

BERKSHIRE INCOME REALTY INC
Form 10-K
March 31, 2009

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

Form 10-K

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

For the fiscal year ended December 31, 2008

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

Commission File number 001-31659

Berkshire Income Realty, Inc.

State of Incorporation - Maryland
Internal Revenue Service – Employer Identification No. 32-0024337
One Beacon Street, Boston, Massachusetts 02108
(617) 523-7722

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

Title of Class	Name of each exchange on which registered
Series A 9% Cumulative Redeemable Preferred Stock	American Stock Exchange

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

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

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

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

Large Accelerated Filer

Non-accelerated filer

Accelerated Filer

Smaller reporting company

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes

No

Aggregate market value of voting and non-voting common equity held by non-affiliates: Not applicable.

There were 1,406,196 shares of Class B common stock outstanding as of March 30, 2009.

There are no documents required to be incorporated by reference to this Annual Report on Form 10K.

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SPECIAL NOTE REGARD FORWARD-LOOKING STATEMENTS

Certain statements contained in this report, including information with respect to our future business plans, constitute “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended (the “33 Act”), and Section 21E of the Securities Exchange Act of 1934, as amended (the “34 Act”). For this purpose, any statements contained herein that are not statements of historical fact may be deemed to be forward-looking statements, subject to a number of risks and uncertainties that could cause actual results to differ significantly from those described in this report. These forward-looking statements include statements regarding, among other things, our business strategy and operations, future expansion plans, future prospects, financial position, anticipated revenues or losses and projected costs, and objectives of management. Without limiting the foregoing, the words “may,” “will,” “should,” “could,” “expects,” “plans,” “anticipates,” “believes,” “estimates,” “predicts,” “potential” or “continue” or the negative of these terms and other comparable terminology are intended to identify forward-looking statements. There are a number of important factors that could cause our results to differ materially from those indicated by such forward-looking statements. These factors include, but are not limited to, changes in economic conditions generally and the real estate and bond markets specifically, legislative/regulatory changes (including changes to laws governing the taxation of real estate investment trusts (“REITs”)), possible sales of assets, the acquisition restrictions placed on the Company by an affiliated entity Berkshire Multifamily Value Fund II, LP, (“BVF II” or “Fund II”), availability of capital, interest rates and interest rate spreads, changes in accounting principles generally accepted in the United States of America (“GAAP”) and policies and guidelines applicable to REITs, those factors set forth herein in Part I, Item 1A. “Risk Factors” and other risks and uncertainties as may be detailed from time to time in our public announcements and our reports filed with the Securities and Exchange Commission (the “SEC”).

The risks listed here are not exhaustive. Other sections of this report may include additional factors that could adversely affect our business and financial performance. Moreover, we operate in a competitive and rapidly changing environment. New risk factors emerge from time to time and it is not possible for management to predict all such risks factors, nor can it assess the impact of all such risk factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements. Given these risks and uncertainties, undue reliance should not be placed on forward-looking statements as a prediction of actual results.

As used herein, the terms “we”, “us”, “BIR” or the “Company” refer to Berkshire Income Realty, Inc., a Maryland corporation incorporated on July 19, 2002. The Company is in the business of acquiring, owning, operating and renovating multifamily apartment communities. Berkshire Property Advisors, L.L.C. (“Berkshire Advisor” or “Advisor”) is an affiliated entity we have contracted with to make decisions relating to the day-to-day management and operation of our business, subject to the Board of Directors (“Board”) oversight. Refer to Part III, Item 13 – Certain Relationships and Related Transactions and Director Independence and Notes to the Consolidated Financial Statements, Note 12 –Related Party Transactions of this Form 10-K for additional information about the Advisor.

