

ASSOCIATED ESTATES REALTY CORP

Form 10-Q

May 04, 2004

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended March 31, 2004

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 1-12486

Associated Estates Realty Corporation

(Exact name of registrant as specified in its charter)

Ohio

(State or other jurisdiction of
incorporation or organization)

34-1747603

(I.R.S. Employer
Identification Number)

5025 Swetland Court, Richmond Hts., Ohio

(Address of principal executive offices)

44143-1467

(Zip Code)

Registrant's telephone number, including area code (216) 261-5000

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 is an accelerated filer

as identified in Rule 12B-2 of the Act. Yes No

Number of shares outstanding as of April 30, 2004: 19,630,322 shares

ASSOCIATED ESTATES REALTY CORPORATION

INDEX

PART I - FINANCIAL INFORMATION		<u>Page</u>
ITEM 1	Consolidated Financial Statements (Unaudited)	
	<u>Consolidated Balance Sheets</u> as of March 31, 2004 and December 31, 2003	3
	<u>Consolidated Statements of Operations</u> for the three month periods ended March 31, 2004 and 2003	4
	<u>Consolidated Statement of Shareholders' Equity</u> for the three month period ended March 31, 2004	5
	<u>Consolidated Statements of Cash Flows</u> for the three month periods ended March 31, 2004 and 2003	6
	<u>Notes to Consolidated Financial Statements</u>	7
ITEM 2	<u>Management's Discussion and Analysis</u> of Financial Condition and Results of Operations	17
ITEM 3	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	25
ITEM 4	<u>Controls and Procedures</u>	25
PART II - OTHER INFORMATION		
ITEM 1	<u>Legal Proceedings</u>	26
ITEM 2	<u>Changes in Securities, Use of Proceeds, and Issuer Purchase of Equity Securities</u>	26
ITEM 6	<u>Exhibits and Reports on Form 8-K</u>	26
SIGNATURES		30

Index

ASSOCIATED ESTATES REALTY CORPORATION

CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

	March 31, <u>2004</u>	December 31, <u>2003</u>
(In thousands, except share amounts)		
ASSETS		

Edgar Filing: ASSOCIATED ESTATES REALTY CORP - Form 10-Q

Real estate assets		
Land	\$ 91,365	\$ 91,367
Buildings and improvements	795,794	796,158
Furniture and fixtures	<u>32,989</u>	<u>32,919</u>
	920,148	920,444
Less: accumulated depreciation	<u>(272,065)</u>	<u>(264,386)</u>
	648,083	656,058
Construction in progress	<u>6,863</u>	<u>5,527</u>
Real estate, net	654,946	661,585
Property held for sale	211	-
Cash and cash equivalents	2,339	2,212
Restricted cash	10,387	10,889
Accounts and notes receivable, net		
Rents	571	631
Affiliates and joint ventures	6,148	5,423
Other	2,565	2,238
Investments in joint ventures, net	8,321	8,727
Goodwill	1,725	1,725
Intangible and other assets, net	<u>10,710</u>	<u>11,363</u>
	\$ 697,923	\$ 704,793
LIABILITIES AND SHAREHOLDERS' EQUITY		
Secured debt	\$ 540,775	\$ 543,391
Unsecured debt	<u>105</u>	<u>105</u>
Total indebtedness	540,880	543,496
Accounts payable and accrued expenses	22,526	24,295
Dividends payable	3,335	3,311
Resident security deposits	4,209	4,187
Funds held on behalf of managed properties		
Affiliates and joint ventures	2,631	2,189
Other	3,060	1,066
Accrued interest	2,568	2,649
Commitments and contingencies (Note 10)	=	=
Total liabilities	579,209	581,193
Operating partnership minority interest	2,172	2,172
Shareholders' equity		
Preferred shares, Class A cumulative, without par value; 3,000,000 authorized; 225,000 issued and outstanding	56,250	56,250
Common shares, without par value, \$.10 stated value; 50,000,000 authorized; 22,995,763 issued and 19,620,322 and 19,478,681 out- standing at March 31, 2004 and December 31, 2003, respectively	2,300	2,300
Paid-in capital	278,368	279,087
Accumulated distributions in excess of accumulated net income	(190,210)	(184,436)
Less: Treasury shares, at cost, 3,375,441 and 3,517,082 shares at March 31, 2004 and December 31, 2003, respectively	<u>(30,166)</u>	<u>(31,773)</u>
Total shareholders' equity	<u>116,542</u>	<u>121,428</u>
	\$ 697,923	\$ 704,793

Edgar Filing: ASSOCIATED ESTATES REALTY CORP - Form 10-Q

The accompanying notes are an integral part

of these consolidated financial statements

Index

ASSOCIATED ESTATES REALTY CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)

(In thousands, except per share amounts)	For the three months ended	
	March 31,	
	<u>2004</u>	<u>2003</u>
Revenues		
Rental	\$ 33,492	\$ 32,846
Property management fees and reimbursements	2,972	3,091
Asset management fees	240	436
Asset disposition fees	233	-
Painting services	1,874	341
Other	<u>1,125</u>	<u>982</u>
Total revenues	39,936	37,696
Expenses		
Property operating and maintenance	16,125	17,556
Depreciation and amortization	8,221	8,688
Direct property management and service companies expenses	3,292	3,263
Painting services	1,442	445
General and administrative	1,836	1,512
Interest expense	<u>10,004</u>	<u>10,029</u>
Total expenses	<u>40,920</u>	<u>41,493</u>
(Loss) income before equity in net loss of joint ventures, minority interest and income from discontinued operations	(984)	(3,797)
Equity in net loss of joint ventures	(258)	(354)
Minority interest in operating partnership	<u>(16)</u>	<u>(22)</u>
(Loss) income from continuing operations	(1,258)	(4,173)
Income from discontinued operations	<u>193</u>	<u>191</u>
Net (loss) income	(1,065)	(3,982)
Preferred share dividends	<u>(1,371)</u>	<u>(1,371)</u>
Net (loss) income applicable to common shares	\$ (2,436)	\$ (5,353)
Earnings per common share - basic:		
(Loss) income applicable to common shares from continuing operations	\$ (.14)	\$ (.29)
Income from discontinued operations	<u>.01</u>	<u>.01</u>
Net (loss) income applicable to common shares	\$ (.13)	\$ (.28)
Earnings per common share - diluted:		
(Loss) income applicable to common shares from continuing operations	\$ (.14)	\$ (.29)
Income from discontinued operations	<u>.01</u>	<u>.01</u>

