

INDEPENDENCE REALTY TRUST, INC

Form 10-K

March 13, 2013

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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

**FORM 10-K**

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

For the fiscal year ended December 31, 2012

or

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

For the Transition Period from \_\_\_\_\_ to \_\_\_\_\_.

Commission file number 333-160093

**INDEPENDENCE REALTY TRUST, INC.**

(Exact name of registrant as specified in its charter)

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**Maryland**  
(State or other jurisdiction of  
incorporation or organization)

**26-4567130**  
(I.R.S. Employer  
Identification No.)

**Cira Centre**  
**2929 Arch St., 17th Floor**

**Philadelphia, PA**  
(Address of principal executive offices)

**(215) 243-9000**

**19104**  
(Zip Code)

(Registrant's telephone number, including area code)

**Securities registered pursuant to Section 12(b) of the Securities Exchange Act of 1934:**

**None**

**Securities registered pursuant to Section 12(g) of the Securities Exchange Act of 1934:**

**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 15(d) of the Act. Yes  No

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

Indicate by check mark whether the registrant has submitted electronically 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  No

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 the 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 definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act (check

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one):

Large accelerated filer  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

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

The aggregate market value of the registrant's common stock held by non-affiliates as of June 29, 2012 was \$0 because all shares of the registrant's common stock were held by an affiliate on that date.

As of March 8, 2013 there were 345,258 outstanding shares of the registrant's common stock issued and outstanding.

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**Special Note Regarding Forward-Looking Statements**

Certain statements included in this annual report on Form 10-K (this Annual Report ) that are not historical facts (including any statements concerning investment objectives, other plans and objectives of management for future operations or economic performance, or assumptions or forecasts related thereto) are forward-looking statements. These statements are only predictions. We caution that forward-looking statements are not guarantees. Actual events or our investments and results of operations could differ materially from those expressed or implied in any forward-looking statements. Forward-looking statements are typically identified by the use of terms such as may, should, expect, could, intend, plan, anticipate, estimate, believe, continue, predict, potential or the negative of such terms and other comparable terminology.

The forward-looking statements included herein are based upon our current expectations, plans, estimates, assumptions and beliefs, which involve numerous risks and uncertainties. Assumptions relating to the foregoing involve judgments with respect to, among other things, future economic, competitive and market conditions and future business decisions, all of which are difficult or impossible to predict accurately and many of which are beyond our control. Although we believe that the expectations reflected in such forward-looking statements are based on reasonable assumptions, our actual results and performance could differ materially from those set forth in the forward-looking statements. Factors which could have a material adverse effect on our operations and future prospects include, but are not limited to:

the fact that we have a limited operating history;

our ability to effectively deploy the proceeds raised in our public offering of common stock;

changes in economic conditions generally and the real estate market specifically;

legislative or regulatory changes (including changes to the laws governing the taxation of REITs);

the availability of capital;

interest rates; and

changes to accounting principles generally accepted in the United States, or GAAP.

Any of the assumptions underlying the forward-looking statements included herein could be inaccurate, and undue reliance should not be placed on any forward-looking statements included herein. All forward-looking statements are made as of the date this Annual Report is filed with the Securities and Exchange Commission, or the SEC, and the risk that actual results will differ materially from the expectations expressed herein will increase with the passage of time. Except as otherwise required by the federal securities laws, we undertake no obligation to publicly update or revise any forward-looking statements made herein, whether as a result of new information, future events, changed circumstances or any other reason. In light of the significant uncertainties inherent in the forward-looking statements included in this Annual Report, including, without limitation, the risks described under Item 1A Risk Factors, the inclusion of such forward-looking statements should not be regarded as a representation by us or any other person that the objectives and plans set forth in this Annual Report will be achieved.

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**PART I**

**ITEM 1. *Business*  
Overview**

Independence Realty Trust, Inc., or the Company, was formed on March 26, 2009 as a Maryland corporation that has elected to be taxed as a real estate investment trust, or REIT, commencing with the taxable year ended December 31, 2011. We are sponsored by RAIT Financial Trust, our sponsor, a publicly traded Maryland REIT whose common shares are listed on the New York Stock Exchange under the symbol RAS. As used herein, the terms we, our and us refer to the Company and, as required by context, Independence Realty Operating Partnership, LP, which we refer to as our operating partnership, and their subsidiaries. We currently hold a portfolio of multifamily properties and intend to invest the net proceeds of our ongoing public offering in a diversified portfolio of multifamily properties that have the potential to generate attractive returns. We own substantially all of our assets and conduct our operations through our operating partnership, of which we are the sole general partner.

We sold 20,000 shares of our common stock to Independence Realty Advisors, LLC, our advisor, on April 30, 2009. Our advisor was purchased on January 20, 2011 by a wholly owned subsidiary of our sponsor. Our advisor transferred its 20,000 shares to RAIT NTR Holdings, LLC, or RAIT NTR, an indirect wholly owned subsidiary of our sponsor, on June 18, 2012.

On June 10, 2011, our Registration Statement on Form S-11 (File No. 333-173391) for an offering of a minimum of 250,000 shares and a maximum of 100,000,000 shares of common stock for sale to the public at a price of \$10.00 per share (subject to certain discounts) in the primary offering and \$9.50 per share pursuant to our distribution reinvestment plan, which we refer to collectively as our offering, was declared effective under the Securities Act of 1933, as amended, or the Securities Act. During the year ended December 31, 2012, we satisfied the minimum offering amount of our offering as a result of our sale of 300,000 shares of our common stock for \$10.00 per share for total gross proceeds of \$3,000,000 to RAIT NTR. During the year ended December 31, 2012 we sold an additional 25,000 shares in our offering to unaffiliated investors. We intend to invest the net proceeds of our ongoing public offering in a diversified portfolio of multifamily properties with strong and stable cash flows that have the potential to generate attractive distributions for our investors, with a primary focus on core and stabilized multifamily properties that are well leased and produce predictable income.

Subject to certain restrictions and limitations, our business is externally managed on a day-to-day basis by our advisor, a wholly owned subsidiary of our sponsor, pursuant to an advisory agreement between us and our advisor. Our advisor conducts our operations and manages our portfolio of real estate investments. We have no paid employees.

We have retained Independence Realty Securities, LLC, or our dealer manager, a wholly owned subsidiary of our sponsor, to serve as our dealer manager for our offering and assume responsibility for marketing our common shares. Because our advisor and our dealer manager are indirectly owned and controlled by our sponsor, they are affiliated with us and are considered related parties. Our advisor and our dealer manager receive compensation and fees for services related to our offering and for the investment and management of our assets.

As of December 31, 2012, we owned eight multifamily properties with 2,004 units located in six states.

Our principal executive offices are located at Cira Centre, 2929 Arch Street, 17th Floor, Philadelphia, Pennsylvania 19104, our telephone number is (215) 243-9000, and our website address is [www.irtreit.com](http://www.irtreit.com). The contents of that website are not incorporated by reference or otherwise made part of this Annual Report.

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### **Investment Objectives and Strategy**

Our primary investment objectives are to:

pay attractive and consistent cash distributions;

preserve invested capital; and

provide a diversified direct investment in multifamily properties.

We have acquired and intend to continue to acquire a diverse portfolio of multifamily properties located in the United States. We plan to diversify our portfolio by size, property location and risk. We intend to continue allocating approximately 70% of our portfolio to investments in well-located, quality multifamily properties with strong and stable cash flows, typically located in supply constrained sub-markets with relatively high expectations of rent growth. As appropriate, we intend to implement strategies at these properties that we anticipate will create sustainable long-term increases in property value and generate attractive returns for our investors by, among other benefits, generating higher rental revenue and reducing resident turnover. We intend to continue allocating approximately 30% of our portfolio to investments in properties that require limited capital expenditures, have existing cash flow and offer opportunities for significantly enhanced return, with a primary focus on multifamily properties, but to a lesser extent other alternative asset classes.

Our board of directors approves all investment decisions involving the acquisitions of properties upon recommendations made by our advisor and in accordance with our investment guidelines.

### **Our Real Estate Portfolio**

As of December 31, 2012, we owned the eight multifamily properties described below.

*Belle Creek.* Belle Creek is located in the Northglenn/Thornton submarket of the Denver, Colorado metropolitan statistical area in the city of Henderson. Belle Creek is a garden style, class A apartment community with 162 units in eight three-story buildings. As of December 31, 2012, Belle Creek had a carrying amount of \$8.8 million, was 91% occupied, and the average effective rent per month was \$909.

*Centrepoint.* Centrepoint is located in the north-northwest submarket of Tucson, Arizona. The property is a garden-style, class A apartment community with 23 two-story buildings and 320 units. As of December 31, 2012, Centrepoint had a carrying amount of \$26.8 million, was 95% occupied, and the average effective rent per month was \$806.

*Copper Mill.* Copper Mill is located in the Far North Central submarket of the Austin, Texas metropolitan statistical area. Copper Mill is a garden style, class B apartment community with 320 units in 23 two-story buildings. As of December 31, 2012, Copper Mill had a carrying amount of \$15.8 million, was 94% occupied, and the average effective rent per month was \$717.

*Crestmont.* Crestmont is located in the Marietta submarket of the Atlanta, Georgia metropolitan statistical area. Crestmont is a garden style, class B apartment community with 228 units in 15 two- and three-story buildings. As of December 31, 2012, Crestmont had a carrying amount of \$14.7 million, was 93% occupied, and the average effective rent per month was \$699.

*Cumberland Glen.* Cumberland Glen is located in the Smyrna submarket of the Atlanta, Georgia metropolitan statistical area. Cumberland Glen is a garden style, class B apartment community with 222 units in 11 three-story buildings. As of December 31, 2012, Cumberland Glen had a carrying amount of \$14.6 million, was 96% occupied, and the average effective rent per month was \$652.

*Heritage Trace.* Heritage Trace is located in the Newport News submarket of the Norfolk, Virginia metropolitan statistical area. Heritage Trace is a garden style, class B apartment community with 200 units in 13 two-story buildings. As of December 31, 2012, Heritage Trace had a carrying amount of \$12.2 million, was 82% occupied, and the average effective rent per month was \$760.

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*Runaway Bay.* Runaway Bay is located in the town of Speedway in Marion County, a suburb of Indianapolis, Indiana. Runaway Bay Apartments is a garden style, class A apartment community with 192 units in 15 two-story buildings and one clubhouse/leasing office on 18.6 acres. As of December 31, 2012, Runaway Bay had a carrying amount of \$15.3 million, was 94% occupied, and the average effective rent per month was \$941.

*Tresa at Arrowhead.* Tresa is located in the Peoria/Sun City submarket of the Phoenix, Arizona metropolitan statistical area in the city of Glendale. Tresa is a garden style, class A apartment community with 360 units in 37 one- and two-story buildings. As of December 31, 2012, Tresa had a carrying amount of \$33.1 million, was 91% occupied, and the average effective rent per month was \$811.

See Item 2. Properties for further information on our portfolio.

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### **Competition**

In attracting and retaining residents to occupy our properties, we compete with numerous other housing alternatives. Our properties compete directly with other rental apartments as well as condominiums and single-family homes that are available for rent or purchase in the sub-markets in which our properties are located. Principal factors of competition include rent or price charged, attractiveness of the location and property and quality and breadth of services and amenities. If our competitors offer leases at rental rates below current market rates, or below the rental rates we currently charge our tenants, we may lose potential tenants and we may be pressured to reduce our rental rates below those we currently charge or to offer more substantial rent abatements, tenant improvements, early termination rights or below-market renewal options in order to retain tenants when our tenants' leases expire.

The number of competitive properties relative to demand in a particular area has a material effect on our ability to lease apartment units at our properties and on the rents we charge. In certain sub-markets there exists an oversupply of single family homes and condominiums and a reduction of households, both of which affect the pricing and occupancy of our rental apartments. Additionally, we compete with other real estate investors, including other multifamily REITs, pension and investment funds, partnerships and investment companies in acquiring, redeveloping and managing multifamily properties. This competition affects our ability to acquire properties and the price that we pay for such acquisitions.

### **Financing Objectives**

We will fund our investments with proceeds from our offering and expect to finance a portion of our investments with debt. We will use debt financing in various forms in an effort to increase the size of our portfolio and potential returns to our stockholders. We expect to use short-term financing in the form of revolving credit facilities and bank warehousing facilities. For longer-term funding, we may utilize financing provided by government agencies, securitization structures, if available, or mortgage financing on any real estate property we acquire.

We intend to focus our investment activities on obtaining a diverse portfolio of properties. Careful use of debt will help us to achieve our diversification goals because we will have more funds available for investment. Except for the limitations in our charter and as described below, there is no limitation on the amount we may borrow for the purchase of any single property. Our charter limits our borrowings to 300% of our net assets (equivalent to 75% of the cost of our net assets) as of the date of any borrowing. Nevertheless, we may exceed the foregoing limits if a majority of our independent directors approve each borrowing in excess of our charter limitation and we disclose such borrowing to our stockholders in our immediately subsequent quarterly report with an explanation from our independent directors of the justification for the excess borrowing. We do not intend to exceed the leverage limit in our charter except in the early stages of our development when the costs of our investments are most likely to exceed our net offering proceeds. Our board of directors must review our aggregate borrowings at least quarterly.

After we have acquired a substantial portfolio of diversified investments, we intend to limit our aggregate leverage to 65% of the combined initial purchase price of all of our real estate properties. During the period when we are beginning our operations, we may employ greater leverage in order to more quickly build a diversified portfolio of assets. As of December 31, 2012, our borrowings as a percentage of our undepreciated investments in real estate was 63%.

### **Regulations**

Our investments are subject to various federal, state, and local laws, ordinances, and regulations, including, among other things, zoning regulations, land use controls, environmental controls relating to air and water quality, noise pollution, and indirect environmental impacts such as increased motor vehicle activity. We believe that we have all permits and approvals necessary under current law to operate our investments.

### **Income Taxes**

We have elected to be taxed as a REIT beginning with the taxable year ended December 31, 2011. Accordingly, we recorded no income tax expense for the years ended December 31, 2012 and 2011.

To qualify as a REIT, we must meet certain organizational and operational requirements, including a requirement to distribute at least 90% of our ordinary taxable income to stockholders. As a REIT, we generally will not be subject to federal income tax on taxable income that we distribute to our stockholders. We believe that we have been organized and operated in such a manner as to qualify and maintain treatment as a REIT and intend to operate in such a manner so that we will qualify and remain qualified as a REIT for federal income tax purposes. For a discussion of risks arising out of our REIT status, see Item 1A Risk Factors United States Federal Income Tax Risks below.



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### **Financial Information About Industry Segments**

Our current business consists of owning, managing, operating, leasing, acquiring, developing, investing in, and disposing of real estate assets. We internally evaluate all of our real estate assets as one industry segment, and, accordingly, we do not report segment information.

### **Available Information**

We are subject to the reporting requirements of the Securities Exchange Act of 1934, as amended, or the Exchange Act, and, as a result, file periodic reports and other information with the SEC. Access to copies of our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and other filings with the SEC, including amendments to such filings, may be obtained free of charge from our website, [www.irtreit.com](http://www.irtreit.com). These filings are available promptly after we file them with, or furnish them to, the SEC. We are not incorporating our website or any information from the website into this Annual Report. The SEC also maintains a website, [www.sec.gov](http://www.sec.gov), that contains our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and other filings with the SEC. Access to these filings is free of charge.

### **ITEM 1A. Risk Factors**

*Stockholders should carefully consider the following risk factors in conjunction with the other information contained in this report. The risks discussed in this Annual Report could adversely affect our business, operating results, prospects and financial condition. This could cause the value of our stock to decline. The risks and uncertainties described below are not the only ones we face, but do represent those risks and uncertainties that we believe are material to us. Additional risks and uncertainties not presently known to us or that, as of the date of this Annual Report, we deem immaterial may also harm our business.*

### **Investment Risks**

*Our limited prior operating history makes it difficult for stockholders to evaluate our likely performance.*

We and our advisor are both entities with limited prior operating histories and we may both be unable to successfully operate our businesses or achieve our investment objectives. The past performance of other real estate investment programs sponsored by our sponsor or affiliates of our sponsor may not be indicative of the performance we may achieve. We may not be able to conduct our business as planned or successfully.

*We differ from our sponsor in a number of respects, and therefore, the past performance of our sponsor may not be indicative of our future results.*

The past performance of our sponsor may not be indicative of our future results and we may not be able to successfully implement our strategies and operate our business. Our business is different in a number of respects from the operations of our sponsor, resulting in returns to our stockholders that vary from those generated by our sponsor.

