

ASSOCIATED ESTATES REALTY CORP
Form 10-K
February 18, 2015

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

Form 10-K

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

For the fiscal year ended December 31, 2014

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)

1 AEC Parkway, Richmond Heights, Ohio 44143-1550
(Address of principal executive offices)

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

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

TITLE OF EACH CLASS	NAME OF EACH EXCHANGE ON WHICH REGISTERED
Common Shares, without par value	New York Stock Exchange NASDAQ Stock Market LLC

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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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 No

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

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

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

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

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

The aggregate market value of the voting stock held by non-affiliates of the Registrant was \$997.0 million as of June 30, 2014.

The number of Common Shares outstanding as of February 3, 2015 was 57,715,771.

DOCUMENTS INCORPORATED BY REFERENCE (To the Extent Indicated Herein).

Notice of Annual Meeting and Proxy Statement for the 2015 Annual Meeting of Shareholders (in Part III).

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 FOR THE YEAR ENDED DECEMBER 31, 2014

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PART I

Except as the context otherwise requires, all references to "we," "our," "us," "AERC," "AEC" and the "Company" in this report collectively refer to Associated Estates Realty Corporation and its consolidated subsidiaries.

Item 1. Business

GENERAL

We are a fully-integrated, self-administered and self-managed equity real estate investment trust ("REIT"). Our common shares are publicly traded on the New York Stock Exchange ("NYSE") and the Nasdaq Global Select Market ("NASDAQ") under the ticker symbol "AEC." Our headquarters, located at 1 AEC Parkway in Richmond Heights, Ohio, is composed of one office building of approximately 42,000 square feet and two adjacent parcels of land containing approximately 1.1 and 3.0 acres, respectively, all of which are suitable for further development or expansion and all of which are subject to a long-term ground lease.

We specialize in multifamily ownership, operation, acquisition, development, disposition and property management activities. We own a taxable REIT subsidiary ("TRS") that performs construction management services for our own account in connection with the development of multifamily properties that we own and operate, including consolidated and unconsolidated joint ventures. As of December 31, 2014, our operating portfolio consisted of 49 apartment communities containing 12,734 units in eight states that are owned, either directly or indirectly, through subsidiaries. See Item 2 for a state-by-state listing of our portfolio. Additionally, in May 2012, in conjunction with our acquisition of land for development of an apartment community, we acquired a commercial building in Los Angeles, California containing approximately 78,800 total square feet of office and commercial space. During 2014, we assumed property management responsibilities for a fee for apartment properties we expect to acquire pursuant to existing contracts. Our consolidated financial statements include the accounts of all subsidiaries, including the TRS, which is separately taxed for federal income tax purposes under the REIT Modernization Act implemented in 1999. Our consolidated financial statements also include the results of a partnership in which we own a 98.1% equity interest.

BUSINESS SEGMENTS

Substantially all of our properties are multifamily communities and, while the economic climate of the markets in which they are located may vary from time to time, the communities offer similar products and services and have similar economic characteristics. Management evaluates the performance of our properties and makes acquisition/disposition decisions on an individual basis. In the aggregate, our multifamily properties provided approximately 98.6% of our consolidated revenue for 2014. We have determined that, as of December 31, 2014, we have one reportable segment, which is multifamily properties.

OPERATING STRATEGY AND BUSINESS OBJECTIVES

Acquisition/Disposition. Our acquisition/disposition strategy in recent years has been to: (i) buy properties located in high growth submarkets outside of the Midwest; (ii) sell properties where market conditions are such that the reinvestment of cash proceeds derived from a sale are expected to provide, over time, a significantly greater return on equity and increased cash flow; (iii) reduce the average age of our portfolio; and (iv) improve the operating margins of our portfolio. In 2014, we acquired the following property:

(Dollar amounts in thousands)

Acquisition Date	Property	Location	Units	Purchase Price
June 10, 2014	Alpha Mill Phase I and Phase II	Charlotte, NC	267	\$45,075

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In 2014, we also disposed of the following five properties:

(Dollar amounts in thousands)

Disposition Date	Property	Location	Units	Sales Price
December 12, 2014	Cypress Shores	Coconut Creek, FL	300	\$44,250
June 16, 2014	Annen Woods	Pikesville, MD	131	20,500
April 28, 2014	Reflections	Columbia, MD	184	38,400
April 2, 2014	Vista Germantown	Nashville, TN	242	53,250
February 24, 2014	Hampton Point	Silver Springs, MD	352	60,000
			1,209	\$216,400

In addition, in 2014, we acquired a land parcel in Woodland Hills, California for \$15.8 million that is entitled for a 379-unit apartment community.

We continue to monitor acquisition opportunities in our existing markets, in particular Central and Southeast Florida, Charlotte, Atlanta and Dallas. We have also identified Southern and Northern California as targeted growth markets. We will also consider opportunistic acquisition and development opportunities in other markets.

We continually monitor the current and expected return on investment of all of our properties. We will consider opportunistic sales of properties in any market, including our targeted growth markets, if we determine that the proceeds from such sales would provide a greater return on investment and increased cash flow when redeployed, or when proceeds could be used to fund development or to reduce debt.