Edgar Filing: ASSOCIATED ESTATES REALTY CORP - Form 10-Q

Net (loss) income applicable to common shares	\$ (.13)	\$ (.28)
Dividends declared per common share	\$.17	\$ -
Weighted average number of common shares outstanding - basic	19,446	19,382
- diluted	19,446	19,382

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

Index

ASSOCIATED ESTATES REALTY CORPORATION
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
(UNAUDITED)

	Total	Class A		Total Paid-in Capital		Accumulated	
		Preferred	Common Shares	Paid-In	Unearned	Distributions	Treasury
(In thousands, except share amounts)	Shares	Shares	(at \$.10 stated value)	Capital	Compensation	Net Income	Shares
							(at cost)
Balance, December 31, 2003	\$ 121,428	\$ 56,250	\$ 2,300	\$ 279,354	\$ (267)	\$ (184,436)	\$ (31,773)
Comprehensive (loss) income:							
Net (loss) income	(1,065)	=	=	=	=	(1,065)	=
Total comprehensive (loss) income	(1,065)	-	-	-	-	(1,065)	-
Amortization of unearned compensation	66	-	-	-	66	-	-
Forfeiture of 1,777 restricted common shares	(4)	-	-	7	9	-	(20)
Issuance of 45,870 restricted common shares							
from treasury shares	26	-	-	(140)	(352)	-	518
Purchase of 8,452 treasury shares	(71)	-	-	-	-	-	(71)
Issuance of 106,000 common shares for stock							
option exercises from treasury shares	871	-	-	(309)	-	-	1,180
Common share dividends declared	(3,338)	-	-	-	-	(3,338)	-
Preferred share dividends declared	(1,371)	=	=	=	=	(1,371)	=
Balance, March 31, 2004	\$ 116,542	\$ 56,250	\$ 2,300	\$ 278,912	\$ (544)	\$ (190,210)	\$ (30,166)

Edgar Filing: ASSOCIATED ESTATES REALTY CORP - Form 10-Q

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

Index

ASSOCIATED ESTATES REALTY CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE THREE MONTH PERIODS ENDED MARCH 31,
(UNAUDITED)

	<u>2004</u>	<u>2003</u>
(In thousands)		
Cash flow from operating activities:		
Net (loss) income	\$ (1,065)	\$ (3,982)
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Depreciation and amortization	8,231	8,693
Loss on fixed asset replacements write-off	63	64
Minority interest in operating partnership	16	22
Equity in net loss of joint ventures	258	354
Capitalized costs on investment in joint ventures	-	(35)
Earnings distributed from joint ventures	147	10
Net change in assets and liabilities:		
- Accounts and notes receivable	(266)	1,720
- Accounts and notes receivable of affiliates and joint ventures	(725)	(50)
- Accounts payable and accrued expenses	(783)	(4,063)
- Other operating assets and liabilities	515	1,301
- Restricted cash	502	968
- Funds held for non-owned managed properties	1,993	(144)
- Funds held for non-owned managed properties of affiliates and joint ventures	443	578
Total adjustments	<u>10,394</u>	<u>9,418</u>
Net cash flow provided by operations	9,329	5,436
Cash flow from investing activities:		
Recurring fixed asset additions	(1,170)	(1,558)
Investment/revenue enhancing and/or non-recurring fixed asset additions	(1,515)	(237)
Net cash flow used for investing activities	(2,685)	(1,795)
Cash flow from financing activities:		
Principal payments on secured debt	(1,616)	(1,686)
Line of credit borrowings	15,000	12,900
Line of credit repayments	(16,000)	(8,900)
Common share dividends paid	(3,314)	(3,310)
Preferred share dividends paid	(1,371)	(1,371)
Operating partnership distributions paid	(16)	(22)

Edgar Filing: ASSOCIATED ESTATES REALTY CORP - Form 10-Q

Issuance of treasury shares related to exercise of stock options	871	-
Other (purchase) issue of treasury shares - net	(71)	(65)
Net cash flow used for financing activities	(6,517)	(2,454)
Increase in cash and cash equivalents	127	1,187
Cash and cash equivalents, beginning of period	2,212	900
Cash and cash equivalents, end of period	\$ 2,339	\$ 2,087
Supplemental disclosure of cash flow information:		
Dividends declared but not paid	\$ 3,335	\$ -
Cash paid for interest (excluding capitalized interest)	9,818	9,969
Fixed asset replacement and other write-offs	1,389	505

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

Index

ASSOCIATED ESTATES REALTY CORPORATION

NOTES TO FINANCIAL STATEMENTS

UNAUDITED

1. BASIS OF PRESENTATION AND ACCOUNTING POLICIES

Business

Associated Estates Realty Corporation (the "Company") is a self-administered and self-managed equity real estate investment trust ("REIT") which specializes in multifamily property management, advisory, development, acquisition, disposition, operation and ownership activities. The Company and its affiliates receive certain property and asset management fees, acquisition, disposition and incentive fees, loan origination and consultation fees, and mortgage servicing fees. MIG II Realty Advisors, Inc. ("MIG"), a subsidiary of the Company, is a registered investment advisor and serves as a real estate advisor to pension funds. The Company owns three taxable REIT subsidiaries (previously the Company had four taxable REIT subsidiaries, however, effective December 31, 2003, the Company merged two taxable REIT subsidiaries into one) which provide management and other services for the Company and third parties. These corporations are referred to herein as "Service Companies."

As of March 31, 2004, the Company owns or property manages 106 apartment communities in twelve states consisting of 24,022 units. The Company wholly owns, either directly or through subsidiaries, or holds ownership interests in 78 of the 106 apartment communities containing 18,313 units in 10 states. Thirteen of those owned or partially owned apartment communities, consisting of

Edgar Filing: ASSOCIATED ESTATES REALTY CORP - Form 10-Q

1,354 units, are affordable housing communities. The Company, or one of its subsidiaries, also property manages 28 communities in which it does not have an ownership interest, consisting of 5,709 units. Additionally, the Company property manages one commercial property containing approximately 270,000 square feet and asset manages a 186-unit apartment community and one commercial property containing approximately 145,000 square feet.

