UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

x **Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the quarterly period ended June 30, 2014, or

o **Transition report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934**

Commission File Number 1-13374

REALTY INCOME CORPORATION

(Exact name of registrant as specified in its charter)

Maryland	**33-0580106**
(State or Other Jurisdiction of Incorporation or Organization)	(IRS Employer Identification Number)

600 La Terraza Boulevard, Escondido, California 92025-3873

(Address of Principal Executive Offices)

Registrant s telephone number, including area code: **(760) 741-2111**

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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

Large accelerated filer x Accelerated filer o Non-accelerated filer o Smaller reporting company o

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

There were 222,634,394 shares of common stock outstanding as of July 15, 2014.

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REALTY INCOME CORPORATION

Form 10-Q

June 30, 2014

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

REALTY INCOME CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

June 30, 2014 and December 31, 2013

(dollars in thousands, except per share data)

	2014 (unaudited)	2013
ASSETS		
Real estate, at cost:		
Land	$ 2,991,946	$ 2,791,147
Buildings and improvements	7,869,046	7,108,328
Total real estate, at cost	10,860,992	9,899,475
Less accumulated depreciation and amortization	(1,249,461)	(1,114,888)
Net real estate held for investment	9,611,531	8,784,587
Real estate held for sale, net	9,598	12,022
Net real estate	9,621,129	8,796,609
Cash and cash equivalents	8,908	10,257
Accounts receivable, net	43,751	39,323
Acquired lease intangible assets, net	1,048,139	935,459
Goodwill	15,556	15,660
Other assets, net	74,919	127,133
Total assets	$ 10,812,402	$ 9,924,441
LIABILITIES AND EQUITY		
Distributions payable	$ 44,353	$ 41,452
Accounts payable and accrued expenses	98,973	102,511
Acquired lease intangible liabilities, net	174,769	148,250
Other liabilities	36,682	44,030
Line of credit payable	70,800	128,000
Term loan	70,000	70,000
Mortgages payable, net	916,454	783,360
Notes payable, net	3,535,957	3,185,480
Total liabilities	4,947,988	4,503,083
Commitments and contingencies		
Stockholders equity:		
Preferred stock and paid in capital, par value $0.01 per share, 69,900,000 shares authorized and 25,150,000 shares issued and outstanding as of June 30, 2014 and December 31, 2013	609,363	609,363
Common stock and paid in capital, par value $0.01 per share, 370,100,000 shares authorized, 222,623,256 shares issued and outstanding as of June 30, 2014 and 207,485,073 shares issued and outstanding at December 31, 2013	6,357,084	5,767,878
Distributions in excess of net income	(1,130,746)	(991,794)
Total stockholders equity	5,835,701	5,385,447
Noncontrolling interests	28,713	35,911
Total equity	5,864,414	5,421,358
Total liabilities and equity	$ 10,812,402	$ 9,924,441

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

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REALTY INCOME CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

For the three and six months ended June 30, 2014 and 2013

(dollars in thousands, except per share data) (unaudited)

	Three months ended June 30, 2014	Three months ended June 30, 2013	Six months ended June 30, 2014	Six months ended June 30, 2013
REVENUE				
Rental	$ 221,868	$ 180,089	$ 435,989	$ 347,887
Tenant reimbursements	6,169	4,485	12,597	10,512
Other	609	1,869	1,632	3,566
Total revenue	228,646	186,443	450,218	361,965
EXPENSES				
Depreciation and amortization	92,894	73,906	182,864	140,655
Interest	52,712	39,232	104,432	80,831
General and administrative	11,587	12,088	24,473	23,716
Property (including reimbursable)	10,127	7,754	20,704	17,326
Income taxes	570	624	1,661	1,201
Provisions for impairment	499	290	2,182	290
Merger-related costs	-	605	-	12,635
Total expenses	168,389	134,499	336,316	276,654
Gain on sales of real estate	1,964	-	3,236	-
Income from continuing operations	62,221	51,944	117,138	85,311
Income from discontinued operations	20	4,572	3,097	44,432
Net income	62,241	56,516	120,235	129,743
Net income attributable to noncontrolling interests	(339)	(77)	(671)	(86)
Net income attributable to the Company	61,902	56,439	119,564	129,657
Preferred stock dividends	(10,482)	(10,482)	(20,965)	(20,965)
Net income available to common stockholders	$ 51,420	$ 45,957	$ 98,599	$ 108,692
Amounts available to common stockholders per common share:				
Income from continuing operations, basic and diluted	$ 0.23	$ 0.21	$ 0.45	$ 0.35
Net income, basic and diluted	$ 0.23	$ 0.23	$ 0.46	$ 0.59
Weighted average common shares outstanding:				
Basic	220,979,955	195,574,014	214,039,692	183,714,191
Diluted	221,360,641	196,076,113	214,406,651	184,153,887

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

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REALTY INCOME CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the six months ended June 30, 2014 and 2013

(dollars in thousands) (unaudited)

	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 120,235	$ 129,743
Adjustments to net income:		
Depreciation and amortization	182,864	140,655
Income from discontinued operations	(3,097)	(44,432)
Amortization of share-based compensation	5,449	7,498
Non-cash rental adjustments	(3,706)	(2,489)
Amortization of net premiums on mortgages payable	(5,394)	(4,441)
Amortization of deferred financing costs	5,267	4,297
Gain on sales of real estate	(3,236)	-
Provisions for impairment on real estate	2,182	290
Cash provided by discontinued operations:		
Real estate	490	3,936
Proceeds from sale of real estate	820	-
Change in assets and liabilities, other than from the impact of our acquisition of American Realty Capital Trust, Inc., or ARCT		
Accounts receivable and other assets	12,745	(6,303)
Accounts payable, accrued expenses and other liabilities	(15,843)	(7,321)
Net cash provided by operating activities	298,776	221,433
CASH FLOWS FROM INVESTING ACTIVITIES		
Investment in real estate, net of cash acquired	(899,405)	(748,374)
Improvements to real estate, including leasing costs	(2,734)	(3,294)
Proceeds from sales of real estate:		
Continuing operations	12,805	8
Discontinued operations	6,918	76,333
Loans receivable	350	(9,584)
Restricted escrow deposits for Section 1031 tax-deferred exchanges and pending acquisitions	(5,280)	(14,448)
Net cash used in investing activities	(887,346)	(699,359)
CASH FLOWS FROM FINANCING ACTIVITIES		
Cash distributions to common stockholders	(234,643)	(191,669)
Cash dividends to preferred stockholders	(20,965)	(20,965)
Borrowings on line of credit	1,054,121	1,533,200
Payments on line of credit	(1,111,321)	(990,200)
Proceeds from notes and bonds payable issued	349,846	-
Principal payment on notes payable	-	(100,000)
Principal payments on mortgages payable	(21,901)	(2,674)
Proceeds from term loan	-	70,000
Repayment of ARCT line of credit	-	(317,207)
Repayment of ARCT term loan	-	(235,000)
Proceeds from common stock offerings, net	528,627	755,136
Distributions to noncontrolling interests	(929)	(287)
Debt issuance costs	(3,243)	(511)
Proceeds from dividend reinvestment and stock purchase plan, net	54,204	1,912
Other items, including shares withheld upon vesting	(6,575)	(6,482)
Net cash provided by financing activities	587,221	495,253
Net increase (decrease) in cash and cash equivalents	(1,349)	17,327
Cash and cash equivalents, beginning of period	10,257	5,248
Cash and cash equivalents, end of period	$ 8,908	$ 22,575

For supplemental disclosures, see note 17.

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

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REALTY INCOME CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2014

(unaudited)

1. Management Statement

The consolidated financial statements of Realty Income Corporation (Realty Income , the Company , we , our or us) were prepare from our books and records without audit and include all adjustments (consisting of only normal recurring accruals) necessary to present a fair statement of results for the interim periods presented. Readers of this quarterly report should refer to our audited consolidated financial statements for the year ended December 31, 2013, which are included in our 2013 Annual Report on Form 10-K, as certain disclosures that would substantially duplicate those contained in the audited financial statements have not been included in this report.

Prior to the date of adoption of Accounting Standards Update 2014-08, *Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity,* or ASU 2014-08, we reported, in discontinued operations, the results of operations of properties that had either been disposed of or classified as held for sale in financial statements issued. See footnote 2.E. below for a description of our early adoption of this recent accounting pronouncement and the impact on our presentation of discontinued operations on our consolidated statements of income.

Certain of the 2013 balances have been revised on our consolidated financial statements as follows:

- We previously reported certain operating activities of our wholly owned taxable REIT subsidiary, Crest Net Lease, Inc., or Crest, as discontinued operations. We have revised the 2013 amounts to report those activities in continuing operations. Subsequent to the revision, results of operations for Crest properties that were disposed of or classified as held for sale as of December 31, 2013, continue to be reported in discontinued operations.

At June 30, 2014, we owned 4,263 properties, located in 49 states and Puerto Rico, containing over 69.1 million leasable square feet.

2. Summary of Significant Accounting Policies and Procedures and Recent Accounting Pronouncements

A. The accompanying consolidated financial statements include the accounts of Realty Income and other entities for which we make operating and financial decisions (i.e., control), after elimination of all material intercompany balances and transactions. We consolidate entities that we control and record a noncontrolling interest for the portion that we do not own. Noncontrolling interest that was created or assumed as part of a business combination was recognized at fair value as of the date of the transaction (see note 10). We have no unconsolidated investments.

B. We have elected to be taxed as a real estate investment trust, or REIT, under the Internal Revenue Code of 1986, as amended, or the Code. We believe we have qualified and continue to qualify as a REIT. Under the REIT operating structure, we are permitted to deduct dividends paid to our stockholders in determining our taxable income. Assuming our dividends equal or exceed our net income, we generally will not be required to pay federal corporate income taxes on such income. Accordingly, no provision has been made for federal income taxes in the accompanying consolidated financial statements, except for federal income taxes of our taxable REIT subsidiaries. The income taxes recorded on our consolidated statements of income represent amounts paid by Realty Income for city and state income and franchise taxes.

C. We recognize an allowance for doubtful accounts relating to accounts receivable for amounts deemed uncollectible. We consider tenant specific issues, such as financial stability and ability to pay rent, when determining collectability of accounts receivable and appropriate allowances to record. The allowance for doubtful accounts was $351,000 at June 30, 2014 and $498,000 at December 31, 2013.