During the three years ended December 31, 2014, we acquired 10 multifamily properties containing a total of 2,607 units for an aggregate purchase price of approximately \$469 million, and we sold 15 multifamily properties containing a total of 4,122 units for an aggregate sales price of approximately \$423 million.

Development. We intend to contribute to our growth by developing new properties. During 2014, we acquired a parcel of land in Woodland Hills, California that is entitled for a 379-unit apartment community. Additionally, during 2014, we continued development on our 175-unit apartment community in the Mid-Wilshire submarket of Los Angeles, California, our 140-unit apartment community with 6,898 square feet of commercial space in Bethesda, Maryland and our 249-unit apartment community in the Turtle Creek neighborhood of the Uptown submarket of Dallas, Texas. We are also developing a 472-unit apartment community with 19,700 square feet of commercial space in the Arts District of downtown Los Angeles, California, and a 410-unit apartment community with 40,000 square feet of commercial space in the South of Market ("SoMa") submarket San Francisco, California. These two projects, known respectively as 950 East Third and 350 8th, are being developed in 50/50 joint venture partnerships. Construction has commenced on the 950 East Third and 350 8th projects. Additionally, the Company was a 50/50 joint venture partner in a property in Monrovia, California known as 5th and Huntington. See Note 3 of the Notes to the Consolidated Financial Statements presented in Part II, Item 8 of this report on Form 10-K. On February 3, 2015, we acquired our partner's 50.0% interest in 5th and Huntington for \$8.4 million, increasing our ownership percentage in the development to 100%.

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Property Operations. We operate in a number of different markets and submarkets. The economic climate in these markets will vary from time to time and, as a result, occupancy and the degree to which we can maintain or increase rents varies. However, our goal is to maximize property net operating income in all of our markets through a combination of increasing rents, maintaining occupancy levels and aggressively managing controllable operating expenses. Strategies to increase revenues include constant monitoring of our markets and submarkets, providing superior resident service and creating highly desirable communities in which to live. We use Property Solutions International to leverage the power of the Internet through enhanced property websites and resident portals that allow integrated resident communication, and by implementing resident billing programs for utilities and refuse collections. We use LRO™, a rental revenue software product that provides comprehensive submarket-based statistical data to assist in maximizing rental revenue while remaining market competitive. We combine this data with our proprietary market knowledge and experience to maximize rental revenues and try to maintain high occupancy levels. With LRO™, we try to generate long-term rent growth by adjusting rents to address market forces in real-time. Our AEC Academy for Career Development provides training and support for our employees, which help us provide better educated and skilled personnel at our communities while minimizing employee turnover. We aggressively manage controllable operating expenses through strategies such as utilizing centralized purchasing contracts benefiting multiple properties and through diligent upkeep and regular maintenance at all of our communities.

Financing and Capital. We use proceeds received from new debt, refinancings, property sales and equity issuances to maximize returns, while remaining keenly focused on strengthening our balance sheet. Increasing both our coverage ratios and the number of unencumbered assets have been two of our principal objectives. During the past three years, we continued to focus on lowering our cost of debt. The weighted average interest rate on our total debt declined 110 basis points from 4.8% per annum at December 31, 2011 to 3.7% per annum at December 31, 2014. Our interest coverage ratio and fixed charge coverage ratios were 3.29:1 and 3.29:1, respectively, at December 31, 2014, up from 2.34:1 and 2.34:1, respectively, at December 31, 2011.

2014 Activities. On July 25, 2014, we amended and restated our \$150 million unsecured term loan. Among other modifications, the amendment extended the maturity date from January 3, 2018 to January 3, 2020, and reduced the interest rate spread across the pricing grid. We also amended our unsecured revolving credit facility to implement corresponding financial covenant modifications.

On February 3, 2014, we entered into a partnership agreement with AIG Global Real Estate (AIG) for the development and operation of 350 8th, a 410-unit apartment community with 40,000 square feet commercial space and underground parking located in the SoMa neighborhood of San Francisco, California. We are a 50.01% partner with AIG, which has contributed \$33.9 million to the partnership. The land upon which the project is being developed was purchased by us for \$46.6 million on May 28, 2013. As of December 31, 2013, this land was included in our consolidated financial statements. Upon the formation of our partnership with AIG, the land and improvements to date, with a carrying value of \$50.3 million, were deconsolidated. On April 25, 2014, the partnership entered into a construction loan agreement for \$143.6 million with a five-year term. We have guaranteed the payment of all future borrowings from this loan and the completion of construction in connection with the partnership's development.

2013 Activities. On October 23, 2013, we consummated a subsidiary merger transaction that had the effect of converting the remaining 74,083 operating partnership units related to the 1998 acquisition of an operating partnership into a right to receive cash merger consideration, pursuant to which \$1.4 million was paid on November 6, 2013.

On October 21, 2013, we completed the issuance of \$100 million of unsecured notes. The notes were offered in a private placement with two maturity tranches: \$45.0 million with a 7-year maturity at 4.29% per annum, and \$55.0 million with a 10.2-year maturity at 4.94% per annum. The \$100 million total issuance had a weighted average term of 8.8 years and a weighted average interest rate of 4.65% per annum. Proceeds from the issuance were used to repay borrowings on our unsecured revolving credit facility.