*Currently, our common stock is not listed on an exchange and there is no public trading market for it, therefore it may be difficult for stockholders to sell their stock. If stockholders sell their stock, it may be at a substantial discount.*

Our common stock is not listed on a stock exchange and there is no current public trading market, nor is there any assurance that a public trading market will ever exist, for our stock. In addition, our charter prohibits the ownership of more than 9.8% in the value of the aggregate of the outstanding shares of our stock or more than 9.8% (in value or number of shares, whichever is more restrictive) of any class or series of the outstanding shares of our stock by a single investor, unless exempted by our board of directors, which may inhibit the ability of our stockholders to sell their stock. We have adopted a share repurchase program which limits the number of shares of stock that may be repurchased annually. Our board of directors may also limit, suspend or terminate our share repurchase program at any time. As a result, it may be difficult for stockholders to sell their shares of stock. If stockholders are able to sell their stock, it might be at a substantial discount from the price they paid. Stockholders should consider our stock illiquid and must be prepared to hold their stock for an indefinite period of time.

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*Due to the risks involved in the ownership of real estate, there is no guarantee of any return for our stockholders, and stockholders may lose some or all of their investment.*

By owning our shares, stockholders will be subjected to the risks associated with the ownership and operation of real estate properties. Our stockholders will be subject to these risks, which include, without limitation:

changes in the general economic climate;

changes in local conditions such as an oversupply of space or reduction in demand for real estate;

changes in interest rates and the availability of financing;

changes in property level operating expenses due to inflation or otherwise; and

changes in laws and governmental regulations, including those governing real estate usage, zoning and taxes.

If our assets decrease in value, the value of an investment in our shares will likewise decrease, and stockholders could lose some or all of their investment.

*We may suffer from delays in locating suitable investments, which could adversely affect the return for our stockholders.*

Our ability to achieve our investment objectives and to make distributions to our stockholders is dependent upon our advisor's performance in the acquisition of, and arranging of financing for, investments, as well as our property manager's performance in the selection of residents and the negotiation of leases. The current market for properties that meet our investment objectives is highly competitive as is the leasing market for such properties. Stockholders will not have the opportunity to evaluate the terms of most of our transactions or other economic or financial data concerning most of our investments. Stockholders must rely entirely on the oversight of our board of directors, the management ability of our advisor and the performance of the property manager. We cannot be sure that our advisor will be successful in obtaining suitable investments on financially attractive terms.

Additionally, as a public company, we are subject to the ongoing reporting requirements under the Securities Exchange Act of 1934, as amended, or the Exchange Act. Pursuant to the Exchange Act, we may be required to file with the SEC financial statements of properties we acquire. To the extent any required financial statements are not available or cannot be obtained, we will not be able to acquire the investment. As a result, we may be unable to acquire certain properties that otherwise would be a suitable investment. We could suffer delays in our investment acquisitions due to these reporting requirements.

Delays we encounter in the selection and acquisition of properties could adversely affect our stockholders' returns. In addition, if we are unable to invest our offering proceeds in real properties in timely manner, we may invest the proceeds in short-term, investment-grade investments or ultimately liquidate. In such an event, our ability to make distributions and pay returns to our stockholders would be adversely affected.

*The cash distributions stockholders receive may be less frequent or lower in amount than they expect.*

Our board of directors will determine the amount and timing of distributions. In making this determination, our directors will consider all relevant factors, including the amount of cash available for distribution, capital expenditure and reserve requirements and general operational requirements. We cannot assure stockholders that sufficient cash will be available to make distributions to them. We may borrow funds, return capital or sell assets to make distributions. With limited prior operations, we cannot predict the amount of distributions stockholders may receive and we may be unable to pay, maintain or increase distributions over time.

The sufficiency of cash flow to fund future distributions with respect to an increased number of outstanding shares will depend on the pace at which we are able to identify and close on suitable cash-generating real property investments. Because the accrual of offering proceeds may

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outpace the investment of these funds in real property acquisitions, cash generated from such investments may become insufficient to fund operating expenses and distributions. Also, because we may receive income from rents or interest at various times during our fiscal year, distributions paid may not reflect our income earned in that particular distribution period. The amount of cash available for distributions will be affected by many factors, including without limitation, our ability to acquire properties as offering proceeds become available, the income from those investments and our operating expense levels. Further, if the aggregate amount of our distributions in any given year exceeds our earnings and profits (as determined for U.S. federal income tax purposes), the excess amount will either be (i) a return of capital or (ii) gain from the sale or exchange of property to the extent that a stockholder's tax basis in our common stock equals or is reduced to zero as the result of our current or prior year distributions, in each case for U.S. federal income tax purposes.

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*Distributions paid from sources other than our cash flow from operations will result in us having fewer funds available for the acquisition of properties, which may adversely affect our ability to fund future distributions with cash flow from operations and may adversely affect the overall return on an investment.*

As mentioned above, we may pay distributions from sources other than from our cash flow from operations. If we have not generated sufficient cash flow from our operations and other sources, such as from borrowings, sale of additional securities, advances from our advisor, our advisor's deferral, suspension and/or waiver of its fees and expense reimbursements, to fund distributions, we may use the offering proceeds. Moreover, our board of directors may change this policy, in its sole discretion, at any time. Distributions made from offering proceeds are a return of capital to stockholders upon which we will have used to pay offering and organization expenses in connection with this offering. We have not established any limit on the amount of proceeds from this offering that may be used to fund distributions. If we fund distributions from the proceeds of our offering, we will have less funds available for acquiring properties. Our inability to acquire properties may have a negative effect on our ability to generate sufficient cash flow from operations to pay distributions. Funding distributions from borrowings could restrict the amount we can borrow for investments, which may affect our profitability. Funding distributions with the sale of assets may affect our ability to generate cash flows. Funding distributions from the sale of additional securities could dilute existing stockholders' interests in us if we sell shares of our common stock to third-party investors. Payment of distributions from the mentioned sources could restrict our ability to generate sufficient cash flow from operations, affect our profitability and/or affect the distributions payable to stockholders upon a liquidity transaction, any or all of which may have an adverse effect on the value of an investment in our shares. In addition, subsequent investors may experience immediate dilution in their investment because a portion of our net offering proceeds may have been used to fund distributions instead of retained in our company and used to make investments.

*Your percentage of ownership may become diluted if we issue new shares of stock.*

Stockholders have no rights to buy additional shares of stock in the event we issue new shares of stock. We may issue common stock, convertible debt or preferred stock pursuant to a subsequent public offering or a private placement, or to sellers of properties we directly or indirectly acquire instead of, or in addition to, cash consideration. Investors purchasing our common stock in any offering who do not participate in any subsequent future stock issuances will experience dilution in the percentage of the issued and outstanding stock they own.

*The properties we own or in the future acquire may not produce the cash flow required to meet our REIT minimum distribution requirements, and we may decide to borrow funds to satisfy such requirements, which could adversely affect our overall financial performance.*

We may decide to borrow funds in order to meet the REIT minimum distribution requirements even if our management believes that the then prevailing market conditions generally are not favorable for such borrowings or that such borrowings would not be advisable in the absence of such tax considerations. If we borrow money to meet the REIT minimum distribution requirement or for other working capital needs, our expenses will increase, our net income will be reduced by the amount of interest we pay on the money we borrow and we will be obligated to repay the money we borrow from future earnings or by selling assets, any or all of which may decrease future distributions to stockholders.

*To maintain our REIT status, we may be forced to forego otherwise attractive opportunities, which may delay or hinder our ability to meet our investment objectives and reduce the overall return on an investment in our shares.*

To continue to qualify as a REIT, we must satisfy certain tests on an ongoing basis concerning, among other things, the sources of our income, nature of our assets and the amounts we distribute to our stockholders. We may be required to make distributions to stockholders at times when it would be more advantageous to reinvest cash in our business or when we do not have funds readily available for distribution. Compliance with the REIT requirements may hinder our ability to operate solely on the basis of maximizing profits and value of an investment in our shares.

## **Risks Related to Our Organization, Structure and Management**

*We are dependent upon our sponsor, advisor and their affiliates to conduct our operations, and therefore, any adverse changes in the financial health of our sponsor, advisor or their affiliates, or our relationship with any of them, could hinder our operating performance and the return for our stockholders.*

We are dependent on our advisor and affiliates to manage our operations and acquire and manage our portfolio of real estate assets. Our advisor will make all decisions with respect to the day to day management of our company. Our advisor will depend upon the fees and other compensation that it will receive from us in connection with the management and sale of our properties to conduct its operations. Any adverse changes in the financial condition of, or our relationship with, our advisor or property manager could hinder their ability to successfully manage our operations and our portfolio of investments.



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***The nature of our sponsor's business, and our dependence on our sponsor and advisor, makes us subject to certain risks that we would not ordinarily be subject to based on our targeted investments.***

Our sponsor, as part of the operation of its business, provides a comprehensive set of debt financing options to the commercial real estate industry along with fixed income trading and advisory services. Its investments consist of commercial mortgages, mezzanine loans, other loans and preferred equity investments, debt securities issued by real estate companies, subordinated debentures, mortgage-backed securities, collateralized debt obligations, or CDOs, and other real estate-related debt, none of which we intend to acquire as part of our investment strategy. As a result of our dependence on our sponsor and advisor, we are indirectly subject to some of the same investment risks as our advisor, including risk of payment defaults and credit risks in our sponsor's investment portfolio, the illiquidity of longer-term, subordinate and non-traditional loans, risk of loss from our sponsor's subordinated real estate investments such as mezzanine loans and preferred equity interests, exposure to interest rate risk, risks associated with its use of derivatives and hedging instruments and the risk of loss in its commercial mortgage loans from delinquency and foreclosure. We would not be subject to these risks if we were not dependent upon our sponsor and advisor, and therefore stockholders may not be able to avoid these risks.

In addition, our sponsor engages in securitization strategies that seek to match the payment terms, interest rate and maturity dates of its financings with the payment terms, interest rate and maturity dates of its investments. In particular, our sponsor financed the majority of its commercial real estate loan portfolio through two non-recourse loan securitizations which aggregate \$1.85 billion of loan capacity. Our sponsor retained all of the most junior debt tranche and all of the preferred equity issued by these securitizations. Our sponsor also financed most of its debt securities portfolio in a series of non-recourse CDOs, which provide long-dated, interest-only, match funded financing to the debt investments. These securitizations typically require that the principal amount of the assets must exceed the principal balance of the related securities issued by them by a certain amount, a practice known as over-collateralization. The securitization terms provide that if delinquencies or losses exceed specified levels, the required levels of over-collateralization may be increased or may be prevented from decreasing. In addition, failure by a securitization entity to satisfy an over-collateralization test typically results in accelerated distributions to the holders of the senior debt securities issued by the securitization entity, and a reduction in payment to the holders of the junior debt tranche and preferred equity of the type our sponsor holds. As a result, our sponsor is in a first-loss position because the rights of the securities it holds are subordinate in right of payment and in liquidation to the rights of senior security holders issued by the securitization entities. In addition, the failure of the securitization financings of our sponsor to meet their performance tests, including these over-collateralization requirements, may reduce our sponsor's net income and its cash flow generated by these securitizations may trigger certain termination provisions in the related collateral management agreements under which our sponsor manages these securitizations and may cause an event of default under the remaining securitizations. This would increase the likelihood of a reduction or elimination of cash flow to our sponsor, upon which we are dependent, and may result in adverse consequences to our operations.

***As a public company, our sponsor may be subject to more litigation than a privately held sponsor with a limited number of investors. Any such litigation may distract our management team.***

Our sponsor, RAIT Financial Trust, is a public company and, as a result, may be subject to more litigation than a privately held sponsor with a limited number of investors. For example, our sponsor and certain of its executive officers and trustees were named defendants in class action securities lawsuits filed in 2007. The lawsuits alleged, among other things, that certain defendants violated the Securities Act of 1933, as amended, or the Securities Act, and the Exchange Act by making materially false and misleading statements and material omissions in registration statements and prospectuses. The lawsuits were settled by written agreement, which was approved by a federal district court in 2009. The settlement was funded within the limits of our sponsor's directors and officers insurance. Under the terms of the settlement, the lawsuits were dismissed with prejudice and all defendants received a full release of all claims asserted against them. There can be no assurance that our sponsor or any of its officers will not be subject to additional litigation in the future, which may distract our management team from our business.

***If our advisor loses or is unable to obtain key personnel, our ability to implement our investment strategies could be hindered, which could adversely affect our ability to make distributions to our stockholders.***

Our success depends to a significant degree upon the contributions of certain of our executive officers and other key personnel of our advisor. We cannot guarantee that all, or any, will remain affiliated with us or our advisor. If any of our key personnel were to cease their affiliation with our advisor, our operating results could suffer. Further, we do not intend to maintain key person life insurance that would provide us with proceeds in the event of death or disability of any of our key personnel.

We believe our future success depends upon our advisor's ability to hire and retain highly skilled managerial, operational and marketing personnel. Competition for such personnel is intense, and we cannot assure stockholders that our advisor will be successful in attracting and retaining such skilled personnel. If our advisor loses or is unable to obtain the services of key personnel, our ability to implement our investment strategies could be delayed or hindered, and the value of an investment in our shares may decline.



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### ***Maryland General Corporation Law prohibits certain business combinations, which may make it more difficult for us to be acquired.***

Under Maryland General Corporation Law, business combinations between a Maryland corporation and an interested stockholder or an affiliate of an interested stockholder are prohibited for five years after the most recent date on which the interested stockholder becomes an interested stockholder. These business combinations include a merger, consolidation, share exchange, or in circumstances specified in the statute, an asset transfer or issuance or reclassification of equity securities. An interested stockholder is defined as (i) any person who beneficially owns 10% or more of the voting power of the then outstanding voting stock of the corporation; or (ii) an affiliate or associate of the corporation who, at any time within the two-year period prior to the date in question, was the beneficial owner of 10% or more of the voting power of the then outstanding voting stock of the corporation.

A person is not an interested stockholder under the statute if the board of directors approved in advance the transaction by which the person otherwise would have become an interested stockholder. However, in approving a transaction, the board of directors may provide that its approval is subject to compliance, at or after the time of approval, with any terms and conditions determined by the board.

After the expiration of the five-year period described above, any business combination between the Maryland corporation and an interested stockholder must generally be recommended by the board of directors of the corporation and approved by the affirmative vote of at least:

80% of the votes entitled to be cast by holders of the then outstanding shares of voting stock of the corporation; and

two-thirds of the votes entitled to be cast by holders of voting stock of the corporation, other than shares held by the interested stockholder with whom or with whose affiliate the business combination is to be effected, or held by an affiliate or associate of the interested stockholder.

These super-majority vote requirements do not apply if the corporation's common stockholders receive a minimum price, as defined under Maryland General Corporation Law, for their shares in the form of cash or other consideration in the same form as previously paid by the interested stockholder for its shares. Maryland General Corporation Law also permits various exemptions from these provisions, including business combinations that are exempted by the board of directors before the time that the interested stockholder becomes an interested stockholder. The business combination statute may discourage others from trying to acquire control of us and increase the difficulty of consummating any offer.

### ***Stockholders have limited control over changes in our policies and operations.***

Our board of directors determines our major policies, including regarding financing, growth, debt capitalization, REIT qualification and distributions. Our board of directors may amend or revise these and other policies without a vote of the stockholders. Our charter sets forth the stockholder voting rights required under the Statement of Policy Regarding Real Estate Investment Trusts, as revised and adopted by the North American Securities Administrators Association on May 7, 2007, or the NASAA REIT Guidelines. Under our charter and the Maryland General Corporation Law, our stockholders generally have a right to vote only on the following matters:

the election or removal of directors;

any amendment of our charter, except that our board of directors may amend our charter without stockholder approval to:

change the name or other designation or the par value of any class or series of stock and the aggregate par value of our stock;

increase or decrease the aggregate number of our shares;

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increase or decrease the number of our shares of any class or series of stock that we have the authority to issue; and

effect certain reverse stock splits;

our liquidation and dissolution; and

our being a party to any merger, consolidation, sale or other disposition of substantially all of our assets or similar reorganization. All other matters are subject to the discretion of our board of directors.

***Our authorized but unissued shares of common and preferred stock may prevent a change in our control.***

Our charter authorizes us to issue additional authorized but unissued shares of common or preferred stock. In addition, our board of directors may, without stockholder approval, amend our charter to increase the aggregate number of shares of our common stock or the number of shares of stock of any class or series that we have authority to issue and classify or reclassify any unissued shares of common or preferred stock and set the preferences, rights and other terms of the classified or reclassified shares. As a result, our board of directors may establish a series of shares of common or preferred stock that could delay or prevent a transaction or a change in control that might involve a premium price for shares of our common stock or otherwise be in the best interest of our stockholders.