PART I

ITEM 1. BUSINESS

Executive Summary

In 2008 BIR adjusted its property holdings with the acquisition of one property, Executive House in Philadelphia, Pennsylvania for approximately \$50,205,000, while selling its interest in four properties, Century (“Century”) for \$52,000,000, St Marin / Karrington (“St. Marin”) for \$61,750,000, Westchester West (“Westchester West”) for \$49,500,000 and Berkshires at Westchase (“Westchase”) for \$12,400,000. Executive House represents the Company’s

entry into a new submarket with its first acquisition in the City of Philadelphia. Additionally, the Company funded the final \$2,327,749 of its \$23,400,000 capital commitment Berkshire Multifamily Value Fund, LP, (“BVF”), a limited partnership, and affiliate of the Company, bringing the Company’s funding to 100% of its total commitment.

During 2008 the Company furthered its strategy of assessing outstanding mortgage debt to aggressively finance, refinance and add supplemental debt to its portfolio to help minimize the effects of rising mortgage interest rates and maximize the cash available for capital investments. Due to financing and refinancing activities in prior years, which have resulted in the majority of the portfolio being financed at favorable rates and maturity periods, and changes in the capital and debt markets, which substantially curtailed the acquisition activity of the Company, the Company only refinanced one loan that matured during the year and assumed a first and second mortgage related to the only property acquired during the year.

The Company obtained a fixed rate first mortgage of \$13,200,000 on Briarwood Village to replace existing debt that matured during the year at a rate of 6.43% for a term of 10 years and first and second mortgages totaling approximately \$30,655,000 were assumed on the acquisition of Executive House, at an average interest rate of approximately 5.75% for an average term of approximately 6 years.

Occupancy levels remained stable in the low to mid 90% range which, approximate average occupancy levels from the prior year at the Company's Same Portfolio Properties ("Same Store"). Occupancy levels benefited from the Company's rental rate setting strategy which, in general, attempts to balance occupancy with rental increases to achieve market level occupancy rates. As in past years when the rental market exhibits signs of softness, BIR will offer short-term rental concessions to new and renewing tenants at properties within markets experiencing the slowdown to maintain occupancy without producing significant fluctuations in market rental rates. The Company employs revenue management software that tracks market rents on a daily basis using various data points and has the functionality to price for amenities that may be specific to units within a property (i.e. end unit with a fireplace). This information allows property management to react timely to changes in market conditions by setting rents for new and renewal leases based on current market conditions and unit amenities. The use of the system has resulted in a curtailment in the use of rent concessions as a means to react to market conditions although the use of concessions remains a part of the leasing strategy, but to a lesser degree, at properties using the software. The administration of the system is carried out at the property and overseen by a newly created centralized administrative function that provides training and support to the field. The system continues to be rolled out to all properties within the portfolio meeting a minimum unit threshold.

The Company continues to employ a strategy of increasing the value of its portfolio by implementing property management efficiencies and physical asset improvements at its properties. As has been the practice in past years, the Company's efforts executing this strategy continued to result in the desired operating results during the year. The Seasons of Laurel Apartments in Maryland underwent a utility conversion and window replacement renovation project that was completed during the year that resulted in the transfer of electrical costs to the tenants resulting from the installation of individual apartment unit electric meters. Costs previously absorbed by the Company were converted to tenant pay and resulted in savings in utility expenses during the year. The project is now complete and 100% of the tenants are now responsible for their individual apartment unit's utility costs. This project, in addition to other renovation and rehabilitation projects at other properties in the portfolio continue to result in positive operating returns when completed. The Company will continue to assess properties and institute renovation projects as circumstances dictate.

In 2009, the Company intends to manage the portfolio through the challenging economic environment we currently face and adjust our operations to best position the Company for continued successful operations thru the current recessionary downturn. The Company will continue to take advantage of investment opportunities, both acquisitions and dispositions, that present themselves and achieve desired investment returns. The Company will continue to consider the adjustment of the portfolio holdings to a higher quality product utilizing sourcing strategies that include market, non-market/seller direct, bank and lender owned real estate and foreclosure auctions within the limitations of the currently strained credit and equity markets. The Company intends to continue to invest funds as they become available in qualifying investment opportunities, if any, in the form of new acquisitions, new development projects and the renovation of established properties. The Company does not currently anticipate selling any properties in the portfolio but will reassess its plans as the markets adjust during the year.