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D. We assign a portion of goodwill to our applicable property sales, which results in a reduction of the carrying amount of our goodwill. In order to allocate goodwill to the carrying amount of properties that we sell, we utilize a relative fair value approach based on the original methodology for assigning goodwill. As we sell properties, our goodwill will likely continue to gradually decrease over time. During our tests for impairment of goodwill during the second quarters of 2014 and 2013, we determined that the estimated fair values of our reporting units exceeded their carrying values. We did not have an impairment on our existing goodwill in 2014 and 2013.

E. In April 2014, the Financial Accounting Standards Board, or FASB, issued ASU 2014-08, which amends Topic 205, *Presentation of Financial Statements*, and Topic 360, *Property, Plant, and Equipment*. The amendments in this ASU changed the definition of discontinued operations by limiting discontinued operations reporting to disposals of components of an entity that represent strategic shifts that have, or will have, a major effect on an entity s operations and financial results. ASU 2014-08 is effective, on a prospective basis, for all disposals or classifications as held for sale of components of an entity that occur within interim and annual periods beginning after December 15, 2014. Early adoption is permitted, but only for disposals or classifications as held for sale that have not been reported in financial statements previously issued. We chose to early adopt ASU 2014-08 beginning with the three-month period ending March 31, 2014. Starting with the first quarter of 2014, the results of operations for all qualifying disposals and properties classified as held for sale that were not previously reported in discontinued operations in our 2013 Annual Report on Form 10-K will be presented within income from continuing operations on our consolidated statements of income.

3. Supplemental Detail for Certain Components of Consolidated Balance Sheets

A. Acquired lease intangible assets, net, consist of the following (dollars in thousands) at:	June 30, 2014	December 31, 2013
Acquired in-place leases	$ 962,363	$ 843,616
Accumulated amortization of acquired in-place leases	(135,514)	(95,084)
Acquired above-market leases	251,793	207,641
Accumulated amortization of acquired above-market leases	(30,503)	(20,714)
	$ 1,048,139	$ 935,459

B. Other assets, net, consist of the following (dollars in thousands) at:	June 30, 2014	December 31, 2013
Deferred financing costs, net	$ 22,867	$ 21,323
Notes receivable issued in connection with property sales	18,537	19,078
Prepaid expenses	12,741	11,674
Credit facility origination costs, net	5,709	7,146
Impounds related to mortgages payable	5,556	5,555
Restricted escrow deposits	5,280	10,158
Corporate assets, net	1,315	1,259
Loans receivable	-	48,844
Other items	2,914	2,096
	$ 74,919	$ 127,133

C. Distributions payable consist of the following declared distributions (dollars in thousands) at:	June 30, 2014	December 31, 2013
Common stock distributions	$ 40,705	$ 37,797
Preferred stock dividends	3,494	3,494
Noncontrolling interests distributions	154	161
	$ 44,353	$ 41,452

D. Accounts payable and accrued expenses consist of the following (dollars in thousands) at:	June 30, 2014	December 31, 2013
Notes payable - interest payable	$ 54,386	$ 55,616
Accrued costs on properties under development	17,974	14,058
Mortgages payable - interest payable	3,244	2,790
Other items	23,369	30,047
	$ 98,973	$ 102,511

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E. Acquired lease intangible liabilities, net, consist of the following (dollars in thousands) at:	June 30, 2014	December 31, 2013
Acquired below-market leases	$ 190,767	$ 158,703
Accumulated amortization of acquired below-market leases	(15,998)	(10,453)
	$ 174,769	$ 148,250

F. Other liabilities consist of the following (dollars in thousands) at:	June 30, 2014	December 31, 2013
Rent received in advance	$ 24,002	$ 31,144
Preferred units issued upon acquisition of ARCT	6,750	6,750
Security deposits	5,930	6,136
	$ 36,682	$ 44,030

4. Investments in Real Estate

We acquire land, buildings and improvements necessary for the successful operations of commercial tenants.

A. Acquisitions during the First Six Months of 2014 and 2013

During the first six months of 2014, we invested $1.06 billion in 402 new properties and properties under development or expansion with an initial weighted average contractual lease rate of 7.1%. The 402 new properties and properties under development or expansion, are located in 39 states, will contain over 6.9 million leasable square feet and are 100% leased with a weighted average lease term of 12.8 years. The tenants occupying the new properties operate in 24 industries and the property types consist of 83.0% retail, 8.5% office, 6.8% industrial and distribution, and 1.7% manufacturing, based on rental revenue. None of our investments during the first six months of 2014 caused any one tenant to be 10% or more of our total assets at June 30, 2014.

We previously disclosed a purchase and sale agreement with Inland Diversified Real Estate Trust, Inc., or Inland, and certain subsidiaries of Inland, to acquire 84 single-tenant, 100% net-leased properties, for $502.9 million, which were acquired during the first six months of 2014.

The $1.06 billion invested during the first six months of 2014 was allocated as follows: $209.2 million to land, $721.4 million to buildings and improvements, $161.8 million to intangible assets related to leases, $901,000 to other assets, net, and $30.9 million to intangible liabilities related to leases and other assumed liabilities. We also recorded net mortgage premiums of $718,000 associated with the $159.7 million of mortgages acquired during the first six months of 2014. There was no contingent consideration associated with these acquisitions.

The properties acquired during the first six months of 2014 contributed total revenues of $24.4 million and income from continuing operations of $9.4 million.

The purchase price allocation for $389.7 million invested by us in the second quarter of 2014 is based on a preliminary measurement of fair value that is subject to change. The allocation for these properties represents our current best estimate of fair value and we expect to finalize the valuations and complete the purchase price allocations in 2014. In the first six months of 2014, we finalized the purchase price allocations for $120.8 million invested in the fourth quarter of 2013 and $400.1 million invested in the first quarter of 2014. There were no material changes to our consolidated balance sheets or income statements as a result of these purchase price allocation adjustments.

In comparison, during the first six months of 2013, Realty Income invested $866.5 million in 206 properties and properties under development or expansion (in addition to our acquisition of American Realty Capital Trust, Inc. or ARCT, which is discussed below), with an initial weighted average contractual lease rate of 7.0%. These 206 properties are located in 35 states, contain over 5.1 million leasable square feet and are 100% leased with a weighted average lease term of 13.8 years. The tenants occupying the new properties operate in 17 industries and the property types consist of 86.1% retail, 5.4% office, 4.7% industrial and distribution, and 3.8% manufacturing, based on rental revenue. These investments are in addition to the $3.2 billion acquisition of ARCT, which added 515 properties to our real estate portfolio during the first quarter of 2013.

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The 515 properties added to our real estate portfolio as a result of the ARCT acquisition are located in 44 states and Puerto Rico, contain over 16.0 million leasable square feet, and are 100% leased with a weighted average lease term of 12.2 years. The 69 tenants occupying the 515 properties acquired operate in 28 industries and the property types consist of 54.0% retail, 32.6% industrial and distribution, and 13.4% office, based on rental revenue. We recorded ARCT merger-related transaction costs of $12.6 million in the first six months of 2013. These merger related transaction costs included, but were not limited to, advisor fees, legal fees, accounting fees, printing fees and transfer taxes.

Our combined total investment in real estate assets, including the ARCT acquisition, during the first six months of 2013 was $4.0 billion.

The $4.0 billion invested during the first six months of 2013 was allocated as follows: $597.6 million to land, $2.79 billion to buildings and improvements, $726.4 million to intangible assets related to leases, $13.7 million to other assets, net, and $96.7 million to intangible liabilities related to leases and other assumed liabilities. We also recorded mortgage premiums of $28.4 million associated with the mortgages acquired. There was no contingent consideration associated with these acquisitions. This allocation has been adjusted from that previously reported in the Quarterly Report on Form 10-Q for the quarter ended June 30, 2013, as a result of measurement period adjustments, previously disclosed in our 2013 Annual Report on Form 10-K, that were recorded during the second half of 2013 upon completion of the real estate valuations for the ARCT portfolio. As a result of these adjustments to the asset allocation, revisions were made to our income statement for the three and six months ended June 30, 2013 for the impact related to rental revenue and depreciation and amortization. The net impact of these revisions increased net income by $1.8 million for the second quarter of 2013 and $3.2 million for the first six months of 2013.

The estimated initial weighted average contractual lease rate for a property is generally computed as estimated contractual net operating income, which, in the case of a net leased property, is equal to the aggregate base rent under the lease for the first full year of each lease, divided by the total cost of the property. Since it is possible that a tenant could default on the payment of contractual rent, we cannot provide assurance that the actual return on the funds invested will remain at the percentages listed above.

In the case of a property under development or expansion, the contractual lease rate is generally fixed such that rent varies based on the actual total investment in order to provide a fixed rate of return. When the lease does not provide for a fixed rate of return on a property under development or expansion, the estimated initial weighted average contractual lease rate is computed as follows: estimated net operating income (determined by the lease) for the first full year of each lease, divided by our projected total investment in the property, including land, construction and capitalized interest costs. Of the $1.06 billion we invested during the first six months of 2014, $35.6 million was invested in 21 properties under development or expansion with an estimated initial weighted average contractual lease rate of 8.5%.

B.   Acquisition Transaction Costs

Acquisition transaction costs (excluding ARCT merger-related costs) of $645,000 and $818,000 were recorded to general and administrative expense on our consolidated statement of income for the first six months of 2014 and 2013, respectively.

C.   Investments in Existing Properties

During the first six months of 2014, we capitalized costs of $2.7 million on existing properties in our portfolio, consisting of $467,000 for re-leasing costs and $2.3 million for building and tenant improvements. In comparison, during the first six months of 2013, we capitalized costs of $3.3 million on existing properties in our portfolio, consisting of $774,000 for re-leasing costs and $2.5 million for building and tenant improvements.

