PREFERRED APARTMENT COMMUNITIES INC
Form 10-Q
August 12, 2013

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

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FORM 10-Q

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x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2013
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 No. 001-34995

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Preferred Apartment Communities, Inc.
(Exact name of registrant as specified in its charter)

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| Maryland | 27-1712193 |
|---|---|
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

3625 Cumberland Boulevard, Suite 1150, Atlanta, GA 30339
(Address of principal executive offices) (Zip Code)
Registrant’s telephone number, including area code: (770) 818-4100

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Sec. 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company (as defined in Rule 12b-2 of the Exchange Act).
Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer x Smaller reporting company ¨
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x
The number of shares outstanding of the registrant’s Common Stock, as of August 8, 2013 was 11,038,587.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements
Preferred Apartment Communities, Inc.
Consolidated Balance Sheets
(Unaudited)

| | June 30, 2013 | December 31, 2012 |
|---|---|---|
| Assets | | |
| Real estate | | |
| Land | $31,300,000 | $13,052,000 |
| Building and improvements | 134,053,563 | 60,284,587 |
| Furniture, fixtures, and equipment | 19,045,363 | 8,771,346 |
| Construction in progress | 471,146 | 3,023 |
| Gross real estate | 184,870,072 | 82,110,956 |
| Less: accumulated depreciation | (9,972,027) | (6,288,998) |
| Net real estate | 174,898,045 | 75,821,958 |
| Real estate loans, net | 54,051,147 | 35,106,197 |
| Total real estate and real estate loans, net | 228,949,192 | 110,928,155 |
| Cash and cash equivalents | 7,542,943 | 2,973,509 |
| Restricted cash | 2,396,226 | 540,232 |
| Notes receivable | 9,069,363 | 2,450,000 |
| Revolving line of credit to related party | 1,992,738 | 936,827 |
| Deferred interest receivable on real estate loans | 1,618,949 | 718,901 |
| Tenant receivables, net of allowance of $14,661 and $18,623 | 16,639 | 11,453 |
| Acquired intangible assets, net of amortization of $10,586,662 and $5,537,067 | 2,103,293 | — |
| Deferred loan costs, net of amortization of $1,099,837 and $258,492 | 1,874,695 | 681,632 |
| Deferred offering costs | 3,991,629 | 3,347,965 |
| Other assets | 832,533 | 703,256 |
| Total assets | $260,388,200 | $123,291,930 |
| Liabilities and equity | | |
| Liabilities | | |
| Mortgage notes payable | $127,516,000 | $55,637,000 |
| Accounts payable and accrued expenses | 3,246,362 | 1,110,964 |
| Revolving credit facility | 14,136,932 | 14,801,197 |
| Accrued interest payable | 303,880 | 202,027 |
| Dividends and partnership distributions payable | 1,953,028 | 851,484 |
| Security deposits and prepaid rents | 543,106 | 330,108 |
| Other deferred income | 32,193 | 301,575 |
| Total liabilities | 147,731,501 | 73,234,355 |
| Commitments and contingencies (Note 11) | | |
| Equity | | |

| | | |
|---|---|---|
| Stockholders' equity | | |
| Series A Redeemable Preferred Stock, $0.01 par value per share; 150,000 shares authorized; | | |
| 59,151 and 19,762 shares issued; 59,121 and 19,762 shares outstanding at June 30, 2013 and December 31, 2012, respectively | 591 | 198 |
| Common Stock, $0.01 par value per share; 400,066,666 shares authorized; 11,037,879 and 5,288,444 shares issued and outstanding at June 30, 2013 and December 31, 2012, respectively | 110,379 | 52,885 |
| Additional paid in capital | 126,704,956 | 59,412,744 |
| Accumulated deficit | (15,118,146) | (9,408,253) |
| Total stockholders' equity | 111,697,780 | 50,057,574 |
| Non-controlling interest | 958,919 | 1 |
| Total equity | 112,656,699 | 50,057,575 |
| Total liabilities and equity | $260,388,200 | $123,291,930 |

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

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Preferred Apartment Communities, Inc.
Consolidated Statements of Operations
(Unaudited)

| | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| Revenues: | | | | |
| Rental revenues | $5,062,433 | $2,241,663 | $9,362,672 | $4,473,385 |
| Other property revenues | 586,262 | 282,039 | 965,052 | 546,220 |
| Interest income on loans and notes receivable | 1,992,950 | 337,279 | 3,288,030 | 476,277 |
| Interest income on note from related party | 27,063 | — | 43,913 | — |
| Total revenues | 7,668,708 | 2,860,981 | 13,659,667 | 5,495,882 |
| | | | | |
| Operating expenses: | | | | |
| Property operating and maintenance | 890,498 | 388,875 | 1,480,075 | 701,008 |
| Property salary and benefits to related party | 553,096 | 238,857 | 1,032,983 | 491,478 |
| Property management fees to related party | 217,719 | 100,494 | 405,361 | 200,507 |
| Real estate taxes | 565,798 | 184,668 | 1,015,577 | 366,908 |
| General and administrative | 175,149 | 46,775 | 286,605 | 91,102 |
| Equity compensation to directors and executives | 290,165 | 286,027 | 599,086 | 605,607 |
| Depreciation and amortization | 4,884,319 | 917,014 | 8,996,622 | 1,894,416 |
| Acquisition costs | 3,525 | — | 202,136 | 912 |
| Acquisition fees to related party | 121,087 | — | 1,029,487 | — |
| Management fees to related party | 467,763 | 188,421 | 851,631 | 368,976 |
| Insurance, professional fees, and other expenses | 274,643 | 208,857 | 579,052 | 412,537 |
| Total operating expenses | 8,443,762 | 2,559,988 | 16,478,615 | 5,133,451 |
| | | | | |
| Operating (loss) income | (775,054) | 300,993 | (2,818,948) | 362,431 |
| Interest expense | 1,242,829 | 535,582 | 2,384,764 | 1,073,657 |
| Loss on early extinguishment of debt | 604,337 | — | 604,337 | — |
| | | | | |
| Net loss | (2,622,220) | (234,589) | (5,808,049) | (711,226) |
| | | | | |
| Plus consolidated net loss attributable to non-controlling interests | 36,670 | — | 98,156 | — |
| | | | | |
| Net loss attributable to the Company | (2,585,550) | (234,589) | (5,709,893) | (711,226) |
| | | | | |
| Cash dividends to preferred stockholders | (745,417) | (78,967) | (1,795,932) | (79,685) |
| Deemed non-cash dividend to holders of Series B Preferred Stock | (7,028,557) | — | (7,028,557) | — |
| Earnings attributable to unvested restricted stock | (4,352) | (4,296) | (9,144) | (7,676) |
| | | | | |
| Net loss attributable to common stockholders | $(10,363,876) | $(317,852) | $(14,543,526) | $(798,587) |
| | | | | |
| Dividends per share declared on Common Stock | $0.15 | $0.13 | $0.295 | $0.26 |
| Net loss per share of Common Stock attributable to common stockholders, basic and diluted | $(1.26) | $(0.06) | $(2.15) | $(0.15) |

| | | | | |
|---|---|---|---|---|
| Weighted average number of shares of Common Stock outstanding, basic and diluted | 8,198,340 | 5,177,170 | 6,752,050 | 5,164,167 |