BUSINESS

In 2002, the Company filed a registration statement on Form S-11 with the SEC with respect to its offers (the “Offering”) to issue its 9% Series A Cumulative Redeemable Preferred Stock (“Preferred Shares”) in exchange for interests (“Interests”) in various mortgage funds (collectively, the “Mortgage Funds”). For each Interest in the Mortgage Funds validly tendered and not withdrawn in the Offering, the Company offered to issue its Preferred Shares based on an exchange ratio applicable to each Mortgage Fund. The registration statement was declared effective on January 9, 2003. Offering costs incurred in connection with the Offering have been reflected as a reduction of Preferred Shares reflected in the financial statements of the Company. On April 4, 2003 and April 18, 2003, the Company issued 2,667,717 and 310,393 Preferred Shares, respectively, with a \$25.00 liquidation preference per share. Simultaneously with the completion of the Offering on April 4, 2003, KRF Company, L.L.C. (“KRF Company”), an affiliate of the Company, contributed its ownership interests in five multifamily apartment communities (the “Properties”) to our operating partnership, Berkshire Income Realty – OP, L.P. (the “Operating Partnership”), in exchange for common limited partner interests in the Operating Partnership. KRF Company then contributed an aggregate of \$1,283,213, or 1% of the fair value of the total net assets of the Operating Partnership, to the Company, which together with the \$100 contributed prior to the Offering, resulted in the issuance of 1,283,313 shares of common stock of the Company to KRF Company. This amount was contributed by the Company to its wholly owned subsidiary, BIR GP, L.L.C., who then contributed the cash to the Operating Partnership in exchange for the sole general partner interest in the Operating Partnership.

The Company’s financial statements include the accounts of the Company, its subsidiary, the Operating Partnership, as well as the various subsidiaries of the Operating Partnership. The Company owns preferred and general partner interests in the Operating Partnership. The remaining common limited partnership interests in the Operating Partnership owned by KRF Company and affiliates are reflected as Minority Interest in Operating Partnership in the financial statements of the Company.

On April 28, 2008, the Operating Partnership completed the sale of 100% of its interest in St. Marin/Karrington Apartments in Coppell, Texas. On May 6, 2008, the Board of Directors (“Board”) authorized the general partner of the Operating Partnership to distribute a portion of the proceeds from the sale of St. Marin/Karrington to the common general and common limited partners as a special distribution in the amount of \$10,000,000, payable on May 15, 2008. On the same day, the Board also declared a common dividend of \$0.169960 per share on the Company’s Class B common stock payable concurrently with the Operating Partnership distribution. The Company retained the balance of the sale proceeds in its operating account for its operating use. The operating results of St. Marin/Karrington have been presented in the consolidated statement of operations as discontinued operations in accordance with FAS 144 “Accounting for the Impairment or Disposal of Long Lived Assets.”

On May 29, 2008, the Operating Partnership completed the sale of 100% of its interest in Westchase Apartments in Houston, Texas. The proceeds from the sale of Westchase were deposited in the Company’s operating account for its operating use. The operating results of Berkshire at Westchase have been presented in the consolidated statement of operations as discontinued operations in accordance with FAS 144 “Accounting for the Impairment or Disposal of Long Lived Assets.”

On June 19, 2008, the Company through its wholly owned subsidiary BIR Blackrock, L.L.C., entered into a subscription agreement to invest in the Leggat McCall Hingham Mezzanine Loan LLC, a Massachusetts Limited Liability Company. Under the terms of the agreement, the Company agreed to invest up to \$1,425,000, or approximately 41%, of the total capital of the investment in order to subscribe for 14.25 units. The Company has funded \$855,000 or 60%, of its commitment as of December 31, 2008.