D. Properties with Existing In-place Leases

Of the $1.06 billion we invested in the first six months of 2014, approximately $789.8 million was used to acquire 149 properties with existing in-place leases. In comparison, of the $4.0 billion invested during the first six months of 2013, approximately $3.97 billion was used to acquire 712 properties with existing in-place leases. The value of the in-place and above-market leases is recorded to acquired lease intangible assets, net on our consolidated balance sheets, and the value of the below-market leases is recorded to acquired lease intangible liabilities, net on our consolidated balance sheets. The values recorded to all of these intangible values, during the second quarter of 2014, are based on a preliminary measurement of fair value that is subject to change.

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The value of the in-place leases is amortized as depreciation and amortization expense. The amounts amortized to expense for the first six months of 2014 and 2013 were $40.8 million and $28.7 million, respectively.

The value of the above-market and below-market leases is amortized as rental revenue on our consolidated statements of income. All of these amounts are amortized over the term of the respective leases. The amounts amortized as a net decrease to rental revenue for capitalized above-market and below-market leases for both the first six months of 2014 and 2013 were $4.2 million. If a lease were to be terminated prior to its stated expiration, all unamortized amounts relating to that lease would be recorded to revenue or expense as appropriate.

The following table presents the impact during the next five years and thereafter related to the net decrease to rental revenue from the amortization of the acquired above-market and below-market lease intangibles and the increase to amortization expense from the amortization of the in-place lease intangibles for properties owned at June 30, 2014 (in thousands):

		Net decrease to rental revenue		**Increase to amortization expense**
2014	$	(4,159)	$	42,409
2015		(8,372)		83,323
2016		(8,384)		82,951
2017		(8,355)		81,726
2018		(8,110)		79,280
Thereafter		(9,141)		457,160
Totals	$	(46,521)	$	826,849

5. Credit Facility

We have a $1.5 billion unsecured acquisition credit facility with an initial term that expires in May 2016 and includes, at our election, a one-year extension option. Under this credit facility, our current investment grade credit ratings provide for financing at the London Interbank Offered Rate, commonly referred to as LIBOR, plus 1.075% with a facility commitment fee of 0.175%, for all-in drawn pricing of 1.25% over LIBOR. The borrowing rate is not subject to an interest rate floor or ceiling. We also have other interest rate options available to us under this credit facility. Our credit facility is unsecured and, accordingly, we have not pledged any assets as collateral for this obligation.

At June 30, 2014, credit facility origination costs of $5.7 million are included in other assets, net, on our consolidated balance sheets. These costs are being amortized over the remaining term of our current $1.5 billion credit facility.

At June 30, 2014, we had a borrowing capacity of $1.43 billion available on our credit facility (subject to customary conditions to borrowing) and an outstanding balance of $70.8 million, as compared to an outstanding balance of $128.0 million at December 31, 2013.

The weighted average interest rate on outstanding borrowings under our credit facility was 1.2% during the first six months of 2014 and 1.3% during the first six months of 2013. At June 30, 2014, the effective interest rate was 1.2%. Our current credit facility is subject to various leverage and interest coverage ratio limitations, and at June 30, 2014, we remain in compliance with these covenants.

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6. Mortgages Payable

During the first six months of 2014, we made $21.9 million in principal payments, including the repayment of two mortgages in full for $18.2 million. Additionally, during the first six months of 2014, we assumed mortgages totaling $159.7 million, excluding net premiums. The mortgages are secured by the properties on which the debt was placed. $145.0 million of mortgages assumed during the first six months of 2014 are considered non-recourse with limited customary exceptions for items such as solvency, bankruptcy, misrepresentation, fraud, misapplication of payments, environmental liabilities, failure to pay taxes, insurance premiums, liens on the property, violations of the single purpose entity requirements, and uninsured losses. The remaining $14.7 million, representing two mortgages, has partial recourse to Realty Income in the aggregate amount of $3.2 million; the remaining balance of $11.5 million is non-recourse and includes the same customary exceptions described in the preceding sentence. We expect to pay off the mortgages as soon as prepayment penalties make it economically feasible to do so.

During the first six months of 2014, aggregate net premiums totaling $718,000 were recorded upon assumption of the mortgages for above-market interest rates, as compared to net premiums totaling $28.4 million recorded in the first six months of 2013. Amortization of these net premiums is recorded as a reduction to interest expense over the remaining term of the respective mortgages, using a method that approximates the effective-interest method.

These mortgages contain customary covenants, such as limiting our ability to further mortgage each applicable property or to discontinue insurance coverage, without the prior consent of the lender. At June 30, 2014, we remain in compliance with these covenants.

We did not incur any deferred financing costs on our mortgages payable assumed in the first six months of 2014 or 2013. The balance of our deferred financing costs, which are classified as part of other assets, net, on our consolidated balance sheets, was $1.0 million at June 30, 2014, and $1.2 million at December 31, 2013, which is being amortized over the remaining term of each mortgage.

The following is a summary of all our mortgages payable as of June 30, 2014 and December 31, 2013, respectively (dollars in thousands):

As Of	Number of Properties(1)	Weighted Average Stated Interest Rate(2)	Weighted Average Effective Interest Rate(3)	Weighted Average Remaining Years Until Maturity	Remaining Principal Balance	Unamortized Premium Balance	Mortgage Payable Balance
6/30/14	266	5.1%	3.9%	4.1	$ 892,279	$ 24,175	$ 916,454
12/31/13	227	5.3%	3.9%	4.3	$ 754,508	$ 28,852	$ 783,360

(1) At June 30, 2014, there were 60 mortgages on the 266 properties, while at December 31, 2013, there were 47 mortgages on the 227 properties. The mortgages require monthly payments, with principal payments due at maturity. The mortgages are at fixed interest rates, except for five mortgages on 14 properties totaling $74.3 million at June 30, 2014, including net unamortized discounts. All of these variable rate mortgages were acquired with arrangements which limit our exposure to interest rate risk.

(2) Stated interest rates ranged from 2.0% through 6.9% at June 30, 2014, while stated interest rates ranged from 2.5% to 6.9% at December 31, 2013.

(3) Effective interest rates range from 2.2% through 9.1% at June 30, 2014, while effective interest rates ranged from 2.4% to 9.2% at December 31, 2013.

The following table summarizes the maturity of mortgages payable, excluding net premiums of $24.2 million, as of June 30, 2014 (dollars in millions):

Year of Maturity		
2014	$	57.4
2015		125.3
2016		248.4
2017		142.3
2018		15.0
Thereafter		303.9
Totals	$	892.3

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7. Term Loan

In January 2013, in conjunction with our acquisition of ARCT, we entered into a $70 million senior unsecured term loan maturing January 21, 2018. Borrowing under the term loan bears interest at the current one month LIBOR, plus 1.2%. In conjunction with this term loan, we also acquired an interest rate swap which essentially fixes our per annum interest rate on the term loan at 2.15%. As a result of entering into our term loan, we incurred deferred financing costs of $303,000 in 2013, which are being amortized over the remaining term of the term loan. The net balance of these deferred financing costs was $217,000 at June 30, 2014, and $248,000 at December 31, 2013, which is classified as part of other assets, net on our consolidated balance sheets.

8. Notes Payable

A. General

Our senior unsecured notes and bonds consist of the following, sorted by maturity date (dollars in millions):

		June 30, 2014		December 31, 2013
5.5% notes, issued in November 2003 and due in November 2015	$	150	$	150
5.95% notes, issued in September 2006 and due in September 2016		275		275
5.375% notes, issued in September 2005 and due in September 2017		175		175
2.0% notes, issued in October 2012 and due in January 2018		350		350
6.75% notes, issued in September 2007 and due in August 2019		550		550
5.75% notes, issued in June 2010 and due in January 2021		250		250
3.25% notes, issued in October 2012 and due in October 2022		450		450
4.65% notes, issued in July 2013 and due in August 2023		750		750
3.875% notes, issued in June 2014 and due in July 2024		350		-
5.875% bonds, $100 issued in March 2005 and $150 issued in June 2011, both due in March 2035		250		250
Total principal amount		3,550		3,200
Unamortized original issuance discounts		(14)		(15)
	$	3,536	$	3,185

The following table summarizes the maturity of our notes and bonds payable as of June 30, 2014, excluding unamortized original issuance discounts (dollars in millions):

Year of Maturity		Notes and Bonds
2014	$	-
2015		150
2016		275
2017		175
2018		350
Thereafter		2,600
Totals	$	3,550

As of June 30, 2014, the weighted average interest rate on our notes and bonds payable was 4.8% and the weighted average remaining years until maturity was 7.4 years.

B. Note Issuance

In June 2014, we issued $350 million of 3.875% senior unsecured notes due July 2024, or the 2024 Notes. The price to the investors for the 2024 Notes was 99.956% of the principal amount for an effective yield of 3.88% per annum. The total net proceeds of approximately $346.6 million from these offerings were used to repay a portion of the outstanding borrowings under our acquisition credit facility. Interest is paid semiannually on the 2024 Notes.

C. Note Repayment

In March 2013, we repaid $100 million of outstanding 5.375% notes, plus accrued and unpaid interest, using proceeds from our March 2013 common stock offering and our credit facility.

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9. Issuance of Common Stock

In April 2014, we issued 13,800,000 shares of common stock, including 1,800,000 shares purchased by the underwriters upon the exercise of their option to purchase additional shares. After underwriting discounts and other offering costs of $22.8 million, the net proceeds of $528.6 million were used to repay borrowings under our acquisition credit facility.

In March 2013, we issued 17,250,000 shares of common stock, including 2,250,000 shares purchased by the underwriters upon the exercise of their option to purchase additional shares. After underwriting discounts and other offering costs of $36.7 million, the net proceeds of $755.1 million were used to redeem our 5.375% notes in March 2013 and repay borrowings under our acquisition credit facility, which were used to fund property acquisitions, including our acquisition of ARCT.

In connection with our January 2013 acquisition of ARCT, we issued a total of 45,573,144 shares of our common stock to ARCT shareholders and we received 208,709 shares of our common stock that were previously held by ARCT. The total value of the 45,573,144 common shares was approximately $2 billion.

10. Noncontrolling Interests

In January 2013, we completed our acquisition of ARCT. Equity issued as consideration for this transaction included common and preferred partnership units issued from Tau Operating Partnership, L.P., or Tau Operating Partnership, the consolidated subsidiary which owns properties acquired through the ARCT acquisition. Realty Income and its subsidiaries hold a 99.3% interest in Tau Operating Partnership, and consolidate the entity.