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***Because of our holding company structure, we depend on our operating partnership and its subsidiaries for cash flow and we will be structurally subordinated in right of payment to the obligations of our operating partnership and its subsidiaries.***

We are a holding company with no business operations of our own. Our only significant asset is and will be the general partnership interests of our operating partnership. We conduct, and intend to conduct, all of our business operations through our operating partnership. Accordingly, our only source of cash to pay our obligations is distributions from our operating partnership and its subsidiaries of their net earnings and cash flows. We cannot assure our stockholders that our operating partnership or its subsidiaries will be able to, or be permitted to, make distributions to us that will enable us to make distributions to our stockholders from cash flows from operations. Each of our operating partnership's subsidiaries is a distinct legal entity and, under certain circumstances, legal and contractual restrictions may limit our ability to obtain cash from such entities. In addition, because we are a holding company, stockholders' claims will be structurally subordinated to all existing and future liabilities and obligations of our operating partnership and its subsidiaries. Therefore, in the event of our bankruptcy, liquidation or reorganization, our assets and those of our operating partnership and its subsidiaries will be able to satisfy stockholders' claims only after all of our and our operating partnership's and its subsidiaries' liabilities and obligations have been paid in full.

***Our board of directors may amend or terminate our share repurchase program, which may impact the ability of stockholders to liquidate their investment.***

Our share repurchase program includes limitations on participation. In addition, our board of directors has the ability, in its sole discretion, to reject any request for repurchase and to amend, suspend or terminate the program. As a result, the ability of stockholders to participate in and receive liquidity on their investment through this program may be restricted. Stockholders should not rely on our share repurchase program to provide them with liquidity.

***Our rights and the rights of our stockholders to recover on claims against our directors are limited, which could reduce our ability and the ability of our stockholders to recover against them if they negligently cause us to incur losses.***

Maryland General Corporation Law provides that a director has no liability in such capacity if he performs his duties in good faith, in a manner he reasonably believes to be in our best interests and with the care that an ordinarily prudent person in a like position would use under similar circumstances. A director who performs his or her duties in accordance with the foregoing standards should not be liable to us or any other person for failure to discharge his or her obligations as a director. We are permitted to purchase and maintain insurance or provide similar protection on behalf of any directors, officers, employees and agents, including our advisor and its affiliates, against any liability asserted which was incurred in any such capacity with us or arising out of such status, except as limited by our charter and/or bylaws. This may result in us having to expend significant funds, which will reduce the available cash for distribution to our stockholders.

Our charter prohibits us from indemnifying our directors, our advisor and its affiliates for any loss or liability that they suffer or holding harmless our directors, the advisor and its affiliates for any loss or liability that we suffer unless certain conditions are met.

As a result of the foregoing, our directors and officers will not be liable for monetary damages unless the director or officer actually received an improper benefit or profit in money, property or services, or is adjudged to be liable to us or our stockholders based on a finding that his or her action, or failure to act, was the result of active and deliberate dishonesty and was material to the cause of action adjudicated in the proceeding.

***If we internalize our management functions, the percentage of our outstanding common stock owned by our other stockholders could be reduced, and we could incur other significant costs associated with being self-managed.***

In the future, our board of directors may consider internalizing the functions performed for us by our advisor by, among other methods, acquiring our advisor's assets. The method by which we could internalize these functions could take many forms. There is no assurance that internalizing our management functions will be beneficial to us and our stockholders. An acquisition of our advisor could also result in dilution of the interests of our stockholders and could reduce earnings per share and funds from operation per share. Additionally, we may not realize the perceived benefits or we may not be able to properly integrate a new staff of managers and employees or we may not be able to effectively replicate the services provided previously by our advisor, property manager or their affiliates. Internalization transactions, including without limitation, transactions involving the acquisition of advisors or property managers affiliated with entity sponsors have also, in some cases, been the subject of litigation. Even if these claims are without merit, we could be forced to spend significant amounts of money defending claims which would reduce the amount of funds available for us to invest in properties or other investments and to pay distributions. All of these factors could have a material adverse effect on our results of operations, financial condition and ability to pay distributions.



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*If we do not successfully implement a liquidity transaction, stockholders may have to hold their investment for an indefinite period.*

Our charter does not require our board of directors to pursue a transaction providing liquidity to our stockholders. If our board of directors does determine to pursue a liquidity transaction, we would be under no obligation to conclude the process within a set time. If we adopt a plan of liquidation, the timing of the sale of assets will depend on real estate and financial markets, economic conditions in areas in which properties are located, and federal income tax effects on stockholders, that may prevail in the future. We cannot guarantee that we will be able to liquidate our assets. After we adopt a plan of liquidation, we would likely remain in existence until all our investments are liquidated. If we do not pursue a liquidity transaction, or delay such a transaction due to market conditions, stockholders' shares may continue to be illiquid and stockholders may, for an indefinite period of time, be unable to convert their shares to cash easily and could suffer losses.

*We will not calculate our net asset value per share until up to 18 months after completion of our offering stage. In addition, the methodologies we will use to calculate net asset value are uncertain. Therefore, stockholders will not be able to determine the net asset value of their shares for a substantial period of time and may not be able to meaningfully compare our net asset value to the net asset value of other non-listed REITs.*

We do not intend to calculate the net asset value per share for our shares until up to 18 months after the completion of our offering stage. We will consider our offering stage complete when we are no longer publicly offering equity securities in a continuous offering, whether through our initial public offering or any future offerings (excluding offers to sell under our distribution reinvestment program). Thereafter, our advisor, or another firm it chooses for that purpose, will determine the value of our properties and our other assets based on such information as our advisor determines appropriate, which may or may not include independent valuations of our properties and our other assets or of our enterprise as a whole. We will disclose our net asset value and the methodologies we use to calculate our net asset value to stockholders in our filings with the SEC. Therefore, stockholders will not be able to determine the net asset value of their shares on an on-going basis during this offering and for a substantial period of time thereafter. In addition, we may utilize net asset value calculation methodologies which differ from methodologies utilized by other public, non-listed REITs. As a result, a comparison of our net asset value with the net asset value of other public, non-listed REITs may not be meaningful. Therefore, it is important that stockholders carefully consider how our calculation methodologies differ, if at all, from other non-listed REITs.

*Our investment objectives and strategies may be changed without stockholder consent.*

Except for the investment limitations contained in our charter, which require stockholder consent to amend, we may change our investment objectives and strategies, and our policies with respect to investments, operations, indebtedness, capitalization and distributions, at any time without the consent of our stockholders, which could result in our making investments that are different from, and possibly riskier or more highly leveraged than, the types of investments described in this prospectus. A change in our investment strategy may, among other things, increase our exposure to interest rate risk, default risk and real estate market fluctuations, all of which could materially affect our ability to achieve our investment objectives.

### **Risks Related to Conflicts of Interest**

*Our executive officers have interests that may conflict with the interests of stockholders.*

Our executive officers are also affiliated with or are executive officers and shareholders of our sponsor. These individuals may have personal and professional interests that conflict with the interests of our stockholders with respect to business decisions affecting us and our operating partnership. As a result, the effect of these conflicts of interest on these individuals may influence their decisions affecting the negotiation and consummation of the transactions whereby we acquire multifamily properties in the future from our sponsor.

*We may have assumed unknown liabilities in connection with the acquisition of the multifamily properties contributed by our sponsor.*

We acquired seven multifamily properties contributed by our sponsor subject to existing liabilities, some of which may be unknown at the time of contribution. Unknown liabilities might include liabilities for cleanup or remediation of undisclosed environmental conditions, claims of tenants, vendors or other persons dealing with such entities, tax liabilities, and accrued but unpaid liabilities incurred in the ordinary course of business. As part of the contribution to us of certain of the multifamily properties in our portfolio, our sponsor made limited representations and warranties to us regarding the properties. Because many liabilities may not be identified at the time of contribution, we may have no recourse against our sponsor.

*We may pursue less vigorous enforcement of terms of the contribution agreements for the multifamily properties we acquired from our sponsor because of conflicts of interest with certain members of our senior management team.*

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Our senior management team has ownership interest in and professional responsibilities with our sponsor, which contributed multifamily properties to our operating partnership. As part of the contribution of these properties, our sponsor made limited representations and warranties to us regarding the properties and interest acquired. Any indemnification from our sponsor related to the contribution is limited. We may choose not to enforce, or to enforce less vigorously, our rights under the contribution agreements due to our ongoing relationship with the principals and executive officers of our sponsor.

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***We face risks relating to financing arrangements with our sponsor for the multifamily properties we acquired from our sponsor that would not be present with third-party financing.***

In connection with our acquisition of the multifamily properties from our sponsor, our sponsor has made, and in the future may make financing available to us. Such financing arrangements may involve risks not otherwise present with other methods of financing, including, for example:

the possibility that our sponsor may sell or securitize our loan agreements with a third party, in which case our loan would become subject to the rights of the assignee or transferee whose interests may not be the same as our sponsor's interests;

that our sponsor may in the future have interests that are or that become inconsistent with our interests, which may cause us to disagree with our sponsor as to the best course of action with respect to the payment terms, remedies available under and refinancing of the loan and which disagreement may not be resolved to our satisfaction;

that in the event of our default on the loan, our sponsor may determine to foreclose upon the collateral without pursuing alternative remedies such as renegotiation of loan terms or workouts that a third-party lender might pursue; and

that our executive officers are also executive officers or employees of our sponsor and would be responsible for negotiating the terms of any loan agreement on our behalf as well as on our sponsor's behalf.

Our sponsor may also make a loan as part of a lending syndicate with third parties, in which case we expect our sponsor would enter into an inter-creditor agreement that will define its rights and priority with respect to the underlying collateral. The third-party lending syndicate may also have interests that differ with our interests as well as the interests of our sponsor.

***Our advisor, executive officers and their affiliates may face conflicts of interest and if inadequate time is devoted to our business, our stockholders may be negatively impacted.***

We do not have any employees, and as a result, will rely on the employees of our advisor and its affiliates for the day-to-day operation of our business. The employees of our sponsor and its affiliates currently control our sponsor, which owns properties in the markets in which we may seek to invest, and they spend a material amount of time managing these properties and other assets that are unrelated to our business. Each of our executive officers is also an officer or employee of our sponsor and/or its affiliates, and as a result, these individuals owe fiduciary duties to these other entities and their stockholders, members and limited partners. Because our sponsor and its affiliates engage in other business activities, the employees of our sponsor and its affiliates may experience conflicts of interest in allocating their time and resources among our business and these other activities. The amount of time that our advisor and its affiliates spend on our business will vary from time to time and is expected to be more while we are raising money and acquiring properties. During times of intense activity in other programs and ventures, they may devote less time and fewer resources to our business than are necessary or appropriate to manage our business. We expect that as our real estate activities expand, our advisor will attempt to hire additional employees who would devote substantially all of their time to our business. There is no assurance that our advisor will devote adequate time to our business. If our advisor suffers or is distracted by adverse financial or operational problems in connection with its operations unrelated to us, it may allocate less time and resources to our operations. If any of the foregoing events occur, the returns on our investments and our ability to make distributions to stockholders may affect the value of their shares.

Some of these individuals could make substantial profits as a result of investment opportunities allocated to entities other than us. As a result, these individuals could pursue transactions that may not be in our best interest, which could have a material effect on our operations and our stockholders. Our advisor, property manager and their respective affiliates may, in the future, be engaged in other activities that could result in potential conflicts of interest with the services that they will provide to us. In addition, our sponsor may compete with us for the acquisition and/or refinancing of properties.

Our advisor and its affiliates will receive substantial fees from us. These fees could influence our advisor's advice to us, as well as the judgment of the affiliates of our advisor who serve as our officers and directors. Among other matters, the compensation arrangements, which might entitle affiliates of our advisor to disposition fees and other possible fees in connection with its services for the seller, could affect the judgment of our advisor or its affiliates with respect to property acquisitions from, or the making of investments in, other programs sponsored by our sponsor. Therefore, considerations relating to their compensation from other programs could result in decisions that are not in the best interests of our

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stockholders, which could hurt our income, and as a result, our ability to make distributions to our stockholders and/or a decline in the value of their shares.

***Property management services are being provided by an affiliated party, which may impact our sale of properties, and as a result, affect the value of an investment in our shares.***

Our property manager is controlled by our sponsor, and is thus subject to an inherent conflict of interest. Specifically, because the property manager will receive significant fees for managing our properties, our advisor may face a conflict of interest when determining whether we should sell properties under circumstances where the property manager would no longer manage the property after the transaction. As a result of this conflict of interest, we may not dispose of properties when it would be in our best interests to do so.

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***If we acquire properties from affiliates of our advisor, the price may be higher than we would pay if the transaction was the result of arm's length negotiations.***

The prices we pay to affiliates of our advisor for our properties will be equal to the prices paid by them, plus the costs incurred by them relating to the acquisition and financing of the properties, or if the price to us is in excess of such cost, substantial justification for such excess will exist and such excess will be reasonable and consistent with current market conditions as determined by a majority of our independent directors. Substantial justification for a higher price could result from improvements to a property by the affiliate of our advisor or increases in market value of the property during the period of time the property is owned by the affiliate as evidenced by an appraisal of the property. In no event will we acquire property from an affiliate at an amount in excess of its current appraised value as determined by an independent appraiser selected by our independent directors not otherwise interested in the transaction. An appraisal is current if obtained within the prior year. These prices will not be the subject of arm's length negotiations, which could mean that the acquisitions may be on terms less favorable to us than those negotiated in an arm's length transaction. Even though we will use an independent third-party appraiser to determine fair market value when acquiring properties from our advisor and its affiliates, we may pay more for particular properties than we would have in an arm's length transaction, which would reduce our cash available for investment in other properties or distribution to our stockholders.

***Payment of fees to our advisor and its affiliates will result in immediate dilution of the value of an investment in our shares and reduce cash available for investment and distribution.***

Our advisor and its affiliates will perform services for us in connection with the management and leasing of our properties. They will be paid significant fees for these services, which will result in immediate dilution of the value of an investment in our shares and reduce the amount of cash available for investment and for distribution to stockholders. Compensation to be paid to our advisor may be increased subject to approval by our independent directors and the limitations in our charter, which would further dilute an investment in our shares and reduce the amount of cash available for investment or distribution to stockholders.

The agreements between us and our advisor or its affiliates, and the fees paid to them pursuant to such agreements, were not reached through arm's length negotiations and may not reflect the terms that would be available from a third party; that is, a third party unaffiliated with our advisor may be willing to provide such services to us at a lower price. These fees increase the risk that the amount available for payment of distributions to our stockholders upon liquidation of our portfolio would be less than the purchase price of the shares of stock in our initial public offering. Substantial up-front fees also increase the risk that our stockholders will not be able to resell their shares of stock at a profit, even if our stock is listed on a national securities exchange. See Compensation Table and Management.

***Our advisor and its affiliates receive fees and other compensation based upon our investments, which may impact operating decisions, and as a result, affect the value of an investment in our shares.***

Our advisor and its affiliates receive fees and other compensation based on our investments, and are in a position to make decisions about our investments in ways that could maximize fees payable to our advisor and its affiliates. Some compensation is payable to our advisor whether or not there is cash available to make distributions to our stockholders. To the extent this occurs, our advisor and its affiliates benefit from us retaining ownership, and leveraging, our assets, while our stockholders may be better served by the sale or disposition of, or lack of leverage on, the assets. For example, because asset management fees payable to our advisor are based on total assets under management, including assets purchased using debt, our advisor may have an incentive to incur a high level of leverage in order to increase the total amount of assets under management. In addition, our advisor's ability to receive fees and reimbursements depends on our continued investment in real properties. Therefore, the interest of our advisor and its affiliates in receiving fees may conflict with the interest of our stockholders in earning income on their investment in our common stock.

***Our advisor may receive substantial fees in connection with the refinancing of any debt that we use to acquire properties or to make other permitted investments, or that is assumed, directly or indirectly, in connection with the acquisition of properties.***

In connection with any refinancing of our debt that we use to acquire properties or to make other permitted investments, including any indebtedness assumed by us in connection with the acquisition of properties, we will pay our advisor a financing coordination fee equal to 1% of the amount available and/or outstanding under such financing, subject to certain limitations. There is no limit on our ability to refinance our indebtedness. As a result, our advisor has an incentive to recommend that we refinance our existing indebtedness, regardless of whether the structure, terms or conditions are favorable to us given our then-existing debt levels and current market conditions. Although our charter limits the amount of indebtedness that we may incur, our advisor may have an incentive to recommend that we refinance our indebtedness and incur additional indebtedness in connection with such refinancing.



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### ***We may compete with other entities affiliated with our sponsor for tenants.***

Our sponsor and its affiliates are not prohibited from engaging, directly or indirectly, in any other business or from possessing interests in any other business ventures, including ventures involved in the acquisition, development, ownership, management, leasing or sale of real estate. Our sponsor and/or its affiliates may own and/or manage properties in the same geographical areas in which we expect to acquire real estate assets. Therefore, our properties may compete for tenants with other properties owned and/or managed by our sponsor and its affiliates. Our sponsor may face conflicts of interest when evaluating tenant opportunities for our properties and other properties owned and/or managed by our sponsor and its affiliates, and these conflicts of interest may have a negative impact on our ability to attract and retain tenants.