On September 18, 2008, the Company's Operating Partnership, through a newly formed and wholly owned subsidiary, BIR Executive House, L.P., completed the acquisition of 100% of the partnership interests in Executive House Associates, the owner of Executive House Apartments, a 302 unit multifamily apartment community located in Philadelphia, Pennsylvania, from an unaffiliated third party. The purchase price of \$50,000,000 and related closing costs consisted of a cash payment of \$20,148,140 plus the assumption of the outstanding mortgage debt secured by the property. The purchase was subject to normal operating pro rations. The cash portion of the purchase price and related closing costs were funded through a \$10,000,000 advance from the revolving credit facility available from an affiliate and available cash. The acquisition of Executive House is intended to be the qualified replacement property in connection with the sale of the Westchester West property, which was identified for replacement pursuant to a transaction structured to comply with the requirements of a reverse 1031 Exchange under the Internal Revenue Code of 1986, as amended, (the "Tax Code"). As required by the Tax Code, a qualified 1031 Exchange intermediary was retained to execute the Executive House acquisition and the Westchester West sale transactions. As of December 31, 2008, the purchase price allocation was final and no further adjustment is contemplated.

On October 29, 2008, the Operating Partnership completed the sale of 100% of its interest in Century Apartments in Cockeysville, Maryland. The Company's share of the proceeds from the sale of Century Apartments were deposited in the Company's operating account for its operating use. The operating results of Century Apartments have been presented in the consolidated statement of operations as discontinued operations in accordance with FAS 144 "Accounting for the Impairment or Disposal of long lived Assets."

On December 30, 2008, the Operating Partnership completed the sale of 100% of its interest in Westchester West Apartments in Silver Spring, Maryland. The proceeds from the sale of Westchester West were deposited in an escrow account with a qualified institution pursuant to a transaction structured to comply with a 1031 Exchange under the Tax Code. Subsequently, the proceeds were distributed from the qualified intermediary and deposited in the Company's operating account for its operating use. The operating results of Westchester West have been presented in the consolidated statement of operations as discontinued operations in accordance with FAS 144 "Accounting for the Impairment or Disposal of Long Lived Assets."

The Company does not have any employees. Its day-to-day business is managed by Berkshire Advisor, an affiliate of KRF Company, the holder of the majority of our common stock, which has been retained pursuant to the advisory services agreement described under Part III, Item 13 – Certain Relationships and Related Transactions and Director Independence. Our properties were managed by BRI OP Limited Partnership pursuant to property management agreements described under Part III, Item 13 – Certain Relationships and Related Transactions and Director Independence until December 31, 2004. As of January 1, 2005, Berkshire Advisor assumed property management responsibilities under the various property management agreements.

Our principal executive offices are located at One Beacon Street, Suite 1500, Boston, Massachusetts 02108 and our telephone number at that address is (617) 523-7722.

We are required to file annual, quarterly, and current reports, and other documents with the SEC under the Securities Exchange Act of 1934, as amended. The public may read and copy any materials that we file with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. Also, the SEC maintains an Internet website that contains reports, proxy and information statements, and other information regarding issuers, including the Company, that file electronically with the SEC. The public can obtain any documents that we file with the SEC at <http://www.sec.gov>. The Company voluntarily provides, free of charge, paper or electronic copies of all filings upon request. Additionally, all filings are available free of charge on our website. Our Internet address is

<http://www.berkshireincomerealty.com>.

ITEM 1A. RISK FACTORS

RISK FACTORS

The following risk factors should be read carefully in connection with evaluating our business and the forward-looking statements contained in this report and other statements we or our representatives make from time to time. Any of the following risks could materially adversely affect our business, our operating results, our financial condition and the actual outcome of matters as to which forward-looking statements are made in this report. In connection with the forward-looking statements that appear in this report, you should also carefully review the cautionary statement referred to herein under “Special Note Regarding Forward-Looking Statements.”

Risk Factors Relating to Our Business

Operating risks and lack of liquidity may adversely affect our investments in real property.