Basis of Presentation

The accompanying unaudited financial statements have been prepared by the Company's management in accordance with generally accepted accounting principles ("GAAP") for interim financial information and applicable rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting only of normal and recurring adjustments) considered necessary for a fair presentation have been included. The reported results of operations are not necessarily indicative of the results that may be expected for the full year. These financial statements should be read in conjunction with the audited financial statements and accompanying notes in the Company's Annual Report on Form 10-K for the year ended December 31, 2003.

Stock Based Employee Compensation

The Company uses the intrinsic value method in accordance with the Accounting Principles Board Opinion No. 25 ("APB No. 25") to account for stock-based employee compensation arrangements. Under this method, the Company does not recognize compensation cost for stock options when the option exercise price equals or exceeds the market value of the common shares on the date of the grant. Restricted stock grants are recorded initially as a reduction to shareholders' equity and recognized as compensation expense over the vesting periods based upon the market value on the date of the grant. The amount of compensation recorded as a reduction to shareholders' equity related to restricted stock grants was \$544,000 and \$267,000 at March 31, 2004 and December 31, 2003, respectively. If the fair value method had been applied to the stock option grants as prescribed by Statement of Financial Accounting Standard ("SFAS") No. 123, "Accounting for Stock-Based Compensation," the fair values of the options granted at the grant dates would be recognized as compensation expense over the vesting periods, and the Company's net (loss) income and earnings per share for the periods ended March 31, 2004 and 2003 would have been as follows:

	For the three months	
	ended March 31,	
(In thousands, except per share data)	<u>2004</u>	<u>2003</u>
Net (loss) income	\$ (1,065)	\$ (3,982)
Total stock compensation cost recognized	62	68
Total stock compensation cost had SFAS 123 been adopted	<u>(87)</u>	<u>(97)</u>
Proforma net (loss) income had SFAS 123 been adopted	\$ (1,090)	\$ (4,011)
Net (loss) income applicable to common shares:		
Net (loss) income as reported	\$ (2,436)	\$ (5,353)
Total stock compensation cost recognized	62	68

Edgar Filing: ASSOCIATED ESTATES REALTY CORP - Form 10-Q

Total stock compensation cost had SFAS 123 been adopted	(87)	(97)
Pro forma net (loss) income had SFAS 123 been adopted	\$ (2,461)	\$ (5,382)
(Loss) income per common share - Basic		
Net (loss) income as reported	\$ (.13)	\$ (.28)
Total stock compensation cost recognized	-	.01
Total stock compensation cost had SFAS 123 been adopted	-	(.01)
Pro forma net (loss) income had SFAS 123 been adopted	\$ (.13)	\$ (.28)
(Loss) income per common share - Diluted		
Net (loss) income as reported	\$ (.13)	\$ (.28)
Total stock compensation cost recognized	-	.01
Total stock compensation cost had SFAS 123 been adopted	-	(.01)
Pro forma net (loss) income had SFAS 123 been adopted	\$ (.13)	\$ (.28)

Recent Accounting Pronouncements

In March 2004, the Emerging Issues Task Force ("EITF") reached a final consensus regarding Issue 03-6, "Participating Securities and the Two-Class Method under FAS 128." The issue addresses a number of questions regarding the computation of earnings per share ("EPS") by companies that have issued securities other than common stock that participate in dividends and earnings of the issuing entity. Such securities are contractually entitled to receive dividends when and if the entity declares dividends on common stock. The issue also provides further guidance in applying the two-class method of calculating EPS once it is determined that a security is participating. The two-class method is an earnings allocation formula that determines earnings per share for each class of common stock and participating security according to dividends declared (or accumulated) and participation rights in undistributed earnings. This consensus is effective for the period ended June 30, 2004, and should be applied by restating prior period earnings per share. The Company is still evaluating the impact of this consensus as it relates to the operating partnership minority interest.

In January 2003, the FASB issued Interpretation No. 46 "Consolidation of Variable Interest Entities." In December 2003, the FASB issued a revision of Interpretation No. 46 which superceded the January 2003 issuance. This Interpretation of Accounting Research Bulletin No. 51, "Consolidated Financial Statements," addresses consolidation by business enterprises of variable interest entities in which the equity investment at risk is not sufficient to permit the entity to finance its activities without additional subordinated financial support from other parties or in which the equity investors do not have the characteristics of a controlling financial interest. This Interpretation requires a variable interest entity to be consolidated by a company if that company is subject to a majority of the risk of loss from the variable interest entity's activities or entitled to receive a majority of the entity's residual returns or both. The Interpretation also requires disclosures about variable interest entities that the company is not required to consolidate, but in which it has a significant variable interest. The consolidation requirements of this Interpretation apply immediately to variable interest entities created after January 31, 2003 and for the consolidated financial statements for periods ending after March 15, 2004 for all variable interest entities. The Company has adopted the provisions of this Interpretation effective January 1, 2004. The Company has completed the evaluation of all of its legal entities in order to determine whether the entities are variable interest entities and whether the Company is considered to be the primary beneficiary or whether it holds a significant variable interest. The Company has determined that certain legal entities, which are currently included in the Company's consolidated financial statements, are variable interest entities. The Company is the primary beneficiary of these entities and therefore will continue to include them in its consolidated financial statements.

Classification of Fixed Asset Additions

The Company considers recurring fixed asset additions to a property to be capital expenditures made to replace worn out assets so as to maintain the property's value. The Company considers investment/revenue enhancing and/or non-recurring fixed assets to be capital expenditures if such improvements increase the value of the property and/or enable the Company to increase rents. The Company considers acquisition and development fixed asset additions to be for the purchase of, or construction of, new properties to be added to the Company's portfolio.

Reclassifications

Certain reclassifications have been made to the 2003 financial statements to conform to the 2004 presentation.

2. DEVELOPMENT OF MULTIFAMILY PROPERTIES

Construction in progress was \$6.9 million and \$5.5 million at March 31, 2004 and December 31, 2003, respectively, which primarily represents projects at certain of the Company's currently operating properties.