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On October 1, 2013, we settled Forward Share Agreements with forward purchasers entered into on May 29, 2013 by delivering 7,047,958 common shares at a price of \$17.25 per share. We received net proceeds of approximately \$115.1 million based on the adjusted net settlement price of \$16.33 per share. Proceeds from the forward sale were applied toward the repayment of debt that matured on October 1, 2013.

On June 19, 2013, we amended the terms of our \$350 million unsecured revolving credit facility. Among the modifications, we reduced the credit spread and extended the maturity from January 12, 2016 to June 15, 2017. Total costs associated with this amendment were \$1.2 million. This facility provides improved flexibility and the ability to capitalize on strategic opportunities without the delays associated with financing contingencies. Our borrowing capacity under the unsecured revolving credit facility is a function of our unencumbered property pool.

On April 12, 2013, we filed a new shelf registration statement on Form S-3 to register the sale and issuance of equity and debt securities in public offerings, which replaced our shelf registration statement that was to expire in June 2013. This current shelf registration expires in April 2016. Additionally, on April 12, 2013, we filed a prospectus supplement to register an at-the-market ("ATM") program, which allows us to sell up to \$75 million of our common shares in open market transactions at the then-current market price per share. The ATM program was originally established in August 2012. Due to the filing of the new shelf registration statement on Form S-3, it was necessary to file a new prospectus supplement to continue the ATM program. As of December 31, 2013, we have sold 107,498 shares under the ATM program for total gross proceeds of \$2.0 million, and have remaining availability of approximately \$73.0 million. There were no shares sold during 2014 under this \$75 million ATM program.

On April 2, 2013, we entered into a forward starting interest rate swap on \$125 million of our \$150 million unsecured term loan, fixing the rate beginning June 2, 2016 at a rate of 1.55% per annum plus the credit spread, which was 1.40% per annum as of December 31, 2014, or an all-in rate of 2.95% per annum until the loan matures in January 2018. The credit spread is subject to change, from time to time, from a minimum of 0.90% per annum to a maximum of 1.90% per annum over LIBOR based upon our qualified ratings as defined in the term loan agreement. See Note 11 of the Notes to the Consolidated Financial Statements presented in Part II, Item 8 of this report on Form 10-K for additional information regarding this swap. See also Note 19 of the Notes to the Consolidated Financial Statements presented in Part II, Item 8 of this report on Form 10-K for additional information.

On February 15, 2013, we purchased our development partner's interest in Vista Germantown, a 242-unit apartment community located in downtown Nashville, Tennessee, for \$4.5 million. Prior to the purchase, we held a 90.0% equity interest in Vista Germantown. This property was included as a consolidated entity in our financial statements before and after the purchase. On April 2, 2014, we disposed of Vista Germantown for a sales price of \$53.3 million.

On January 22, 2013, we completed the issuance of \$150 million of unsecured notes. The notes were offered in a private placement with two maturity tranches: \$63.0 million with an 8-year maturity at 4.02% per annum, and \$87.0 million with a 10-year maturity at 4.45% per annum. The \$150 million total issuance had a weighted average term of 9.2 years and a weighted average interest rate of 4.27% per annum. Net proceeds from the issuance were used to repay borrowings on our unsecured revolving credit facility.

2012 Activities. On October 19, 2012, we completed modifications to our unsecured term loan, which included increasing the outstanding principal amount to \$150 million from \$125 million and extending the maturity date from June 2016 to January 2018. An investment grade pricing grid was also added to determine the interest rate on the loan upon our achieving investment grade credit ratings. Total costs associated with this modification were \$600,000.

During 2012, we sold 681,178 shares under our \$25 million ATM program for total gross proceeds of \$11.3 million, or \$11.1 million net of sales commissions and other costs. The net proceeds were used to reduce borrowings on our unsecured revolving credit facility and for general corporate purposes. At June 30, 2012, all \$25 million of common shares available for issuance under the ATM program had been sold and the program was completed. In August 2012, we entered into an ATM program that would allow us to sell up to \$75 million of our common shares in open market transactions at the then market price per share.

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On June 27, 2012, we sold 6,325,000 of our common shares in an underwritten public offering at a price of \$14.40 per share, which resulted in total net proceeds of approximately \$87.2 million. The net proceeds were used to fund property acquisitions and development and for general corporate purposes.

In January 2012, we increased our \$250 million unsecured revolving credit facility to \$350 million. This facility provided additional financial flexibility. Debt procurement costs associated with this modification were \$2.3 million. Our borrowing capacity under the unsecured revolving credit facility was a function of our unencumbered property pool.

General Contractor/Construction. We perform construction management services for our own account in connection with the development of multifamily properties we own and operate as well as unconsolidated joint ventures. Among other things, we believe we will realize significant cost savings and improved quality of our development properties as a result of our in-house development and construction management capabilities.

INCOME TAXES

See Note 10 of the Notes to the Consolidated Financial Statements presented in Part II, Item 8 of this report on Form 10-K.

COMPETITIVE CONDITIONS

See Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" of this report on Form 10-K.

CUSTOMERS

Our business, taken as a whole, is not dependent upon any single customer or a few customers.

EMPLOYEES

On February 3, 2015, we employed approximately 410 people.

EXECUTIVE OFFICERS

The following information regarding our executive officers is provided pursuant to Instruction 3 to Item 401(b) of Regulation S-K.