Varying degrees of risk affect real property investments. The investment returns available from equity investments in real estate depend in large part on the amount of income earned and capital appreciation generated by the related properties as well as the expenses incurred. If our assets do not generate revenue sufficient to meet operating expenses, including debt service and capital expenditures, our income and ability to service our debt and other obligations could be adversely affected. Some significant expenditures associated with an investment in real estate, such as mortgage and other debt payments, real estate taxes and maintenance costs, generally are not reduced when circumstances cause a reduction in revenue from the investment. In addition, income from properties and real estate values are also affected by a variety of other factors, such as interest rate levels, governmental regulations and applicable laws and the availability of financing.

Equity real estate investments, such as ours, are relatively illiquid. This illiquidity limits our ability to vary our portfolio in response to changes in economic or other conditions. We cannot be certain that we will recognize full value for any property that we are required to sell for liquidity reasons. Our inability to respond rapidly to changes in the performance of our investments could adversely affect our financial condition and results of operations.

Our properties are subject to operating risks common to apartment ownership in general. These risks include: our ability to rent units at the properties; competition from other apartment communities; excessive building of comparable properties that might adversely affect apartment occupancy or rental rates; increases in operating costs due to inflation and other factors, which increases may not necessarily be offset by increased rents; increased affordable housing requirements that might adversely affect rental rates; inability or unwillingness of residents to pay rent increases; and future enactment of rent control laws or other laws regulating apartment housing, including present and possible future laws relating to access by disabled persons or the right to convert a property to other uses, such as condominiums or cooperatives. If operating expenses increase, the local rental market may limit the extent to which rents may be increased to meet increased expenses without decreasing occupancy rates. If any of the above were to occur, our ability to meet our debt service and other obligations could be adversely affected.

In order to achieve or enhance our desired financial results we may make investments that involve more risk than market rate core and core-plus acquisitions.

In many of the markets where we may seek to acquire multifamily apartment communities we may face significant competition from well capitalized real estate investors, including private investors, publicly traded REITs and institutional investors. This competition can result in sellers obtaining premiums on their real estate, which sometimes pushes the price beyond what we may consider to be a prudent purchase price. To mitigate these factors our sourcing strategy includes non-market/seller direct deals, bank and lender owned real estate and foreclosure auctions. Some of these acquisition strategies can involve more risk than market rate core and core-plus acquisitions, but may allow the Company to realize higher returns if the underlying assumptions are achieved. However, if the underlying assumptions are not achieved, the additional risks associated with these broader sourcing strategies could result in lower profits, or higher losses, than would be realized in market rate acquisitions.

We may renovate our properties, which could involve additional operating risks.

We expect to be working on the renovation of multifamily properties that we may acquire. We may also acquire completed multifamily properties. The renovation of real estate involves risks in addition to those involved in the ownership and operation of established multifamily properties, including the risks that specific project approvals may take longer to obtain than expected, that construction may not be completed on schedule or budget and that the properties may not achieve anticipated rent or occupancy levels.

We may not be able to pay the costs of necessary capital improvements on our properties, which could adversely affect our financial condition.

We anticipate funding any required capital improvements on our properties using cash flow from operations, cash reserves or additional financing if necessary. However, the anticipated sources of funding may not be sufficient to make the necessary improvements. If our cash flow from operations and cash reserves proves to be insufficient, we might have to fund the capital improvements by borrowing money. If we are unable to borrow money on favorable terms, or at all, we may not be able to make necessary capital improvements, which could harm our financial condition.

Our tenants-in-common or future venture partners may have interests or goals that conflict with ours, which may restrict our ability to manage some of our investments and adversely affect our results of operations.

