals	(32,646)
Impairment loss	(4,295)
<b>Balance at December 31, 2014</b>	214,585
Additions	46,489
Disposals	(65,802)
Impairment loss	(6,373)
<b>Balance at December 31, 2015</b>	188,899
Additions	25,618
Disposals	(68,256)
Impairment loss	(2,877)
<b>Balance at December 31, 2016</b>	<u>\$143,384</u>
<u>ACCUMULATED DEPRECIATION</u>	<u>Total</u>
(b) <b>Balance at January 1, 2014</b>	\$ 84,112
Depreciation for the period ended December 31, 2014	6,549
Depreciation on assets sold or disposed	(13,884)
Impairment loss	(1,374)
<b>Balance at December 31, 2014</b>	75,403
Depreciation for the period ended December 31, 2015	5,400
Depreciation on assets sold or disposed	(19,938)
Impairment loss	(2,665)
<b>Balance at December 31, 2015</b>	58,200
Depreciation for the period ended December 31, 2016	5,190
Depreciation on assets sold or disposed	(33,477)
Impairment loss	(1,400)
<b>Balance at December 31, 2016</b>	<u>\$ 28,513</u>
(c) The aggregate cost of land, buildings, furniture and equipment for Federal income tax purposes is approximately \$148.4 million (unaudited).	
(d) Depreciation is computed based upon the following useful lives:	
Buildings and improvements	15—40 years
Furniture and equipment	3—12 years
(e) The Company has mortgages payable on the properties as noted. Additional mortgage information can be found in Note 6 to the consolidated financial statements.	



## CORPORATE INFORMATION

### BOARD OF DIRECTORS

**J. William Blackham**  
President, Chief Executive Officer,  
Condor Hospitality Trust, Inc.

**Daphne Dufresne**<sup>3</sup>  
Managing Partner,  
GenNx360 Capital Partners

**Daniel Elsztain**<sup>2,3,4</sup>  
Chief Real Estate Business Officer,  
IRSA

**James Friend**<sup>CB,1</sup>  
Chairman of the Board, Condor;  
President and Chief Executive Officer,  
Friend Development Group

**Jeff Giller**  
Partner,  
StepStone Real Estate L.P.

**Donald Landry**<sup>3\*,4\*</sup>  
President and Owner,  
Top Ten Hospitality Advisors

**Mark Linehan**<sup>1</sup>  
President and Chief Executive Officer,  
Wynmark

**Brendan MacDonald**<sup>2,3,4</sup>  
Partner,  
StepStone Real Estate L.P.

**John Sabin**<sup>1\*,2\*</sup>  
Chief Financial Officer,  
Revolution LLC, and  
Case Foundation

#### Committee Membership

- 1 Audit Committee
- 2 Compensation Committee
- 3 Investment Committee
- 4 Nominating Committee

\*Denotes Chairman of Committee  
CB Chairman of the Board

### EXECUTIVE OFFICERS

**J. William Blackham**  
President, Chief Executive Officer

**Jonathan Gantt**  
Senior Vice President,  
Chief Financial Officer

**Jeffrey Dougan**  
Senior Vice President,  
Chief Operating Officer

**Arinn Cavey**  
Chief Accounting Officer

**Lauren Green**  
Corporate Counsel, Secretary

### CORPORATE HEADQUARTERS

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Suite 220  
Bethesda, MD 20814  
Phone: (301) 861-3305  
Website: [www.condorhospitality.com](http://www.condorhospitality.com)

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Omaha, NE 68114  
Phone: (402) 371-2520

1800 West Pasewalk Avenue  
Suite 200  
Norfolk, NE 68701  
Phone: (402) 371-2520  
Fax: (402) 371-4229

### ANNUAL MEETING

The annual meeting of shareholders will be held on Tuesday, May 16, 2017, at 4:00 p.m. Eastern Time at the Courtyard New York Manhattan/ Midtown East located at 866 Third Avenue, New York, NY 10022.

### STOCK EXCHANGE LISTING

Condor Hospitality Trust, Inc. trades on the NASDAQ Global Market System under the symbol "CDOR".

### TRANSFER AGENT

American Stock Transfer and Trust Company, LLC  
6201 15th Avenue  
Brooklyn, NY 11219  
Phone: (800) 937-5449  
[www.amstock.com](http://www.amstock.com)

### INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

KPMG LLP  
1676 International Drive  
McLean, VA 22102

### INVESTOR RELATIONS CONTACT

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Chief Financial Officer  
Condor Hospitality Trust, Inc.  
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Bethesda, MD 20814  
Phone: (301) 861-3305  
Email: [investors@trustcondor.com](mailto:investors@trustcondor.com)

### FORM 10-K

Additional copies of the Company's 2016 Annual Report on Form 10-K, as filed with the SEC, is available on the Company's website or in print by contacting Investor Relations: 4800 Montgomery Lane Suite 220 Bethesda, MD 20814 Phone: (301) 861-3305 Email: [investors@trustcondor.com](mailto:investors@trustcondor.com)



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