Name	Age	Position with the Company
Jeffrey I. Friedman	63	Chairman of the Board, President and Chief Executive Officer
Lou Fatica	48	Senior Vice President, Treasurer and Chief Financial Officer
Jason A. Friedman	40	Senior Vice President, Acquisitions and Development
Scott D. Irwin	48	Senior Vice President, General Counsel and Secretary
John T. Shannon	53	Senior Vice President, Operations

Jeffrey I. Friedman is Chairman of the Board, President and Chief Executive Officer of Associated Estates. Mr. Friedman was named President in 2000 and has served as Chairman and CEO since 1993. He originally joined the Company in 1974.

Mr. Friedman also currently serves on the Board of Directors of the Greater Cleveland Sports Commission and the Board of Trustees of the Cleveland Clinic.

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With more than 40 years of real estate experience, Mr. Friedman has been an instrumental part of building a team of apartment experts who deliver on the highest of standards in apartment living, professional fulfillment and shareholder value. In 1993, Mr. Friedman took the Company public. Since then, he has led the growth of the company from assets valued at approximately \$160 million, to assets valued in excess of \$2 billion. Under Mr. Friedman's guidance, Associated Estates has a diversified portfolio of high-quality properties in high growth submarkets with a national footprint. The Company has increased average property revenue per occupied unit from below \$900 in 2007 to nearly \$1,300 in 2014; increased the quarterly cash dividend by 18% over the last three years, while maintaining one of the lowest payout ratios in the multifamily sector; and achieved investment grade ratings from Moody's, Fitch and S&P. As the Chairman and CEO of one of 10 publicly traded multifamily REITs in the country, Mr. Friedman is active in several professional organizations, which include the National Association of Real Estate Investment Trusts, Chief Executives Organization and the National Multi-Housing Council.

Mr. Friedman's past Board positions include United Way, Boy Scouts of America, Cleveland Center for Contemporary Art and the Jewish Community Center of Cleveland. He was honored by Ernst & Young as an "Entrepreneur of the Year" in 2011. He holds a Bachelor of Science degree from The Ohio State University. He is also a graduate of Leadership Cleveland which is designed to enhance and leverage leadership resources within the Cleveland Community. Mr. Friedman is the father of Jason A. Friedman.

Lou Fatica, Senior Vice President, Chief Financial Officer and Treasurer, joined Associated Estates in 1999 as Controller and was promoted to Vice President, Controller in 2000. He assumed his current role in 2001. Mr. Fatica is responsible for financial operations including capital markets, reporting, internal audit and Sarbanes-Oxley compliance as well as tax, treasury and finance functions for the Company. He has more than 25 years of finance and accounting experience and is a Certified Public Accountant ("CPA"). He earned his bachelor's degree in Accounting from Cleveland State University. Mr. Fatica is a member of the American Institute of Certified Public Accountants, the Ohio Society of CPAs, and serves as a member of the Board of Directors of the Hillcrest Family YMCA.

Jason A. Friedman, Senior Vice President, Acquisition and Development, joined Associated Estates in 2009. Mr. Jason A. Friedman is responsible for overseeing the Company's acquisition efforts including the purchase of new assets. Additionally, Mr. Jason A. Friedman is responsible for all new development and construction activities including the purchasing of new land, design and entitlement. He has more than 16 years of real estate experience, including acquisitions, development, construction and financing. He earned his bachelor's degree in Communications and Business from Auburn University. Mr. Jason A. Friedman is a member of the Urban Land Institute, National Multi-Housing Council, National Association of Home Builders, Young Presidents Organization, and National Association of Real Estate Investment Trusts (NAREIT). He also serves as a board member for the American Red Cross and the Domestic Violence and Child Advocacy Center.

Scott D. Irwin, Senior Vice President, General Counsel and Secretary, joined Associated Estates in 2013. Mr. Irwin is responsible for all aspects of the Company's legal matters, providing advice and counsel in the negotiation, structuring and implementation of the Company's property acquisition, development, disposition, financing and capital markets activities, as well as risk management, corporate governance, public company reporting and litigation. From 2010 to 2013, Mr. Irwin served as Executive Vice President, General Counsel and Secretary of Buffets, Inc., one of the largest family dining restaurant companies in the United States. He has more than 22 years of overall experience in law, specializing in finance, corporate governance and compliance, acquisitions and divestitures, labor and employment, and litigation. Mr. Irwin earned his bachelor's degree, summa cum laude, from Kent State University, where he was inducted into Phi Beta Kappa. His Juris Doctorate was awarded, summa cum laude, by The Ohio State University College of Law, where he was elected to the Order of the Coif.

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John T. Shannon, Senior Vice President of Operations, joined Associated Estates in 2004. Mr. Shannon is responsible for the overall direction and guidance of property operations with the objective of maximizing growth and profitability, while fostering a culture committed to providing excellence in service. He also has oversight responsibilities for dispositions, marketing, ancillary services; and he provides day-to-day support of the Company's strategic goals. He has 25 years of property management experience. Mr. Shannon earned his bachelor's degree in Business Administration with a concentration in real estate finance and construction management from the University of Denver.

ENVIRONMENTAL CONSIDERATIONS

See Item 1A, "Risk Factors" for information concerning the potential effects of environmental regulations on our operations.