The accompanying notes are an integral part of these consolidated financial statements.
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Preferred Apartment Communities, Inc.
Consolidated Statements of Stockholders' Equity
For the six months ended June 30, 2013 and 2012
(Unaudited)

| | Series A Redeemable Preferred Stock | Common Stock | Additional Paid in Capital | Accumulated (Deficit) | Total Stockholders' Equity | Non Controlling Interest | Total Equity |
|---|---|---|---|---|---|---|---|
| Balance at January 1, 2012 | $— | $51,493 | $43,828,030 | $(9,261,623) | $34,617,900 | $1 | $34,617,901 |
| Issuance of Units | 100 | — | 10,015,450 | — | 10,015,550 | — | 10,015,550 |
| Syndication and offering costs | — | — | (1,065,067) | — | (1,065,067) | — | (1,065,067) |
| Equity compensation to executives and directors | — | 30 | 605,577 | — | 605,607 | — | 605,607 |
| Vesting of restricted stock | — | 260 | (260) | — | — | — | — |
| Net loss | — | — | — | (711,226) | (711,226) | — | (711,226) |
| Dividends to series A preferred stockholders ($5.00 per share per month) | — | — | (79,685) | — | (79,685) | — | (79,685) |
| Dividends to common stockholders ($0.26 per share) | — | — | (1,350,657) | — | (1,350,657) | — | (1,350,657) |
| Balance at June 30, 2012 | $100 | $51,783 | $51,953,388 | $(9,972,849) | $42,032,422 | $1 | $42,032,423 |
| | | | | | | | |
| Balance at January 1, 2013 | $198 | $52,885 | $59,412,744 | $(9,408,253) | $50,057,574 | $1 | $50,057,575 |
| Issuance of Units | 393 | — | 38,455,112 | — | 38,455,505 | — | 38,455,505 |
| Syndication and offering costs | — | — | (6,387,968) | — | (6,387,968) | — | (6,387,968) |
| Equity compensation to executives and directors | — | 21 | 599,065 | — | 599,086 | — | 599,086 |
| Vesting of restricted stock | — | 330 | (330) | — | — | — | — |
| Vesting of Class B Units and conversion to Class A Units | — | — | (479,841) | — | (479,841) | 479,841 | — |
| Class B Units current period amortization | — | — | (449,289) | — | (449,289) | 449,289 | — |
| Conversion of Series B Preferred Stock to Common Stock | — | 57,143 | 39,942,857 | — | 40,000,000 | — | 40,000,000 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Net loss | — | — | — | (5,709,893) | (5,709,893) | (98,156) | (5,808,049) |
| Reallocation adjustment to non-controlling interests | — | — | (159,504) | — | (159,504) | 159,504 | — |
| Distributions to non-controlling interests | — | — | — | — | — | (31,560) | (31,560) |
| Dividends to series A preferred stockholders ($5.00 per share per month) | — | — | (1,105,457) | — | (1,105,457) | — | (1,105,457) |
| Dividends to series B preferred stockholders ($17.26 per share) | — | — | (690,476) | — | (690,476) | — | (690,476) |
| Dividends to common stockholders ($0.295 per share) | — | — | (2,431,957) | — | (2,431,957) | — | (2,431,957) |
| Balance at June 30, 2013 | $591 | $110,379 | $126,704,956 | $(15,118,146) | $111,697,780 | $958,919 | $112,656,699 |

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

Preferred Apartment Communities, Inc.
Consolidated Statements of Cash Flows
(Unaudited)

| | Six months ended June 30, | |
|---|---|---|
| | 2013 | 2012 |
| Operating activities: | | |
| Net loss | $(5,808,049) | $(711,226) |
| Reconciliation of net loss to net cash provided by operating activities: | | |
| Depreciation expense | 3,683,029 | 1,892,113 |
| Amortization expense | 5,313,593 | 2,303 |
| Amortization of below market lease | (261,695) | — |
| Deferred fee income amortization | (145,519) | (13,031) |
| Deferred loan cost amortization | 422,395 | 42,986 |
| Deferred interest income on real estate loans | (900,048) | — |
| Equity compensation to executives and directors | 599,086 | 605,607 |
| Deferred cable income amortization | (5,468) | — |
| Changes in operating assets and liabilities: | | |
| (Increase) in tenant receivables | (5,187) | (8,955) |
| (Increase) in other assets | (48,239) | (237,577) |
| Increase in accounts payable and accrued expenses | 476,796 | 67,596 |
| (Decrease) in accrued interest payable | (88,486) | (6,628) |
| Increase in security deposits | 12,090 | 2,070 |
| (Decrease) increase in prepaid rents | (4,547) | 145,853 |
| Increase in deferred income | — | 16,275 |
| Net cash provided by operating activities | 3,239,751 | 1,797,386 |
| | | |
| Investing activities: | | |
| Investments in real estate loans | (25,626,531) | (8,914,128) |
| Notes receivable issued | (7,546,203) | (905,290) |
| Notes receivable repaid | 956,665 | — |
| Draws on line of credit by related party | (3,597,995) | — |
| Repayments of line of credit by related party | 2,390,186 | — |
| Acquisition fees received on real estate loans | 1,017,440 | 179,430 |
| Acquisition fees paid on real estate loans | (508,720) | (89,715) |
| Acquisition of properties, net | (33,476,928) | — |
| Additions to real estate assets - improvements | (642,428) | (221,925) |
| (Increase) in restricted cash | (811,880) | (131,672) |
| Net cash used in investing activities | (67,846,394) | (10,083,300) |
| | | |
| Financing activities: | | |
| Proceeds from mortgage notes payable | 59,045,000 | — |
| Payments for mortgage extinguishment | (56,594,389) | — |
| Payments for mortgage loan costs | (1,607,394) | — |
| Proceeds from revolving lines of credit | 30,129,147 | — |
| Payments on revolving lines of credit | (30,793,414) | — |
| Proceeds from sales of Series B Preferred Stock, net of offering costs | 36,956,575 | — |
| Proceeds from sales of Units, net of offering costs | 35,947,555 | 9,086,527 |

| | | |
|---|---|---|
| Common Stock dividends paid | (1,543,539) | (1,320,096) |
| Preferred stock dividends paid | (1,598,854) | (36,892) |
| Class A Unit distributions | (15,513) | — |
| Payments for deferred offering costs | (749,097) | (1,066,429) |
| Net cash provided by financing activities | 69,176,077 | 6,663,110 |
| | | |
| Net increase (decrease) in cash and cash equivalents | 4,569,434 | (1,622,804) |
| Cash and cash equivalents, beginning of period | 2,973,509 | 4,548,020 |
| Cash and cash equivalents, end of period | $7,542,943 | $2,925,216 |

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

Preferred Apartment Communities, Inc.
Consolidated Statements of Cash Flows (unaudited) - continued

| | | |
|---|---|---|
| Supplemental cash flow information: | | |
| Cash paid for interest | $2,668,558 | $1,022,468 |
| | | |
| Supplemental disclosure of non-cash activities: | | |
| Accrued capital expenditures | $200,191 | $32,712 |
| Dividends payable - common | $1,660,034 | $677,476 |
| Dividends payable - preferred | $276,946 | $42,793 |
| Deemed non-cash dividend to holders of Series B Preferred Stock | $7,028,557 | $— |
| Partnership distributions to non-controlling interest | $16,048 | $— |
| Accrued and payable deferred offering costs | $499,932 | $448,560 |
| Reclass of offering costs from deferred asset to equity | $189,325 | $142,485 |
| Mortgage loans assumed on acquisitions | $69,428,389 | $— |
| Mezzanine loan balance applied to purchase of property | $6,326,898 | $— |

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

Preferred Apartment Communities, Inc.
Notes to Consolidated Financial Statements
June 30, 2013
(Unaudited)

1. Organization

Preferred Apartment Communities, Inc. was formed as a Maryland corporation on September 18, 2009, and elected to be taxed as a real estate investment trust, or REIT, under the Internal Revenue Code of 1986, as amended, or the Code, effective with its tax year ended December 31, 2011. Unless the context otherwise requires, references to the "Company", "we", "us", or "our" refer to Preferred Apartment Communities, Inc., together with its consolidated subsidiaries, including Preferred Apartment Communities Operating Partnership, L.P., or the Operating Partnership. The Company was formed primarily to acquire and operate multifamily properties in select targeted markets throughout the United States. As part of its business strategy, the Company may enter into forward purchase contracts or purchase options for to-be-built multifamily communities and may make mezzanine loans, provide deposit arrangements, or provide performance assurances, as may be necessary or appropriate, in connection with the construction of multifamily communities and other properties. As a secondary strategy, the Company also may acquire or originate senior mortgage loans, subordinate loans or mezzanine debt secured by interests in multifamily properties, membership or partnership interests in multifamily properties and other multifamily related assets and invest not more than 10% of its total assets in other real estate related investments, as determined by its Manager (as defined below) as appropriate for the Company. The Company is externally managed and advised by Preferred Apartment Advisors, LLC, or its Manager, a Delaware limited liability company and related party (see Note 6).