### ***If we invest in joint ventures, the objectives of our partners may conflict with our objectives.***

In accordance with our acquisition strategies, we may make investments in joint ventures or other partnership arrangements between us and affiliates of our sponsor or with unaffiliated third parties. Investments in joint ventures which own real properties may involve risks otherwise not present when we purchase real properties directly. For example, our co-venturer may file for bankruptcy protection, have economic or business interests or goals which are inconsistent with our interests or goals, or take actions contrary to our instructions, requests, policies or objectives. Among other things, actions by a co-venturer might subject real properties owned by the joint venture to liabilities greater than those contemplated by the terms of the joint venture or other adverse consequences.

These diverging interests could result in, among other things, exposing us to liabilities of the joint venture in excess of our proportionate share of these liabilities. The partition rights of each owner in a jointly owned property could reduce the value of each portion of the divided property. Moreover, there is an additional risk that the co-venturers may not be able to agree on matters relating to the property they jointly own. In addition, the fiduciary obligation that our sponsor or our board of directors may owe to our partner in an affiliated transaction may make it more difficult for us to enforce our rights.

## **General Risks Related to Investments in Real Estate**

### ***Economic conditions may adversely affect the residential real estate market and our income.***

A residential property's income and value may be adversely affected by international, national and regional economic conditions. Recently, the U.S. and international markets have experienced increased levels of volatility due to a combination of many factors, including decreasing values of home prices and commercial real estate, limited access to credit markets, increased energy costs, increased unemployment rates, and a national and global recession. If such conditions exist in the future, the residential real estate industry may experience a significant decline in business caused by a reduction in overall renters. Renewed adverse economic conditions may also have an adverse affect on our operations if the tenants occupying the residential properties we acquire cease making rent payments to us.

In addition, local real estate conditions such as an oversupply of properties or a reduction in demand for properties, availability of for sale properties, competition from other similar properties, our ability to provide adequate maintenance, insurance and management services, increased operating costs (including real estate taxes), the attractiveness and location of the property and changes in market rental rates, may adversely affect a property's income and value. A rise in energy costs could result in higher operating costs, which may affect our results from operations. In addition, local conditions in the markets in which we own or intend to own properties may significantly affect occupancy or rental rates at such properties. The risks that may adversely affect conditions in those markets include: layoffs, plant closings, relocations of significant local employers and other events negatively impacting local employment rates and the local economy; an oversupply of, or a lack of demand for, apartments; a decline in household formation; the inability or unwillingness of residents to pay rent increases; and rent control, rent stabilization and other housing laws, which could prevent us from raising rents.

### ***Rising expenses could reduce cash flow and funds available for future acquisitions, which may have a material affect on the value of an investment in our shares.***

Our properties will be subject to increases in tax rates, utility costs, operating expenses, insurance costs, repairs and maintenance, administrative and other expenses. Some of the leases on our properties may require the tenants to pay all or a portion of the expenses; however, renewals of leases or future leases may not be negotiated on that basis, in which event we will have to pay those expenses. Such increased expenses could adversely affect funds available for future acquisitions or cash available for distributions.

### ***Failure to generate sufficient cash flows from operations may reduce distributions to stockholders.***

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We intend to rely primarily on our cash flow from operations to make distributions to our stockholders. The cash flow from equity investments in our multifamily properties depends on the amount of revenue generated and expenses incurred in operating our properties. The revenue generated and expenses incurred in operating our properties depends on many factors, some of which are beyond our control. For instance, rents from our properties may not increase as expected. If our properties do not generate revenue sufficient to meet our operating expenses, debt service and capital expenditures, our cash flows and ability to make distributions to stockholders will be adversely affected.

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***If we purchase assets at a time when the residential real estate market is experiencing substantial influxes of capital investment and competition for properties, the real estate we purchase may not appreciate or may decrease in value.***

The residential real estate market may experience substantial influxes of capital from investors. This substantial flow of capital, combined with significant competition for real estate, may result in inflated purchase prices for such assets. To the extent we purchase real estate in such an environment, we are subject to the risk that, if the real estate market subsequently ceases to attract the same level of capital investment, or if the number of companies seeking to acquire such assets decreases, our returns will be lower and the value of our assets may not appreciate or may decrease significantly below the amount we paid for such assets.

***We may not make a profit if we sell a property, which could adversely impact our ability to make cash distributions to our stockholders.***

The prices that we can obtain when we determine to sell a property will depend on many factors that are presently unknown, including the operating history, tax treatment of real estate investments, demographic trends in the area and available financing. There is a risk that we will not realize any significant appreciation on our investment in a property. Accordingly, the ability of our stockholders to recover all or any portion of their investment under such circumstances will depend on the amount of funds so realized and claims to be satisfied therefrom.

***Our properties may not be diversified by geographic location or by type, which may increase the risk of an investment in our shares.***

If we are unable to diversify our investments by region, our performance will be linked to a greater extent to economic conditions in the regions in which we acquire properties. Therefore, to the extent that there are adverse economic conditions in the regions in which our properties are located and in the market for real estate properties, such conditions could result in a reduction of our income, and thus affect the amount of distributions we can make to our stockholders. Further, we do not anticipate diversifying our investments in properties by industry, that is, we plan to invest primarily in the multifamily industry. Therefore, a downturn in such industry will likely have a more pronounced effect on the amount of cash available to us for distribution or on the value of our assets than if we had diversified our investments by property type.

***We may incur liabilities in connection with properties we acquire.***

Our anticipated acquisition activities are subject to many risks. We may acquire properties 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, 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, as mentioned above, absent a determination that an expedited acquisition is necessary, we intend to perform customary due diligence regarding each property or entity we acquire. We also will attempt to obtain appropriate representations and undertakings 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, without limitation:

liabilities for clean-up of undisclosed environmental contamination;

claims by tenants 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 suffer losses that are not covered by insurance.***

If we suffer losses that are not covered by insurance or that are in excess of insurance coverage, we could lose invested capital and anticipated profits. We intend to cause comprehensive insurance to be obtained for our properties, including casualty, liability, fire, extended coverage and rental loss customarily obtained for similar properties in amounts which our advisor determines are sufficient to cover reasonably foreseeable

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losses, and with policy specifications and insured limits that we believe are adequate and appropriate under the circumstances. Material losses may occur in excess of insurance proceeds with respect to any property as insurance proceeds may not provide sufficient resources to fund the losses. However, there are types of losses, generally of a catastrophic nature, such as losses due to wars, earthquakes, floods, hurricanes, pollution, environmental matters, mold or terrorism which are either uninsurable or not economically insurable, or may be insured subject to limitations, such as large deductibles or co-payments.

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Insurance companies have recently begun to exclude acts of terrorism from standard coverage. Terrorism insurance is currently available at an increased premium, and it is possible that the premium will increase in the future or that terrorism coverage will become unavailable. In some cases, mortgage lenders have begun to insist that specific coverage against terrorism be purchased by owners as a condition for providing loans. We intend to obtain terrorism insurance if required by our lenders, but the terrorism insurance that we obtain may not be sufficient to cover loss for damages to our properties as a result of terrorist attacks. In addition, we may not be able to obtain insurance against the risk of terrorism because it may not be available or may not be available on terms that are economically feasible. In such instances, we may be required to provide other financial support, either through financial assurances or self-insurance, to cover potential losses. We cannot assure our stockholders that we will have adequate coverage for such losses.

In addition, many insurance carriers are excluding asbestos-related claims from standard policies, pricing asbestos endorsements at prohibitively high rates or adding significant restrictions to such coverage.

Because of our inability to obtain specialized coverage at rates that correspond to our perceived level of risk, we may not obtain insurance for acts of terrorism or asbestos-related claims. We will continue to evaluate the availability and cost of additional insurance coverage from the insurance market. If we decide in the future to purchase insurance for terrorism or asbestos, 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, would remain obligated for any mortgage debt or other financial obligations related to the property. Any loss of this nature would adversely affect us. Although we intend to adequately insure our properties, we cannot assure that we will successfully do so.

***We may be unable to secure funds for future capital improvements, which could adversely impact our ability to make cash distributions to our stockholders.***

When residents do not renew their leases or otherwise vacate their space, in order to attract replacement residents, we may be required to expend funds for capital improvements to the vacated apartment units. In addition, we may require substantial funds to renovate a multifamily community in order to sell it, upgrade it or reposition it in the market. If we have insufficient capital reserves, we will have to obtain financing from other sources. We intend to establish capital reserves in an amount we, in our discretion, believe is necessary. A lender also may require escrow of capital reserves in excess of any established reserves. If these reserves or any reserves otherwise established are designated for other uses or are insufficient to meet our cash needs, we may have to obtain financing from either affiliated or unaffiliated sources to fund our cash requirements. We cannot assure our stockholders that sufficient financing will be available or, if available, will be available on economically feasible terms or on terms acceptable to us. Moreover, certain reserves required by lenders may be designated for specific uses and may not be available for capital purposes such as future capital improvements. Additional borrowing will increase our interest expense, therefore, our financial condition and our ability to make cash distributions to our stockholders may be adversely affected.

***Short-term leases expose us to the effects of declining market rent, which could adversely impact our ability to make cash distributions to our stockholders.***

We expect that most of our leases will be for a term of one year or less. Because these leases generally permit the residents to leave at the end of the lease term without any penalty, our rental revenues may be impacted by declines in market rents more quickly than if our leases were for longer terms.

***The profitability of our acquisitions is uncertain.***

We intend to acquire properties selectively. Acquisition of properties entails risks that investments will fail to perform in accordance with expectations. In undertaking these acquisitions, we will incur certain risks, including the expenditure of funds on, and the devotion of management's time to, transactions that may not come to fruition. Additional risks inherent in acquisitions include risks that the properties will not achieve anticipated occupancy levels and that estimates of the costs of improvements to bring an acquired property up to standards established for the market position intended for that property may prove inaccurate.

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***We will face competition from third parties, including other multifamily communities, which may limit our profitability and the return for our stockholders.***

The residential multifamily industry is highly competitive. This competition could reduce occupancy levels and revenues at our multifamily properties, which would adversely affect our operations. We compete with many other entities engaged in real estate investment activities, including individuals, corporations, bank and insurance company investment accounts, other REITs, real estate limited partnerships, and other entities engaged in real estate investment activities. Many of these entities have significant financial and other resources, including operating experience, allowing them to compete effectively with us. Competitors with substantially greater financial resources than us may be able to accept more risk than we can effectively manage. In addition, those competitors that are not REITs may be at an advantage to the extent they can utilize working capital to finance projects, while we (and our competitors that are REITs) will be required by the annual distribution provisions under the Code to distribute significant amounts of cash from operations to our stockholders. Our competitors include those in other apartment communities both in the immediate vicinity where our multifamily properties will be located and the broader geographic market. Such competition may also result in overbuilding of multifamily communities, causing an increase in the number of apartment units available and potentially decreasing our occupancy and apartment rental rates. We may also be required to expend substantial sums to attract new residents. The resale value of the property could be diminished because the market value of a particular property will depend principally upon the value of the leases of such property. In addition, increases in operating costs due to inflation may not be offset by increased apartment rental rates. Further, costs associated with real estate investment, such as real estate taxes and maintenance costs, generally are not reduced when circumstances cause a reduction in income from the investment. These events would cause a significant decrease in revenues and could cause us to reduce the amount of distributions to our stockholders.

***The large quantity of foreclosed homes and low residential mortgage rates may result in potential renters purchasing residences rather than leasing them, and as a result, cause a decline in occupancy rates.***

The large quantity of foreclosed homes, along with the low residential mortgage interest rates currently available and government sponsored programs to promote home ownership, has resulted in a record high level on the National Association of Realtors Housing Affordability Index, an index used to measure whether or not a typical family could qualify for a mortgage loan on a typical home. The foregoing factors may encourage potential renters to purchase residences rather than lease them, thereby causing a decline in the occupancy rates of our properties.

***Failure to succeed in new markets or in new property classes may have adverse consequences on our performance.***

We may make acquisitions outside of our existing market areas or the property classes of our primary focus if appropriate opportunities arise. Our sponsor's, advisor's or any of our affiliates' historical experience in their existing markets in owning and operating certain classes of property does not ensure that we will be able to operate successfully in new markets, should we choose to enter them, or that we will be successful in new property classes. We may be exposed to a variety of risks if we choose to enter new markets, including an inability to accurately evaluate local market conditions, to identify appropriate acquisition opportunities, to hire and retain key personnel, and a lack of familiarity with local governmental and permitting procedures. In addition, we may abandon opportunities to enter new markets or acquire new classes of property that we have begun to explore for any reason and may, as a result, fail to recover expenses already incurred.

***Acquiring or attempting to acquire multiple properties in a single transaction may adversely affect our operations.***

We are likely to acquire multiple properties in a single transaction. Such portfolio acquisitions are more complex and expensive than single-property acquisitions, and the risk that a multiple-property acquisition does not close may be greater than in a single-property acquisition. Portfolio acquisitions may also result in us owning investments in geographically dispersed markets, placing additional demands on our ability to manage the properties in the portfolio. In addition, a seller may require that a group of properties be purchased as a package even though we may not want to purchase one or more properties in the portfolio. In these situations, if we are unable to identify another person or entity to acquire the unwanted properties, we may be required to operate, or attempt to dispose of, these properties. To acquire multiple properties in a single transaction we may be required to accumulate a large amount of cash. We expect the returns that we can earn on such cash to be less than the ultimate returns on real property, and therefore, accumulating such cash could reduce the funds available for distributions. Any of the foregoing events may have an adverse effect on our operations.

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***If we sell properties by providing financing to purchasers, we will bear the risk of default by the purchaser.***

If we decide to sell any of our properties, we intend to use our commercially reasonable efforts to sell them for cash. However, in some instances we may sell our properties by providing financing to purchasers. If we provide financing to purchasers, we will bear the risk of default by the purchaser and will be subject to remedies provided by law, which could negatively impact distributions to our stockholders. There are no limitations or restrictions on our ability to take such purchase money obligations. We may, therefore, take a purchase money obligation secured by a mortgage as full or partial payment for the purchase price of a property. The terms of payment to us generally will be affected by custom in the area where the property being sold is located and the then-prevailing economic conditions. If we receive promissory notes or other property in lieu of cash from property sales, the distribution of the proceeds of sales to our stockholders, or their reinvestment in other assets, will be delayed until the promissory notes or other property are actually paid, sold or refinanced or we have otherwise disposed of such promissory notes or other property. In some cases, we may receive initial down payments in cash and other property in the year of sale in an amount less than the selling price and subsequent payments will be spread over a number of years. If any purchaser defaults under a financing arrangement with us, it could negatively impact our ability to make distributions to our stockholders.

***Our revenue and net income may vary significantly from one period to another due to investments in opportunity-oriented properties and portfolio acquisitions, which could increase the variability of our cash available for distributions.***

We may make investments in opportunity-oriented properties in various phases of development, redevelopment or repositioning and portfolio acquisitions, which may cause our revenues and net income to fluctuate significantly from one period to another. Projects do not produce revenue while in development or redevelopment. During any period when our projects in development or redevelopment or those with significant capital requirements increase without a corresponding increase in stable revenue-producing properties, our revenues and net income will likely decrease. Many factors may have a negative impact on the level of revenues or net income produced by our portfolio of investments, including higher than expected construction costs, failure to complete projects on a timely basis, failure of the properties to perform at expected levels upon completion of development or redevelopment, and increased borrowings necessary to fund higher than expected construction or other costs related to the project. Further, our net income and stockholders' equity could be negatively affected during periods with large portfolio acquisitions, which generally require large cash outlays and may require the incurrence of additional financing. Any such reduction in our revenues and net income during such periods could cause a resulting decrease in our cash available for distributions during the same periods.

***We may have difficulty selling real estate investments, and our ability to distribute all or a portion of the net proceeds from such sale to our stockholders may be limited.***

Real estate investments are relatively illiquid, and as a result, we will have a limited ability to vary our portfolio in response to changes in economic or other conditions. We will also have a limited ability to sell assets in order to fund working capital and similar capital needs. When we sell any of our properties, we may not realize a gain on such sale. We may elect not to distribute any proceeds from the sale of properties to our stockholders; for example, we may use such proceeds to:

purchase additional properties;

repay debt, if any;

buy out interests of any co-venturers or other partners in any joint venture in which we are a party;

create working capital reserves; or

make repairs, maintenance, tenant improvements or other capital improvements or expenditures to our remaining properties.

Our ability to sell our properties may also be limited by our need to avoid a 100% penalty tax that is imposed on gain recognized by a REIT from the sale of property characterized as dealer property. In order to ensure that we avoid such characterization, we may be required to hold our properties for a minimum period of time and comply with certain other requirements in the Code.