3. SALE OF PROPERTIES

The Company reports, as discontinued operations, the results of operations and gain/loss related to the sale of real estate assets in accordance with SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." Real estate assets that are classified as "held for sale" are also reported as discontinued operations. The Company generally classifies properties as "held for sale" when all significant contingencies surrounding the closing have been resolved. In most transactions, these contingencies are not satisfied until the actual closing of the transaction.

On January 9, 2004, the Company entered into a contract to sell one of its Market Rate properties located in Northeast Ohio. At March 31, 2004, all significant contingencies related to this transaction had been satisfied and, as such, the Company classified this property as "held for sale." This transaction is expected to close during the second quarter. The results of operations for this property for the three months ended March 31, 2004 and 2003 are included in discontinued operations. The net book value of the real estate assets for this property at March 31, 2004, was \$211,000. The Company anticipates that it will record a gain related to the sale of approximately \$9.5 million when the transaction is closed.

The following chart summarizes "Income from discontinued operations" for the three months ended March 31, 2004 and 2003:

	For the three months	
	ended March 31,	
	<u>2004</u>	<u>2003</u>
(In thousands)		
Total property revenues	\$ 561	\$ 549
Total revenues	561	549
Property operating and maintenance expense	359	353
Real estate asset depreciation and amortization	10	5
Interest expense	=	=
Total expenses	<u>369</u>	<u>358</u>
Operating (loss) income	193	191
Gain on disposition of properties	=	=
Income from discontinued operations	\$ 193	\$ 191

4. DEBT

Lines of Credit

The Company has a \$15.0 million secured line of credit with a maturity date of July 31, 2006. There were borrowings of \$4.0 million and \$5.0 million outstanding on this line of credit at March 31, 2004 and December 31, 2003, respectively. Borrowings under this line of credit bear interest at the rate of LIBOR plus 1.5% or 2.84% at March 31, 2004, and are currently limited to \$9.3 million.

The Company also has a \$14.0 million line of credit. There were no regular borrowings outstanding under this line at March 31, 2004 or December 31, 2003. Approximately \$1.6 million of this line of credit is reserved exclusively for derivative transactions. The remaining \$12.4 million is available for regular borrowings and letter of credit transactions. At March 31, 2004, letters of credit totaling \$2.4 million have been issued against this line. Borrowings under this line of credit bear interest at either the prime rate or LIBOR plus 2.0% at the Borrower's option. This line of credit matures December 31, 2004.

5. GOODWILL AND OTHER INTANGIBLE ASSETS

In June 1998, the Company merged with MIG Realty Advisors, Inc. and, as a result, recorded goodwill and an intangible asset subject to amortization. The intangible asset, which is the only intangible asset currently recorded on the Company's books, represents asset advisory and property management contracts. The asset advisory and property management contracts are attributed to properties owned by pension fund clients and are generally terminable upon 30 days notice. The intangible asset and goodwill have been allocated fully to the Management and Service Operations Segment.

On March 17, 2003, MIG was directed by one of its advisory clients to initiate the sale of all of the client's real estate investments. Two of the six assets were sold in 2003 and two were sold during the three months ended March 31, 2004. Because of the sale of these investments, the Company will no longer receive the property and asset management fee revenue associated with them.

In November 2003, the Company was informed by another of its advisory clients that it intended to sell the four commercial properties for which MIG provided asset management services. MIG manages or advises both commercial and multifamily properties for this client. Two of these properties were sold during 2003 and one was sold during the three months ended March 31, 2004. Because of the sale of these investments, the Company will no longer receive the asset management fee revenue associated with them.

Edgar Filing: ASSOCIATED ESTATES REALTY CORP - Form 10-Q

Information on the intangible asset is as follows:

Intangible Asset Subject to Amortization

			Net
	Intangible	Deferred	Intangible
	Subject to	Tax	Asset
(In thousands)	<u>Amortization</u>	<u>Liability</u>	<u>Amortization</u>
Intangible Asset Subject to Amortization:			
Gross carrying amount	\$ 5,405	\$ (625)	\$ 4,780
Less: Accumulated amortization	(4,996)	606	(4,390)
Less: Impairment write down	(312)	=	(312)
Balance as of March 31, 2004	\$ 97	\$ (19)	\$ 78
Estimated remaining amortization expense:			
For the three months ended June 30, 2004	\$ 97	\$ (19)	\$ 78

The net amount of the intangible asset amortization expense recorded for the three months ended March 31, 2004 and 2003 was \$78,000.

Goodwill

The carrying amount of goodwill at March 31, 2004 was \$1.7 million. The Company completed its annual review of goodwill during the quarter ended March 31, 2004. The review included the effect of the above mentioned advisory client directive to liquidate its real estate holdings and a second client's notification to sell four commercial properties. In performing this analysis, the Company estimates holding periods of the assets, changes in fair market value of the assets and cash flows related to the operations of the assets to determine the range of potential alternatives and assigns a probability of the various alternatives under consideration by management. Should the estimates used to determine alternatives or the probabilities of the occurrence thereof change, an impairment may result which could materially impact the results of operations of the Company. Based on its analysis, the Company determined that the goodwill was not impaired as of March 31, 2004. Therefore, there were no changes to the carrying amount of goodwill during the three months ended March 31, 2004. For further information concerning goodwill, see Note 12.

6. TRANSACTIONS WITH AFFILIATES AND JOINT VENTURES

Management and Other Services

The Company provides management and other services to (and is reimbursed for certain expenses incurred on behalf of) certain non-owned properties in which the Company's Chief Executive Officer and/or other related parties have varying ownership interests. The entities which own these properties, as well as other related parties, are referred to as "affiliates." The Company or one of its subsidiaries or Service Companies also provides similar services to joint venture properties.

Summarized affiliate and joint venture transaction activity is as follows:

(In thousands)	For the three months	
	ended March 31,	
	2004	2003
Property management fee and other		
miscellaneous service revenues - affiliates	\$ 188	\$ 409
- joint ventures	63	71
Painting service revenues - affiliates	1,842	57
- joint ventures	3	23
Expenses incurred on behalf		
of and reimbursed by ⁽¹⁾ - affiliates	386	967

Edgar Filing: ASSOCIATED ESTATES REALTY CORP - Form 10-Q

- joint ventures	28	105
Interest income - affiliates	24	26
Interest expense - affiliates	3	10
- joint ventures	-	1

(1) Primarily payroll and employee benefits, reimbursed at cost.