The Company completed its initial public offering, or IPO, on April 5, 2011. As of June 30, 2013, the Company had 11,037,879 shares of common stock, par value $0.01 per share, or Common Stock, issued and outstanding and owned the same number of units in the Operating Partnership, which represented a weighted-average ownership percentage of 98.31% for the six-month period ended June 30, 2013. The number of partnership units not owned by the Company totaled 106,988 at June 30, 2013 and represent Class B Unit awards to the Company's four executive officers that vested and became earned on January 3, 2013, and were automatically converted to Class A Units of the Operating Partnership at that date. The Class A Units are convertible at any time at the option of the holder into the Company's choice of either cash or Common Stock. In the case of cash, the value is determined based upon the trailing 20-day volume weighted average price of the Company's Common Stock.

The consolidated financial statements include the accounts of the Company and the Operating Partnership. The Company controls the Operating Partnership through its sole general partner interest and plans to conduct substantially all of its business through the Operating Partnership.

2. Summary of Significant Accounting Policies

Basis of Presentation

The unaudited consolidated financial statements include all of the accounts of the Company and the Operating Partnership presented in accordance with accounting principles generally accepted in the United States of America, or GAAP. All significant intercompany transactions have been eliminated in consolidation. Certain adjustments have been made consisting of normal recurring accruals, which, in the opinion of management, are necessary for a fair presentation of the Company's financial condition and results of operations. These financial statements should be read in conjunction with our audited financial statements and notes thereto included in our 2012 Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 15, 2013.

Use of Estimates

The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

Acquisitions and Impairments of Real Estate Assets

The Company generally records its initial investments in income-producing real estate at fair value at the acquisition date in accordance with ASC 805-10, Business Combinations. The aggregate purchase price of acquired properties is apportioned to the tangible and identifiable intangible assets and liabilities acquired at their estimated fair values. The value of acquired land, buildings and improvements is estimated by formal appraisals, observed comparable sales transactions, and information gathered during

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pre-acquisition due diligence activities and the valuation approach considers the value of the property as if it were vacant. The values of furniture, fixtures, and equipment are estimated by calculating their replacement cost and reducing that value by factors based upon estimates of their remaining useful lives. Intangible assets include the values of in-place leases and customer relationships. In-place lease values are estimated by calculating the estimated time to fill a hypothetically empty apartment complex to its stabilization level (estimated to be 92% occupancy) based on historical observed move-in rates for each property. Carrying costs during these hypothetical expected lease-up periods are estimated, considering current market conditions and include real estate taxes, insurance and other operating expenses and estimates of lost rentals at market rates. The intangible assets are calculated by estimating the net cash flows of the in-place leases to be realized, as compared to the net cash flows that would have occurred had the property been vacant at the time of acquisition and subject to lease-up. The acquired in-place lease values are amortized to operating expense over the average remaining non-cancelable term of the respective in-place leases. The values of customer relationships are estimated by calculating the product of the avoided hypothetical lost revenue and the average renewal probability and are amortized to operating expense over the average remaining historical period of residency, plus an estimate of the average expected renewal period. The above-market or below-market lease values are recorded as a reduction or increase, respectively, to rental income over the remaining average non-cancelable term of the respective leases. Acquired intangible assets have no residual value.

The Company evaluates its tangible and identifiable intangible real estate assets for impairment when events such as declines in a property's operating performance, deteriorating market conditions, or environmental or legal concerns bring recoverability of the carrying value of one or more assets into question. The total undiscounted cash flows of the asset group, including proceeds from disposition, are compared to the net book value of the asset group. If this test indicates that impairment exists, an impairment loss is recorded in earnings equal to the shortage of the book value to the discounted net cash flows of the asset group.

Loans Held for Investment

The Company carries its investments in real estate loans at amortized cost with assessments made for impairment in the event recoverability of the principal amount becomes doubtful. If, upon testing for impairment, the fair value result is lower than the carrying amount of the loan, a valuation allowance is recorded to lower the carrying amount to fair value, with a loss recorded in earnings. Recoveries of valuation allowances are only recognized in the event of maturity or a sale or disposition in an amount above carrying value. The balances of real estate loans presented on the consolidated balance sheets consist of drawn amounts on the loans, net of deferred loan fee revenue. See the 'Revenue Recognition' section of this note for other loan-related policy disclosures required by ASC 310-10-50-6.

Cash and Cash Equivalents and Restricted Cash

The Company considers all highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents. Restricted cash includes cash restricted by state law or contractual requirement and relates primarily to tax and insurance escrows and resident security deposits.

Fair Value Measurements

Certain assets and liabilities are required to be carried at fair value, or if they are deemed impaired, to be adjusted to reflect this condition. The Company follows the guidance provided by ASC 820, Fair Value Measurements and Disclosures, in accounting and reporting for real estate assets where appropriate, as well as debt instruments both held for investment and as liabilities. The standard requires disclosure of fair values calculated under each level of inputs

within the following hierarchy:

•Level 1 – Quoted prices in active markets for identical assets or liabilities at the measurement date.
•Level 2 – Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly.
•Level 3 – Unobservable inputs for the asset or liability.

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Preferred Apartment Communities, Inc.
Notes to Consolidated Financial Statements – (continued)
June 30, 2013
(Unaudited)

Deferred Loan Costs

Deferred loan costs are amortized using the straight-line method, which approximates the effective interest method, over the terms of the related indebtedness.

Deferred Offering Costs

Deferred offering costs represent costs incurred by the Company related to current equity offerings, excluding costs specifically identifiable to a closing, such as commissions, dealer-manager fees, and other registration fees. For issuances of equity that occur on one specific date, associated offering costs are reclassified as a reduction of proceeds raised on the date of issue. Our ongoing offering of units, consisting of one share of Series A Redeemable Preferred Stock, or Series A Preferred Stock, and one warrant, or Warrant, to purchase 20 shares of Common Stock, or Units, generally closes on a bimonthly basis in variable amounts. Such offering is referred to herein as the Primary Series A Offering, pursuant to our registration statement on Form S-11 (registration number 333-176604), as may be amended from time to time. Deferred offering costs related to the Primary Series A Offering are reclassified to the stockholders' equity section of the consolidated balance sheet as a reduction of proceeds raised on a pro-rata basis equal to the ratio of total Units issued to the maximum number of Units that are expected to be issued.

Non-controlling Interest

Non-controlling interest represents the equity interest of the Operating Partnership that is not owned by the Company. Non-controlling interest is adjusted for contributions, distributions and earnings or loss attributable to the non-controlling interest in the consolidated entity in accordance with the Agreement of Limited Partnership of the Operating Partnership, as amended.

Redeemable Preferred Stock

Shares of the Series A Preferred Stock issued pursuant to the Primary Series A Offering (further described in note 5) are redeemable at the option of the holder, subject to a declining redemption fee schedule. Redemptions are therefore outside the control of the Company. However, the Company retains the right to fund any redemptions of Series A Preferred Stock in either Common Stock or cash at its option. Therefore, the Company records the Series A Preferred Stock as a component of permanent stockholders' equity.