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*We may acquire properties with lock-out provisions, or agree to such provisions in connection with obtaining financing, which may prohibit us from selling a property, or may require us to maintain specified debt levels for a period of years on some properties.*

We may acquire properties in exchange for operating partnership units and agree to restrictions on sales or refinancing, called lock-out provisions, that are intended to preserve favorable tax treatment for the owners of such properties who sell them to us. Additionally, we may agree to lock-out provisions in connection with obtaining financing for the acquisition of properties. Lock-out provisions could materially restrict us from selling, otherwise disposing of or refinancing properties. This would affect our ability to turn our investments into cash and thus affect cash available to return capital to our stockholders. Lock-out provisions could impair our ability to take actions during the lock-out period that would otherwise be in the best interests of our stockholders, and therefore, might have an adverse impact on the value of the shares, relative to the value that would result if the lock-out provisions did not exist. In particular, lock-out provisions could preclude us from participating in major transactions that could result in a disposition of our assets or a change in control even though that disposition or change in control might be in the best interests of our stockholders.

*Actions of our joint venture partners could subject us to liabilities in excess of those contemplated or prevent us from taking actions which are in the best interests of our stockholders, which could result in lower investment returns to our stockholders.*

We may enter into joint ventures with affiliates and other third parties to acquire or improve properties. We may also purchase properties in partnerships, co-tenancies or other co-ownership arrangements. Such investments may involve risks not otherwise present when acquiring real estate directly, including, for example:

joint venturers may share certain approval rights over major decisions;

a co-venturer, co-owner or partner may at any time have economic or business interests or goals which are or which become inconsistent with our business interests or goals, including inconsistent goals relating to the sale of properties held in the joint venture or the timing of termination or liquidation of the joint venture;

the possibility that our co-venturer, co-owner or partner in an investment might become insolvent or bankrupt;

the possibility that we may incur liabilities as a result of an action taken by our co-venturer, co-owner or partner;

that such co-venturer, co-owner or partner may be in a position to take action contrary to our instructions or requests or contrary to our policies or objectives, including our policy with respect to qualifying and maintaining our qualification as a REIT;

disputes between us and our joint venturers may result in litigation or arbitration that would increase our expenses and prevent our officers and directors from focusing their time and effort on our business and result in subjecting the properties owned by the applicable joint venture to additional risk; or

that under certain joint venture arrangements, neither venture partner may have the power to control the venture, and an impasse could be reached which might have a negative influence on the joint venture.

These events might subject us to liabilities in excess of those contemplated and thus reduce the return on an investment in our shares. If we have a right of first refusal or buy/sell right to buy out a co-venturer, co-owner or partner, we may be unable to finance such a buy-out if it becomes exercisable or we may be required to purchase such interest at a time when it would not otherwise be in our best interest to do so. If our interest is subject to a buy/sell right, we may not have sufficient cash, available borrowing capacity or other capital resources to allow us to elect to purchase an interest of a co-venturer subject to the buy/sell right, in which case we may be forced to sell our interest as the result of the exercise of such right when we would otherwise prefer to keep our interest. Finally, we may not be able to sell our interest in a joint venture if we desire to exit the venture.

**Risks Associated with Debt Financing**

*We plan to incur mortgage indebtedness and other borrowings, which may increase our business risks.*

We intend to acquire properties subject to existing financing or by borrowing new funds. In addition, we intend to incur or increase our mortgage debt by obtaining loans secured by selected, or all of our, real properties to obtain funds to acquire additional real properties and/or make capital improvements to properties. We may also borrow funds, if necessary, to satisfy the requirement that we generally distribute to stockholders as dividends at least 90% of our annual REIT taxable income (excluding net capital gain), or otherwise as is necessary or advisable to assure that we maintain our qualification as a REIT for U.S. federal income tax purposes.

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We intend to incur mortgage debt on a particular property if we believe the property's projected cash flow is sufficient to service the mortgage debt. However, if there is a shortfall in cash flow requiring us to use cash from other sources to make the mortgage payments on the property, then the amount available for distributions to stockholders may be affected. In addition, incurring mortgage debt increases the risk of loss since defaults on indebtedness secured by properties may result in foreclosure actions initiated by lenders and our loss of the property securing the loan which is in default. For tax purposes, a foreclosure of any of our properties would be treated as a sale of the property for a purchase price equal to the outstanding balance of the debt secured by the mortgage. If the outstanding balance of the debt secured by the mortgage exceeds our tax basis in the property, we would recognize taxable income on foreclosure, but would not receive any cash proceeds. We may, in some circumstances, give a guaranty on behalf of an entity that owns one or more of our properties. In these cases, we will be responsible to the lender for satisfaction of the debt if it is not paid by such entity. If any mortgages contain cross-collateralization or cross-default provisions, there is a risk that more than one real property may be affected by a default.

Any mortgage debt which we place on properties may contain clauses providing for prepayment penalties. If a lender invokes these penalties upon the sale of a property or the prepayment of a mortgage on a property, the cost to us to sell the property could increase substantially, and may even be prohibitive. This could lead to a reduction in our income, which would reduce cash available for distribution to stockholders and may prevent us from borrowing more money.

We may also finance our property acquisitions using interest-only mortgage indebtedness. During the interest-only period, the amount of each scheduled payment will be less than that of a traditional amortizing mortgage loan. The principal balance of the mortgage loan will not be reduced (except in the case of prepayments) because there are no scheduled monthly payments of principal during this period. After the interest-only period, we will be required either to make scheduled payments of amortized principal and interest or to make a lump-sum or balloon payment at maturity. These required principal or balloon payments will increase the amount of our scheduled payments and may increase our risk of default under the related mortgage loan. If the mortgage loan has an adjustable interest rate, the amount of our scheduled payments also may increase at a time of rising interest rates. Increased payments and substantial principal or balloon maturity payments will reduce the funds available for distribution to our stockholders because cash otherwise available for distribution will be required to pay principal and interest associated with these mortgage loans.

There is no limitation on the amount we may invest in any single property or other asset or, subject to the limitations in our charter, on the amount we can borrow for the purchase of any individual property or other investment. Under our charter, the maximum amount of our secured and unsecured borrowings in relation to net assets cannot exceed 300% of net assets (the equivalent of 75% of the cost of our net assets) on the date of any borrowing in the absence of a satisfactory showing that a higher level of borrowing is appropriate, approval by a majority of independent directors and disclosure to our stockholders. Net assets means our total assets, other than intangibles, at cost before deducting depreciation, reserves for bad debts or other non-cash reserves less our total liabilities, calculated at least quarterly on a basis consistently applied. This restriction does not, however, apply to individual properties, and therefore, does not limit our ability to borrow more than 75% of the contract purchase price for any individual property.

***If mortgage debt is unavailable at reasonable rates, we may not be able to finance the properties, which could reduce the number of properties we can acquire and the amount of cash distributions we can make.***

When we place mortgage debt on properties, we run the risk of being unable to refinance the properties when the loans come due, or of being unable to refinance on favorable terms. If interest rates are higher when the properties are refinanced, we may not be able to finance the properties at reasonable rates and our income could be reduced. If this occurs, it would reduce cash available for distribution to our stockholders, and it may prevent us from borrowing more money.

***Our ability to obtain financing on reasonable terms could be impacted by negative capital market conditions.***

Recently, domestic financial markets have experienced unusual volatility, uncertainty and a tightening of liquidity in both the investment grade debt and equity capital markets. The commercial real estate debt markets have also experienced volatility as a result of certain factors including the tightening of underwriting standards by lenders and credit rating agencies and the restricted Collateralized Mortgage Backed Securities market. Credit spreads for major sources of capital widened significantly as investors have demanded a higher risk premium. This resulted in lenders increasing the cost for debt financing. Should the overall cost of borrowings increase again as it did in recent years, either by increases in the index rates or by increases in lender spreads, we would need to factor such increases into the economics of our acquisitions. This may result in our acquisitions generating lower overall economic returns and potentially reducing cash flow available for distribution.

The recent dislocations in the debt markets have reduced the amount of capital that was available to finance real estate, which, in turn, (a) prevented real estate investors from relying on capitalization rate compression to generate returns and (b) slowed real estate transaction activity. If these or similar dislocations in the debt market were renewed, they could have a material impact on revenues and income from the acquisition and operations of real properties and mortgage loans.



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Consequently, in light of the recent volatility in the credit markets, there is greater uncertainty regarding our ability to access them in order to attract financing on reasonable terms. Investment returns on our assets and our ability to make acquisitions could be adversely affected by our inability to secure financing on reasonable terms, if at all.

### ***The return on an investment in our shares may be reduced if we are required to register as an investment company under the Investment Company Act.***

We are not registered, and do not intend to register our company or any of our subsidiaries, as an investment company under the Investment Company Act. If we become obligated to register the company or any of our subsidiaries as an investment company, the registered entity would have to comply with a variety of substantive requirements under the Investment Company Act imposing, among other things, limitations on capital structure, restrictions on specified investments, prohibitions on transactions with affiliates and compliance with reporting, record keeping, voting, proxy disclosure and other rules and regulations that would significantly change our operations.

We intend to conduct our operations, directly and through wholly or majority-owned subsidiaries, so that we and each of our subsidiaries are exempt from registration as an investment company under the Investment Company Act. Under Section 3(a)(1)(A) of the Investment Company Act, a company is deemed to be an investment company if it is, or holds itself out as being, engaged primarily, or proposes to engage primarily, in the business of investing, reinvesting or trading in securities. Under Section 3(a)(1)(C) of the Investment Company Act, a company is deemed to be an investment company if it is engaged, or proposes to engage, in the business of investing, reinvesting, owning, holding or trading in securities and owns or proposes to acquire investment securities having a value exceeding 40% of the value of its total assets (exclusive of U.S. government securities and cash items) on an unconsolidated basis. We believe that our company and most, if not all, of our wholly and majority-owned subsidiaries will not be considered investment companies under either Section 3(a)(1)(A) or Section 3(a)(1)(C) of the Investment Company Act.

Additionally, Rule 3a-1 under the Investment Company Act generally provides that an issuer will not be deemed to be an investment company under the Investment Company Act provided that (1) it does not hold itself out as being engaged primarily, or propose to engage primarily, in the business of investing, reinvesting or trading in securities, and (2) on an unconsolidated basis except as otherwise provided no more than 45% of the value of its total assets, consolidated with the assets of any wholly owned subsidiary (exclusive of government securities and cash items), consists of, and no more than 45% of its net income after taxes, consolidated with the net income of any wholly owned subsidiary (for the last four fiscal quarters combined), is derived from, securities other than government securities, securities issued by employees securities companies, securities issued by certain majority owned subsidiaries of such company and securities issued by certain companies that are controlled primarily by such company. We believe that we, our operating partnership and the subsidiaries of our operating partnership will satisfy this exclusion, and we will monitor our holdings to ensure continuing and ongoing compliance with Rule 3a-1.

A change in the value of any of our assets could cause us to fall within the definition of investment company and negatively affect our ability to maintain our exemption from regulation under the Investment Company Act. To avoid being required to register the company or any of its subsidiaries as an investment company under the Investment Company Act, we may be unable to sell assets we would otherwise want to sell and may need to sell assets we would otherwise wish to retain. In addition, we may have to acquire additional income- or loss-generating assets that we might not otherwise have acquired or may have to forgo opportunities to acquire interests in companies that we would otherwise want to acquire and would be important to our investment strategy.

If we were required to register our company as an investment company but failed to do so, we would be prohibited from engaging in our business, and criminal and civil actions could be brought against us. In addition, our contracts would be unenforceable unless a court required enforcement, and a court could appoint a receiver to take control of us and liquidate our business.

### ***High levels of debt or increases in interest rates could increase the amount of our loan payments, which could reduce the cash available for distribution to stockholders.***

As mentioned above, we intend to incur debt. High debt levels would cause us to incur higher interest charges, would result in higher debt service payments, and could be accompanied by restrictive covenants. Interest we pay could reduce cash available for distribution to stockholders. Additionally, if we incur variable rate debt, increases in interest rates would increase our interest costs, which would reduce our cash flow and our ability to make distributions to our stockholders. If we need to repay existing debt during periods of rising interest rates, we could be required to liquidate one or more of our investments in properties at times which may not permit realization of the maximum return on such investments and could result in a loss.



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***Lenders may require us to enter into restrictive covenants relating to our operations, which could limit our ability to make distributions to our stockholders.***

In providing financing to us, a lender may impose restrictions on us that affect our ability to incur additional debt, make certain investments, reduce liquidity below certain levels, make distributions to our stockholders and otherwise affect our distribution and operating policies. In general, we expect our loan agreements to restrict our ability to encumber or otherwise transfer our interest in the respective property without the prior consent of the lender. Such loan documents may contain other negative covenants that may limit our ability to discontinue insurance coverage, replace our advisor or impose other limitations. Any such restriction or limitation may have an adverse effect on our operations and our ability to make distributions to our stockholders. Further, such restrictions could make it difficult for us to satisfy the requirements necessary to maintain our qualification as a REIT for U.S. federal income tax purposes.

***Some of our mortgage loans may have due on sale provisions, which may impact the manner in which we acquire, sell and/or finance our properties.***

In purchasing properties subject to financing, we may obtain financing with due-on-sale and/or due-on-encumbrance clauses. Due-on-sale clauses in mortgages allow a mortgage lender to demand full repayment of the mortgage loan if the borrower sells the mortgaged property. Similarly, due-on-encumbrance clauses allow a mortgage lender to demand full repayment if the borrower uses the real estate securing the mortgage loan as security for another loan. These clauses may cause the maturity date of such mortgage loans to be accelerated and such financing to become due. In such event, we may be required to sell our properties on an all-cash basis, to acquire new financing in connection with the sale, or to provide seller financing. It is not our intent to provide seller financing, although it may be necessary or advisable for us to do so in order to facilitate the sale of a property. It is unknown whether the holders of mortgages encumbering our properties will require such acceleration or whether other mortgage financing will be available. Such factors will depend on the mortgage market and on financial and economic conditions existing at the time of such sale or refinancing.

***Lenders may be able to recover against our other properties under our mortgage loans.***

In financing our property acquisitions, we will seek to obtain secured nonrecourse loans. However, only recourse financing may be available, in which event, in addition to the property securing the loan, the lender may look to our other assets for satisfaction of the debt. Therefore, should we be unable to repay a recourse loan with the proceeds from the sale or other disposition of the property securing the loan, the lender could look to one or more of our other properties for repayment. Also, in order to facilitate the sale of a property, we may allow the buyer to purchase the property subject to an existing loan whereby we remain responsible for the debt.

***If we are required to make payments under any bad boy carve-out guaranties that we may provide in connection with certain mortgages and related loans, our business and financial results could be materially adversely affected.***

In obtaining certain nonrecourse loans, we may provide standard carve-out guaranties. These guaranties are only applicable if and when the borrower directly, or indirectly through agreement with an affiliate, joint venture partner or other third party, voluntarily files a bankruptcy or similar liquidation or reorganization action or takes other actions that are fraudulent or improper (commonly referred to as bad boy guaranties). Although we believe that bad boy carve-out guaranties are not guaranties of payment in the event of foreclosure or other actions of the foreclosing lender that are beyond the borrower's control, some lenders in the real estate industry have recently sought to make claims for payment under such guaranties. In the event such a claim were made against us under a bad boy carve-out guaranty, following foreclosure on mortgages or related loan, and such claim were successful, our business and financial results could be materially adversely affected.

***We may be subject to risks related to interest rate fluctuations, and the derivative financial instruments that we may use may be costly and ineffective and may reduce the overall returns for our stockholders.***

We may be subject to risks related to interest rate fluctuations if any of our debt is subject to a floating interest rate. To the extent that we use derivative financial instruments in connection with our floating interest rate debt, we will be exposed to credit, basis and legal enforceability risks. Derivative financial instruments may include interest rate swap contracts, interest rate cap or floor contracts, futures or forward contracts, options or repurchase agreements. In this context, credit risk is the failure of the counterparty to perform under the terms of the derivative contract. If the fair value of a derivative contract is positive, the counterparty owes us, which creates credit risk for us. Basis risk occurs when the index upon which the contract is based is more or less variable than the index upon which the hedged asset or liability is based, thereby making the hedge less effective. Finally, legal enforceability risks encompass general contractual risks, including the risk that the counterparty will breach the terms of, or fail to perform its obligations under, the derivative contract. If we are unable to manage these risks effectively, our results of operations, financial condition and ability to make distributions to stockholders will be adversely affected.