One or more of our properties that we acquire may be owned through tenancies-in-common or by venture partnerships between us and the seller of the property, an independent third party or another investment entity sponsored by our affiliates. Our investment through tenancies-in-common or in venture partnerships that own properties may, under certain circumstances, involve risks that would not otherwise be present. For example, our tenant-in-common or venture partner may experience financial difficulties and may at any time have economic or business interests or goals that are inconsistent with our economic or business interests or our policies or goals. In addition, actions by, or litigation involving, any tenant-in-common or venture partner might subject the property owned through a tenancy-in-common or by the venture to liabilities in excess of those contemplated by the terms of the tenant-in-common or venture agreement. Also, there is a risk of impasse between the parties since generally either party may disagree with a proposed transaction involving the property owned through a tenancy-in-common or venture partnership and impede any proposed action, including the sale or other disposition of the property.

Our inability to dispose of a property we may acquire in the future without the consent of a tenant-in-common or venture partner would increase the risk that we could be unable to dispose of the property, or dispose of it promptly, in response to economic or other conditions. The inability to respond promptly to changes in performance of the property could adversely affect our financial condition and results of operations.

We may face significant competition and we may not compete successfully.

We may face significant competition in seeking investments including competition from our affiliate BVF II. We may be unable to acquire a desired property because of competition from other well capitalized real estate investors, such as publicly traded REIT's, institutional investors and other investors, including companies that may be affiliated with the Advisor. When we are successful in acquiring a desired property, competition from other real estate investors may significantly increase our purchase price. Some of our competitors may have greater financial and other resources than us and may have better relationships with lenders and sellers, and we may not be able to compete successfully for investments.

We plan to borrow, which may adversely affect our return on our investments and may reduce income available for distribution.

Where possible, we may seek to borrow funds to increase the rate of return on our investments and to allow us to make more investments than we otherwise could. Borrowing by us presents an element of risk if the cash flow from our properties and other investments is insufficient to meet our debt service and other obligations. A property encumbered by debt increases the risk that the property will operate at a loss and may ultimately be forfeited upon foreclosure by the lender. Loans that do not fully amortize during the term, such as “bullet” or “balloon-payment” loans, present refinancing risks. Variable rate loans increase the risk that the property may become unprofitable in adverse economic conditions. Loans that require guaranties, including full principal and interest guaranties, master leases, debt service guaranties and indemnities for liabilities such as hazardous waste, may result in significant liabilities for us.

Under our current investment policies, we may not incur indebtedness if by doing so our ratio of debt to total assets, at fair market value, exceeds 75%. However, we may reevaluate our borrowing policies from time to time, and the Board may change our investment policies without the consent of our stockholders. At December 31, 2008 and 2007, our ratio of debt to total assets, at fair value, was 70.15% and 61.45%, respectively.

Our insurance on our real estate may not cover all losses.

We carry comprehensive liability, fire, terrorism, extended coverage and rental loss insurance covering all of our properties, with policy specifications and insured limits that we believe are adequate and appropriate under the circumstances. Many insurance carriers are excluding asbestos-related claims and mold remediation-related claims from standard policies, pricing asbestos and mold remediation endorsements at prohibitively high rates or adding significant restrictions to this coverage. Because of our inability to obtain specialized coverage at rates that correspond to the perceived level of risk, we have not obtained insurance for asbestos-related claims or mold remediation-related risks. We continue to evaluate the availability and cost of additional insurance coverage from the insurance market. If we decide in the future to purchase coverage for asbestos or mold remediation insurance, the cost could have a negative impact on our results of operations. If an uninsured loss or a loss in excess of insured limits occurs on a property, we could lose our capital invested in the property, as well as the anticipated future revenues from the property and, in the case of debt that is recourse to us, we would remain obligated for any mortgage debt or other financial obligations related to the property. Any loss of this nature could adversely affect us.