Property management fees and other miscellaneous receivables due from affiliates and joint venture properties aggregated \$2.4 million and \$1.8 million at March 31, 2004 and December 31, 2003, respectively.

Advances to Affiliates and Joint Ventures

In the normal course of business, the Company has advanced funds on behalf of affiliates and joint ventures. Funds advanced to affiliates and joint ventures aggregated \$83,000 and \$354,000 at March 31, 2004, respectively, and \$83,000 and \$170,000 at December 31, 2003, respectively, and represented funds not yet repaid to the Company. The Company also holds funds for the benefit of affiliates and joint ventures which in the aggregate amounted to \$2.5 million and \$171,000 at March 31, 2004, respectively, and \$2.0 million and \$139,000 at December 31, 2003, respectively.

Notes Receivable

At March 31, 2004 and December 31, 2003, two notes of equal amounts were receivable from the Company's Chief Executive Officer aggregating \$3.4 million (included in "Accounts and notes receivables-affiliates and joint ventures" in the Consolidated Balance Sheets) both of which mature May 1, 2005. One of the notes is partially secured by 150,000 of the Company's common shares; the other note is unsecured. For the three months ended March 31, 2004 and 2003, the interest rates charged on these notes were approximately 2.8% and 3.1%, respectively. The Company recognized interest income of \$24,000 and \$26,000 for the three months ended March 31, 2004 and 2003, respectively, relating to these notes.

Professional Services Agreements

Effective July 1, 2002, the Company entered into a professional services agreement with Gelber & Associates Corporation ("Gelber") in which a brother-in-law of the Company's Chief Executive Officer is a principal. Under the agreement, Gelber will consult with the Company on the purchase of natural gas. Gelber will receive a service fee of \$3,000 plus 30.0% of any savings, as defined in the agreement, realized by the Company. The Company paid Gelber \$11,000 and \$13,000 during the three months ended March 31, 2004 and 2003, respectively.

At March 31, 2004, Merit Painting Services ("Merit"), a subsidiary of the Company, was retained by JAS Construction, Inc. ("JAS") under subcontracts for the performance of certain rehabilitation work at seven properties owned by an unrelated party. JAS is owned by the son of the Company's Chief Executive Officer. The total amounts of the subcontracts are yet to be determined because the contract prices are based upon per unit charges and the number of units where work is to be performed is currently unknown. During the three months ended March 31, 2004, \$1.8 million of revenue in connection with these contracts was reported in painting revenues in the Company's Consolidated Statements of Operations. As of March 31, 2004, \$732,000 was still owed Merit and is included in "Accounts and notes receivable affiliates and joint ventures" in the Company's Consolidated Balance Sheets.

7. SHARES

During the three months ended March 31, 2004, the Company issued 45,870 restricted common shares from treasury shares. Of these shares, 32,010 vest three years from the date of grant and the remaining 13,860 shares vest in equal increments over three years from the date of grant. The Company's policy on the reissuance of treasury shares is to account for the issuance on the first-in first-out method. At March 31, 2004, the Company held 3,375,441 treasury shares at a cost of \$30.2 million.

8. EARNINGS PER SHARE

Earnings per share ("EPS") has been computed pursuant to the provisions of SFAS No. 128, "Earnings per Share." There were 1.8 million and 2.3 million options to purchase common shares outstanding at March 31, 2004 and 2003, respectively. None of the options were included in the calculation of diluted earnings per share for the periods presented as their inclusion would be antidilutive to the net loss applicable to common shares from continuing operations.

The exchange of operating partnership minority interests into common shares was also not included in the computation of diluted EPS because the Company plans to settle these OP units in cash.

9. INTERIM SEGMENT REPORTING

The Company has four reportable segments: (1) Acquisition/Disposition Multifamily Properties; (2) Same Store Market Rate ("Market Rate") Multifamily Properties; (3) Affordable Housing Multifamily Properties; and (4) Management and Service Operations. The Company has identified these segments based upon how management makes decisions regarding resource allocation and performance assessment. The Acquisition/Disposition properties represent acquired or developed properties which have not yet reached stabilization (the Company considers a property stabilized when its occupancy rate reaches 93.0% or one year following the purchase or delivery of the final units, whichever occurs first), and properties that have been sold or are classified as "held for sale" in accordance with SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." The Market Rate properties

Edgar Filing: ASSOCIATED ESTATES REALTY CORP - Form 10-Q

are same store conventional multifamily residential apartments. The Affordable Housing properties are multifamily properties for which the rents are subsidized and certain aspects of the operations are regulated by HUD pursuant to Section 8 of the National Housing Act of 1937. The Management and Service Operations provide management and advisory services to the Acquisition/Disposition, Market Rate and Affordable Housing properties which are owned by the Company, as well as to clients and properties not owned by the Company. All of the Company's segments are located in the United States.

The accounting policies of the reportable segments are the same as those described in the "Basis of Presentation and Significant Accounting Policies" in the Company's Form 10-K for the year ended December 31, 2003. The Company evaluates the performance of its reportable segments based on Net Operating Income ("NOI"). NOI is determined by deducting property operating and maintenance expenses from total revenues for the Acquisition/Disposition (excluding amounts classified as discontinued operations), Market Rate and Affordable Housing segments and deducting direct property management and service companies expenses and painting services expenses from total revenues for the Management and Service Operations segment. The Company considers NOI to be an appropriate supplemental measure of its performance because it reflects the operating performance of its real estate portfolio and management and service companies at the property and management and service company level and is used to assess regional property level performance. NOI should not be considered (i) as an alternative to net income (determined in accordance with GAAP), (ii) as an indicator of the Company's financial performance, (iii) as cash flow from operating activities (determined in accordance with GAAP) or (iv) as a measure of the Company's liquidity; nor is it necessarily indicative of sufficient cash flow to fund all of the Company's needs. Certain other real estate companies may define NOI in a different manner.