In June 2013, we completed the acquisition of a portfolio of properties by issuing common units in a newly formed entity, Realty Income, L.P. The units issued as consideration for the acquisition represent a 2.2% ownership in Realty Income, L.P. at June 30, 2014. Realty Income holds the remaining 97.8% interests in this entity, and consolidates the entity.

A. Neither of the common partnership units has voting rights. Both common partnership units are entitled to monthly distributions equal to the amount paid to common stockholders of Realty Income, and are redeemable in cash or Realty Income common stock, at our option, and at a conversion ratio of one to one, subject to certain exceptions. Noncontrolling interests with redemption provisions that permit the issuer to settle in either cash or common stock, at the option of the issuer, were evaluated to determine whether temporary or permanent equity classification on the balance sheet was appropriate. We evaluated this guidance and determined that the units meet the requirements to qualify for presentation as permanent equity.

The following table represents the change in the carrying value of all noncontrolling interests through June 30, 2014 (dollars in thousands):

	Tau Operating Partnership units(1)	Realty Income, L.P. units(2)	Total
Carrying value at December 31, 2013	$ 13,489	$ 22,422	$ 35,911
Reallocation of equity	-	(6,647)	(6,647)
Redemptions	-	(294)	(294)
Distributions	(347)	(581)	(928)
Allocation of net income	124	547	671
Carrying value at June 30, 2014	$ 13,266	$ 15,447	$ 28,713

	Tau Operating Partnership units(1)	Realty Income, L.P. units(2)	Total
Fair value of units issued during 2013	$ 13,962	$ 22,601	$ 36,563
Distributions	(691)	(680)	(1,371)
Allocation of net income	218	501	719
Carrying value at December 31, 2013	$ 13,489	$ 22,422	$ 35,911

(1) 317,022 Tau Operating Partnership units were issued on January 22, 2013 and remain outstanding as of June 30, 2014.

(2) 534,546 Realty Income, L.P. units were issued on June 27, 2013, and 524,546 units remain outstanding as of June 30, 2014.

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During the first six months of 2014 we recorded an equity reclassification adjustment of $6.6 million between noncontrolling interests and additional paid in capital to adjust the carrying value of the Realty Income, L.P. noncontrolling interests to be in-line with their equity ownership interest in the entity.

B. The Tau Operating Partnership preferred units were recorded at fair value as of the date of acquisition. Since they are redeemable at a fixed price on a determinable date, we have classified them in other liabilities on our consolidated balance sheets. Payments on these preferred units are made monthly at a rate of 2% per annum and are included in interest expense. As of June 30, 2014, the preferred units have a carrying value of $6.75 million.

11. Fair Value of Financial Assets and Liabilities

Fair value is defined as the price that would be received from the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The disclosure for assets and liabilities measured at fair value requires allocation to a three-level valuation hierarchy. This valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. Categorization within this hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

We believe that the carrying values reflected on our consolidated balance sheets reasonably approximate the fair values for cash and cash equivalents, accounts receivable, escrow deposits, loans receivable, line of credit payable, term loan and all other liabilities, due to their short-term nature or interest rates and terms that are consistent with market, except for our notes receivable issued in connection with property sales, mortgages payable (which includes net mortgage premiums) and our senior notes and bonds payable, which are disclosed below (dollars in millions):

At June 30, 2014		**Carrying value per balance sheet**		**Estimated fair value**
Notes receivable issued in connection with property sales	$	18.5	$	20.4
Mortgages payable assumed in connection with acquisitions		916.5		915.1
Notes payable, net of unamortized original issuance discounts		3,536.0		3,828.3

At December 31, 2013		**Carrying value per balance sheet**		**Estimated fair value**
Notes receivable issued in connection with property sales	$	19.1	$	21.1
Mortgages payable assumed in connection with acquisitions		783.4		780.0
Notes payable, net of unamortized original issuance discounts		3,185.5		3,340.7

The estimated fair values of our notes receivable issued in connection with property sales and our mortgages payable have been calculated by discounting the future cash flows using an interest rate based upon the relevant Treasury yield curve, plus an applicable credit-adjusted spread. Because this methodology includes unobservable inputs that reflect our own internal assumptions and calculations, the measurement of estimated fair values, related to our notes receivable and mortgages payable, is categorized as level three on the three-level valuation hierarchy.

The estimated fair values of our senior notes and bonds payable are based upon indicative market prices and recent trading activity of our senior notes and bonds payable. Because this methodology includes inputs that are less observable by the public and are not necessarily reflected in active markets, the measurement of the estimated fair values, related to our senior notes and bonds payable, is categorized as level two on the three-level valuation hierarchy.

12. Gain on Sales of Real Estate

During the second quarter of 2014, we sold six properties for $7.0 million, which resulted in a gain of $2.0 million. During the first six months of 2014, we sold 17 properties for $19.7 million, which resulted in a gain of $5.8 million. Only the results of operations specifically related to the properties classified as held for sale at December 31, 2013 and sold during the first six months of 2014 have been reclassified as discontinued operations.

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In comparison, during the second quarter of 2013, Realty Income sold 17 properties for $23.7 million, which resulted in a gain of $5.7 million. During the first six months of 2013, we sold 34 properties for $83.7 million which resulted in a gain of $44.3 million. The results of operations for the dispositions during 2013 have been reclassified as discontinued operations.

During the first six months of 2014, Crest sold one property for $820,000, which resulted in no gain. The results of operations for this property have been reclassified as discontinued operations. During the first six months of 2013, Crest did not sell any properties.

13. Impairments

We review long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. A provision is made for impairment if estimated future operating cash flows (undiscounted and without interest charges) plus estimated disposition proceeds (undiscounted) are less than the current book value of the property. Key factors that we estimate in this analysis include projected rental rates, estimated holding periods, capital expenditures and property sales capitalization rates. If a property is classified as held for sale, it is carried at the lower of carrying cost or estimated fair value, less estimated cost to sell, and depreciation of the property ceases.

During the second quarter of 2014 we recorded total provisions for impairment of $499,000 on two properties classified as held for sale in the following industries: one in the home improvement industry and one in the restaurant-casual dining industry. For the first six months of 2014, we recorded total provisions for impairment of $2.2 million on three sold properties and three properties classified as held for sale in the following industries: one in the consumer electronics industry, one in the home furnishings industry, one in the home improvement industry, and three in the restaurant-casual dining industry. These properties were not previously classified as held for sale in financial statements issued prior to the date of adoption of ASU 2014-08; accordingly, these provisions for impairment are included in income from continuing operations on our consolidated statements of income for the three and six months ended June 30, 2014.

In comparison, for the second quarter of 2013, we recorded total provisions for impairment of $2.5 million on one sold property and two properties classified as held for sale in the following industries: one in the automotive service industry, one in the grocery store industry, and one in our other industry. For the first six months of 2013, we recorded total provisions for impairment of $3.0 million on seven sold properties and two properties classified as held for sale in the following industries: one in the automotive parts industry, two in the automotive service industry, two in the child care industry, one in the grocery store industry, one in the pet supplies and services industry, one in the restaurant-casual dining industry, and one in our other industry. Except for a provision for impairment of $290,000 that was recorded in income from continuing operations for one property not previously classified as held for sale as of December 31, 2013, the remaining provisions for impairment are included in income from discontinued operations on our consolidated statement of income for the three and six months ended June 30, 2013.

14. Discontinued Operations

Operations from nine properties were classified as held for sale at June 30, 2014. We do not depreciate properties that are classified as held for sale. The results of operations for eight of these properties that have not previously been classified as held for sale are included in income from continuing operations, and the results of operations of the one remaining property that was classified as held for sale as of December 31, 2013 have been reclassified to discontinued operations on our consolidated statement of income for the three and six months ended June 30, 2014.

No debt was assumed by buyers of our properties, or repaid as a result of our property sales, and we do not allocate interest expense to discontinued operations related to real estate held for investment.

The following is a summary of income from discontinued operations on our consolidated statements of income (dollars in thousands):

Income from discontinued operations	**Three months ended June 30, 2014**	**2013**	**Six months ended June 30, 2014**	**2013**
Gain on sales of real estate	$ -	$ 5,744	$ 2,607	$ 44,304
Rental revenue	33	1,322	97	4,110
Tenant reimbursements	(2)	67	-	99
Other revenue	6	397	13	408
Depreciation and amortization	-	(615)	-	(1,110)
Property expenses (including reimbursable)	(17)	(98)	(118)	(638)
Provisions for impairment	-	(2,206)	-	(2,662)
Crest s income (loss) from discontinued operations	-	(39)	498	(79)
Income from discontinued operations	$ 20	$ 4,572	$ 3,097	$ 44,432
Per common share, basic and diluted	$ 0.00	$ 0.02	$ 0.01	$ 0.24

15. Distributions Paid and Payable

A. Common Stock

We pay monthly distributions to our common stockholders. The following is a summary of the monthly distributions paid per common share for the first six months of 2014 and 2013:

Month	**2014**	**2013**
January	$ 0.1821667	$ 0.1517500
February	0.1821667	0.1809167
March	0.1821667	0.1809167
April	0.1824792	0.1812292
May	0.1824792	0.1812292
June	0.1824792	0.1812292
Total	$ 1.0939377	$ 1.0572710

At June 30, 2014, a distribution of $0.1827917 per common share was payable and was paid in July 2014.

B. Class E Preferred Stock

In 2006, we issued 8.8 million shares of our 6.75% Monthly Income Class E Cumulative Redeemable Preferred Stock, or Class E preferred stock, at a price of $25.00 per share. Since December 7, 2011, the shares of Class E preferred stock were redeemable, at our option, for $25.00 per share. During each of the first six months of 2014 and 2013, we paid six monthly dividends to holders of our Class E preferred stock totaling $0.84375 per share, or $7.4 million, and at June 30, 2014, a monthly dividend of $0.140625 per share was payable and was paid in July 2014.