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### ***Complying with REIT requirements may limit our ability to hedge risk effectively.***

The REIT provisions of the Code may limit our ability to hedge the risks inherent to our operations. As mentioned above, from time to time, we may enter into hedging transactions with respect to one or more of our assets or liabilities. Any income or gain derived by us from transactions that hedge certain risks, such as the risk of changes in interest rates, will not be treated as gross income for purposes of either the 75% or the 95% gross income tests, which are separate tests based on the composition of our gross income that we must satisfy to qualify as a REIT, unless specific requirements are met. Such requirements include that the hedging transaction be properly identified within prescribed time periods and that the transaction either (i) hedges risks associated with indebtedness issued by us that is incurred to acquire or carry real estate assets or (ii) manages the risks of currency fluctuations with respect to income or gain that qualifies under the 75% or 95% gross income tests (or assets that generate such income). To the extent that we do not properly identify such transactions as hedges, hedge with other types of financial instruments, or hedge other types of indebtedness, the income from those transactions is not likely to be treated as qualifying income for purposes of the 75% and 95% gross income tests. As a result of these rules, we may have to limit the use of hedging techniques that might otherwise be advantageous, which could result in greater risks associated with interest rate or other changes than we would otherwise incur.

### **Compliance with Laws**

#### ***The costs of compliance with environmental laws and other governmental laws and regulations may adversely affect our income and the cash available for any distributions.***

All real property and the operations conducted on real property are subject to federal, state and local laws and regulations relating to environmental protection and human health and safety. Examples of Federal laws include: National Environmental Policy Act, the Comprehensive Environmental Response, Compensation, and Liability Act, the Solid Waste Disposal Act as amended by the Resource Conservation and Recovery Act, the Federal Water Pollution Control Act, the Federal Clean Air Act, the Toxic Substances Control Act, the Emergency Planning and Community Right to Know Act and the Hazard Communication Act. These laws and regulations generally govern wastewater discharges, air emissions, the operation and removal of underground and above-ground storage tanks, the use, storage, treatment, transportation and disposal of solid and hazardous materials, and the remediation of contamination associated with disposals. Some of these laws and regulations may impose joint and several liability on residents, owners or operators for the costs of investigation or remediation of contaminated properties, regardless of fault or the legality of the original disposal. In addition, the presence of these substances, or the failure to properly remediate these substances, may adversely affect our ability to sell or rent the property or to use the property as collateral for future borrowing.

There may also be potential liability associated with lead-based paint arising from lawsuits alleging personal injury and related claims. The existence of lead paint is especially a concern in residential units. A structure built prior to 1978 may contain lead-based paint and may present a potential for exposure to lead; however, structures built after 1978 are not likely to contain lead-based paint.

Properties' values may also be affected by their proximity to electric transmission lines. Electric transmission lines are one of many sources of electro-magnetic fields, or EMFs, to which people may be exposed. Research completed regarding potential health concerns associated with exposure to EMFs has produced inconclusive results. Notwithstanding the lack of conclusive scientific evidence, some states now regulate the strength of electric and magnetic fields emanating from electric transmission lines, and other states have required transmission facilities to measure for levels of EMFs. On occasion, lawsuits have been filed (primarily against electric utilities) that allege personal injuries from exposure to transmission lines and EMFs, as well as from fear of adverse health effects due to such exposure. This fear of adverse health effects from transmission lines has been considered both when property values have been determined to obtain financing and in condemnation proceedings. We may not, in certain circumstances, search for electric transmission lines near our properties, but are aware of the potential exposure to damage claims by persons exposed to EMFs.

Recently, indoor air quality issues, including mold, have been highlighted in the media and the industry is seeing mold claims from lessees rising. Due to such recent increase in mold claims and given that the law relating to mold is unsettled and subject to change, we could incur losses from claims relating to the presence of, or exposure to, mold or other microbial organisms, particularly if we are unable to maintain adequate insurance to cover such losses. We may also incur unexpected expenses relating to the abatement of mold on properties that we may acquire.

Limited quantities of asbestos-containing materials are present in various building materials such as floor coverings, ceiling texture material, acoustical tiles and decorative treatment. Environmental laws govern the presence, maintenance and removal of asbestos. These laws could be used to impose liability for release of, and exposure to, hazardous substances, including asbestos-containing materials, into the air. Such laws require that owners or operators of buildings containing asbestos (i) properly manage and maintain the asbestos, (ii) notify and train those who may come into contact with asbestos and (iii) undertake special precautions, including removal or other abatement, if asbestos would be disturbed during renovation or demolition of a building. These laws may allow third parties to seek recovery from owners or operators of real

properties for personal injury associated with exposure to asbestos fibers. As the owner of our properties, we may be liable for any such costs.

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Compliance with new or more stringent laws or regulations or stricter interpretation of existing laws may require material expenditures by us. We cannot assure stockholders that future laws, ordinances or regulations will not impose any material environmental liability, or that the current environmental condition of our properties will not be affected by the operations of residents, existing conditions of the land, operations in the vicinity of the properties, or the activities of unrelated third parties. In addition, there are various local, state and federal fire, health, life-safety and similar regulations that we may be required to comply with. Failure to comply with applicable laws and regulations could result in fines and/or damages, suspension of personnel of our advisor and/or other sanctions.

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

Under various federal, state and local environmental laws, ordinances and regulations, a current or previous owner or operator of real property may be liable for the cost of removal or remediation of hazardous or toxic substances on, under or in such property. The costs of removal or remediation could be substantial. These laws often impose liability whether or not the owner or operator knew of, or was responsible for, the presence of the hazardous or toxic substances.

Environmental laws also may impose restrictions on the manner in which property may be used or businesses may be operated, and these restrictions may require substantial expenditures. Environmental laws provide for sanctions in the event of noncompliance and may be enforced by governmental agencies or, in certain circumstances, by private parties. Certain environmental laws and common law principles govern the presence, maintenance, removal and disposal of certain building materials, including asbestos and lead-based paint (which are both discussed above).

The cost of defending against such claims of liability, of compliance with environmental regulatory requirements, of remediating any contaminated property, or of paying personal injury claims could materially adversely affect our business, assets or results of operations and, consequently, amounts available for distribution to stockholders.

We cannot assure stockholders that properties which we acquire will not have any material environmental conditions, liabilities or compliance concerns. Accordingly, we have no way of determining at this time the magnitude of any potential liability to which we may be subject arising out of environmental conditions or violations with respect to the properties we own.

### ***Our costs associated with and the risk of failing to comply with the Americans with Disabilities Act may affect cash available for distributions.***

Our properties are generally expected to be subject to the Americans with Disabilities Act of 1990, as amended, or the Disabilities Act. Under the Disabilities Act, all places of public accommodation are required to comply with federal requirements related to access and use by disabled persons. The Disabilities Act has separate compliance requirements for public accommodations and commercial facilities that generally require that buildings and services be made accessible and available to people with disabilities. The Disabilities Act's requirements could require removal of access barriers and could result in the imposition of injunctive relief, monetary penalties or, in some cases, an award of damages. We will attempt to acquire properties that comply with the Disabilities Act or place the burden on the seller or a third party to ensure compliance with such laws. However, we cannot assure stockholders that we will be able to acquire properties or allocate responsibilities in this manner. If we cannot, our funds used for compliance with these laws may affect cash available for distributions and the amount of distributions to stockholders.

The multifamily properties we acquire must comply with Title III of the Disabilities Act, to the extent that such properties are public accommodations and/or commercial facilities as defined by the Disabilities Act. Compliance with the Disabilities Act could require removal of structural barriers to handicapped access in certain public areas of our multifamily properties where such removal is readily achievable. The Disabilities Act does not, however, consider residential properties, such as multifamily properties to be public accommodations or commercial facilities, except to the extent portions of such facilities, such as the leasing office, are open to the public.

### ***We must comply with the Fair Housing Amendments Act of 1988, or the FHAA, and failure to comply may affect cash available for distributions.***

We must comply with the FHAA, which requires that apartment communities first occupied after March 13, 1991 be accessible to handicapped residents and visitors. Compliance with the FHAA could require removal of structural barriers to handicapped access in a community, including the interiors of apartment units covered under the FHAA. Recently there has been heightened scrutiny of multifamily housing communities for compliance with the requirements of the FHAA and Disabilities Act and an increasing number of substantial enforcement actions and private lawsuits have been brought against apartment communities to ensure compliance with these requirements. Noncompliance with the FHAA could result in the imposition of fines, awards of damages to private litigants, payment of attorneys' fees and other costs to plaintiffs, substantial

litigation costs and substantial costs of remediation.

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### **United States Federal Income Tax Risks**

*If we fail to continue to qualify as a REIT, we will be subjected to tax on our income, and the amount of distributions we make to our stockholders will be less.*

We intend to continue to qualify as a REIT under the Code. A REIT generally is not taxed at the corporate level on income and gains that it distributes to its stockholders on a timely basis. Although we do not intend to request a ruling from the Internal Revenue Service, or the IRS, as to our REIT status, we have received the opinion of our tax counsel, Alston & Bird LLP, with respect to our qualification as a REIT. Investors should be aware, however, that opinions of counsel are not binding on the IRS or on any court. The opinion of Alston & Bird LLP represents only the view of our counsel based on our counsel's review and analysis of existing law and on certain representations as to factual matters and covenants made by us, including representations relating to the values of our assets and the sources of our income and representations related to our future conduct. Alston & Bird LLP has no obligation to advise us or the holders of our common stock of any subsequent change in the matters stated, represented or assumed in its opinion or of any subsequent change in applicable law. Qualification as a REIT involves the application of highly technical and complex rules for which there are only limited judicial or administrative interpretations. The determination of various factual matters and circumstances not entirely within our control may affect our ability to continue to qualify as a REIT. In addition, new legislation, regulations, administrative interpretations or court decisions could significantly change the tax laws with respect to qualification as a REIT or the U.S. federal income tax consequences of such qualification, including changes with retroactive effect.

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

we would not be allowed to deduct our distributions to our stockholders when computing our taxable income;

we would be subject to U.S. federal income tax (including any applicable alternative minimum tax) on our taxable income at regular corporate rates;

we could be disqualified from being taxed as a REIT for the four taxable years following the year during which qualification was lost, unless entitled to relief under certain statutory provisions;

we would have less cash to make distributions to our stockholders; and

we might be required to borrow additional funds or sell some of our assets in order to pay corporate tax obligations we may incur as a result of our disqualification.

Although we intend to operate in a manner intended to qualify as a REIT, it is possible that future economic, market, legal, tax or other considerations may cause our board of directors to determine to delay or revoke our REIT election. Even if we qualify as a REIT, we expect to incur some taxes, such as state and local taxes, taxes imposed on certain subsidiaries and potential U.S. federal excise taxes.

*To continue to qualify as a REIT we must meet annual distribution requirements, which may result in us distributing amounts that may otherwise be used for our operations.*

To obtain the favorable tax treatment accorded to REITs, we generally are required each year to distribute to our stockholders at least 90% of our REIT taxable income (excluding net capital gain), determined without regard to the deduction for distributions paid. We are subject to U.S. federal income tax on our undistributed taxable income and net capital gain and to a 4% nondeductible excise tax on any amount by which distributions we pay with respect to any calendar year are less than the sum of (i) 85% of our ordinary income, (ii) 95% of our capital gain net income and (iii) 100% of our undistributed income from prior years. These requirements could cause us to distribute amounts that otherwise would be spent on investments in real estate assets, and it is possible that we might be required to borrow funds, possibly at unfavorable rates, or sell assets to fund these distributions. Although we intend to make distributions sufficient to meet the annual distribution requirements and to avoid U.S. federal income and excise taxes on our earnings, it is possible that we might not always be able to do so.

*Complying with REIT requirements may cause us to forgo otherwise attractive opportunities.*

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To continue to qualify as a REIT, we must continually satisfy various tests regarding sources of income, nature and diversification of assets, amounts distributed to shareholders and the ownership of common shares. In order to satisfy these tests, we may be required to forgo investments that might otherwise be made. Accordingly, compliance with the REIT requirements may hinder our investment performance.

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In particular, at least 75% of our total assets at the end of each calendar quarter must consist of real estate assets, government securities, and cash or cash items. For this purpose, real estate assets generally include interests in real property, such as land, buildings, leasehold interests in real property, stock of other entities that qualify as REITs, interests in mortgage loans secured by real property, investments in stock or debt instruments during the one-year period following the receipt of new capital and regular or residual interests in a real estate mortgage investment conduit, or REMIC. In addition, the amount of securities of a single issuer that we hold must generally not exceed either 5% of the value of such issuer's gross assets or 10% of the vote or value of such issuer's outstanding securities.

A REIT's net income from prohibited transactions is subject to a 100% penalty tax. In general, prohibited transactions are sales or other dispositions of property, other than foreclosure property, but including any mortgage loans, held in inventory or primarily for sale to customers in the ordinary course of business. The prohibited transaction tax may apply to any sale of assets to a securitization and to any sale of securitization securities, and therefore may limit our ability to sell assets to or equity in securitizations and other assets.

It may be possible to reduce the impact of the prohibited transaction tax and the holding of assets not qualifying as real estate assets for purposes of the REIT asset tests by conducting certain activities, holding non-qualifying REIT assets or engaging in securitization transactions through our TRSs, subject to certain limitations as described below. To the extent that we engage in such activities through TRSs, the income associated with such activities may be subject to full U.S. federal corporate income tax.

***Stockholders may have current tax liability on distributions that they elect to reinvest in shares of our common stock.***

If stockholders participate in our distribution reinvestment program, they will be deemed to have received a cash distribution equal to the fair market value of the stock received pursuant to the program. For U.S. federal income tax purposes, stockholders will be taxed on this amount in the same manner as if they have received cash. Further, to the extent that we have current or accumulated earnings and profits (as determined for U.S. federal income tax purposes), they will have ordinary taxable income except to the extent, if any, we have designated such amount as a capital gain dividend. To the extent that we make a distribution in excess of such earnings and profits, the distribution will be treated first as a tax-free return of capital, which will reduce the tax basis in their stock, and the amount of the distribution in excess of such basis will be taxable as a gain realized from the sale of their common stock. As a result, unless the stockholder is a tax-exempt entity, it may have to use funds from other sources to pay its tax liability on the value of the common stock received.

***Certain of our business activities are potentially subject to the prohibited transaction tax, which could reduce the return for stockholders.***

Our ability to dispose of property during the first few years following acquisition is restricted to a substantial extent as a result of our REIT status. Under applicable provisions of the Code regarding prohibited transactions by REITs, we will be subject to a 100% tax on any gain recognized on the sale or other disposition of any property (other than foreclosure property) that we own, directly or through any subsidiary entity, including our operating partnership, but excluding our taxable REIT subsidiaries, that is deemed to be inventory or property held primarily for sale to customers in the ordinary course of trade or business. Whether property is inventory or otherwise held primarily for sale to customers in the ordinary course of a trade or business depends on the particular facts and circumstances surrounding each property. No assurance can be given that any particular property we own, directly or through any subsidiary entity, including our operating partnership, but excluding our taxable REIT subsidiaries, will not be treated as inventory or property held primarily for sale to customers in the ordinary course of a trade or business.

***The use of taxable REIT subsidiaries would increase our overall tax liability.***

Some of our assets may need to be owned or sold, or some of our operations may need to be conducted, by taxable REIT subsidiaries. Any of our taxable REIT subsidiaries will be subject to U.S. federal and state income tax on their taxable income. The after-tax net income of our taxable REIT subsidiaries would be available for distribution to us. Further, we will incur a 100% excise tax on transactions with our taxable REIT subsidiaries that are not conducted on an arm's length basis. For example, to the extent that the rent paid by one of our taxable REIT subsidiaries exceeds an arm's length rental amount, such amount is potentially subject to the excise tax. We intend that all transactions between us and our taxable REIT subsidiaries will be conducted on an arm's length basis, and therefore, any amounts paid by our taxable REIT subsidiaries to us will not be subject to the excise tax; provided, however, no assurance can be given that no excise tax would arise from such transactions.

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***Legislative or regulatory action could adversely affect the returns to our investors.***

In recent years, numerous legislative, judicial and administrative changes have been made in the provisions of U.S. federal income tax laws applicable to investments similar to an investment in shares of our common stock. Additional changes to the tax laws are likely to continue to occur, and we cannot assure stockholders that any such changes will not adversely affect the taxation of a stockholder. Any such changes could have an adverse effect on an investment in our shares or on the market value or the resale potential of our assets. Stockholders are urged to consult with their own tax adviser with respect to the impact of recent legislation on their investment in our shares and the status of legislative, regulatory or administrative developments and proposals and their potential effect on an investment in our shares. Stockholders also should note that our counsel's tax opinion was based upon existing law and Treasury Regulations, applicable as of the date of its opinion, all of which will be subject to change, either prospectively or retroactively.