Revenue Recognition

Rental revenue is recognized when earned from residents, which is over the terms of rental agreements, typically of 13 months' duration. Differences from the straight-line method, which recognize the effect of any up-front concessions and other adjustments ratably over the lease term, are not material. The Company evaluates the collectability of amounts due from residents and maintains an allowance for doubtful accounts for estimated losses resulting from the inability of residents to make required payments then due under lease agreements. The balance of amounts due from residents are generally deemed uncollectible 30 days beyond the due date, at which point they are fully reserved.

Interest income on real estate loans and notes receivable is recognized on an accrual basis over the lives of the loans using the effective interest method. In the event that a loan or note is refinanced with the proceeds of another loan issued by the Company, any unamortized loan fee revenue from the first loan will be recognized as interest revenue over the term of the new loan. Direct loan origination fees and origination or acquisition costs applicable to real estate

loans are amortized over the lives of the loans as adjustments to interest income. The accrual of interest on all these instruments is stopped when there is concern as to the ultimate collection of principal or interest, which is generally a delinquency of 30 days in required payments of interest or principal. Any payments received on such non-accrual loans are recorded as interest income when the payments are received. Real estate loan assets are reclassified as accrual-basis once interest and principal payments become current. Certain real estate loan assets include limited purchase options and exit fees or additional interest payments that are due the Company at maturity or in the event of a sale of the property or refinancing of the loan by the borrower to a third party. If the Company purchases the subject property, any accrued exit fee will be treated as additional consideration for the acquired project.

Promotional fees received from service providers at the Company’s properties are deferred and recognized on a straight-line basis over the term of the agreement.

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The PAC Rewards program, implemented in the first quarter of 2012, allows residents to accumulate reward points on a monthly basis for actions such as resident referrals and making rent payments online. A resident must rent an apartment from the Company for at least 14 months before reward points may be redeemed for services or upgrades to a resident's unit. The Company accrues a liability for the estimated cost of these future point redemptions, net of a 35% breakage fee, which is the Company's current estimate of rewards points that will not be redeemed. In accordance with Staff Accounting Bulletin 13.A.3c, the Company deems its obligations under PAC Rewards as inconsequential to the delivery of services according to the lease terms. Therefore, the expense related to the PAC Rewards Program is included in property operating and maintenance expense on the consolidated statements of operations.

Stock-Based Compensation

The Company accounts for stock-based compensation in accordance with guidance provided by ASC 505, Equity-Based Payments to Non-Employees and ASC 718, Stock Compensation. We calculate the fair value of equity compensation instruments at the date of grant based upon estimates of their expected term, the expected volatility of and dividend yield on our Common Stock over this expected term period and the market risk-free rate of return. We will also estimate forfeitures of these instruments and accrue the compensation expense, net of estimated forfeitures, over the vesting period(s). We record the fair value of restricted stock awards based upon the closing stock price on the trading day immediately preceding the date of grant.

Acquisition Costs

The Company expenses property acquisition costs as incurred, which include costs such as due diligence, legal, certain accounting, environmental and consulting, when the acquisition constitutes a business combination. The Company capitalizes these costs for transactions deemed to be asset acquisitions.

Capitalization and Depreciation

The Company capitalizes replacements of furniture, fixtures and equipment, as well as carpet, appliances, air conditioning units, certain common area items, and other assets. Significant repair and renovation costs that improve the usefulness or extend the useful life of the properties are also capitalized. These assets are then depreciated on a straight-line basis over their estimated useful lives, as follows:

- Buildings 30 - 40 years
- Furniture, fixtures & equipment 5 - 10 years
- Improvements to buildings and land 5 - 10 years

Operating expenses related to unit turnover costs, such as carpet cleaning, mini-blind replacements, and minor repairs are expensed as incurred.

Income Taxes

The Company has elected to be taxed as a REIT under the Code. To continue to qualify as a REIT, the Company must meet certain organizational and operational requirements, including a requirement to distribute at least 90% of the Company's annual REIT taxable income to its stockholders (which is computed without regard to the dividends paid deduction or net capital gain which does not necessarily equal net income as calculated in accordance with GAAP).

As a REIT, the Company generally will not be subject to federal income tax to the extent it distributes qualifying dividends to its stockholders. If the Company fails to qualify as a REIT in any taxable year, it will be subject to federal income tax on its taxable income at regular corporate income tax rates and generally will not be permitted to qualify for treatment as a REIT for federal income tax purposes for the four taxable years following the year during which qualification is lost unless the Internal Revenue Service grants the Company relief under certain statutory provisions. Such an event could materially adversely affect the Company's net income and net cash available for distribution to stockholders. The Company intends to operate in such a manner as to maintain its election for treatment as a REIT.

The Company's provision for income taxes is based on income before taxes reported for financial statement purposes after adjustment for transactions that do not have tax consequences. Deferred tax assets and liabilities are realized according to the

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estimated future tax consequences attributable to differences between the carrying value of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using the enacted tax rates as of the date of the balance sheet. The effect of a change in tax rates on deferred tax assets and liabilities is reflected in the period that includes the statutory enactment date. A deferred tax asset valuation allowance is recorded when it has been determined that it is more likely than not that deferred tax assets will not be realized. If a valuation allowance is needed, a subsequent change in circumstances in future periods that causes a change in judgment about the realization of the related deferred tax amount could result in the reversal of the deferred tax valuation allowance.

The Company recognizes a liability for uncertain tax positions. An uncertain tax position is defined as a position taken or expected to be taken in a tax return that is not based on clear and unambiguous tax law and which is reflected in measuring current or deferred income tax assets and liabilities for interim or annual periods. The Company may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The Company measures the tax benefits recognized based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate resolution. The Company recognizes interest and penalties related to unrecognized tax benefits in its provision for income taxes.

Earnings (Loss) Per Share

Basic earnings (loss) per share is computed by dividing net income or loss available to common stockholders by the weighted average number of shares of Common Stock outstanding for the period. Net income or loss attributable to common stockholders is calculated by deducting dividends due to preferred stockholders, as well as nonforfeitable dividends due to holders of unvested restricted stock, which are participating securities under the two-class method of calculating earnings per share. Diluted earnings (loss) per share is computed by dividing earnings or net loss available to common stockholders by the weighted average number of shares of Common Stock outstanding adjusted for the effect of dilutive securities such as share grants or warrants. No adjustment is made for potential Common Stock equivalents that are anti-dilutive during the period.

Recent Adoption of Accounting Pronouncements

In December 2011, the FASB issued ASU 2011-10, Property, Plant and Equipment (Topic 360): Derecognition of in Substance Real Estate – a Scope Clarification. This new standard clarifies the guidance concerning deconsolidation of a subsidiary that is in substance real estate upon the event of default of that subsidiary’s nonrecourse debt. Generally, deconsolidation of a subsidiary in this circumstance is not appropriate until the collateral is legally transferred to the lender and the indebtedness is extinguished. This guidance is effective for annual and interim periods beginning after June 15, 2012. Our adoption of this guidance did not have a material effect on our financial position or results of operations.

3. Real Estate Assets
On June 25, 2013, the Company completed the acquisition of a 96-unit townhome-style multifamily community adjacent to our Trail Creek community in Hampton, Virginia, or Trail II, for approximately $18.2 million, less a capital improvements reserve of $250,000, a value believed to approximate the fair value of the assets. The construction of Trail II was partially financed by a $6.0 million mezzanine loan held by the Company, which was applied to the purchase at the closing of the property acquisition, along with an exit fee for accrued interest of $283,062.