C. Class F Preferred Stock

In February 2012, we issued 14.95 million shares of 6.625% Monthly Income Class F Cumulative Redeemable Preferred Stock, or Class F preferred stock, at a price of $25.00 per share. In April 2012, we issued an additional 1.4 million shares of our Class F preferred stock at a price of $25.2863 per share. Beginning February 15, 2017, the shares of Class F preferred stock are redeemable, at our option, for $25.00 per share, plus any accrued and unpaid dividends. During each of the first six months of 2014 and 2013, we paid six monthly dividends to holders of our Class F preferred stock totaling $0.828126 per share, or $13.5 million, and at June 30, 2014, a monthly dividend of $0.138021 per share was payable and was paid in July 2014.

We are current in our obligations to pay dividends on our Class E and Class F preferred stock.

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16. Net Income Per Common Share

Basic net income per common share is computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding during each period. Diluted net income per common share is computed by dividing net income available to common stockholders for the period by the weighted average number of common shares that would have been outstanding assuming the issuance of common shares for all potentially dilutive securities outstanding during the reporting period.

The following is a reconciliation of the denominator of the basic net income per common share computation to the denominator of the diluted net income per common share computation. The numerator has been adjusted for income allocated to convertible common units determined to be dilutive.

	Three months ended June 30,		Six months ended June 30,	
	2014	**2013**	**2014**	**2013**
Weighted average shares used for the basic net income per share computation	220,979,955	195,574,014	214,039,692	183,714,191
Incremental shares from share-based compensation	63,664	185,077	49,937	159,456
Weighted average partnership common units convertible to common shares that were dilutive	317,022	317,022	317,022	280,240
Weighted average shares used for diluted net income per share computation	221,360,641	196,076,113	214,406,651	184,153,887
Unvested shares from share-based compensation that were anti-dilutive	59,149	16,600	59,569	16,600
Weighted average partnership common units convertible to common shares that were anti-dilutive	529,161	23,497	531,839	11,813

17. Supplemental Disclosures of Cash Flow Information

Cash paid for interest was $104.2 million in the first six months of 2014 and $78.6 million in the first six months of 2013.

Interest capitalized to properties under development was $220,000 in the first six months of 2014 and $369,000 in the first six months of 2013.

Cash paid for income taxes was $2.9 million in the first six months of 2014 and $1.5 million in the first six months of 2013.

The following non-cash investing and financing activities are included in the accompanying consolidated financial statements:

A. Share-based compensation expense was $5.4 million for the first six months of 2014 and was $7.5 million for the first six months of 2013.

B. See note 13 for a discussion of impairments recorded by Realty Income for the first six months of 2014 and 2013.

C. During the first six months of 2014, we acquired mortgages payable to third-party lenders of $159.7 million, recorded $718,000 of net premiums, and recorded $901,000 of interest rate swap value to other assets, net, related to property acquisitions. During the first six months of 2013, we acquired mortgages payable (excluding the mortgages payable discussed in items D and E) of $113.7 million to third-party lenders and recorded $5.7 million of net premiums related to property acquisitions.

D. During the first six months of 2013, the following components were acquired in connection with our acquisition of ARCT: (1) real estate investments and related intangible assets of $3.2 billion, (2) other assets of $19.5 million, (3) lines of credit payable of $317.2 million, (4) a term loan for $235.0 million, (5) mortgages payable of $539.0 million, (6) intangible liabilities of $79.7 million, (7) other liabilities of $29.0 million, and (8) noncontrolling interests of $14.0 million.

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E. During the first six months of 2013, we acquired $55.9 million of real estate through the assumption of a $32.4 million mortgage payable, the issuance of 534,546 units by Realty Income, L.P. and cash of $1.0 million.

F. During the first six months of 2014, we applied $48.9 million of loans receivable to the purchase price of five properties acquired during the period.

G. Accrued costs on properties under development resulted in an increase in buildings and improvements and accounts payable of $3.9 million at June 30, 2014, and $836,000 at June 30, 2013.

18. Segment Information

We evaluate performance and make resource allocation decisions on an industry by industry basis. For financial reporting purposes, we have grouped our tenants into 48 activity segments. All of the properties are incorporated into one of the applicable segments. Because almost all of our leases require the tenant to pay operating expenses, rental revenue is the only component of segment profit and loss we measure.

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The following tables set forth certain information regarding the properties owned by us, classified according to the business of the respective tenants, as of June 30, 2014 (dollars in thousands):

[redacted]

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[redacted]

19. Common Stock Incentive Plan

In 2012, our Board of Directors adopted and stockholders approved the Realty Income Corporation 2012 Incentive Award Plan, or the 2012 Plan, to enable us to motivate, attract and retain the services of directors, employees and consultants considered essential to our long-term success. The 2012 Plan offers our directors, employees and consultants an opportunity to own stock in Realty Income or rights that will reflect our growth, development and financial success. Under the terms of the 2012 Plan, the aggregate number of shares of our common stock subject to options, restricted stock, stock appreciation rights, restricted stock units and other awards, will be no more than 3,985,734 shares. The 2012 Plan has a term of 10 years from the date it was adopted by the Board of Directors.

The amount of share-based compensation costs recognized in general and administrative expense on our consolidated statements of income was $2.8 million during the second quarter of 2014, $3.7 million during the second quarter of 2013, $5.4 million during the first six months of 2014 and $7.5 million during the first six months of 2013.

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A. Restricted Stock

The following table summarizes our common stock grant activity under the 2012 Plan. Our common stock grants vest over periods ranging from immediately to five years.

	For the six months ended June 30, 2014			For the year ended December 31, 2013		
	Number of shares		Weighted average price(1)	Number of shares		Weighted average price(1)
Outstanding nonvested shares, beginning of year	722,263	$	23.37	895,550	$	19.94
Shares granted	250,993	$	39.67	484,060	$	41.13
Shares vested	(316,415)	$	36.51	(654,650)	$	30.91
Shares forfeited	(15,804)	$	38.81	(2,697)	$	37.30
Outstanding nonvested shares, end of each period	641,037	$	32.40	722,263	$	23.37

(1) Grant date fair value.

During the first six months of 2014, we issued 250,993 shares of common stock under the 2012 Plan. These shares vest over the following service periods: 30,829 vested immediately, 8,000 vest over a service period of two years, 4,000 vest over a service period of three years, 30,535 vest over a service period of four years, and 177,629 vest over a service period of five years. Additionally, during 2013, 51,454 shares of performance-based common stock was granted, of which 12,864 shares vested at the end of 2013 based on the achievement of certain 2013 performance metrics, and of which 12,864 may vest at the end of 2014, 2015 and 2016, if certain performance metrics are reached.

As of June 30, 2014, the remaining unamortized share-based compensation expense related to restricted stock totaled $21.0 million, which is being amortized on a straight-line basis over the service period of each applicable award.

Due to a historically low turnover rate, we do not estimate a forfeiture rate for our nonvested shares. Accordingly, unexpected forfeitures will lower share-based compensation expense during the applicable period. Under the terms of our 2012 Plan, we pay non-refundable dividends to the holders of our nonvested shares. Applicable accounting guidance requires that the dividends paid to holders of these nonvested shares be charged as compensation expense to the extent that they relate to nonvested shares that do not or are not expected to vest. However, since we do not estimate forfeitures given our historical trends, we did not record any compensation expense related to dividends paid in the first six months of 2014 or 2013.

B. Performance Shares

During the first six months of 2014, we granted performance share awards, as well as dividend equivalent rights. Eighty percent (80%) of the total award value is market-based and subject to two Total Shareholder Return (TSR) market measures: 60% relative to the MSCI US REIT Index and 20% relative to the NAREIT Freestanding Index. The remaining 20% is performance-based, and will vest based on our debt-to-EBITDA ratio achieved during the performance period. The number of performance shares that vest based on the achievement of the performance goals will vest 50% on January 1, 2017 and 50% on January 1, 2018, subject to continued employment.

During the first six months of 2014, 71,705 performance shares, with an estimated fair value of $3.0 million and an average grant date fair value of $41.46, were granted to our executive officers. The performance period for these awards began on January 1, 2014 and will end on December 31, 2016. The fair value of the market-based awards was estimated on the date of grant using a Monte Carlo Simulation model.

As of June 30, 2014, the remaining unamortized share-based compensation expense related to the performance shares totaled $2.8 million. The portion related to the market-based awards is being amortized on a straight-line basis over the service period, and the portion related to the performance-based awards is being amortized on a tranche-by-tranche basis over the service period.

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20. Dividend Reinvestment and Stock Purchase Plan

We have a Dividend Reinvestment and Stock Purchase Plan, or the DRSPP, to provide our common stockholders, as well as new investors, with a convenient and economical method of purchasing our common stock and reinvesting their distributions. The DRSPP also allows our current stockholders to buy additional shares of common stock by reinvesting all or a portion of their distributions. The DRSPP authorizes up to 6,000,000 common shares to be issued. During the first six months of 2014, we issued 1,240,305 shares and raised approximately $54.4 million under the DRSPP. During the first six months of 2013, we issued 44,549 shares and raised approximately $2.0 million under the DRSPP. From the inception of the DRSPP, in April 2011, through June 30, 2014, we have issued 2,804,647 shares and raised approximately $114.5 million.

In 2013, we revised our DRSPP to pay for a majority of the plan-related fees, which were previously paid by investors, and to institute a waiver approval process, allowing larger investors or institutions, per a formal approval process, to purchase shares at a small discount, if approved by us. In June 2014, we issued 1,135,897 shares and raised $50.0 million under the waiver approval process.

21. Commitments and Contingencies

In the ordinary course of business, we are party to various legal actions which we believe are routine in nature and incidental to the operation of our business. We believe that the outcome of the proceedings will not have a material adverse effect upon our consolidated financial position or results of operations.

At June 30, 2014, we have contingent payments of $3.9 million for tenant improvements and leasing costs. In addition, as of June 30, 2014, we had committed $41.6 million under construction contracts, which is expected to be paid in the next twelve months.

22. Subsequent Events

In July 2014, we declared the following dividends, which will be paid in August 2014:

- $0.1827917 per share to our common stockholders;
- $0.140625 per share to our Class E preferred stockholders; and
- $0.138021 per share to our Class F preferred stockholders.