Although REITs continue to receive substantially better tax treatment than entities taxed as corporations, it is possible that future legislation would result in a REIT having fewer tax advantages, and it could become more advantageous for a company that invests in real estate to elect to be taxed for U.S. federal income tax purposes as a corporation. As a result, our charter provides our board of directors with the power, under certain circumstances, to revoke or otherwise terminate our REIT election and cause us to be taxed as a corporation, without the vote of our stockholders. Our board of directors has fiduciary duties to us and our stockholders and could only cause such changes in our tax treatment if it determines in good faith that such changes are in the best interest of our stockholders.

***If the operating partnership fails to maintain its status as a partnership, its income may be subject to taxation.***

We intend to maintain the status of the operating partnership as a partnership for U.S. federal income tax purposes. However, if the IRS were to successfully challenge the status of the operating partnership as a partnership for such purposes, it would be taxable as a corporation. In such event, this would reduce the amount of distributions that the operating partnership could make to us. This would also result in our losing REIT status, and becoming subject to a corporate level tax on our own income. This would substantially reduce our cash available to pay distributions and the yield on an investment in our shares. In addition, if any of the partnerships or limited liability companies through which the operating partnership owns its properties, in whole or in part, loses its characterization as a partnership for U.S. federal income tax purposes, it would be subject to taxation as a corporation, thereby reducing distributions to the operating partnership. Such a recharacterization of an underlying property owner could also threaten our ability to maintain REIT status.

***Distributions to tax-exempt investors may be classified as unrelated business taxable income, or UBTI, and tax-exempt investors would be required to pay tax on such income and to file income tax returns.***

Neither ordinary nor capital gain distributions with respect to our common stock nor gain from the sale of stock should generally constitute UBTI to a tax-exempt investor. However, there are certain exceptions to this rule, including:

under certain circumstances, part of the income and gain recognized by certain qualified employee pension trusts with respect to our stock may be treated as UBTI if our stock is predominately held by qualified employee pension trusts, such that we are a pension-held REIT (which we do not expect to be the case);

part of the income and gain recognized by a tax exempt investor with respect to our stock would constitute UBTI if such investor incurs debt in order to acquire the common stock; and

part or all of the income or gain recognized with respect to our stock held by social clubs, voluntary employee benefit associations, supplemental unemployment benefit trusts and qualified group legal services plans which are exempt from U.S. federal income taxation under Sections 501(c)(7), (9), (17) or (20) of the Code may be treated as UBTI.

We encourage stockholders to consult their own tax advisor to determine the tax consequences applicable to them if they are a tax-exempt investor.

***Distributions to foreign investors may be treated as an ordinary income distribution to the extent that it is made out of current or accumulated earnings and profits.***

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In general, foreign investors will be subject to regular U.S. federal income tax with respect to their investment in our stock if the income derived therefrom is effectively connected with the foreign investor's conduct of a trade or business in the United States. A distribution to a foreign investor that is not attributable to gain realized by us from the sale or exchange of a U.S. real property interest within the meaning of the Foreign Investment in Real Property Tax Act of 1980, as amended, or FIRPTA, and that we do not designate as a capital gain dividend, will be treated as an ordinary income distribution to the extent that it is made out of current or accumulated earnings and profits (as determined for U.S. federal income tax purposes). Generally, any ordinary income distribution will be subject to a U.S. federal income tax equal to 30% of the gross amount of the distribution, unless this tax is reduced by the provisions of an applicable treaty.

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### ***Foreign investors may be subject to FIRPTA tax upon the sale of their shares of our stock.***

A foreign investor disposing of a U.S. real property interest, including shares of stock of a U.S. corporation whose assets consist principally of U.S. real property interests, is generally subject to FIRPTA tax, on the gain recognized on the disposition. Such FIRPTA tax does not apply, however, to the disposition of stock in a REIT if the REIT is domestically controlled. A REIT is domestically controlled if less than 50% of the REIT's stock, by value, has been owned directly or indirectly by persons who are not qualifying U.S. persons during a continuous five-year period ending on the date of disposition or, if shorter, during the entire period of the REIT's existence. While we intend to qualify as domestically controlled, we cannot assure stockholders that we will do so. If we were to fail to so qualify, gain realized by foreign investors on a sale of shares of our stock would be subject to FIRPTA tax, unless the shares of our stock were traded on an established securities market and the foreign investor did not at any time during a specified testing period directly or indirectly own more than 5% of the value of our outstanding common stock.

### ***Foreign investors may be subject to FIRPTA tax upon the payment of a capital gain dividend.***

A foreign investor also may be subject to FIRPTA tax upon the payment of any capital gain dividend by us, which dividend is attributable to gain from sales or exchanges of U.S. real property interests. Additionally, capital gain dividends paid to foreign investors, if attributable to gain from sales or exchanges of U.S. real property interests, would not be exempt from FIRPTA and would be subject to FIRPTA tax.

We encourage stockholders to consult their own tax advisor to determine the tax consequences applicable to them if they are a foreign investor.

## **Employee Benefit Plan Risks**

***If stockholders fail to meet the fiduciary and other standards under ERISA or the Code as a result of ownership of our stock, they could be subject to liability and penalties.***

Special considerations apply to the purchase of stock by employee benefit plans subject to the fiduciary rules of Title I of ERISA, including pension or profit sharing plans and entities that hold assets of such plans, or ERISA Plans, and plans and accounts that are not subject to ERISA, but are subject to the prohibited transaction rules of Section 4975 of the Code, including IRAs, Keogh Plans, and medical savings accounts (collectively, we refer to ERISA Plans and plans subject to Section 4975 of the Code as Benefit Plans). Stockholders who investing the assets of any Benefit Plan, should satisfy themselves that:

their investment is consistent with their fiduciary obligations under ERISA and the Code;

their investment is made in accordance with the documents and instruments governing the Benefit Plan, including the Benefit Plan's investment policy;

their investment satisfies the prudence and diversification requirements of Sections 404(a)(1)(B) and 404(a)(1)(C) of ERISA, if applicable, and other applicable provisions of ERISA and the Code;

their investment will not impair the liquidity of the Benefit Plan;

their investment will not produce UBTI for the Benefit Plan;

they will be able to value the assets of the plan annually in accordance with ERISA requirements and applicable provisions of the Benefit Plan; and

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their investment will not constitute a prohibited transaction under Section 406 of ERISA or Section 4975 of the Code.

Fiduciaries may be held personally liable under ERISA for losses as a result of failure to satisfy the fiduciary standards of conduct and other applicable requirements of ERISA. In addition, if an investment in our stock constitutes a prohibited transaction under ERISA or the Code, the fiduciary of the plan who authorized or directed the investment may be subject to imposition of excise taxes with respect to the amount invested and an IRA investing in the stock may lose its tax exempt status.

Plans that are not subject to ERISA or the prohibited transactions of the Code, such as government plans or church plans, may be subject to similar requirements under state law. Such plans should satisfy themselves that the investment satisfies applicable law. We have not, and will not, evaluate whether an investment in our stock is suitable for any particular plan. Rather, we will accept entities as stockholders if an entity otherwise meets the suitability standards set forth in Investor Suitability Standards.

**Table of Contents****ITEM 1B. Unresolved Staff Comments**

None.

**ITEM 2. Properties**

The below table summarizes our investments in real estate, all of which are fee simple interests in multifamily properties as of December 31, 2012 (dollars in thousands, except average effective rent):

Property Name	State	Total Cost	Accumulated Depreciation	Carrying Amount	Encumbrances	Units	Average Occupancy	Average Effective Rent (a)(b)
Crestmont Apartments	GA	\$ 16,439	\$ (1,776)	\$ 14,663	\$ (6,750)	228	93.4%	\$ 699
Cumberland Glen Apartments	GA	16,422	(1,807)	14,615	(6,900)	222	95.5	652
Copper Mill Apartments	TX	17,663	(1,927)	15,736	(7,350)	320	94.1	717
Heritage Trace Apartments	VA	13,683	(1,489)	12,194	(5,500)	200	81.5	760
Belle Creek Apartments	CO	9,725	(893)	8,832	(10,575)	162	91.4	909
Tresa at Arrowhead	AZ	35,800	(2,675)	33,125	(27,500)	360	91.1	811
Centrepoint Apartments	AZ	28,430	(1,663)	26,767	(17,600)	320	94.7	806
Runaway Bay Apartments	IN	15,403	(53)	15,350	(10,238)	192	94.3	941
<b>Total</b>		<b>\$ 153,565</b>	<b>\$ (12,283)</b>	<b>\$ 141,282</b>	<b>\$ (92,413)</b>	<b>2,004</b>	<b>92.0%</b>	<b>\$ 787</b>

(a) Based on operating performance for the year ended December 31, 2012.

(b) Average effective rent is rent per unit per month.

For additional information on our real estate portfolio, see Part I, Item I, Business Our Real Estate Portfolio.

**ITEM 3. Legal Proceedings**

We are not subject to any material pending legal proceedings.

**ITEM 4. Mine Safety Disclosures**

Not applicable.

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**PART II**

**ITEM 5. *Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities***  
**Market Information**

Our shares of common stock are not currently listed on a national securities exchange or any over-the-counter market. Subject to then existing market conditions, we expect to consider alternatives for providing liquidity to our stockholders beginning five to seven years from the completion of our offering stage. We will consider our offering stage complete when we are no longer publicly offering equity securities in a public offering, whether through our ongoing public offering or follow-on offerings. For this purpose, we do not consider a public offering of equity securities to include offerings on behalf of selling stockholders or offerings related to a distribution reinvestment program, employee benefit plan or the redemption of interests in our operating partnership. While we expect to seek a liquidity transaction in this time frame, there can be no assurance that a suitable transaction will be available or that market conditions for a transaction will be favorable during that time frame. Our board of directors has the discretion to consider a liquidity transaction at any time if it determines such event to be in our best interests. A liquidity transaction could consist of a sale of our assets, a sale or merger of the company, a listing of our shares on a national securities exchange or a similar transaction. Some types of liquidity transactions require, after approval by our board of directors, approval of our stockholders. We do not have a stated term, as we believe setting a finite date for a possible, but uncertain future liquidity transaction may result in actions that are not necessarily in the best interest or within the expectations of our stockholders. A public market for our shares may allow us to increase our size, portfolio diversity, stockholder liquidity and access to capital. There is no assurance, however, that we will list our shares or that a public market will develop if we list our shares.

If we do not begin the process of listing our shares of common stock on a national securities exchange by the end of the mentioned period, or have not otherwise completed a liquidity transaction by such date, our charter requires that our board of directors determine, at least annually, whether a liquidity transaction is in our best interest. If a majority of our board of directors, including a majority of our independent directors, determines that a liquidity transaction is not then in the best interests of our stockholders, our charter requires that a majority of our board of directors, including a majority of our independent directors, revisit the issue of liquidation at least annually. Further postponement of listing or stockholder action regarding liquidation would only be permitted if a majority of our board of directors, including a majority of our independent directors, again determined that liquidation would not be in the best interest of our stockholders. If we sought and failed to obtain stockholder approval of our liquidation, our charter would not require us to list or liquidate, and we could continue to operate as before. If we sought and obtained stockholder approval of our liquidation, we would begin an orderly sale of our properties and other assets.

Even if we decide to liquidate, we are under no obligation to conclude our liquidation within a set time because the timing of the sale of our assets will depend on real estate and financial markets, economic conditions of the areas in which the properties are located, and U.S. federal income tax effects on stockholders that may prevail in the future. We cannot provide any assurance that we will be able to liquidate any or all of our assets. After commencing liquidation, we would continue in existence until all properties and other assets are liquidated.

In order for members of Financial Industry Regulatory Authority, Inc., or FINRA, and their associated persons to participate in our offering or any future offering of our common stock, we are required pursuant to FINRA Rule 5110 to disclose in each Annual Report distributed to our stockholders a per share estimated value of our shares of common stock, the method by which it was developed and the date of the data used to develop the estimated value. In addition, our advisor must prepare annual statements of estimated share values to assist fiduciaries of retirement plans subject to the annual reporting requirements of ERISA in the preparation of their reports relating to an investment in our common shares. For these purposes, the estimated value of the shares shall be deemed to be \$10.00 per share as of December 31, 2012. The basis for this valuation is the fact that we are currently conducting a public offering of our common stock at the price of \$10.00 per share.

**Stockholder Information**

As of March 8, 2013, there were seven holders of record of our common shares.

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To remain qualified as a REIT, we are required to distribute 90% of our annual taxable income to our stockholders. In connection with a distribution to our stockholders, our board of directors approved a monthly distribution of a certain dollar amount per share of our common stock. If we do not have sufficient funds from operations to make distributions, we may need to borrow funds, request that our advisor, in its discretion, defer its receipt of fees and reimbursements of expenses or, to the extent necessary, utilize offering proceeds in order to make cash distributions. Our stockholders may choose whether to have distributions paid in cash or to have distributions otherwise payable to them in cash invested in additional shares of our common stock pursuant to the terms and conditions of our distribution reinvestment program.

		Common Shares		Limited Partnership Units	
		Dividends Declared per Share	Annualized Rate of Return(a)	Distributions Declared per Unit	Annualized Rate of Return(a)
<b>2011</b>	First Quarter	\$	0%	\$	0%
	Second Quarter		0		0
	Third Quarter	0.15	6.0	0.15	6.0
	Fourth Quarter	0.15	6.0	0.15	6.0
<b>2012</b>	First Quarter	\$ 0.15	6.0%	\$ 0.15	6.0%
	Second Quarter	0.15	6.0	0.15	6.0
	Third Quarter	0.15	6.0	0.15	6.0
	Fourth Quarter	0.15	6.0	0.15	6.0
<b>2013</b>	First Quarter	\$ 0.15	6.0%	\$ 0.15	6.0%

(a) Based on a price per share and per unit of \$10.00.

For the year ended December 31, 2012, including amounts paid to or allocable to our non-controlling interests, we paid cash distributions of \$3.2 million, as compared to cash flows from operations of \$4.5 million and FFO of \$3.8 million. FFO is a non-GAAP financial measure. For a reconciliation of FFO to net income (loss), see Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations Non-GAAP Financial Measures.

We intend to pay comparable cash distributions in the future, but cannot guarantee that we will pay distributions at this rate or at all.

**Use of Offering Proceeds**

We sold 20,000 shares of our common stock to our advisor on April 30, 2009, for \$10.00 per share. The issuance of these shares was exempt from the registration requirements of the Securities Act pursuant to Section 4(2) of the Securities Act and Regulation D promulgated thereunder. Our advisor is an indirect, wholly owned subsidiary of our sponsor. We invested the proceeds from this sale in partnership units of our operating partnership and, as a result, hold a 0.38% interest in our operating partnership. Our advisor contributed \$2,000 to our operating partnership in exchange for 200 limited partner units in our operating partnership. On January 20, 2011, our advisor transferred all of its interests in our operating partnership to RAIT NTR Holdings, LLC, an indirect, wholly owned subsidiary of our sponsor. The holders of limited partnership units have the right to redeem these units for cash equal to the value of an equivalent number of our common shares, or, at our option, we may purchase such units for cash or by issuing an equal number of our common shares, as permitted by the limited partnership agreement of our operating partnership.

On June 10, 2011, our Registration Statement on Form S-11 (File No. 333-173391) for an offering of a maximum of 100,000,000 shares of common stock for sale to the public, which we refer to as our offering, at a price of \$10.00 per share (subject to certain discounts) in the primary portion of the offering and \$9.50 pursuant to our distribution reinvestment plan, was declared effective under the Securities Act by the SEC. As of March 8, we had issued 345,258 shares of our common stock pursuant to our offering. We have used proceeds received previously as part of the consideration used to acquire a portfolio of multifamily properties.

As of December 31, 2012, we had invested in eight multifamily properties for a total purchase price of approximately \$152 million. These acquisitions were funded from the issuance by our operating partnership of limited partnership units, cash and the incurrence of approximately \$92.4 million of mortgage indebtedness.

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From the effective date of our registration statement through December 31, 2012, we incurred actual selling commissions, dealer manager fees and organization and other offering costs in our offering in the amounts set forth below. The dealer manager reallocated all of the selling commissions and a portion of the dealer manager fee to participating broker-dealers.

Type of Expense	Amount	Percentage of Offering Proceeds
Selling commissions	\$ 17,500	0.01%
Dealer manager fees	7,500	0.00%
Other organization and other offering costs	32,500	0.01%
Total expenses related to the offering	\$ 57,500	0.02%

From the commencement of the offering through December 31, 2012, the net offering proceeds to us, after deducting the total expenses related to the offering as described above, were \$3,192,500. We have issued 63 shares pursuant to our distribution reinvestment plan through December 31, 2012. For the year ended December 31, 2012, the ratio of our costs of raising capital to the capital raised was 2%.