The Company allocated the purchase price of Trail II to the acquired assets and liabilities based upon their fair values, as follows:

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| | Trail II |
|---|---|
| Land | $ 1,548,000 |
| Buildings and improvements | 13,411,080 |
| Furniture, fixtures and equipment | 1,968,402 |
| In-place leases | 908,286 |
| Customer relationships | 129,316 |
| Restricted cash and security deposits | 264,689 |
| Prepaids, reserves and other assets | 62,517 |
| Security deposit liabilities | (14,803 ) |
| Accounts payable, accrued expenses and other liabilities | (14,505 ) |
| Below market leases | (106,398 ) |
| Net assets acquired | $ 18,156,584 |
| Cash paid | $ 11,829,686 |
| Reinvested mezzanine funds | 6,326,898 |
| Total consideration | $ 18,156,584 |

See note 6 for details regarding the acquisition fee paid related to this transaction.

On January 23, 2013, the Company completed the acquisition of the following three entities from Williams Multifamily Acquisition Fund, LP, a Delaware limited partnership, or WMAF, an entity whose properties were also managed by Preferred Residential Management LLC.

- Ashford Park REIT, Inc, the fee-simple owner of a 408-unit multifamily community located in Atlanta, Georgia, or Ashford Park, for a total purchase price of approximately $39.6 million, exclusive of assumed mortgage debt, acquisition-related and financing-related transaction costs.

- Lake Cameron REIT, Inc, the fee-simple owner of a 328-unit multifamily community located in suburban Raleigh, North Carolina, or Lake Cameron, for a total purchase price of approximately $30.5 million, exclusive of assumed mortgage debt, acquisition-related and financing-related transaction costs.

- McNeil Ranch REIT, Inc, the fee-simple owner of a 192-unit multifamily community located in Austin, Texas, or McNeil Ranch, for a total purchase price of approximately $21.0 million, exclusive of assumed mortgage debt, acquisition-related and financing-related transaction costs.

The purchase price for each of these three underlying properties was established by the 95% unaffiliated third party equity investor in WMAF, pursuant to terms of the WMAF partnership agreement. The Company allocated the purchase prices of the three properties to the acquired assets and liabilities based upon their fair values, as follows:

| | Ashford Park | Lake Cameron | McNeil Ranch | Total |
|---|---|---|---|---|
| Land | $ 10,600,000 | $ 4,000,000 | $ 2,100,000 | 16,700,000 |
| Buildings and improvements | 23,067,264 | 21,248,442 | 15,962,582 | 60,278,288 |
| Furniture, fixtures and equipment | 3,226,260 | 3,195,131 | 1,593,637 | 8,015,028 |
| In-place leases | 2,445,317 | 1,787,929 | 1,414,373 | 5,647,619 |
| Customer relationships | 375,859 | 313,498 | 161,903 | 851,260 |

| | | | | |
|---|---|---|---|---|
| Restricted cash | 405,437 | 110,019 | 528,659 | 1,044,115 |
| Prepaids, reserves and other assets | 67,642 | 41,609 | 36,153 | 145,404 |
| Security deposit liabilities | (57,825) | (57,606) | (60,931) | (176,362) |
| Intangible liabilities | (164,700) | — | (112,495) | (277,195) |
| Accounts payable, accrued expenses and other liabilities | (363,226) | (138,950) | (650,350) | (1,152,526) |
| Net assets acquired | $39,602,028 | $30,500,072 | $20,973,531 | $91,075,631 |

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| | Ashford Park | Lake Cameron | McNeil Ranch | Total |
|---|---|---|---|---|
| Cash Paid | $ 902,028 | $ 13,000,072 | $ 7,745,142 | $ 21,647,242 |
| Mortgage Assumed | 38,700,000 | 17,500,000 | 13,228,389 | 69,428,389 |
| Total consideration | $ 39,602,028 | $ 30,500,072 | $ 20,973,531 | $ 91,075,631 |

The combined entities of Ashford Park, Lake Cameron, and McNeil Ranch contributed approximately $3.0 million and $5.1 million of revenue and approximately $2.6 million and $5.5 million of net loss to the Company's consolidated results for the three-month and six-month periods ended June 30, 2013, respectively.

The Company recorded depreciation and amortization of tangible and intangible assets on all its multifamily communities as follows:

| | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| Depreciation: | | | | |
| Buildings and improvements | $ 959,891 | $ 411,835 | $ 1,817,926 | $ 823,634 |
| Furniture, fixtures, and equipment | 994,271 | 504,027 | 1,865,103 | 1,068,479 |
| | 1,954,162 | 915,862 | 3,683,029 | 1,892,113 |
| Amortization: | | | | |
| Acquired intangible assets | 2,929,005 | — | 5,311,290 | — |
| Website development costs | 1,152 | 1,152 | 2,303 | 2,303 |
| Total depreciation and amortization | $ 4,884,319 | $ 917,014 | $ 8,996,622 | $ 1,894,416 |

Amortization of acquired intangible assets for the six-month period ended June 30, 2013 commenced on January 23, 2013, the date of acquisition of the three newly-acquired WMAF communities, and on June 25, 2013, the acquisition date of Trail II. The intangible assets will be amortized in full during 2013 over a period ranging from the average remaining lease term, which was approximately six to seven months, to the average remaining lease term plus the average estimated renewal period. See note 15 for pro forma operating results of the Company, including the newly-acquired properties.

4. Real Estate Loans, Notes Receivable, and Line of Credit

Overton

On May 8, 2013, the Company made a mezzanine loan of up to $16,600,000 to Newport Overton Holdings, LLC, or Overton, a Georgia limited liability company, to partially finance the construction of a 294-unit multifamily community located in suburban Atlanta, Georgia. At June 30, 2013, Overton had drawn $9,241,927 of the loan amount.

The Overton mezzanine loan matures on November 1, 2016 with options to extend to May 1, 2018, and pays current monthly interest of 8% per annum. The loan accrues an additional 6% interest which will be due at maturity or if the property is sold to, or refinanced by, a third party. There are no contingent events that are necessary to occur for the Company to realize the additional interest. The Company also has an option, but not an obligation, to purchase the property between and including July 8, 2016 and December 8, 2016 for a pre-negotiated purchase price of $51,500,000. If the Company exercises the purchase option and acquires the property, the additional accrued interest will be treated as additional consideration for the acquired project.

The mezzanine loan is collateralized by a pledge of 100% of the membership interests of Newport Overton, LLC, a Georgia limited liability company, and by unconditional guaranties of payment and performance by Robert F. Krause, Jr. and Richie Stephens, unaffiliated third parties and principals of the borrower. Prepayment of the mezzanine loan is permitted in whole, but not in part, without the Company's consent. The mezzanine loan is subordinate to a senior loan of up to an aggregate amount of approximately $31.7 million that is held by an unrelated third party. Messrs. Krause and Stephens have guaranteed the completion of the project in accordance with the plans and specifications and have entered into joint and several repayment guaranties of the mezzanine loan through receipt of a certificate of occupancy of the property. All of the guaranties are subject to the rights held by the senior lender pursuant to a standard intercreditor agreement.

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In connection with the closing of the Overton mezzanine loan, the Company received a total loan fee of 2% of the aggregate amount of the loan, or $332,000, and paid a cumulative acquisition fee of 1% of the aggregate amount of the mezzanine loan, or $166,000, to the Manager out of these funds (See note 6).

Crosstown Walk

On April 30, 2013, the Company amended the real estate acquisition bridge loan it made on June 29, 2012 by conversion to a mezzanine loan of up to $10,962,000 to Iris Crosstown Partners LLC, or Crosstown Walk, a Georgia limited liability company, to partially finance the construction of a 342-unit multifamily community located in suburban Tampa, Florida. In conjunction with this transaction, Crosstown Walk repaid the balance of the bridge loan previously made to Crosstown Walk, plus accrued interest, the total of which was $4,710,189, and at June 30, 2013, Crosstown Walk had drawn $7,275,859 of the loan amount.