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

FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q, including the documents incorporated by reference, contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Exchange Act of 1934, as amended. When used in this quarterly report, the words estimated , anticipated , expect , believe , intend and similar expressions are intended to identify forward-looking statements. Forward-looking statements include discussions of strategy, plans, or intentions of management. Forward-looking statements are subject to risks, uncertainties, and assumptions about Realty Income Corporation, including, among other things:

- Our anticipated growth strategies;
- Our intention to acquire additional properties and the timing of these acquisitions;
- Our intention to sell properties and the timing of these property sales;
- Our intention to re-lease vacant properties;
- Anticipated trends in our business, including trends in the market for long-term net leases of freestanding, single-tenant properties; and
- Future expenditures for development projects.

Future events and actual results, financial and otherwise, may differ materially from the results discussed in the forward-looking statements. In particular, some of the factors that could cause actual results to differ materially are:

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- Our continued qualification as a real estate investment trust;
- General business and economic conditions;
- Competition;
- Fluctuating interest rates;
- Access to debt and equity capital markets;
- Continued volatility and uncertainty in the credit markets and broader financial markets;
- Other risks inherent in the real estate business including tenant defaults, potential liability relating to environmental matters, illiquidity of real estate investments, and potential damages from natural disasters;
- Impairments in the value of our real estate assets;
- Changes in the tax laws of the United States of America;
- The outcome of any legal proceedings to which we are a party or which may occur in the future; and
- Acts of terrorism and war.

Additional factors that may cause risks and uncertainties include those discussed in the sections entitled Business , Risk Factors and Management s Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K, for the fiscal year ended December 31, 2013.

Readers are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date that this quarterly report was filed with the Securities and Exchange Commission, or SEC. While forward-looking statements reflect our good faith beliefs, they are not guarantees of future performance. We undertake no obligation to publicly release the results of any revisions to these forward-looking statements that may be made to reflect events or circumstances after the date of this quarterly report or to reflect the occurrence of unanticipated events. In light of these risks and uncertainties, the forward-looking events discussed in this quarterly report might not occur.

THE COMPANY

Realty Income, The Monthly Dividend Company®, is a publicly traded real estate company with the primary business objective of generating dependable monthly cash dividends from a consistent and predictable level of cash flow from operations. Our monthly dividends are supported by the cash flow from our portfolio of properties leased to commercial tenants. We have in-house acquisition, portfolio management, asset management, credit research, real estate research, legal, finance and accounting, and capital markets expertise. Over the past 45 years, Realty Income has been acquiring and managing freestanding commercial properties that generate rental revenue under long-term net lease agreements.

Realty Income (NYSE: O) was founded in 1969, and in 1994 was listed on the New York Stock Exchange, or NYSE. We elected to be taxed as a real estate investment trust, or REIT, requiring us to distribute dividends to our stockholders aggregating at least 90% of our taxable income (excluding net capital gains).

We seek to increase distributions to stockholders and funds from operations, or FFO, per share, through both active portfolio management and the acquisition of additional properties.

Generally, our portfolio management efforts seek to achieve:

- Contractual rent increases on existing leases;
- Rent increases at the termination of existing leases, when market conditions permit; and
- The active management of our property portfolio, including re-leasing vacant properties, and selectively selling properties, thereby mitigating our exposure to certain tenants and markets.

At June 30, 2014, we owned a diversified portfolio:

- Of 4,263 properties;
- With an occupancy rate of 98.3%, or 4,189 properties leased and 74 properties available for lease;
- Leased to 228 different commercial tenants doing business in 47 separate industries;
- Located in 49 states and Puerto Rico;
- With over 69.1 million square feet of leasable space; and
- With an average leasable space per property of approximately 16,200 square feet, including approximately 11,050 square feet per retail property.

Of the 4,263 properties in the portfolio, 4,242, or 99.5%, are single-tenant properties, and the remaining 21 are multi-tenant properties. At June 30, 2014, of the 4,242 single-tenant properties, 4,169 were leased with a weighted average remaining lease term (excluding rights to extend a lease at the option of the tenant) of approximately 10.6 years.

Investment Philosophy

We believe that owning an actively managed, diversified portfolio of commercial properties under long-term, net leases produces consistent and predictable income. Net leases typically require the tenant to be responsible for monthly rent and property operating expenses including property taxes, insurance and maintenance. In addition, tenants of our properties typically pay rent increases based on: 1) increases in the consumer price index (typically subject to ceilings), 2) additional rent calculated as a percentage of the tenants   gross sales above a specified level, or 3) fixed increases. We believe that a portfolio of properties under long-term leases generally produces a more predictable income stream than many other types of real estate portfolios, while continuing to offer the potential for growth in rental income.

We estimate that approximately 44% of our annualized rental revenue comes from properties leased to investment grade companies or their subsidiaries. At June 30, 2014, our top 20 tenants represent approximately 52% of our annualized revenue and eight of these tenants have investment grade credit ratings.

Investment Strategy

When identifying new properties for acquisition, we generally focus on providing capital to owners and operators of commercial tenants by acquiring the real estate they consider important to the successful operation of their business.

We primarily focus on acquiring properties with many of the following attributes:

- Tenants with reliable and sustainable cash flow;
- Tenants with revenue and cash flow from multiple sources;
- Tenants that are willing to sign a long-term lease (10 or more years);
- Tenants that are large owners and users of real estate;
- Real estate that is critical to the tenant s ability to generate revenue (i.e. they need the property in which they operate in order to conduct their business);
- Real estate with property valuations that approximate replacement cost;
- Properties with rental or lease payments that approximate market rents; and
- Property transactions where we can achieve an attractive spread over our cost of capital.

From a retail perspective, our investment strategy is to target tenants with a service, non-discretionary, and/or low price point component to their business. We believe these characteristics better position tenants to operate in a variety of economic conditions and to compete more effectively with internet retailers. As a result of the execution of this strategy, over 90% of our retail rental revenue for the second quarter of 2014 was derived from tenants with a service, non-discretionary, and/or low price point component to their business. We believe rental revenue generated from businesses with these characteristics is generally more durable and stable.

Diversification is also a key objective of our investment strategy. We believe that diversification of the portfolio by tenant, industry, geographic location, and property type leads to more predictable investment results for our shareholders by reducing vulnerability that can come with any single concentration. Our investment efforts have led to a diversified property portfolio that, as of June 30, 2014, consisted of 4,263 properties located in 49 states and Puerto Rico, leased to 228 different commercial tenants doing business in 47 industry segments. Each of the 47 industry segments represented in our property portfolio individually accounted for no more than 10.2% of our rental revenue for the quarter ended June 30, 2014. We typically acquire and lease properties to tenants in transactions where we can achieve an attractive risk-adjusted return. Since 1970, our occupancy rate at the end of each year has never been below 96%.

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Credit Strategy

We believe the principal financial obligations for most of our tenants typically include their bank and other debt, payment obligations to suppliers and real estate lease obligations. Because we typically own the land and building in which a tenant conducts its business or which are critical to the tenant s ability to generate revenue, we believe the risk of default on a tenant s lease obligations is less than the tenant s unsecured general obligations. It has been our experience that since tenants must retain their profitable and critical locations in order to survive, and in the event of reorganization, they are less likely to reject a lease for a profitable or critical location because this would terminate their right to use the property. Thus, as the property owner, we believe we will fare better than unsecured creditors of the same tenant in the event of reorganization. If a property is rejected by the tenant during reorganization, we own the property and can either lease it to a new tenant or sell the property. In addition, we believe that the risk of default on real estate leases can be further mitigated by monitoring the performance of the tenants individual locations and considering whether to sell locations that are weaker performers.

In order to qualify for inclusion in our portfolio, new property acquisitions must meet stringent investment and credit requirements. The properties must generate attractive current yields and the tenant must meet our credit profile. We have established a four-part analysis that examines each potential investment based on:

- Industry, company, market conditions and credit profile;
- Store profitability for retail locations, if profitability data is available;
- The importance of the real estate location to the operations of the company s business; and
- Overall real estate characteristics, including property value and comparative rental rates.

Prior to entering into any transaction, our investment professionals, assisted by our research department, conduct a review of a tenant s credit quality. The information reviewed may include reports and filings, including any public credit ratings, financial statements, debt and equity analyst reports, and reviews of corporate credit spreads, stock prices, market capitalization and other financial metrics. We conduct additional due diligence, including additional financial reviews of the tenant and a more comprehensive review of the business segment and industry in which the tenant operates. We continue to monitor our tenants credit quality on an ongoing basis by reviewing the available information previously discussed, and providing summaries of these findings to management.

Acquisition Strategy

We seek to invest in industries in which several, well-organized, regional and national commercial tenants are capturing market share through service, quality control, economies of scale, strong consumer brands, advertising, and the selection of prime locations. Our acquisition strategy is to act as a source of capital to regional and national commercial tenants by acquiring and leasing back their real estate locations. In addition, we frequently acquire large portfolios of properties net leased to multiple tenants in a variety of industries. We have an internal team dedicated to sourcing such opportunities, often using our relationships with various tenants, owners/developers and advisers to uncover and secure transactions. We also undertake thorough research and analysis to identify what we consider to be appropriate industries, tenants and property locations for investment. This research expertise is instrumental to uncovering net lease opportunities in markets where our real estate financing program adds value. In selecting potential investments, we generally seek to acquire real estate that has the following characteristics:

- Properties that are freestanding, commercially-zoned with a single tenant;
- Properties that are strategic locations for regional and national commercial tenants;
- Properties that we deem to be profitable for the tenants and/or can generally be characterized as important to the operations of the company s business;
- Properties that are located within attractive demographic areas, relative to the business of our tenants, with high visibility and easy access to major thoroughfares; and
- Properties that can be purchased with the simultaneous execution or assumption of long-term, net lease agreements, offering both current income and the potential for rent increases.

Portfolio Management Strategy

The active management of the property portfolio is an essential component of our long-term strategy. We continually monitor our portfolio for any changes that could affect the performance of the industries, tenants and locations in which we have invested. We also regularly analyze our portfolio with a view toward optimizing its returns and enhancing our credit quality.

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We regularly review and analyze:

- The performance of the various industries of our tenants; and
- The operation, management, business planning and financial condition of our tenants.

We have an active asset management program that incorporates the sale of assets when we believe the reinvestment of the sale proceeds will:

- Generate higher returns;
- Enhance the credit quality of our real estate portfolio;
- Extend our average remaining lease term; or
- Decrease tenant or industry concentration.

