

# 2019 ANNUAL REPORT



**STERLING** | MULTIFAMILY TRUST



## OUR VISION

TO BE THE MOST RELIABLE, WELL-  
MANAGED AND TRANSPARENT REIT IN  
THE UNITED STATES.



## OUR MISSION

TO PROVIDE LOW-RISK AND INCOME-  
PRODUCING REAL ESTATE INVESTMENT  
OPPORTUNITIES TO INVESTORS.

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# FINANCIAL HIGHLIGHTS

YEAR-ENDED DECEMBER 31 ( IN THOUSANDS )

	2019	PERCENT CHANGE	2018
<b>INCOME STATEMENT</b>			
Rental Revenues	\$ 120,339	3.7 %	\$ 116,051
Total Expenses	104,825	4.9	100,162
Total Other Income	545	(9.1)	6,089
Net Income	16,059	(27.0)	21,978
Funds From Operations	38,054	(5.2)	40,154
<b>BALANCE SHEET</b>			
Total Real Estate Investments	\$ 802,028	1.4 %	\$ 790,696
Total Assets	699,686	(2.1)	714,467
Total Liabilities	420,639	(2.3)	430,716
Shareholder Equity	279,047	(1.7)	283,751
<b>SHAREHOLDER DATA</b> (Weighted Average Balances)			
Common Shares/UPREIT Units Outstanding	27,099	2.7 %	26,398
UPREIT Units Outstanding	17,831	1.3	17,607
Common Shares Outstanding	9,268	5.4	8,791

# OUR VALUES

## RESPECT

We develop and maintain relationships based on trust, cooperation, collaboration and open communication with investors, state and federal agencies, brokers and our many service providers.

## EXCELLENCE

We achieve excellence by fostering a work environment that supports learning, innovation, and change. We strive for continuous improvement, recognizing these components as essential to achieving excellence.

## INTEGRITY

Integrity is the foundation of our credibility. We set high standards for our work and follow the highest ethical and professional standards.

## TRANSPARENCY

To best serve our investors, we provide accurate, complete and conservative information. We produce reports that are objective, useful, clear and candid. The results of our work are intended to add value to our investors.

## STEWARDSHIP

We dare to lead with a focus beyond today. We are committed to our investors long-term, working to build a stronger trust for future generations and acting at all times with an owner's mentality.





# DEAR VALUED INVESTORS,



On behalf of your Board of Trustees, Officers and the entire Sterling Team, thank you for the continued opportunity to serve you. 2019 was another solid year for Sterling Multifamily Trust. Investor returns once again grew, adding to a track record of 17 years of increased returns. This puts the Trust in an elite group of REITs that have never suspended or reduced their dividend, a legacy which we are incredibly proud of and a trend we are driven to maintain.

## 2019 Highlights

In 2019, funds from operations (FFO) on stabilized assets improved by 2.34% over the prior year and adjusted funds from operations (AFFO) remained flat. Over the last five years, our portfolio has produced a generous return on investment for our shareholders, averaging 11.39% per year as compared to the MSCI US REIT Index at 7.03% and the S&P 500 at 11.7% over the same time period. We believe our return performance is paramount, considering our conservative investment strategy and low tolerance for risk.

Sterling's multifamily real estate portfolio performed well in 2019 and net operating income (NOI) remained consistent with the prior year. We prudently focused on operating margin enhancement, where revenue growth and cost containment efforts have remained a critical focus. Several initiatives were put in place to optimize our expectation of best-in-class operations to continue driving organic growth efficiently. Growing revenues and controlling expenses are not unique concepts; however, they remain fundamentally proven and vastly correlated to enhancing shareholder returns.

The Trust continued to hold a diverse base of commercial real estate that was acquired prior to becoming exclusively focused on multifamily assets in 2016. Our commercial portfolio remained a pillar in our overall portfolio, representing roughly 26% of our asset base and contributing approximately 37% to our FFO. We remain committed to these assets and will assess opportunities to transition individual assets if proven beneficial to the portfolio.

Sterling's acquisition activity was idle in 2019. Despite several opportunities presented throughout the year, we were unwilling to lower our acquisition standards below the acceptable return criteria of our investors. In addition, an ultra-competitive investment climate with low return requirements of institutional and private investors pushed real estate pricing to all-time highs. Our conservative and intelligent investment philosophy remains a fundamental differentiator for long-term and sustainable returns, demonstrating a core principle we believe sets this Trust apart from many other investment opportunities. We remain compelled to grow our asset base, but a larger portfolio does not always correlate to a better performing portfolio, and we remain steadfast in our strategy.