The Crosstown Walk mezzanine loan pays current interest of 8% per annum and matures on November 1, 2016, with options to extend through May 1, 2018. The Company is accruing an additional 6% interest which will be due upon maturity and repayment of the loan or refinancing with a third party. There are no contingent events that are necessary to occur for the Company to realize the additional interest. In conjunction with the loan, the Company received an exclusive option to purchase the stabilized property between July 1, 2016 and December 31, 2016, for a pre-negotiated purchase price of $39,654,273. If the Company exercises the purchase option and acquires the property, the additional accrued interest will be treated as additional consideration for the acquired project.

The mezzanine loan is collateralized by a pledge of 100% of the membership interests of Iris Crosstown Apartments LLC, a Florida limited liability company, a wholly owned subsidiary of Crosstown Walk, and the ultimate owner of the property, and by unconditional guaranties of payment and performance by W. Daniel Faulk, Jr., Richard A. Denny, and J. Michael Morris, unaffiliated third parties and principals of the borrower. Prepayment of the mezzanine loan is permitted in whole, but not in part, without the Company's consent. The mezzanine loan is subordinate to a senior loan of up to an aggregate amount of approximately $25.9 million that is held by an unrelated third party. Messrs. Faulk, Denny and Morris have guaranteed the completion of the project in accordance with the plans and specifications and have entered into joint and several repayment guaranties of the mezzanine loan through receipt of a certificate of occupancy of the property. All of the guaranties are subject to the rights held by the senior lender pursuant to a standard intercreditor agreement.

In connection with the closing of the Crosstown Walk mezzanine loan, the Company received a total loan fee of $124,807, which was equal to 2% of the aggregate amount of the mezzanine loan, or $219,240, less $94,433 in acquisition fees paid from the preceding bridge loan that was financed into the mezzanine loan, and paid an acquisition fee of 1% of the net amount received, or $109,620, less $47,216 in acquisition fees paid from the preceding bridge loan that was financed into the mezzanine loan, to the Manager out of these funds (See note 6).

Lely

On March 28, 2013, the Company made a mezzanine loan of up to $12,713,242 to Lely Apartments LLC, or Lely, a Georgia limited liability company, to partially finance the construction of a 308-unit multifamily community located in Naples, Florida. At June 30, 2013, Lely had drawn $6,364,561 of the loan amount.

The Lely mezzanine loan matures on February 28, 2016, with options to extend until February 28, 2018, and pays current monthly interest of 8% per annum. The loan accrues an additional 6% interest which will be due at maturity or if the property is sold to, or refinanced by, a third party. There are no contingent events that are necessary to occur for the Company to realize the additional interest. The Company also has an option, but not an obligation, to purchase the property between and including April 1, 2016 and August 30, 2016 for a pre-negotiated purchase price of $43,500,000. If the Company exercises the purchase option and acquires the property, the additional accrued interest will be treated as additional consideration for the acquired project.

The mezzanine loan is collateralized by a pledge of 100% of the membership interests of Aster Lely Apartments, LLC, a Georgia limited liability company, a wholly owned subsidiary of Lely, and the ultimate owner of the property, and by unconditional guaranties of payment and performance by Clark Butler and Jeff D. Warshaw, unaffiliated third parties and principals of the borrower. Prepayment of the mezzanine loan is permitted in whole, but not in part, without the Company’s consent. The mezzanine loan is subordinate to a senior loan of up to an aggregate amount of approximately $25.0 million that is held by an unrelated third party.

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Messrs. Butler and Warshaw have guaranteed the completion of the project in accordance with the plans and specifications and have entered into joint and several repayment guaranties of the mezzanine loan through receipt of a certificate of occupancy of the property. All of the guaranties are subject to the rights held by the senior lender pursuant to a standard intercreditor agreement.

In connection with the closing of the Lely mezzanine loan, the Company received a total loan fee of $245,132, which was equal to 2% of the aggregate amount of the mezzanine loan, or $254,265, less the $9,133 in acquisition fees paid from the preceding bridge loan that was financed into the mezzanine loan, and paid an incremental acquisition fee of 1% of the incremental amount in excess of the bridge loan, or $122,566, to the Manager out of these funds (See note 6).

Madison-Rome

On September 28, 2012, the Company made a land acquisition bridge loan in the amount of $5,360,042 to Madison Retail - Rome LLC, or Madison-Rome, a Delaware limited liability company, to partially finance the construction of an 88,351 (unaudited) square foot retail complex located in Rome, Georgia. On November 13, 2012, the loan was converted to a mezzanine construction loan and at June 30, 2013, Madison-Rome had drawn $5,269,637 of the loan amount.

The Madison-Rome loan matures on September 20, 2015, with no option to extend and pays current monthly interest of 8% per annum. An additional exit fee equal to the difference between the 8% interest paid and a 14% cumulative annual simple interest return will be due and payable to the Company if Madison-Rome refinances the loan with a third party or when the loan balance is repaid. There are no contingent events that are necessary to occur for the Company to realize the exit fee.

The Madison-Rome loan is collateralized by a pledge of 100% of the membership interests of Madison-Rome. Prepayment is permitted in whole, but not in part, without our consent. The Madison-Rome loan is subordinate to a senior loan up to an aggregate amount of approximately $11.5 million which is held by an unrelated third party and is subject to the rights held by the senior lender pursuant to a standard intercreditor agreement.

The Madison-Rome loan is secured by unconditional guaranties of payment and performance by Stephen H. Whisenant and Charles N. Worthen, unaffiliated third parties and principals of the borrower. In connection with the closing of the Madison-Rome loan, the Company received a loan fee of 2% of the aggregate loan amount, or $107,201 and paid an acquisition fee of 1% of the aggregate amount of the loan, or $53,600, to the Manager out of these funds.

City Park

On September 6, 2012, the Company made a mezzanine loan of up to $10,000,000 to Oxford City Park Development LLC, or City Park, a Georgia limited liability company, to partially finance the construction of a 284-unit multifamily community located in Charlotte, North Carolina. At June 30, 2013, City Park had drawn the entire loan amount.

The City Park mezzanine loan matures on September 5, 2017, with no option to extend and pays current monthly interest of 8% per annum. The loan accrues an additional 6% interest which will be due at maturity or if the property is sold to, or refinanced by, a third party. There are no contingent events that are necessary to occur for the Company to realize the additional interest. The Company also has an option, but not an obligation, to purchase the property between and including November 1, 2015 and March 31, 2016 for a pre-negotiated purchase price of $30,945,845. If

the Company exercises the purchase option and acquires the property, the additional accrued interest will be treated as additional consideration for the acquired project.

The mezzanine loan is collateralized by a pledge of 100% of the membership interests of City Park. Prepayment of the mezzanine loan is permitted in whole, but not in part, without the Company's consent. The mezzanine loan is subordinate to a senior loan of up to an aggregate amount of approximately $18.6 million that is held by an unrelated third party. W. Daniel Faulk, Jr. and Richard A. Denny have guaranteed the completion of the project in accordance with the plans and specifications. In addition, Messrs. Faulk and Denny have entered into joint and several repayment guaranties of the mezzanine loan. All of the guaranties are subject to the rights held by the senior lender pursuant to a standard intercreditor agreement.

In connection with the closing of the City Park mezzanine loan and subsequently in connection with future drawn amounts on the loan, the Company received a total loan fee of 2% of the amount drawn on the loan, or $148,505, and paid a cumulative acquisition fee of 1% of the aggregate amount of the mezzanine loan, or $74,253, to the Manager out of these funds. Additional loan fees will be recorded on subsequent drawn amounts up to the full aggregate amount of the loan.