AVAILABLE INFORMATION

Shareholders may obtain, free of charge from our Internet site at AssociatedEstates.com, a copy of our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act of 1934, as amended, as soon as reasonably practicable after we file such material electronically with, or furnish it to, the Securities and Exchange Commission ("SEC").

REPORTS TO SECURITY HOLDERS

We issue annual reports to our security holders that contain financial statements.

Item 1A. Risk Factors

We are subject to certain risks and uncertainties as described below. These risks and uncertainties are not the only ones we face and there may be additional risks that we do not presently know of or that we currently consider immaterial. All of these risks could adversely affect our business, financial condition, results of operations and cash flows. Our ability to pay dividends on, and the market price of, our equity securities may be adversely affected if any of such risks result in a material adverse effect upon our operations and/or financial condition.

We are subject to risks inherent in the real estate business and operation of a REIT. We own and manage multifamily apartment communities that are subject to varying degrees of risk generally incident to the ownership of real estate. Our financial condition, the value of our properties and our ability to make distributions to our shareholders will be dependent upon our continued access to the debt and equity markets, and our ability to operate our properties in a manner sufficient to generate income in excess of operating expenses and debt service charges, which may be affected by the following risks, some of which are discussed in more detail below:

changes in the economic climate in the markets in which we own and manage properties, including interest rates, the overall level of economic activity, the availability of consumer credit and mortgage financing, unemployment rates and other factors;

elimination of, or limitations on, federal government support for Fannie Mae and/or Freddie Mac that may result in significantly reduced availability of mortgage financing sources, as well as increases in interest rates for mortgage financing;

our ability to refinance debt on favorable terms at maturity;

risks of a lessening of demand for the multifamily units we own;

competition from other available multifamily units, single family units available for rental or purchase, and changes in market rental rates;

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- the failure of development projects or redevelopment activities to achieve expected results due to, among other causes, construction and contracting risks, unanticipated increases in materials and/or labor, delays in project completion and/or lease-up that result in increased costs and/or reduce the profitability of a completed project, and the absence of our right to control all activities and decisions of joint venture developments where the applicable agreement allocate decision making authority to, or require the consent of, our joint venture partner;
- the failure to enter into development joint venture arrangements on acceptable terms;
- increases in property and liability insurance costs;
- unanticipated increases in real estate taxes and other operating expenses;
- weather conditions that adversely affect operating expenses;
- expenditures that cannot be anticipated, such as utility rate and usage increases and unanticipated repairs;
- our inability to control operating expenses or achieve increases in revenue;
- shareholder ownership limitations that may discourage a takeover otherwise considered favorable by shareholders;
- the cost, disruption and diversion of management's attention associated with campaigns commenced by activist investors seeking to influence the Company to take particular actions favored by the activist or gain representation on our Board of Directors;
- information security breaches and other disruptions that could comprise our information or expose us to business interruption;
- the results of litigation involving us;
- changes in tax legislation;
- risks of personal injury and property damage claims that are not covered by our insurance;
- catastrophic property damage losses that are not covered by our insurance;
- risks associated with property acquisitions, such as failure to achieve expected results or matters not discovered in due diligence;
- risks related to the perception of residents and prospective residents as to the attractiveness, convenience and safety of our properties or the neighborhoods in which they are located; and
- those risks factors and special considerations set forth in the documents the Company files from time to time with the SEC.

We are dependent on rental income from our multifamily apartment communities. If we are unable to attract and retain residents, or if our residents are unable to pay their rental obligations, our financial condition and funds available for distribution to our shareholders may be adversely affected.

Our multifamily apartment communities are subject to competition. Our apartment communities are located in developed areas that include other apartment communities and compete with other housing alternatives, such as condominiums, single family and multifamily rental homes and owner occupied single family and multifamily homes. Foreclosed single family homes that become rental properties could create additional competition in certain of our markets. Such competition may impact our rental rates, and affect our ability to attract and retain residents.

Our insurance may not be adequate to cover certain risks. There are certain types of risks, generally of a catastrophic nature, such as earthquakes, floods, windstorms, acts of war and terrorist attacks, that may be uninsurable, are not economically insurable, or are not fully covered by insurance. Moreover, certain risks, such as mold and environmental exposures and certain employment related claims, generally are not covered by our insurance. Other risks are subject to various limits, sub-limits, deductibles and self- insurance retentions, which help to control insurance costs, but which may result in increased exposures to uninsured losses. Significant uninsured losses could have a material adverse effect on our business, financial condition and results of operations.

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Secured debt financing could adversely affect our performance. At December 31, 2014, eight of our 49 operating properties were encumbered by project specific, non-recourse, and non-cross-collateralized mortgage debt. There is a risk that these properties may not have sufficient cash flow from operations to pay required principal and interest. Additionally, at December 31, 2014, we had two construction loans with balances that are collateralized by the respective development properties, as well as an additional unconsolidated construction loan for which we are the guarantor which has no borrowings. We may not be able to refinance these loans at an amount equal to the loan balance, and the terms of any refinancing may not be as favorable as the terms of existing indebtedness. If we are unable to make required payments on indebtedness that is secured by a mortgage, the property securing the mortgage may be foreclosed with a consequent loss of income and value to us. Although Fannie Mae and Freddie Mac continue to provide needed financing to qualified borrowers, such as us, there is no assurance those mortgage capital sources will remain available or available on competitively favorable terms. Additional sources of secured financing are provided by life insurance companies, commercial banks and commercial mortgage-backed securities, which from time-to-time offer terms competitive with Fannie Mae and Freddie Mac. We believe we currently have access to such financing at competitive terms. However, there can be no assurance that such financing will be available or that we will qualify for such financing in the future. In addition, there are currently numerous proposals before Congress that could curtail the lending ability of Fannie Mae and Freddie Mac.