At June 30, 2014, we classified real estate with a carrying amount of $9.6 million as held for sale on our balance sheet. For the remainder of 2014, we intend to continue our active disposition efforts to further enhance our real estate portfolio and anticipate approximately $75 million in property sales for all of 2014. We intend to invest these proceeds into new property acquisitions, if there are attractive opportunities available. However, we cannot guarantee that we will sell properties during the next 12 months at our estimated values or be able to invest the property sale proceeds in new properties.

Impact of Real Estate and Credit Markets

In the commercial real estate market, property prices generally continue to fluctuate. Likewise, during certain periods, the U.S. credit markets have experienced significant price volatility, dislocations and liquidity disruptions, which may impact our access to and cost of capital. We continually monitor the commercial real estate and U.S. credit markets carefully and, if required, will make decisions to adjust our business strategy accordingly.

RECENT DEVELOPMENTS

Increases in Monthly Dividends to Common Stockholders

We have continued our 45-year policy of paying monthly dividends. We increased the dividend three times during 2014.

2014 Dividend increases	Month Paid	Dividend per share	Increase per share
1st increase	Jan 2014	$ 0.1821667	$ 0.0003125
2nd increase	Apr 2014	0.1824792	0.0003125
3rd increase	Jul 2014	0.1827917	0.0003125

The dividends paid per share totaled $1.0939377 in the first six months of 2014 as compared to $1.057271 in the first six months of 2013, an increase of $0.0366667, or 3.5%.

The increase in July was our 67th consecutive quarterly increase and the 76th increase in the amount of the dividend since our listing on the NYSE in 1994. In June 2014 and July 2014, we declared dividends of $0.1827917 per share, which were paid in July 2014 and will be paid in August 2014, respectively.

The monthly dividend of $0.1827917 per share represents a current annualized dividend of $2.1935004 per share, and an annualized dividend yield of approximately 4.9% based on the last reported sale price of our common stock on the NYSE of $44.42 on June 30, 2014. Although we expect to continue our policy of paying monthly dividends, we cannot guarantee that we will maintain our current level of dividends, that we will continue our pattern of increasing dividends per share, or what our actual dividend yield will be in any future period.

Acquisitions during the Second Quarter of 2014

During the second quarter of 2014, we invested $405.1 million in 73 new properties and properties under development or expansion, with an estimated initial weighted average contractual lease rate of 7.3%. The 73 new properties and properties under development or expansion are located in 27 states, will contain over 2.4 million leasable square feet and are 100% leased, with a weighted average lease term of 10.6 years. The tenants occupying the new properties operate in 22 industries and the property types consist of 75.9% retail, 14.6% office, 5.2% industrial and distribution, and 4.3% manufacturing, based on rental revenue.

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Acquisitions during the First Six Months of 2014

During the first six months of 2014, we invested $1.06 billion in 402 new properties and properties under development or expansion with an initial weighted average contractual lease rate of 7.1%. The 402 new properties and properties under development or expansion, are located in 39 states, will contain over 6.9 million leasable square feet and are 100% leased, with a weighted average lease term of 12.8 years. The tenants occupying the new properties operate in 24 industries and the property types consist of 83.0% retail, 8.5% office, 6.8% industrial and distribution, and 1.7% manufacturing, based on rental revenue. None of our investments during the first six months of 2014 caused any one tenant to be 10% or more of our total assets at June 30, 2014.

We previously disclosed a purchase and sale agreement with Inland Diversified Real Estate Trust, Inc., or Inland, and certain subsidiaries of Inland, to acquire 84 single-tenant, 100% net-leased properties, for $502.9 million, which were acquired during the first six months of 2014.

The estimated initial weighted average contractual lease rate for a property is generally computed as estimated contractual net operating income, which, in the case of a net leased property, is equal to the aggregate base rent under the lease for the first full year of each lease, divided by the total cost of the property. Since it is possible that a tenant could default on the payment of contractual rent, we cannot provide assurance that the actual return on the funds invested will remain at the percentage listed above.

In the case of a property under development or expansion, the contractual lease rate is generally fixed such that rent varies based on the actual total investment in order to provide a fixed rate of return. When the lease does not provide for a fixed rate of return on a property under development or expansion, the estimated initial weighted average contractual lease rate is computed as follows: estimated net operating income (determined by the lease) for the first full year of each lease, divided by our projected total investment in the property, including land, construction and capitalized interest costs. Of the $1.06 billion we invested during the first six months of 2014, $35.6 million was invested in 21 properties under development or expansion with an estimated initial weighted average contractual lease rate of 8.5%. We may continue to pursue development or expansion opportunities under similar arrangements in the future.

Portfolio Discussion

Leasing Results

At June 30, 2014, we had 74 properties available for lease out of 4,263 properties in our portfolio, which represents a 98.3% occupancy rate. Since December 31, 2013, when we reported 70 properties available for lease and a 98.2% occupancy rate, we:

- Had 85 lease expirations;
- Re-leased 76 properties; and
- Sold five properties.

Of the 76 properties re-leased during the first six months of 2014, 67 properties were re-leased to either existing or new tenants without vacancy, and nine were re-leased to new tenants after a period of vacancy. The annual rent on these leases was $12.5 million, as compared to the previous rent on these same properties of $12.4 million.

At June 30, 2014, our average annualized rental revenue was approximately $13.09 per square foot on the 4,189 leased properties in our portfolio. At June 30, 2014, we classified nine properties with a carrying amount of $9.6 million as held for sale on our balance sheet.

Investments in Existing Properties

In the second quarter of 2014, we capitalized costs of $1.4 million on existing properties in our portfolio, consisting of $275,000 for re-leasing costs and $1.1 million for building and tenant improvements. In the second quarter of 2013, we capitalized costs of $1.6 million on existing properties in our portfolio, consisting of $362,000 for re-leasing costs and $1.3 million for building and tenant improvements.

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In the first six months of 2014, we capitalized costs of $2.7 million on existing properties in our portfolio, consisting of $467,000 for re-leasing costs and $2.3 million for building and tenant improvements. In the first six months of 2013, we capitalized costs of $3.3 million on existing properties in our portfolio, consisting of $774,000 for re-leasing costs and $2.5 million for building and tenant improvements.

As part of our re-leasing costs, we typically pay leasing commissions and sometimes provide tenant rent concessions. Leasing commissions are paid based on the commercial real estate industry standard and any rent concessions provided are minimal. We do not consider the collective impact of the leasing commissions or tenant rent concessions to be material to our financial position or results of operations.

The majority of our building and tenant improvements relate to roof repairs, HVAC improvements, and parking lot resurfacing and replacements. It is not customary for us to offer significant tenant improvements on our properties as tenant incentives. The amounts of our capital expenditures can vary significantly, depending on the rental market, tenant credit worthiness, and the willingness of tenants to pay higher rents over the terms of the leases.

Note Issuance

In June 2014, we issued $350 million of 3.875% senior unsecured notes due July 2024, or the 2024 Notes. The price to the investors for the 2024 Notes was 99.956% of the principal amount for an effective yield of 3.88% per annum. The total net proceeds of approximately $346.6 million from these offerings were used to repay a portion of the outstanding borrowings under our acquisition credit facility. Interest is paid semiannually on the 2024 Notes.

Issuance of Common Stock

In April 2014, we issued 13,800,000 shares of common stock, including 1,800,000 shares purchased by the underwriters upon the exercise of their option to purchase additional shares. After underwriting discounts and other offering costs of $22.8 million, the net proceeds of $528.6 million were used to repay borrowings under our acquisition credit facility.

Modifications to Compensation Program

During April 2014, the Compensation Committee of the Board of Directors made modifications to the existing compensation program. The modified compensation program now consists of distinct short-term and long-term incentive plans based on separate metrics. The redesigned short-term incentive plan includes a mix of cash and equity awards. Under the long-term incentive plan, an individual s award is granted in performance-vesting equity awards, which vest based strictly on achieving future performance goals. With respect to the performance based restricted shares, the award is based on objective performance metrics and determined primarily by relative stockholder return metrics with a smaller component based on balance sheet metrics. As part of this new program, the Compensation Committee of the Board of Directors granted performance-vesting shares with an approximate grant date fair value of $3.0 million to our executive officers during April 2014.

Net Income Available to Common Stockholders

Net income available to common stockholders was $51.4 million in the second quarter of 2014, compared to $46.0 million in the second quarter of 2013, an increase of $5.4 million. On a diluted per common share basis, net income was $0.23 in the second quarter of 2014 and 2013.

Net income available to common stockholders was $98.6 million in the first six months of 2014, compared to $108.7 million in the first six months of 2013, a decrease of $10.1 million. On a diluted per common share basis, net income available to common stockholders was $0.46 in the first six months of 2014, as compared to $0.59 in the first six months of 2013, a decrease of $0.13, or 22.0%. Net income available to common stockholders in the first six months of 2013 was impacted by an unusually large gain on property sales, which represents $0.19 on a diluted per common share basis. Net income available to common stockholders in the first six months of 2013 includes $12.6 million of merger-related costs, for the acquisition of American Realty Capital Trust, Inc., ARCT, which represents $0.07 on a diluted per common share basis. Additionally, net income for the second quarter and first six months of 2013 has been adjusted from that previously reported in our June 30, 2013 Quarterly Report on Form 10-Q as a result of measurement period adjustments that were recorded during the second half of 2013 upon completion of the real estate valuations for our acquisition of ARCT. As a result of these adjustments to the asset allocation, revisions were made to our consolidated statement of income for the first six months of 2013 for the impact related to rental revenue and depreciation and amortization. Because of these revisions, net income for the first six months of 2013 increased by $3.2 million, which represents $0.02 on a diluted per common share basis.

The calculation to determine net income available to common stockholders includes gains from the sale of properties. The amount of gains varies from period to period based on the timing of property sales and can significantly impact net income available to common stockholders.

Gains from the sale of properties during the second quarter of 2014 were $2.0 million, as compared to $5.7 million during the second quarter of 2013. Gains from the sale of properties during the first six months of 2014 were $5.8 million, as compared to $44.3 million during the first six months of 2013.