Information on the Company's segments for the three months ended March 31, 2004 and 2003 is as follows:

	For the three months ended March 31, 2004				
	Acquisition/ Disposition	Market Rate	Affordable Housing	Management and Service Operations	Total Consolidated
(In thousands)					
Total segment revenues	\$ -	\$ 32,199	\$ 2,415	\$ 7,415	\$ 42,029
Elimination of intersegment revenues	-	(72)	(3)	(2,018)	(2,093)
Consolidated revenues	-	32,127	2,412	5,397	39,936
Equity in net loss of joint ventures	(1)	(221)	(36)	-	(258)
Income from discontinued operations	193	-	-	-	193
*NOI	-	17,219	1,193	665	19,077
Total assets	211	657,677	8,879	31,156	697,923

*Intersegment revenues and expenses have been eliminated in the computation of NOI for each of the segments.

	For the three months ended March 31, 2003				
	Acquisition/ Disposition	Market Rate	Affordable Housing	Management and Service Operations	Total Consolidated
(In thousands)					
Total segment revenues	\$ -	\$ 31,460	\$ 2,339	\$ 6,023	\$ 39,822
Elimination of intersegment revenues	-	(64)	(2)	(2,060)	(2,126)
Consolidated revenues	-	31,396	2,337	3,963	37,696
Equity in net loss of joint ventures	(108)	(238)	(8)	-	(354)
Income from discontinued operations	191	-	-	-	191

Edgar Filing: ASSOCIATED ESTATES REALTY CORP - Form 10-Q

*NOI	-	15,019	1,161	252	16,432
Total assets	90	683,683	9,282	32,046	725,101

*Intersegment revenues and expenses have been eliminated in the computation of NOI for each of the segments.

A reconciliation of total segment NOI to total consolidated net (loss) income for the three months ended March 31, 2004 and 2003 is as follows:

(In thousands)	For the three months	
	ended March 31,	
	2004	2003
Total NOI for reportable segments	\$ 19,077	\$ 16,432
Depreciation and amortization	(8,221)	(8,688)
General and administrative expense	(1,836)	(1,512)
Interest expense	(10,004)	(10,029)
Equity in net loss of joint ventures	(258)	(354)
Minority interest in operating partnership	(16)	(22)
Income from discontinued operations	193	191
Consolidated net (loss) income	\$ (1,065)	\$ (3,982)

10. CONTINGENCIES

Legal Proceedings

The Company is subject to legal proceedings, lawsuits and other claims, including proceedings by government authorities (collectively "Litigation"). Litigation is subject to uncertainties and outcomes are difficult to predict. Consequently, the Company is unable to estimate ultimate aggregate monetary liability or financial impact with respect to the Litigation matters described in the following paragraphs as of March 31, 2004 and no accruals have been made for these matters. The Company believes that other Litigation will not have a material adverse impact on the Company after final disposition.

Pending Lawsuits

Edgar Filing: ASSOCIATED ESTATES REALTY CORP - Form 10-Q

On August 10, 2001, Fluor Daniel, Inc. ("FDI") filed a Demand For Arbitration with the American Arbitration Association ("AAA") arising out of construction services provided by FDI to MIG/Orlando Development, LTD ("MOD"), an affiliate of the Company, pursuant to a construction contract between FDI and MOD for the construction of a 460-unit apartment community located in Orlando, Florida. FDI claims that it suffered damages of \$1.6 million in performing the work because of the owner's breach of the construction contract. Both MOD and the Company were named as party defendants in this litigation; however, during 2002, the Company was dismissed as a party to this litigation. MOD filed a counterclaim with the AAA against FDI seeking liquidated damages of \$1.9 million arising out of FDI's failure to complete the project in a timely manner as required by the terms of the construction contract. MOD acquired this project in 1998 as part of the Company's acquisition of MIGRA from a group that included persons who were officers and directors of the Company, which group could have a material interest adverse to the Company because of indemnification obligations owing to the Company in connection with this litigation. The arbitration proceedings in this matter have been temporarily stayed pending a renewed mediation effort. Should such mediation efforts fail, the Company intends to vigorously defend this claim and pursue its counterclaim, but cannot predict the final outcome of this dispute.

On or about April 14, 2002, Melanie and Kyle Kopp commenced an action against the Company in the Franklin County, Ohio Court of Common Pleas seeking undetermined damages, injunctive relief and class action certification. This case arose out of the Company's Suredeposit program. This program allows cash short prospective residents to purchase a bond in lieu of paying a security deposit. The bond serves as a fund to pay those resident obligations that would otherwise have been funded by the security deposit. Plaintiffs allege that the non-refundable premium paid for the bond is a disguised form of security deposit, which is otherwise required to be refundable in accordance with Ohio's Landlord-Tenant Act. Plaintiffs further allege that certain nonrefundable pet deposits required by the Company are similarly security deposits that must be refundable in accordance with Ohio's Landlord-Tenant Act. On or about January 15, 2004, the plaintiffs filed a motion for class certification. The Company subsequently filed a motion for summary judgment. Both motions are pending before the Court. The Company intends to vigorously defend itself against these claims.

On or about April 29, 2003, Housing Advocates, Inc., filed a lawsuit against the Company and others in the Cuyahoga County, Ohio Court of Common Pleas. The complaint alleges violations of handicap design laws in connection with the development of the Company's Residence at Barrington property located in Aurora, Ohio. The complaint seeks injunctive relief, damages and attorneys fees. The Company intends to vigorously defend itself against these claims.

Government Investigations

On or about August 7, 2002, the Maryland Attorney General served the Company with a subpoena seeking information concerning certain of the Company's leasing practices in connection with the Company's Maryland properties. The subpoena seeks extensive information going back a number of years, including information about the Company's Suredeposit programs and certain non-refundable deposits. The Company understands that other landlords operating in Maryland have been served with similar subpoenas. Presently, the Maryland Attorney General has not asserted any claims against the Company, however, the Company is aware of at least one instance where the Maryland Attorney General brought an action against another landlord operating multifamily properties in Maryland alleging that such landlord was engaging in leasing practices contrary to applicable law. The Company is attempting to cooperate with the Maryland Attorney General.