Additionally, the policy specifications of our insurance coverage on our properties include deductibles related to an insured loss. The deductibles applicable to an insured loss caused by “Named Storms”, as defined in the insurance policy, which are usually in the form of a hurricane, at certain of the properties we operate, are higher than deductibles for other insured losses covered by the policy. Specifically, the deductibles for “Named Storms” are based on a percentage of the insured property value with a specific minimum amount. Both the percentage and the related minimum amounts are higher than the standard policy deductibles for insured losses caused by a “Named Storm” in certain higher risk counties of certain states, including Florida, North Carolina, Texas and Virginia and even higher amounts for insured losses caused by a “Named Storm” in the counties of Dade, Broward and Palm Beach, Florida. Losses resulting from “Named Storms” could adversely affect us.

Environmental compliance costs and liabilities with respect to our real estate may adversely affect our results of operations.

Our operating costs may be affected by our obligation to pay for the cost of complying with existing environmental laws, ordinances and regulations, as well as the cost of complying with future legislation with respect to the assets, or

loans collateralized by assets, with environmental problems that materially impair the value of assets. Under various federal, state or local environmental laws, ordinances and regulations, an owner of real property may be liable for the costs of removal or remediation of hazardous or toxic substances located on or in the property. These laws often impose liability without regard to whether the owner knew of, or was responsible for, the presence of the hazardous or toxic substances.

The costs of any required remediation or removal of these substances may be substantial. In addition, the owner's liability as to any property is generally not limited under these laws, ordinances and regulations and could exceed the value of the property and/or the aggregate assets of the owner. The presence of hazardous or toxic substances, or the failure to remediate properly, may also adversely affect the owner's ability to sell or rent the property or to borrow using the property as collateral. Under these laws, ordinances and regulations, an owner or any entity who arranges for the disposal of hazardous or toxic substances, such as asbestos, at a disposal facility may also be liable for the costs of any required remediation or removal of the hazardous or toxic substances at the facility, whether or not the facility is owned or operated by the owner or entity. In connection with the ownership of any of our properties, or participation in ventures, or the disposal of hazardous or toxic substances, we may be liable for any of these costs.

Other federal, state and local laws may impose liability for the release of hazardous material, including asbestos-containing materials, into the environment, or require the removal of damaged asbestos containing materials in the event of remodeling or renovation, and third parties may seek recovery from owners of real property for personal injury associated with exposure to released asbestos-containing materials or other hazardous materials. We do not currently have insurance for asbestos-related claims.

Recently there has been an increasing number of lawsuits against owners and managers of multifamily properties alleging personal injury and property damage caused by the presence of mold in residential real estate. Some of these lawsuits have resulted in substantial monetary judgments or settlements. We do not currently have insurance for all mold-related risks. Environmental laws may also impose restrictions on the manner in which a property may be used or transferred or in which businesses may be operated, and these restrictions may require additional expenditures. In connection with the ownership of properties, we may be potentially liable for any of these costs. The cost of defending against claims of liability or remediating contaminated property and the cost of complying with environmental laws could materially adversely affect our results of operations and financial condition.

We have been notified of the presence of asbestos in certain structural elements in our properties, which we are addressing in accordance with various operations and maintenance plans. The asbestos operations and maintenance plans require that all structural elements that contain asbestos not be disturbed. In the event the asbestos containing elements are disturbed either through accident, such as a fire, or as a result of planned renovations at the property, those elements would require removal by a licensed contractor, who would provide for containment and disposal in an authorized landfill. The property managers of our properties have been directed to work proactively with licensed ablation contractors whenever there is any question regarding possible exposure.

We are not aware of any environmental liability relating to our properties that we believe would have a material adverse effect on our business, assets or results of operations. Nevertheless, it is possible that there are material environmental liabilities of which we are unaware with respect to our properties. Moreover, we cannot be certain that future laws, ordinances or regulations will not impose material environmental liabilities or that the current environmental condition of our properties will not be affected by residents and occupants of our properties, by the uses or condition of properties in the vicinity of our properties, such as leaking underground storage tanks, or by third parties unaffiliated with us.

Our failure to comply with various regulations affecting our properties could adversely affect our financial condition.