Financial covenants could limit our ability to achieve our strategic objectives. The agreements governing our unsecured credit facility and term loan contain certain restrictions, requirements and other limitations on our ability to incur additional secured and unsecured debt, commence project construction, acquire additional land or development projects and make other strategic investments or business acquisitions or dispositions. These agreements also contain certain financial and operating covenants including, among other things, maintenance of certain financial ratios. Additionally, our unsecured notes contain certain provisions that mirror the requirements of our unsecured credit facility and term loan. Our unsecured credit facility, term loan and unsecured notes are cross-defaulted, and also contain cross default provisions with all of our other outstanding indebtedness of \$25.0 million or more.

Real estate investments are generally illiquid, and we may not be able to sell our properties when it is economically or strategically advantageous to do so. Real estate investments generally cannot be sold quickly, and our ability to sell properties may be adversely affected by market conditions. We may not be able to further diversify or vary our portfolio in accordance with our strategies or in response to economic or other conditions. In addition, provisions of the Internal Revenue Code of 1986, as amended (the "Code"), limit the ability of a REIT to sell its properties in some situations when it may be economically advantageous to do so, thereby potentially adversely affecting our ability to make distributions to our shareholders.

Litigation may result in unfavorable outcomes. Like many real estate operators, we are frequently involved in lawsuits, including those pertaining to premises liability claims, housing discrimination claims and alleged violations of landlord-tenant laws, which may give rise to class action litigation or governmental investigations. Any material litigation not covered by insurance, such as a class action, could result in substantial costs being incurred.

The costs of complying with laws and regulations could adversely affect our cash flow. Our properties must comply with Title III of the Americans with Disabilities Act (the "ADA") to the extent they are "public accommodations" or "commercial facilities" as defined in the ADA. The ADA does not consider apartment communities to be public accommodations or commercial facilities, except for portions of such communities, such as leasing offices and commercial space, that are open to the public. In addition, the Fair Housing Amendments Act of 1988 (the "FHAA") requires apartment communities first occupied after March 13, 1990 to be accessible to disabled individuals. Other state and local laws also require apartment communities to be disability accessible. The FHAA also prohibits discrimination against protected classes of individuals. Noncompliance with these laws could result in the imposition of fines or an award of damages to private litigants. We have been subject to lawsuits alleging violations of accessible design laws in connection with certain of our properties.

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Under various federal, state and local laws, an owner or operator of real estate may be liable for the costs of removal or remediation of certain hazardous or toxic substances on, under or in the property. This liability may be imposed without regard to whether the owner or operator knew of, or was responsible for, the presence of the substances. Other laws impose on owners and operators certain requirements regarding conditions and activities that may affect human health or the environment. Failure to comply with applicable requirements could complicate our ability to lease or sell an affected property, and could subject us to monetary penalties, costs required to achieve compliance and potential liability to third parties. All of our properties and development sites have been the subject of environmental assessments completed by qualified independent environmental consulting companies. While these environmental assessments have not revealed, nor are we aware of, any environmental liability that our management believes would have a material adverse effect, there can be no assurance that we will not incur such liabilities in the future. There have been an increasing number of lawsuits against owners and managers of multifamily properties alleging personal injury and property damage caused by the presence of mold in residential real estate. As some of these lawsuits have resulted in substantial monetary judgments or settlements, insurance carriers have reacted by excluding mold-related claims from standard policies and pricing mold endorsements at prohibitively high rates. While we have adopted programs designed to minimize the existence of mold in any of our properties, as well as guidelines for promptly addressing and resolving reports of mold to minimize any impact mold might have on our residents and our properties, should mold become an issue in the future, our financial condition or results of operations may be adversely affected. Further, it is possible that material environmental contamination or conditions exist, or could arise in the future in our apartment communities or on the land upon which they are located or be present in land or improvements which we may acquire in the future.

Changes in applicable laws could adversely affect our operations or expose us to liability. In addition to the costs of compliance with applicable laws currently in effect, applicable laws are subject to change and new legislation may be enacted, all of which may have the effect of increasing our costs of compliance and/or exposing us to increased potential liabilities. Compliance with changes in: (i) laws increasing the potential liability for environmental conditions existing on properties or the restrictions on discharges or other conditions; (ii) rent control or rent stabilization laws; (iii) increased construction costs for additional accommodations for disabled residents; (iv) required employee benefits, such as health care coverage, or additional employer obligations; or (v) other governmental rules and regulations or enforcement policies affecting the use and operation of our communities, including changes to building codes and fire and life-safety codes, may result in lower revenue growth or significant unanticipated expenditures.