City Vista

On August 31, 2012, the Company made a mezzanine loan of up to $12,153,000 to Oxford City Vista Development LLC, or City Vista, a Georgia limited liability company, to partially finance the construction of a 272-unit multifamily community located in Pittsburgh, Pennsylvania. At June 30, 2013, City Vista had drawn $10,398,192 of the loan amount.

The City Vista mezzanine loan matures on June 1, 2016, with an option to extend until July 1, 2017 and pays current monthly interest of 8% per annum. The loan accrues an additional 6% interest which will be due at maturity or if the property is sold to, or refinanced by, a third party. There are no contingent events that are necessary to occur for the Company to realize the additional interest. The Company also has an option, but not an obligation, to purchase the property between and including February 1, 2016 and May 31, 2016 for a pre-negotiated purchase price of $43,560,271. If the Company exercises the purchase option and acquires the property, the additional accrued interest will be treated as additional consideration for the acquired project.

The mezzanine loan is collateralized by a pledge of 100% of the membership interests of City Vista. Prepayment of the mezzanine loan is permitted in whole, but not in part, without the Company's consent. The mezzanine loan is subordinate to a senior loan of up to an aggregate amount of approximately $28.4 million that is held by an unrelated third party. W. Daniel Faulk, Jr. and Richard A. Denny, unaffiliated third parties and principals of the borrower, have guaranteed the completion of the project in accordance with the plans and specifications. In addition, Messrs. Faulk and Denny have entered into joint and several repayment guaranties of the mezzanine loan. All of the guaranties are subject to the rights held by the senior lender pursuant to a standard intercreditor agreement.

In connection with the closing of the City Vista mezzanine loan and subsequently in connection with future drawn amounts on the loan, the Company received a total loan fee of 2% of the amount drawn on the loan, or $159,618 and paid a cumulative acquisition fee of 1% of the aggregate amount of the mezzanine loan, or $79,809, to the Manager out of these funds. Additional loan fees will be recorded on subsequent drawn amounts up to the full aggregate amount of the loan.

Summit II

On May 7, 2012, the Company made a mezzanine loan in the amount of $6,103,027 to Oxford Summit Apartments II LLC, or Summit II, a Georgia limited liability company, to partially finance the construction of a 140-unit multifamily community located adjacent to the Company's existing Summit Crossing multifamily community in suburban Atlanta, Georgia. At June 30, 2013, Summit II had drawn the entire loan amount.

The Summit II mezzanine loan matures on May 8, 2017, with no option to extend and pays current monthly interest of 8% per annum. The loan accrues an additional 6% interest which will be due at maturity or if the property is sold to, or refinanced by, a third party. The Company also has an option, but not an obligation, to purchase the property between and including October 1, 2014 and February 28, 2015 for a pre-negotiated purchase price of $30,945,845. If the property is sold to, or refinanced by, a third party before or after the option period, we will be entitled to receive an exit fee equal to the amount required to provide us with a 14% simple interest return on the loan, in addition to loan fees received at closing, which totaled 2% of the loan amount. Since the minimum exit fee, assuming the purchase option is not exercised, is the amount needed to provide a 14% simple interest return, the Company is accruing each period the additional exit fee earned based on the 14% rate assuming the loan was paid off at period end. There are no

contingent events that are necessary to occur for the Company to realize the additional interest. The accrued exit fee is recorded as interest income in the consolidated statements of operations. If the Company exercises the purchase option and acquires the property, the additional accrued interest will be treated as additional consideration for the acquired project.

The mezzanine loan is collateralized by a pledge of 100% of the membership interests of Oxford Summit II. Prepayment of the mezzanine loan is permitted in whole but not in part without the Company's consent. The mezzanine loan is subordinate to a senior loan of up to an aggregate amount of $12,384,000 that is held by an unrelated third party. W. Daniel Faulk, Jr. and Richard A. Denny have guaranteed the completion of the project in accordance with the plans and specifications. In addition, Messrs. Faulk and Denny have entered into joint and several repayment guaranties of the mezzanine loan. The repayment guaranties expire at the completion of construction of the property. All of the guaranties are subject to the rights held by the senior lender pursuant to a standard intercreditor agreement.

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In connection with the closing of the Summit II mezzanine loan, the Company received a loan fee of 2% of the loan amount, or $122,061 and paid an acquisition fee of 1% of the aggregate amount of the mezzanine loan, or $61,030, to the Manager out of these funds, of which WOF received $610 through its special limited liability company interest in our Manager.

Notes Receivable

On June 25, 2013, the Company amended the bridge loan it made on March 20, 2013 in the amount of $500,000 to 360 Residential, LLC, a Georgia limited liability company, by increasing the aggregate amount of the loan to $1,000,000. The loan bears interest at 8% per annum and interest only payments are due on a monthly basis until the maturity date of March 20, 2014. The loan may be prepaid at any time, in whole or in part, without penalty and accrues a cumulative compounded 6% exit fee which is due at repayment or maturity. The amounts payable under the terms of the loan are backed by guaranties of payment and performance by Clark Butler and Jeff D. Warshaw, unaffiliated third parties and principals of the borrower.

On May 3, 2013, the Company closed on a land acquisition loan in the aggregate amount of $6,000,000 to TPKG 13th Street Development LLC, a Delaware limited liability company, or 13th Street. At closing, 13th Street immediately borrowed $4,841,949 on the loan, which bears current interest at 8% per annum plus an additional exit fee payable in the amount necessary to provide the Company with a cumulative simple annual rate of return of 14% per annum through August 31, 2013. The accrued exit fee scales upward to 20% per annum on January 1, 2014 and thereafter. The exit fee will be due to the Company in the event of a sale of the property, maturity of the loan, or a refinancing with a third party, and there are no contingent events necessary for the Company to realize this additional interest. The loan is collateralized by a pledge of 100% of the membership interests of 13th Street. The maturity date of the loan is January 15, 2014.

On January 24, 2013, the Company was issued a promissory note in the amount of $1,500,000 by Pecunia Management, LLC, or Pecunia, a Florida limited liability company. The loan bears interest at 10% per annum and interest only payments are due on a monthly basis until the maturity date of January 23, 2015. The loan may be prepaid at any time, in whole or in part, without penalty. The amounts payable under the terms of the loan are backed by an assignment of Pecunia's rights to dealer manager fees payable by the Company to International Assets Advisory, LLC, or IAA, a wholly-owned subsidiary of Pecunia,  pursuant to the Dealer Manager Agreement between the Company and IAA, dated November 18, 2011, with respect to the Primary Series A Offering. See note 17 for details regarding the transfer of this promissory note.

On December 17, 2012, the Company made a loan in the amount of $1,300,000 to Riverview Associates, Ltd., or Riverview, a Georgia limited partnership, in the form of a promissory note. The loan bears interest at 8% per annum and interest only payments are due on a monthly basis until the maturity date of December 31, 2013. The loan may be prepaid at any time, in whole but not in part, without penalty. The amounts payable under the terms of the loan are backed by an assignment of project documents and by a guaranty of payment and performance by Stephen H. Whisenant, an unaffiliated third party and principal of the borrower.

On November 15, 2012, the Company made a loan in the amount of $650,000 to IAA in the form of a subordinated loan. The loan bears interest at 10% per annum and interest only payments are due on a monthly basis until the maturity date of November 15, 2013. The loan may not be prepaid prior to maturity. The amounts payable under the terms of the loan are backed by rights of withholding commissions due IAA by the Company in connection with securing placements of the Primary Series A Offering. As of June 30, 2013, the Company has retained certain accrued dealer manager fees totaling $375,000 as additional security on this loan.

On September 14, 2012, the Company made a loan in the amount of $500,000 to Newport Development, LLC, or Newport, a Georgia limited liability company and unaffiliated third party, in the form of a promissory note. The full amount of the loan plus accrued interest was repaid on May 8, 2013.