On or about December 22, 2003, the Montgomery County, Maryland Office of Landlord Tenant Affairs commenced an investigation into possible violations of state and county Landlord-Tenant laws involving two properties operated by the Company located in Montgomery County, Maryland. The matters being investigated are for the most part the same leasing practices being investigated by the Maryland Attorney General. The Company is attempting to cooperate with the County.

11. GUARANTEES

In connection with the refinancing of the Watergate Apartments, the Company has guaranteed completion of certain improvements totaling approximately \$7.0 million. This obligation was secured by a \$3.5 million letter of credit. On March 2, 2004, this letter of credit was reduced to \$1.75 million in accordance with the provisions of the original agreement. The Company has also guaranteed the payment of 50.0% of the balance or approximately \$12.7 million at March 31, 2004, of the construction loan in connection with Idlewyde Apartments Phase II, a 535-unit multifamily community located in Atlanta, Georgia which was developed by the Company and its pension fund joint venture partner. This loan matures December 10, 2005. The Company has recorded no liability in relation to this guarantee at March 31, 2004. The Company has guaranteed the payment of 50.0% of the balance or approximately \$7.8 million at March 31, 2004, of the construction loan in connection with the development of Courtney Chase Apartments, a 288-unit multifamily community located in Orlando, Florida which was developed by the Company and its pension fund joint venture partner. This loan matures June 1, 2005, with an option to extend the maturity for two additional years. The Company has recorded no liability in relation to this guarantee at March 31, 2004.

12. SUBSEQUENT EVENTS

Advisory Business

On April 19, 2004, the Company received notice from one of MIG's pension fund clients of its intention to transfer its business to another advisor. The Company is currently analyzing its goodwill related to the advisory business for possible impairment. The Company has a recorded goodwill balance of approximately \$1.7 million at March 31, 2004. Any impairment charge, if taken, would result in a non-cash impact on net income (loss) for the second quarter of 2004.

Dividends Declared

On May 1, 2004, the Company paid a dividend of \$0.17 per common share, which was declared on March 19, 2004 to shareholders of record on April 15, 2004.

Index

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The following discussion should be read in conjunction with the consolidated financial statements and notes thereto included in Part I, Item 1 of this report on Form 10-Q. Historical results and percentage relationships set forth in the Consolidated Statements of Operations contained in the consolidated financial statements, including trends which might appear, should not be taken as indicative of future operations. This discussion may also contain forward-looking statements based on current judgments and current knowledge of management, which are subject to certain risks, trends and uncertainties that could cause actual results to vary from those projected. Accordingly, readers are cautioned not to place undue reliance on forward-looking statements. These forward-looking statements are intended to be covered by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. The words "expects," "projects," "believes," "plans," and similar expressions are intended to identify forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of the document. Investors are cautioned that the Company's forward-looking statements involve risks and uncertainty, including without limitation the following:

- changes in economic conditions in the markets in which the Company owns and manages properties, including interest rates, the overall level of economic activity, the availability of consumer credit and mortgage financing, unemployment rates and other factors;
- risks of a lessening of demand for the multifamily units owned or managed by the Company;
- competition from other available multifamily units and change in market rental rates;
- increases in property and liability insurance costs;
- changes in government regulations affecting the Affordable Housing Properties and other properties operated by the Company;
- changes in or termination of contracts relating to third party management and advisory business;
- inability to renew current Housing Assistance Payment ("HAP") contracts at existing rents;
- weather and other conditions that might adversely affect operating expenses;
- expenditures that cannot be anticipated such as utility rate and usage increases, unanticipated repairs, and real estate tax valuation reassessments;
- inability of the Company to achieve anticipated reductions in operating expenses and increases in revenues;
- the results of litigation filed or to be filed against the Company;
- risks related to the Company's joint ventures; and
- risks of personal injury claims and property damage related to mold claims because of diminished insurance coverage.

Overview. The Company is engaged primarily in the ownership and operation of multifamily residential units. Additionally, the Company and its subsidiaries provide asset and property management services to third party owners of multifamily residential units for which the Company is paid fees. Approximately 84.0% of the Company's consolidated revenues were generated from the leasing of the owned residential units for the three months ended March 31, 2004. Approximately 93.0% of the revenues generated by the owned properties during the three months ended March 31, 2004 are related to Market Rate properties. The operating performance of the properties and cash flows from operations, particularly the Market Rate properties, have been impacted by low mortgage rates, which have resulted in an increase in home purchases by existing and potential apartment residents, the overall weak economy and related unemployment rates. Increasing insurance costs and real estate taxes across the multifamily housing industry have also increased property operating expenses and reduced cash flows from operations.

The Company's total rental revenue collections are impacted by a combination of rental rates, rent concessions and occupancy levels, which the Company attempts to adjust from time to time in order to maintain projected revenues. Indicators that the Company uses in measuring these factors include average economic occupancy, physical occupancy and net collected rent. These indicators are more fully described in the Results of Operations comparison.

For 2004, the Company expects its performance to be driven primarily by improvements in the Market Rate portfolio. The Company expects to increase net collected rents within a range of 2.0% to 2.5% for the year, by focusing on reducing the amount of rent concessions while maintaining the physical occupancy levels achieved at the end of the fourth quarter of 2003. The Company anticipates a reduction in property operating expenses of approximately 3.0% to 3.5%, which it expects to accomplish through continued careful management of controllable expenses. As a result, the Company anticipates growth in Net Operating Income ("NOI") for the Market Rate portfolio in the range of 6.5% to 8.5% for the year 2004 as compared to the year 2003. The Company does not anticipate changes in acquisition, disposition or development activity in 2004 that would materially change these expected results.

LIQUIDITY AND CAPITAL RESOURCES

The Company anticipates that it will meet its liquidity requirements for the remainder of 2004 generally through its net cash provided by operations, secured borrowings (primarily through the use of the Company's two lines of credit, which had \$15.3 million of additional borrowings available at March 31, 2004), and property sales' proceeds. The Company believes that these sources will be sufficient to meet operating requirements, capital additions, mortgage amortization payments and the payment of dividends in accordance with REIT requirements.