We are subject to risks associated with development, acquisition, disposition and expansion of multifamily apartment communities. Development projects, acquisitions, dispositions and expansions of apartment communities are subject to a number of risks, including:

- availability of acceptable financing;
- competition with other entities for investment opportunities, dispositions, development or construction services or tenants;
- failure by our properties to achieve anticipated operating results;
- failure to avoid retained liabilities with respect to property dispositions or assumed liabilities with respect to property acquisitions;
- development costs of a property exceeding estimates;
- delays in construction of developments or expansions due to, among other causes, weather, required governmental approvals and/or unavailability of labor and materials;
- expenditure of funds on, and the devotion of management time to, transactions that may not come to fruition;
- construction and construction business risks, including, without limitation, rapid and unanticipated increases in prices of building materials and commodities; and
- additional costs due to environmental contamination and compliance.

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Failure to succeed in new markets, or in activities ancillary to the development, ownership and operation of multifamily apartment communities, may adversely effect our operations. We may, from time to time, commence development activity or make acquisitions outside of our existing market areas when appropriate opportunities arise. Our experience in our existing markets in acquiring, developing, owning and operating multifamily apartment communities does not ensure that we will be able to operate successfully in new markets when we choose to enter them. Entering new markets may expose us to a variety of risks, including an inability to accurately evaluate local apartment market conditions; an inability to identify appropriate acquisition opportunities; an inability to hire and retain key personnel; and lack of familiarity with local governmental requirements. Although we are primarily in the multifamily business, we may also own and lease ancillary commercial space when such ancillary rental activities are a component of our multifamily rental activities. We may be unsuccessful in owning and leasing ancillary commercial space at or adjacent to our apartment communities, which could have an adverse effect on our results of operations.

We impose stock ownership limitations that may discourage a takeover otherwise considered favorable by shareholders. With certain limited exceptions, our Second Amended and Restated Articles of Incorporation, as amended, prohibit the ownership of more than 4.0% of our outstanding common shares (the "Ownership Limit"), and more than 9.8% of the shares of any series of any class of our preferred shares by any person unless we grant a waiver. Absent such a waiver, any shares owned in excess of such Ownership Limit are subject to repurchase by us and other consequences as set forth in our Second Amended and Restated Articles of Incorporation, as amended. A transfer of shares may be void if it causes a person to violate the Ownership Limit. The Ownership Limit could delay or prevent a change in control and, therefore, could adversely affect our security holders' ability to realize a premium over the then prevailing market price for their shares. At our 2015 Annual Meeting, we will ask shareholders to approve our Third Amended and Restated Articles of Incorporation, which eliminates the Ownership Limit.

We have a shareholders rights plan which would delay or prevent a change in control. We have a shareholders rights plan that may be triggered if any person or group becomes the beneficial owner of, or announces an offer to acquire, 15.0% or more of our common shares. While our Board of Directors believes our shareholders rights plan could assist in maximizing value for our shareholders in a change in control transaction, our shareholders rights plan would likely have the effect of precluding an acquisition of control of us without our consent. In December 2014, our Board of Directors approved the elimination of our shareholder rights plan, which is expected to be completed during the first quarter of 2015.

We may fail to qualify as a REIT. Commencing with our taxable year ending December 31, 1993, we have operated in a manner so as to permit us to qualify as a REIT under the Code, and we intend to continue to operate in such a manner. Many of the REIT requirements, however, are highly technical and complex. We cannot, therefore, guarantee that we have qualified or will qualify in the future as a REIT. The determination that we are a REIT requires an analysis of various factual matters that may not be totally within our control. For example, to qualify as a REIT, our gross income must generally come from rental and other real estate or passive related sources that are itemized in the REIT tax laws. We are also required to distribute to security holders at least 90.0% of our REIT taxable income excluding capital gains. If we were to fail to qualify as a REIT in any taxable year, we would not be allowed a deduction for distributions to our shareholders in computing our taxable income and would be subject to federal income tax (including any applicable alternative minimum tax) on our taxable income at regular corporate rates. Unless we are entitled to relief under certain Code provisions, we also would be disqualified from treatment as a REIT for the four taxable years following the year during which REIT qualification was lost. As a result, the cash available for distribution to our shareholders could be reduced or eliminated for each of the years involved.

Changes in tax laws could adversely affect the value of our common stock. If Congress enacts legislation that eliminates the REIT provisions from the Code or otherwise decreases the advantages of qualified REIT status under the Code, such as imposing a direct tax on some or all of our real estate related income, such legislation would likely have an adverse impact upon the market value of our common shares and may also result in a reduction of the dividends payable on our common shares.

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We depend on our key personnel. Our success depends to a significant degree upon the continued contribution of key members of our management team, who may be difficult to replace. The loss of services of these executives could have a material adverse effect on us. There can be no assurance that the services of such personnel will continue to be available to us. Our Chairman of the Board, President and Chief Executive Officer, Mr. Jeffrey I. Friedman, is a party to an employment agreement with us. Other than Mr. Friedman, we do not have employment agreements with key personnel. We do not hold key-man life insurance on any of our key personnel.

Any material weaknesses identified in our internal control over financial reporting could have an adverse effect on our share price. Section 404 of the Sarbanes-Oxley Act of 2002 requires us to evaluate and report on our internal control over financial reporting. If we identify one or more material weaknesses in our internal control over financial reporting, we could lose investor confidence in the accuracy and completeness of our financial reports, which in turn could have an adverse effect on our share price.