Various laws, ordinances, and regulations affect multifamily residential properties, including regulations relating to recreational facilities, such as activity centers and other common areas. We believe that each of our properties has all material permits and approvals to operate its business.

Our multifamily residential properties must comply with Title II of the Americans with Disabilities Act (the “ADA”) to the extent that such properties are public accommodations and/or commercial facilities as defined by the ADA. Compliance with the ADA requires removal of structural barriers to handicapped access in certain public areas of our properties where such removal is readily achievable. The ADA does not, however, consider residential properties to be public accommodations or commercial facilities, except to the extent portions of such facilities, such as a leasing office, are open to the public. We believe that our properties comply in all material respects with all current requirements under the ADA and applicable state laws. Noncompliance with the ADA could result in imposition of fines or an award of damages to private litigants. The cost of defending against any claims of liability under the ADA or the payment of any fines or damages could adversely affect our financial condition.

The Fair Housing Act (the “FHA”) requires, as part of the Fair Housing Amendments Act of 1988, apartment communities first occupied after March 13, 1990 to be accessible to the handicapped. Noncompliance with the FHA could result in the imposition of fines or an award of damages to private litigants. We believe that our properties that are subject to the FHA are in compliance with such law. The cost of defending against any claims of liability under the FHA or the payment of any related fines or damages could adversely affect our financial condition.

We face risks associated with property acquisitions.

We intend to acquire additional properties in the future, either directly or by acquiring entities that own properties. These acquisition activities are subject to many risks. We may acquire properties or entities that are subject to liabilities or that have problems relating to environmental condition, state of title, physical condition or compliance with zoning laws, building codes, or other legal requirements. In each case, our acquisition may be without any recourse, or with only limited recourse, with respect to unknown liabilities or conditions.

As a result, if any liability were asserted against us relating to those properties or entities, or if any adverse condition existed with respect to the properties or entities, we might have to pay substantial sums to settle or cure it, which could adversely affect our cash flow and operating results. However, some of these liabilities may be covered by insurance. In addition, we intend to perform customary due diligence regarding each property or entity we acquire. We also intend to obtain appropriate representations and indemnities from the sellers of the properties or entities we acquire, although it is possible that the sellers may not have the resources to satisfy their indemnification obligations if a liability arises. Unknown liabilities to third parties with respect to properties or entities acquired might include: liabilities for clean-up of undisclosed environmental contamination; claims by tenants, vendors or other persons dealing with the former owners of the properties; liabilities incurred in the ordinary course of business; and claims for indemnification by general partners, directors, officers and others indemnified by the former owners of the properties.

We may acquire multifamily apartment communities through foreclosure auctions, which limit our ability to perform due diligence.

One of our acquisition strategies seeks to acquire multifamily apartment communities through foreclosure auctions. Generally when a property is foreclosed on by a lender, there is minimal time between the announcement of foreclosure and the auction to dispose of the property and access to the property for due diligence is either severely limited or unavailable. The lack of time and access for due diligence can result in only limited knowledge of problems, including environmental issues, that are identified after the acquisition has taken place. While the Company generally includes provisions for unforeseen problems into its underwriting models, there is no assurance that these provisions will be sufficient to remediate all of the issues identified after closing. If significant issues are identified after closing, which were not provided for during the underwriting, this sourcing strategy could result in lower profits, or higher losses, than would be realized in market rate acquisitions, where full due diligence is available.

Development risks could affect available capital and operating profitability.

We intend to develop new apartment units on property that we own or may acquire in the future. These development projects are subject to many risks including governmental approvals, which we have no assurance will be obtained. We may develop properties that have problems relating to environmental conditions, compliance with zoning laws, building codes, or other legal requirements or may be subject to unknown liabilities to third parties with respect to undisclosed environmental contamination, claims by vendors or claims by other persons. The cost to construct the projects may require capital in excess of projected amounts and possibly render the economic viability of the project unfeasible. The apartment units in the completed project may command rents and occupancy rates at less than anticipated levels and result in operating expenses at higher than forecasted levels.