The Company anticipates the following commitments for capital expenditures for the remainder of 2004:

. \$8.4 million for recurring capital expenditures. This includes replacement of worn carpet and appliances and property common area parking lots, roofs and similar items in accordance with the Company's current property expenditure plan. This commitment is expected to be funded largely from cash flow provided by operating activities;

. \$2.4 million for investment/revenue enhancing expenditures. This commitment is expected to be funded largely from borrowings on the Company's lines of credit; and

. \$400,000 for non-recurring capital expenditures. This commitment is expected to be funded largely from cash flow provided by operating activities.

While the Company currently estimates that its net cash provided by operations for 2004 should exceed 2003, certain factors could adversely impact the Company's results of operations in 2004 including, but not limited to, continued low mortgage interest rates, continuation of a recessionary economy (primarily employment levels) and higher than anticipated insurance and utility costs. The Company believes that if net cash provided by operations is below 2004 projections, the other sources of cash previously mentioned will be sufficient to cover the liquidity requirements of the Company.

Edgar Filing: ASSOCIATED ESTATES REALTY CORP - Form 10-Q

Cash Flows. Significant sources and uses of cash in the three months ended March 31, 2004 and 2003, respectively, are summarized as follows:

Cash Sources (Uses):

(In thousands)	For the three months	
	ended March 31,	
	2004	2003
Net cash provided by operating activities	\$ 9,329	\$ 5,436
Real estate and fixed asset additions	(2,685)	(1,795)
(Decreases) increases in debt - net	(2,616)	2,314
Cash dividends and operating partnership distributions paid	(4,701)	(4,703)
Exercise of stock options	871	-
Net cash from other financing activities	(71)	(65)
Cash increase	\$ 127	\$ 1,187

Cash Flows Provided by Operating Activities. Cash flows from operating activities have historically been driven by net income (loss) levels and fluctuations in accounts payable and accounts receivable balances. The \$3.9 million increase in cash flow from operating activities in 2004 compared to 2003 was primarily a result of a decrease in net loss of \$2.9 million. Additionally, cash provided in the form of funds held for managed properties increased \$2.0 million in 2004. These increases were partially offset by a net decrease of \$619,000 in accounts payable and accounts receivable and a decrease of \$466,000 in restricted cash.

Cash Flows Used For Investing Activities. Cash used for investing activities increased \$890,000 in 2004 compared to 2003 primarily as a result of an increase in fixed asset addition expenditures in 2004. The Company anticipates total fixed asset expenditures to be approximately \$11.2 million for the remainder of 2004.

Cash Flows Used for Financing Activities. Cash used for financing activities increased \$4.1 million in 2004 compared to 2003 primarily as a result of a reduction in debt of \$2.6 million in 2004 compared to an increase in debt of \$2.3 million in 2003, representing a total change of \$4.9 million. This was partially offset by \$871,000 provided from the issuance of treasury shares related to stock option exercises in 2004.

Dividends. On March 19, 2004, the Company declared a dividend of \$0.17 per common share which was paid on May 1, 2004 to shareholders of record on April 15, 2004.

Financing and Other Commitments. The Company has a \$15.0 million secured line of credit with a maturity date of July 31, 2006. There were borrowings of \$4.0 million and \$5.0 million outstanding on this line of credit at March 31, 2004 and December 31, 2003, respectively. Borrowings under this line of credit bear interest at the rate of LIBOR plus 1.5%, or 2.84% at March 31, 2004, and are currently limited to \$9.3 million.

The Company also has a \$14.0 million line of credit. There were no regular borrowings outstanding under this line at March 31, 2004 or December 31, 2003. Approximately \$1.6 million of this line of credit is reserved exclusively for derivative transactions. The remaining \$12.4 million is available for regular borrowings and letter of credit transactions. At March 31, 2004, letters of credit totaling \$2.4 million have been issued against this line. Borrowings under this line of credit bear interest at either the prime rate or LIBOR plus 2.0% at the Borrower's option. This line of credit matures on December 31, 2004. The Company intends to seek an extension upon maturity.

At March 31, 2004, the Company had one Medium-Term Note outstanding in the amount of \$105,000. This loan bears interest at 6.88%, is unsecured and matures in December 2004. The Company intends to repay this loan in full at maturity.

Guarantees. In connection with the refinancing of the Watergate Apartments, the Company has guaranteed completion of certain improvements totaling approximately \$7.0 million. This obligation was secured by a \$3.5 million letter of credit. On March 2, 2004, this letter of credit was reduced to \$1.75 million in accordance with the provisions of the original agreement. The Company has also guaranteed the payment of 50.0% of the balance or approximately \$12.7 million at March 31, 2004, of the construction loan in connection with Idlewyld Apartments Phase II, a 535-unit multifamily community located in Atlanta, Georgia, which was developed by the Company and its pension fund joint venture partner. This loan matures December 10, 2005. The Company has recorded no liability in relation to this guarantee at March 31, 2004. The Company has guaranteed the payment of 50.0% of the balance or approximately \$7.8 million at March 31, 2004, of the construction loan in connection with the development of Courtney Chase Apartments, a 288-unit multifamily community located in Orlando, Florida which was developed by the Company and its pension fund joint venture partner. This loan matures June 1, 2005, with an option to extend the maturity for two additional years. The Company has recorded no liability in relation to this guarantee at March 31, 2004.

Off-Balance Sheet Investments. The Company has investments in three joint ventures that own a total of four multifamily apartment communities. The operations of these properties are similar to the operations of the Company's wholly owned portfolio. These investments enable the Company to exercise influence over the operations of the properties and share in their profits, while earning additional fee income. The Company accounts for its investments in unconsolidated joint ventures under the equity method of accounting as the Company exercises influence, but does not control these entities. These investments are initially recorded at cost as investments in joint ventures and subsequently adjusted for equity in earnings and cash contributions and distributions.

Joint Venture Financing Commitments. The Company has two guarantee obligations related to its joint ventures. These obligations were previously discussed under Guarantees.

At March 31, 2004, all of the Company's joint venture investments were encumbered by debt. The Company's share of this debt was \$26.3 million.

Acquisitions, Dispositions and Development. Any future multifamily property acquisitions or developments would be financed with the most appropriate sources of capital, which may include the assumption of mortgage indebtedness, bank and other institutio