A currently pending proxy contest, and any other actions of activist stockholders, could cause us to incur substantial costs, divert management's attention and resources, and have an adverse effect on our business. On November 17, 2014, Land & Buildings Investment Management, LLC, a shareholder that, together with its affiliates, held 2.9% of our outstanding common shares, issued by press release a public letter to our shareholders announcing its intent to nominate a slate of seven individual candidates for election to our Board of Directors at our 2015 Annual Meeting of Shareholders.

As a result of this pending proxy contest, or if other activist shareholder activities ensue, our business could be adversely affected because responding to proxy contests and reacting to other actions by activist shareholders can be costly and time-consuming, disrupt our operations and divert the attention of management and our employees. We have retained the services of various professionals to advise us on this matter, including legal, financial and communications advisors, the costs of which may negatively impact our future financial results. In addition, perceived uncertainties as to our future direction, strategy or leadership created as a consequence of these and any similar activist shareholder initiatives may result in the loss of potential business opportunities, harm our ability to attract new investors and joint venture partners, and cause our common share price to experience periods of volatility or stagnation. Moreover, if individuals are elected to our Board of Directors with a specific agenda, it may adversely affect our ability to effectively and timely implement our current initiatives, retain and attract experienced executives and employees, and execute on our long-term strategy.

Item 1B. Unresolved Staff Comments

None.

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Item 2. Properties

Our Portfolio. The following table represents our portfolio as of December 31, 2014, which consists of properties we owned, directly or indirectly, or joint ventures in which we have an ownership interest.

	Total Number of Properties	Total Number of Units
State		
Florida	4	1,294
Georgia	2	354
Indiana	3	836
Michigan	7	2,216
North Carolina	7	1,671
Ohio	15	2,884
Texas	4	1,093
Virginia	7	2,386
	49	12,734
Development Projects		
7001 Arlington at Bethesda ⁽¹⁾	—	—
Cantabria at Turtle Creek ⁽²⁾	—	—
The Desmond on Wilshire ⁽³⁾	—	—
	49	12,734
Joint Venture Development Projects		
950 East Third ⁽⁴⁾	—	—
350 8th ⁽⁵⁾	—	—
Total Portfolio	49	12,734
	Location	Acres
Land Parcels		
Westlake	Westlake, OH	39.0
Wyndemere	Franklin, OH	10.0
5th and Huntington ⁽⁶⁾	Monrovia, CA	2.9
Warner Center ⁽⁷⁾	Woodland Hills, CA	4.6

Total undeveloped acres 56.5

(1) Development in process in Bethesda, Maryland of 140 units with 7,000 square feet of ground floor commercial space.

(2) Development in process in Dallas, Texas of 249 units.

(3) Development in process in Los Angeles, California of 175 units.

(4) Joint venture development in process in Los Angeles, California of 472 units.

(5) Joint venture development in process in San Francisco, California of 410 units.

Planned joint venture development in Monrovia, California of 154 units. On February 3, 2015, we purchased our partner's 50.0% interest in 5th and Huntington for \$8.4 million, increasing our ownership percentage in the development to 100%. See Note 19 of the Notes to the Consolidated Financial Statements presented in Part II, Item 8 of this report on Form 10-K for further information related to this subsequent event.

(7) Planned development in Woodland Hills, California of 379 units.

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	Total Number of Units	Age ⁽¹⁾
State		
Florida		
Doral West	388	16
Vista Lago	316	11
Waterstone at Wellington	222	16
Windsor Pines	368	16
	1,294	
Georgia		
Cambridge at Buckhead	168	19
Morgan Place	186	25
	354	
Indiana		
Center Point	344	17
Residence at White River	228	23
Steeplechase at Shiloh	264	16
	836	
Michigan		
Arbor Landings	328	15
Clinton Place	202	26
Georgetown Park	480	15
Landings at the Preserve	190	23
Oaks at Hampton	544	26
Spring Valley	224	27
Summer Ridge	248	23
	2,216	
North Carolina		
Alpha Mill Phase 1	167	4
Alpha Mill Phase 2 ⁽²⁾	100	—
St. Mary's Square	134	1
Southpoint Village	211	6
The Apartments at Blakeney	295	6
The Apartments at the Arboretum	205	5
The Lofts at Weston Lakeside	215	1
The Park at Crossroads	344	8
	1,671	

(1) Age of property is determined by the number of years since construction of the property was completed.

(2) Construction completed during 2014.

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	Total Number of Units	Age ⁽¹⁾
State		
Ohio		
Bedford Commons	112	27
Heathermoor	280	25
Kensington Grove	76	19
Lake Forest	192	20
Mallard's Crossing	192	24
Perimeter Lakes	189	22
Residence at Barrington	288	15
Saw Mill Village	340	27
Sterling Park	128	20
The Residence at Christopher Wren	264	21
Village at Avon	312	13
Village of Western Reserve	108	16
Westchester Townhomes	136	25
Westlake Seven	7	29
Williamsburg Townhomes	260	24
	2,884	
Texas		
Rienzi at Turtle Creek	152	12
San Raphael	222	15
San Raphael Phase II	99	1
The Brixton	224	17
21 Forty Medical District	396	5
	1,093	
Virginia		
Ashborough	504	10
Dwell Vienna Metro	250	6
River Forest	300	8
Riverside Station	304	9