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We will pay our advisor 1.0% of the gross offering proceeds for organizational and offering expenses (other than dealer manager fees and selling commissions). Our advisor and its affiliates are responsible for the payment of our organization and offering expenses, other than selling commissions and the dealer manager fee, to the extent they exceed 1.0% of our gross offering proceeds. As of December 31, 2012, we had reimbursed our advisor for \$32,500 of organization and offering expenses. As of December 31, 2012, our advisor had incurred \$4.2 million of organization and offering expenses on our behalf. We also pay selling commissions and a dealer manager fee to our dealer manager as described in the prospectus. As of December 31, 2012, we paid \$0 of selling commissions and \$7,500 of dealer manager fees to our dealer manager.

**Share Repurchase Program**

We have adopted a share repurchase program that may enable stockholders to sell their shares to us in limited circumstances. During the year ended December 31, 2012, we did not repurchase any of our securities under our share repurchase program.

**ITEM 6. Selected Financial Data**

We were formed on March 26, 2009 and commenced our offering on June 10, 2011, but did not commence real estate operations until April 29, 2011 when we acquired six multifamily properties. As a result, we had no material results of operations for the period from March 26, 2009 (inception) to April 29, 2011. Subsequent to April 29, 2011, we acquired two additional multifamily properties, the Centrepoint Apartments on December 16, 2011 and the Runaway Bay Apartments on October 11, 2012. In general, we expect our results of operations to improve in future periods as a result of anticipated future acquisitions of real estate. The following table summarizes selected financial data about our company (dollars in thousands, except share and per share data). The following selected financial data information should be read in conjunction with Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations, and our consolidated financial statements, including the notes thereto, included elsewhere herein.

	2012	As of and for the Years Ended December 31 2011	2010	As of and for the period from March 26, 2009 (inception) to December 31, 2009
<b>Operating Data:</b>				
Total revenue	\$ 16,629	\$ 8,668	\$ 5	\$ 2
Total expenses	16,202	(9,038)	(1)	(1)
Net income (loss)	427	(370)	4	1
Net income (loss) allocable to common shares	(123)	(112)	4	1
Earnings (loss) per share:				
Basic	\$ (0.45)	\$ (5.60)	\$ 0.20	\$ 0.06
Diluted	\$ (0.45)	\$ (5.60)	\$ 0.20	\$ 0.06
<b>Balance Sheet Data:</b>				
Investments in real estate	\$ 141,282	\$ 128,124	\$	\$
Total assets	146,197	131,352	209	206
Total indebtedness	92,413	82,175		
Total liabilities	95,346	84,294	2	3
Total equity	50,851	47,058	207	203
<b>Other Data:</b>				
Common shares outstanding	345,063	20,000	20,000	20,000
Limited partnership units outstanding	5,274,900	5,274,900		
Cash distributions declared per common share/unit	\$ 0.60	\$ 0.30	\$	\$



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

**Overview**

We were formed on March 26, 2009 as a Maryland corporation and have elected to be taxed as a real estate investment trust, or REIT, beginning with the taxable year ended December 31, 2011. We are externally managed by our advisor, Independence Realty Advisors, LLC, an indirect, wholly owned subsidiary of our sponsor, RAIT Financial Trust (NYSE: RAS ). We own substantially all of our assets and conduct our operations through Independence Realty Operating Partnership, LP, or our operating partnership, of which we are the sole general partner. As used herein, the terms we, our and us refer to our company and, as required by context, our operating partnership and their subsidiaries.

We have invested and intend to continue to invest in a diversified portfolio of multifamily properties located throughout the United States. We target primarily core and stabilized multifamily properties that are well leased and produce predictable income. To a lesser extent we seek to acquire properties that require limited capital expenditures, have existing cash flow and offer opportunities for enhanced returns, with a primary focus on multifamily properties and a lesser focus on other asset classes.

Our investment objectives are to:

pay attractive and consistent cash distributions;

preserve invested capital; and

provide a diversified direct investment in multifamily properties.

On June 10, 2011, our Registration Statement on Form S-11 (File No. 333-173391) for an offering of a maximum of 100,000,000 shares of common stock for sale to the public at a price of \$10.00 per share (subject to certain discounts) in the primary offering and \$9.50 per share pursuant to our distribution reinvestment plan, which we refer to collectively as our offering, was initially declared effective under the Securities Act of 1933, as amended, or the Securities Act. During the quarter ended March 31, 2012, we satisfied the minimum offering amount of our offering as a result of our sale of 300,000 shares of our common stock for \$10.00 per share for total gross proceeds of \$3,000,000 to RAIT NTR Holdings, LLC, an indirect wholly owned subsidiary of our sponsor. During the year ending December 31, 2012, we sold an additional 25,000 shares of our common stock for \$10.00 per share for total proceeds of \$250,000 to unaffiliated third parties. On February 28, 2013, our board of directors approved an extension of our offering to June 10, 2014. We intend to invest the net proceeds of our ongoing public offering in a diversified portfolio of multifamily properties with strong and stable cash flows that have the potential to generate attractive distributions for our investors, with a primary focus on core and stabilized multifamily properties that are well leased and produce predictable income.

**Non-GAAP Financial Measures**

***Funds from Operations and Modified Funds from Operations***

Due to certain unique operating characteristics of real estate companies, as discussed below, the National Association of Real Estate Investment Trusts, or NAREIT, an industry trade group, has promulgated a measure known as funds from operations, or FFO, which we believe to be an appropriate supplemental measure to reflect the operating performance of a real estate investment trust, or REIT. The use of FFO is recommended by the REIT industry as a supplemental performance measure. FFO is not equivalent to our net income (loss) as determined under GAAP.

We define FFO, a non-GAAP financial measure, consistent with the standards established by the White Paper on FFO approved by the Board of Governors of NAREIT, as revised in February 2004, or the White Paper. The White Paper defines FFO as net income (loss) computed in accordance with GAAP, excluding gains or losses from sales of property and non-cash impairment charges of real estate related investments, plus real estate related depreciation and amortization, and after adjustments for unconsolidated partnerships and joint ventures. In particular, we believe it is appropriate to disregard impairment charges, as this is a fair value adjustment that is largely based on market fluctuations and assessments regarding general market conditions which can change over time. An asset will only be evaluated for impairment if certain impairment indications exist and if the carrying, or book value, exceeds the total estimated undiscounted future cash flows (including net rental and lease revenues, net proceeds on the sale of the property, and any other ancillary cash flows at a property or group level under GAAP) from such asset. Investors should note, however, that determinations of whether impairment charges have been incurred are based partly on

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anticipated operating performance, because estimated undiscounted future cash flows from a property, including estimated future net rental and lease revenues, net proceeds on the sale of the property, and certain other ancillary cash flows, are taken into account in determining whether an impairment charge has been incurred. While impairment charges are excluded from the calculation of FFO as described above, investors are cautioned that due to the fact that impairments are based on estimated future undiscounted cash flows and the relatively limited term of our operations, it could be difficult to recover any impairment charges. Our FFO calculation complies with NAREIT's policy described above.

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The historical accounting convention used for real estate assets requires straight-line depreciation of buildings and improvements, which implies that the value of real estate assets diminishes predictably over time, especially if such assets are not adequately maintained or repaired and renovated as required by relevant circumstances and/or as requested or required by lessees for operational purposes in order to maintain the value disclosed. We believe that since real estate values historically rise and fall with market conditions, including inflation, interest rates, the business cycle, unemployment and consumer spending, presentations of operating results for a REIT using historical accounting for depreciation may be less informative. Historical accounting for real estate involves the use of GAAP. Any other method of accounting for real estate such as the fair value method cannot be construed to be any more accurate or relevant than the comparable methodologies of real estate valuation found in GAAP. Nevertheless, we believe that the use of FFO, which excludes the impact of real estate related depreciation and amortization, provides a more complete understanding of our performance to investors and to management, and when compared year over year, reflects the impact on our operations from trends in occupancy rates, rental rates, operating costs, general and administrative expenses, and interest costs, which may not be immediately apparent from net income. However, FFO, and modified FFO, or MFFO, as described below, should not be construed to be more relevant or accurate than the current GAAP methodology in calculating net income or in its applicability in evaluating our operating performance. The method used to evaluate the value and performance of real estate under GAAP should be construed as a more relevant measure of operational performance and considered more prominently than the non-GAAP FFO and MFFO measures and the adjustments to GAAP in calculating FFO and MFFO.

Changes in the accounting and reporting promulgations under GAAP (for acquisition fees and expenses from a capitalization/depreciation model to an expensed-as-incurred model) that were put into effect in 2009 and other changes to GAAP accounting for real estate subsequent to the establishment of NAREIT's definition of FFO have prompted an increase in cash-settled expenses, specifically acquisition fees and expenses for all industries as items that are expensed under GAAP, that are typically accounted for as operating expenses. Under our advisory agreement with our advisor, we will not pay any acquisition fees to our advisor in connection with our purchase of properties and we will reimburse our advisor for acquisition expenses only to the extent that acquisition fees and acquisition expenses collectively do not exceed 6% of the contract price of our assets. We may have to pay acquisition fees to unaffiliated parties in connection with our purchase of properties and we expect to incur acquisition expenses. Management believes these fees and expenses do not affect our overall long-term operating performance. Publicly registered, non-listed REITs typically have a significant amount of acquisition activity and are substantially more dynamic during their initial years of investment and operation. While other start-up entities may also experience significant acquisition activity during their initial years, we believe that public, non-listed REITs, like us, are unique in that they have a limited life with targeted exit strategies within a relatively limited time frame after acquisition activity ceases. Our board of directors has the discretion to consider a liquidity transaction at any time if it determines such event to be in our best interests. However, our board of directors presently intends to consider alternatives for providing liquidity to our stockholders beginning five to seven years from the completion of our offering stage (including follow-on offerings) during which we will attempt to raise additional capital through the sale of our shares. Any liquidity event will depend on market conditions and may take any one of several forms, including a listing of our stock on a national securities exchange, a merger of our company, a sale of our entire portfolio or the sale of our individual assets. Thus, we will not continuously purchase assets and will have a limited life.

Due to the above factors and other unique features of publicly registered, non-listed REITs, the Investment Program Association, or IPA, an industry trade group, has standardized a measure known as MFFO, which the IPA has recommended as a supplemental measure for publicly registered non-listed REITs and which we believe to be another appropriate supplemental measure to reflect the operating performance of a public, non-listed REIT having the characteristics described above. MFFO is not equivalent to our net income or loss as determined under GAAP, and MFFO may not be a useful measure of the impact of long-term operating performance on value if we do not continue to operate with a limited life and targeted exit strategy, as currently intended. We believe that, because MFFO excludes costs that we consider more reflective of investing activities and other non-operating items included in FFO and also excludes acquisition fees and expenses that affect our operations only in periods in which properties are acquired, MFFO can provide, on a going forward basis, an indication of the sustainability (that is, the capacity to continue to be maintained) of our operating performance after the period in which we are acquiring our properties and once our portfolio is in place. By providing MFFO, we believe we are presenting useful information that assists investors and analysts to better assess the sustainability of our operating performance after our offering has been completed and our properties have been acquired. We also believe that MFFO is a recognized measure of sustainable operating performance by the non-listed REIT industry. Further, we believe MFFO is useful in comparing the sustainability of our operating performance after our offering and acquisitions are completed with the sustainability of the operating performance of other real estate companies that are not as involved in acquisition activities. Investors are cautioned that MFFO should only be used to assess the sustainability of our operating performance after our offering has been completed and properties have been acquired, as it excludes acquisition costs that have a negative effect on our operating performance during the periods in which properties are acquired.

We define MFFO, a non-GAAP financial measure, consistent with the IPA's Guideline 2010-01, *Supplemental Performance Measure for Publicly Registered, Non-Listed REITs: Modified Funds from Operations*, or the Practice Guideline, issued by the IPA in November 2010. The Practice Guideline defines MFFO as FFO further adjusted for the following items, as applicable, included in the determination of GAAP net income: acquisition fees and expenses; amounts relating to deferred rent receivables and amortization of above and below market leases and liabilities (which are adjusted in order to reflect such payments from a GAAP accrual basis to a



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cash basis of disclosing the rent and lease payments); accretion of discounts and amortization of premiums on debt investments; mark-to-market adjustments included in net income; nonrecurring gains or losses included in net income from the extinguishment or sale of debt, hedges, foreign exchange, derivatives or securities holdings where trading of such holdings is not a fundamental attribute of the business plan, unrealized gains or losses resulting from consolidation from, or deconsolidation to, equity accounting, and after adjustments for consolidated and unconsolidated partnerships and joint ventures, with such adjustments calculated to reflect MFFO on the same basis. The accretion of discounts and amortization of premiums on debt investments, nonrecurring unrealized gains and losses on hedges, foreign exchange, derivatives or securities holdings, unrealized gains and losses resulting from consolidations, as well as other listed cash flow adjustments are adjustments made to net income in calculating the cash flows provided by operating activities and, in some cases, reflect gains or losses which are unrealized and may not ultimately be realized. While we rely on our advisor for managing interest rate, hedge and foreign exchange risk, we do not retain an outside consultant to review all our hedging agreements. Inasmuch as interest rate hedges are not a fundamental part of our operations, we believe it is appropriate to exclude such non-recurring gains and losses in calculating MFFO, as such gains and losses are not reflective of on-going operations.

Our MFFO calculation complies with the IPA's Practice Guideline described above. In calculating MFFO, we exclude acquisition related expenses, amortization of above and below market leases, fair value adjustments of derivative financial instruments, deferred rent receivables and the adjustments of such items related to noncontrolling interests. Under GAAP, acquisition fees and expenses are characterized as operating expenses in determining operating net income. These expenses are paid in cash by us. All paid and accrued acquisition fees and expenses will have negative effects on returns to investors, the potential for future distributions, and cash flows generated by us, unless earnings from operations or net sales proceeds from the disposition of other properties are generated to cover the purchase price of the property, these fees and expenses and other costs related to such property. In the event that proceeds from our initial public offering are not available to fund our reimbursement of acquisition fees and expenses incurred by our advisor, such fees and expenses will need to be reimbursed to our advisor from other sources, including debt, operational earnings or cash flow, net proceeds from the sale of properties, or from ancillary cash flows. The acquisition of properties, and the corresponding acquisition fees and expenses, is the key operational feature of our business plan to generate operational income and cash flow to fund distributions to our stockholders. Further, under GAAP, certain contemplated non-cash fair value and other non-cash adjustments are considered operating non-cash adjustments to net income in determining cash flow from operating activities. In addition, we view fair value adjustments of derivatives and gains and losses from dispositions of assets as non-recurring items or items which are unrealized and may not ultimately be realized, and which are not reflective of on-going operations and are therefore typically adjusted for when assessing operating performance.

Our management uses MFFO and the adjustments used to calculate MFFO in order to evaluate our performance against other public, non-listed REITs which have limited lives with short and defined acquisition periods and targeted exit strategies shortly thereafter. As noted above, MFFO may not be a useful measure of the impact of long-term operating performance on value if we do not continue to operate in this manner. We believe that our use of MFFO and the adjustments used to calculate MFFO allow us to present our performance in a manner that reflects certain characteristics that are unique to public, non-listed REITs, such as their limited life, limited and defined acquisition period and targeted exit strategy, and hence that the use of such measures is useful to investors. By excluding expensed acquisition costs, the use of MFFO provides information consistent with management's analysis of the operating performance of the properties. Additionally, fair value adjustments, which are based on the impact of current market fluctuations and underlying assessments of general market conditions, but can also result from operational factors such as rental and occupancy rates, may not be directly related or attributable to our current operating performance. By excluding such changes that may reflect anticipated and unrealized gains or losses, we believe MFFO provides useful supplemental information.

Presentation of this information is intended to provide useful information to investors as they compare the operating performance to that of other public, non-listed REITs, although it should be noted that not all public, non-listed REITs calculate FFO and MFFO the same way, so comparisons with other public, non-listed REITs may not be meaningful. Furthermore, FFO and MFFO are not necessarily indicative of cash flow available to fund cash needs and should not be considered as an alternative to net income (loss) or income (loss) from continuing operations as an indication of our performance, as an alternative to cash flows from operations as an indication of our liquidity, or indicative of funds available to fund our cash needs, including our ability to make distributions to our stockholders. FFO and MFFO should be reviewed in conjunction with GAAP measurements as an indication of our performance. MFFO has limitations as a performance measure in an offering such as ours where the price of a share of common stock is a stated value and there is no regular net asset value determination during the offering stage and for a period thereafter. MFFO is useful in assisting management and investors in assessing the sustainability of operating performance in future operating periods, and in particular, after the offering and acquisition stages are complete and net asset value is disclosed. MFFO is not a useful measure in evaluating net asset value because impairments are taken into account in determining net asset value but not in determining MFFO.

Neither the SEC, NAREIT nor any other regulatory body has passed judgment on the acceptability of the adjustments that we use to calculate FFO or MFFO. In the future, the SEC, NAREIT or another regulatory body may decide to standardize the allowable adjustments across the non-listed REIT industry and in response to such standardization we may hav