On March 26, 2012, the Company made a loan in the amount of $650,000 to Oxford Properties, LLC, a Georgia limited liability company, or Oxford, in the form of a promissory note. The loan bore interest at 15% per annum and interest only payments were due beginning May 1, 2012, and continued on a monthly basis until the repayment of the loan, which occurred on September 6, 2012.

Preferred Apartment Communities, Inc.
Notes to Consolidated Financial Statements – (continued)
June 30, 2013
(Unaudited)

Line of Credit
On June 12, 2013, the Company amended the revolving line of credit to its Manager which originated on August 21, 2012 in the aggregate amount of $1.0 million by increasing the aggregate borrowing amount to $2.0 million. The purpose of the line of credit is to provide liquidity to the Manager in support of its ongoing business operations. The credit line bears interest at 8.0% per annum, with interest payable monthly. The line is secured by a collateral assignment of the Manager's right to fees under the third amended and restated management agreement between the Company and the Manager, or the Management Agreement. At June 30, 2013, the amount drawn on the line of credit by the Manager was $1,992,738. See note 17 for details related to an amendment to this instrument subsequent to June 30, 2013, regarding an extension of the maturity date and an increase to the aggregate borrowing limit.
The Company recorded interest income and other revenue from these instruments as follows:

| | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| Interest income: | | | | |
| Real estate loans: | | | | |
| Summit II | $122,060 | $74,128 | 244,121 | $74,128 |
| Trail II | 113,333 | 120,000 | 233,333 | 240,000 |
| Crosstown Walk | 121,467 | 1,232 | 214,802 | 1,232 |
| City Park | 172,390 | — | 310,316 | — |
| City Vista | 182,538 | — | 337,545 | — |
| Overton | 102,504 | — | 102,504 | — |
| Lely | 57,724 | — | 59,626 | — |
| Madison-Rome | 103,889 | — | 205,838 | — |
| Total | 975,905 | 195,360 | 1,708,085 | 315,360 |
| Accrued exit fees | 678,848 | 106,776 | 1,121,837 | 119,846 |
| Net loan fee revenue recognized | 88,383 | 7,104 | 115,694 | 11,429 |
| Total interest income on real estate loans | 1,743,136 | 309,240 | 2,945,616 | 446,635 |
| Total interest income on notes and line of credit | 276,877 | 28,039 | 386,327 | 29,642 |
| Total interest income | $2,020,013 | $337,279 | $3,331,943 | $476,277 |

The Company extends loans for purposes such as to partially finance the development of multifamily residential communities, to acquire land in anticipation of developing and constructing multifamily residential communities, and for other real estate or real estate related projects. Certain of these loans include characteristics such as exclusive options to purchase the project at a fixed price within a specific time window following project completion and stabilization, the rights to incremental exit fees over and above the amount of periodic interest paid during the life of the loans, or both. These characteristics can cause the loans to create variable interests to the Company and require further evaluation as to whether the variable interest creates a variable interest entity, or VIE, which would necessitate consolidation of the project. The Company considers the facts and circumstances pertinent to each entity borrowing under the loan, including the relative amount of financing the Company is contributing to the overall project cost,

decision making rights or control held by the Company, guarantees provided by third parties, and rights to expected residual gains or obligations to absorb expected residual losses that could be significant from the project. If the Company is deemed to be the primary beneficiary of a VIE, consolidation treatment would be required.

The Company has evaluated its real estate loans, where appropriate, for accounting treatment as loans versus real estate development projects, as required by ASC 310. For each loan, the majority of the characteristics and the facts and circumstances indicate that loan accounting treatment is appropriate.

The Company's real estate loans partially finance the development activities of the borrowers' associated legal entities. Each of these loans create variable interests in each of these entities, and according to the Company's analysis, are deemed to be VIEs. Due to the combined factors of the sufficiency of the borrowers' investment at risk, the existence of payment and performance guaranties provided by the borrowers, as well as the limitations on the fixed-price purchase options on the Summit II, City Park, City Vista, Overton, Crosstown Walk, and Lely loans, the Company has concluded that it is not the primary beneficiary of the

borrowing entities. It has no decision making authority or power to direct activity, except normal lender rights, which are subordinate to the senior loans on the projects. Therefore, since the Company has concluded it is not the primary beneficiary, it has not consolidated these entities in its consolidated financial statements. The Company's maximum exposure to loss from these loans is their drawn amount as of June 30, 2013 of approximately $54.7 million. The maximum aggregate amount of loans to be funded as of June 30, 2013 was approximately $73.9 million.
The Company is subject to a concentration of credit risk that could be considered significant with regard to the Summit II, Crosstown Walk, City Park and City Vista real estate loans, as identified specifically by the two named principals of the borrowers, W. Daniel Faulk, Jr. and Richard A. Denny, and as evidenced by repayment guaranties offered in support of these loans. These loans total approximately $33.8 million and in the event of a total failure to perform by the borrowers and guarantors, would subject the Company to a total possible loss of that amount. The Company generally requires secured interests in one or a combination of the membership interests of the borrowing entity or the entity holding the project, guaranties of loan repayment, and project completion performance guaranties as credit protection with regard to its real estate loans, as is customary in the mezzanine loan industry. The Company has performed assessments of the guaranties with regard to the obligors' ability to perform according to the terms of the guaranties if needed and has concluded that the guaranties reduce the Company's risk and exposure to the above-described credit risk in place as of June 30, 2013.

The borrowers and guarantors behind these real estate loans (excluding the Madison-Rome, Overton, and Lely loans) collectively qualify as a major customer as defined in ASC 280-10-50, as the revenue recorded from this customer exceeded ten percent of the Company's total revenues. The Company recorded revenue from transactions with this major customer for the three-month period ended June 30, 2013 of approximately $1.3 million.

5. Redeemable Preferred Stock
On November 18, 2011, the Securities and Exchange Commission declared effective our registration statement on Form S-11 (registration number 333-176604) for our Primary Series A Offering of up to a maximum of 150,000 Units, with each Unit consisting of one share of Series A Preferred Stock and one Warrant to purchase 20 shares of our Common Stock, which is being offered and sold by IAA on a "reasonable best efforts" basis. Each share of Preferred Stock ranks senior to Common Stock and carries a cumulative annual 6% dividend of the stated per share value of $1,000, payable monthly as declared by the Company’s board of directors. Dividends begin accruing on the date of issuance. The Preferred Stock is redeemable at the option of the holder beginning two years following the date of issue subject to a 10% redemption fee. After year three the redemption fee decreases to 5%, after year four it decreases to 3%, and after year five there is no redemption fee. Any redeemed shares of Preferred Stock are entitled to any accrued but unpaid dividends at the time of redemption and any redemptions may be in cash or Common Stock, at the Company’s discretion. The Warrant is exercisable by the holder at an exercise price of 120% of the current market price per share of the Common Stock on the date of issuance of such warrant with a minimum exercise price of $9.00 per share. The current market price per share is determined using the volume weighted average closing market price for the 20 trading days prior to the date of issuance of the Warrant. The Warrants are not exercisable until one year following the date of issuance and expire four years following the date of issuance.
On August 16, 2012, the Company filed a registration statement on Form S-11 (registration number 333-183355) for a follow-on offering of an additional 850,000 Units, or Follow-On Offering, which registration statement has not yet been declared effective by the Securities and Exchange Commission. The terms of the Follow-On Offering and features of the Units in the Follow-On Offering are substantially the same as the Primary Series A Offering.

As of June 30, 2013, offering costs specifically identifiable to Unit offering closing transactions, such as commissions, dealer manager fees, and other registration fees, totaled approximately $5.2 million. These costs are reflected as a reduction of stockholders' equity at the time of closing. In addition, the costs related to the offering not related to a

specific closing transaction totaled approximately $4.2 million. As of June 30, 2013, the Company had issued