Funds from Operations Available to Common Stockholders (FFO)

In the second quarter of 2014, our FFO increased by $24.8 million, or 21.1%, to $142.4 million, compared to $117.6 million in the second quarter of 2013. On a diluted per common share basis, FFO was $0.64 in the second quarter of 2014 and $0.60 in the second quarter of 2013, an increase of 6.7%.

In the first six months of 2014, our FFO increased by $55.6 million, or 25.1% to $276.9 million, compared to $221.3 million in the first six months of 2013. On a diluted per common share basis, FFO was $1.29 in the first six months of 2014, compared to $1.20 in the first six months of 2013, an increase of $0.09, or 7.5%. FFO, for the first six months of 2013, was normalized to exclude $12.6 million of merger-related costs for the acquisition of ARCT, which represents $0.07 on a diluted per common share basis. All references to FFO for the first six months of 2013 reflect the adjustment for merger-related costs for the acquisition of ARCT. As a result of measurement period adjustments related to ARCT real estate valuations (as discussed in Net Income Available to Common Stockholders above), FFO decreased by $2.8 million, or $0.02 per share, for the first six months of 2013.

Adjusted Funds from Operations Available to Common Stockholders (AFFO)

In the second quarter of 2014, our AFFO increased by $25.6 million, or 22.1%, to $141.2 million, compared to $115.6 million in the second quarter of 2013. On a diluted common share basis, AFFO was $0.64 in the second quarter of 2014 and $0.59 in the second quarter of 2013, an increase of 8.5%.

In the first six months of 2014, our AFFO increased by $54.3 million, or 24.7%, to $273.8 million versus $219.5 million in the first six months of 2013. On a diluted per common share basis, AFFO was $1.28 in the first six months of 2014, compared to $1.19 in the first six months of 2013, an increase of $0.09, or 7.6%.

See our discussion of FFO and AFFO (which are not financial measures under U.S. generally accepted accounting principles, or GAAP), later in this Management s Discussion and Analysis of Financial Condition and Results of Operations, which includes a reconciliation of net income available to common stockholders to FFO and AFFO.

LIQUIDITY AND CAPITAL RESOURCES

Capital Philosophy

Historically, we have met our long-term capital needs by issuing common stock, preferred stock and long-term unsecured notes and bonds. Over the long term, we believe that common stock should be the majority of our capital structure. However, we may issue additional preferred stock or debt securities. We may issue common stock when we believe that our share price is at a level that allows for the proceeds of any offering to be accretively invested into additional properties. In addition, we may issue common stock to permanently finance properties that were financed by our credit facility or debt securities. However, we cannot assure you that we will have access to the capital markets at times and at terms that are acceptable to us.

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Our primary cash obligations, for the current year and subsequent years, are included in the Table of Obligations, which is presented later in this section. We expect to fund our operating expenses and other short-term liquidity requirements, including property acquisitions and development costs, payment of principal and interest on our outstanding indebtedness, property improvements, re-leasing costs and cash distributions to common and preferred stockholders, primarily through cash provided by operating activities, borrowing on our $1.5 billion credit facility, and occasionally through public securities offerings.

Conservative Capital Structure

We believe that our stockholders are best served by a conservative capital structure. Therefore, we seek to maintain a conservative debt level on our balance sheet and solid interest and fixed charge coverage ratios. At June 30, 2014, our total outstanding borrowings of senior unsecured notes and bonds, term loan, mortgages payable and credit facility borrowings were $4.58 billion, or approximately 30.3% of our total market capitalization of $15.14 billion.

We define our total market capitalization at June 30, 2014 as the sum of:

- Shares of our common stock outstanding of 222,623,256, plus total common units of 841,568, multiplied by the closing sales price of our common stock on the NYSE of $44.42 per share on June 30, 2014, or $9.93 billion;
- Aggregate liquidation value (par value of $25 per share) of the Class E preferred stock of $220.0 million;
- Aggregate liquidation value (par value of $25 per share) of the Class F preferred stock of $408.8 million;
- Outstanding borrowings of $70.8 million on our credit facility;
- Outstanding mortgages payable of $892.3 million, excluding net mortgage premiums of $24.2 million;
- Outstanding borrowings of $70.0 million on our term loan; and
- Outstanding senior unsecured notes and bonds of $3.55 billion, excluding unamortized original issuance discounts of $14.0 million.

Universal Shelf Registration

In February 2013, we filed a shelf registration statement with the SEC, which is effective for a term of three years and will expire in February 2016. This replaces our prior shelf registration statement. In accordance with SEC rules, the amount of securities to be issued pursuant to this shelf registration statement was not specified when it was filed and there is no specific dollar limit. The securities covered by this registration statement include (1) common stock, (2) preferred stock, (3) debt securities, (4) depositary shares representing fractional interests in shares of preferred stock, (5) warrants to purchase debt securities, common stock, preferred stock or depositary shares, and (6) any combination of these securities. We may periodically offer one or more of these securities in amounts, prices and on terms to be announced when and if the securities are offered. The specifics of any future offerings, along with the use of proceeds of any securities offered, will be described in detail in a prospectus supplement, or other offering materials, at the time of any offering.

Mortgage Debt

As of June 30, 2014, we had $892.3 million of mortgages payable, all of which were assumed in connection with our property acquisitions. Additionally, at June 30, 2014, we had net premiums totaling $24.2 million on these mortgages. We expect to pay off the mortgages payable as soon as prepayment penalties have declined to a level that will make it economically feasible to do so. During the first six months of 2014, we made $21.9 million in principal payments, which includes the repayment of two mortgages in full for $18.2 million.

Term Loan

In January 2013, in conjunction with our acquisition of ARCT, we entered into a $70 million senior unsecured term loan maturing in January 2018. Borrowing under the term loan bears interest at LIBOR, plus 1.20%. In conjunction with this term loan, we also acquired an interest rate swap which essentially fixes our per annum interest rate on the term loan at 2.15%.

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$1.5 Billion Acquisition Credit Facility

We have a $1.5 billion unsecured acquisition credit facility with an initial term that expires in May 2016 and includes, at our election, a one-year extension option. Under this credit facility, our current investment grade credit ratings provide for financing at the London Interbank Offered Rate, commonly referred to as LIBOR, plus 1.075% with a facility commitment fee of 0.175%, for all-in drawn pricing of 1.25% over LIBOR. The borrowing rate is not subject to an interest rate floor or ceiling. We also have other interest rate options available to us under this credit facility. Our credit facility is unsecured and, accordingly, we have not pledged any assets as collateral for this obligation.

At June 30, 2014, we had a borrowing capacity of $1.43 billion available on our credit facility and an outstanding balance of $70.8 million. The interest rate on borrowings outstanding under our credit facility, at June 30, 2014, was 1.2% per annum. We must comply with various financial and other covenants in our credit facility. At June 30, 2014, we remain in compliance with these covenants. We expect to use our credit facility to acquire additional properties and for other corporate purposes. Any additional borrowings will increase our exposure to interest rate risk. We regularly review our credit facility and may seek to extend or replace our credit facility, to the extent we deem appropriate.

We generally use our credit facility for the short-term financing of new property acquisitions. Thereafter, when capital is available on acceptable terms, we generally seek to refinance those borrowings with the net proceeds of long-term or permanent financing, which may include the issuance of common stock, preferred stock or debt securities. We cannot assure you, however, that we will be able to obtain any such refinancing, or that market conditions prevailing at the time of the refinancing will enable us to issue equity or debt securities upon acceptable terms.

Notes Outstanding

Our senior unsecured note and bond obligations consist of the following as of June 30, 2014, sorted by maturity date (dollars in millions):

5.5% notes, issued in November 2003 and due in November 2015	$	150
5.95% notes, issued in September 2006 and due in September 2016		275
5.375% notes, issued in September 2005 and due in September 2017		175
2.0% notes, issued in October 2012 and due in January 2018		350
6.75% notes, issued in September 2007 and due in August 2019		550
5.75% notes, issued in June 2010 and due in January 2021		250
3.25% notes, issued in October 2012 and due in October 2022		450
4.65% notes, issued in July 2013 and due in August 2023		750
3.875% notes, issued in June 2014 and due in July 2024		350
5.875% bonds, $100 issued in March 2005 and $150 issued in June 2011, both due in March 2035		250
Total principal amount	$	3,550
Unamortized original issuance discounts		(14)
	$	3,536

All of our outstanding notes and bonds have fixed interest rates and contain various covenants, which we remain in compliance with at June 30, 2014. Additionally, interest on all of our senior note and bond obligations is paid semiannually.

The following is a summary of the key financial covenants for our senior unsecured notes, as defined and calculated per the terms of our senior notes and bonds. These calculations, which are not based on U.S. GAAP measurements, are presented to investors to show our ability to incur additional debt under the terms of our senior notes and bonds only and are not measures of our liquidity or performance. The actual amounts as of June 30, 2014 are:

Note Covenants	**Required**	**Actual**
Limitation on incurrence of total debt	≤ 60% of adjusted assets	42.0%
Limitation on incurrence of secured debt	≤ 40% of adjusted assets	8.4%
Debt service coverage (trailing 12 months)(1)	≥ 1.5 x	3.7x
Maintenance of total unencumbered assets	≥ 150% of unsecured debt	250.7%

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(1) This covenant is calculated on a pro forma basis for the preceding four-quarter period on the assumption that: (i) the incurrence of any Debt (as defined in the covenants) incurred by us since the first day of such four-quarter period and the application of the proceeds therefrom (including to refinance other Debt since the first day of such four-quarter period), (ii) the repayment or retirement of any of our Debt since the first day of such four-quarter period, and (iii) any acquisition or disposition by us of any asset or group since the first day of such four-quarters had in each case occurred on July 1, 2013, and subject to certain additional adjustments. Such pro forma ratio has been prepared on the basis required by that debt service covenant, reflects various estimates and assumptions and is subject to other uncertainties, and therefore does not purport to reflect what our actual debt service coverage ratio would have been had transactions referred to in clauses (i), (ii) and (iii) of the preceding sentence occurred as of July 1, 2013, nor does it purport to reflect our debt service coverage ratio for any future period. The following is our calculation of debt service coverage at June 30, 2014 (in thousands, for trailing twelve months):

Net income attributable to the Company	$	235,470
Plus: interest expense		197,102
Plus: provision for taxes		1,761
Plus: depreciation and amortization		349,458