## Patient, Conservative, Value Creation

Sterling's sustainable business model and patient buying approach have allowed our investment strategy to adapt its capital management focus as the market continues to evolve. In 2019, due to an adverse acquisition climate, our core investment focus centered on continued reinvestment in our existing assets. Recycling operating capital has improved the quality of our portfolio, where we selectively invested \$15.4 million into our existing assets to enhance building integrity and consumer appeal, fueling long-term operating cash flow. We expect this approach to continue over the next few years and to be a stable source of organic value growth within our existing properties.

Despite the inherent market headwinds for real estate buying, the Trust turned its capital deployment efforts to construction and development opportunities, where investment value was more compelling. In June, we broke ground on a 114-unit addition to our Glen Pond apartment community in Eagan, MN. This budgeted \$16 million addition to an already stabilized high-performing community will be completed in the Summer of 2020, providing a complimentary feature to this well-located existing community. This development

demonstrates a creative and opportunistic approach aligned with our strategy that advances our portfolio by utilizing existing land to strengthen the value of this tremendous apartment community.

Sterling has also structured two joint venture agreements for suburban class 'A' apartment developments in the Minneapolis-St. Paul market. These two, favorably-located communities will feature spacious, high-end homes with first-class amenities. The combined value of these two developments is budgeted at \$68 million. Delivery of the completed assets is expected in late 2020 and early 2021. The development of these apartment communities is poised for initial and long-term success where the economics are highly attractive in the supply-constrained suburban markets of Minneapolis-St. Paul.

#### **Well Positioned for the Future**

In 2019, we took additional steps to strengthen our financial position by further improving an already healthy balance sheet. We reduced our overall debt by 2.34% and total debt to market capitalization decreased by 1.6%, ending the year at 44.8%. We continue to take advantage of a low interest rate environment by retiring high-yielding debt and replacing it with long-term mortgages at record low interest rates. In doing so, we were able to reduce our average interest rate by 0.11% compared to the prior year. This healthy position will not only provide us with flexibility and liquidity to maneuver through various market conditions, but it will also provide us with access to capital to reinvest and grow our business without incurring shareholder dilution.

We have often referenced our favorable positioning in the multifamily real estate sector, where our apartment homes play a vitally important role in the economy by providing high-quality, well-located and affordable housing for individuals and families. Our multifamily real estate portfolio is anchored by a tier of assets where rental price points are attainable for a wide base of renters. We believe this value proposition will continue to drive demand in all market climates and will provide investors with sustainable and durable long-term cash flow.

Our diverse geography will play an essential role in our success in 2020. Multifamily development continues to be steady across the United States; and in our core markets, the balance between supply and demand varies greatly. However, we firmly believe that over the long term these strong and stable locations will provide attractive investment returns on multifamily real estate. The single most important variable for driving apartment demand is job growth, and all of our markets continue to bolster an ecosystem that supports a healthy local economy.

By several measures, 2019 was a successful year for Sterling Multifamily Trust. We enter 2020 stronger and poised for growth opportunity. Staying disciplined and focused on adhering to our long-term strategy to deliver sustainable investor returns is our commitment to you. We look forward to continuing our legacy of high performance.

A sincere thank you to our Board of Trustees and the dedicated people at Sterling Management for their ongoing insight, support and dedication to our mission. On behalf of the entire Sterling team, we thank you, our loyal investor, for your confidence in us and your continued support.

Sincerely,



Bruce Furness  
Chairman of the Board



Kenneth P. Regan  
Chief Executive Officer



EASTBRIDGE APARTMENTS

# OUR BUSINESS



EAGLE RUN APARTMENTS

## THE REIT STRUCTURE

A Real Estate Investment Trust ("REIT") is an investment vehicle created by the United States Congress through the Real Estate Investment Act, enacted in 1960. This Act authorized real estate ownership structures to be treated similar to mutual funds, providing for a tax-exempt pass-through entity with broad-based ownership distributing most of its earnings and capital gains to investors. Investment in a REIT offers diversification benefits since REITs often render differing investment strategies in terms of property type and geographic focus.

## STERLING MULTIFAMILY TRUST

Sterling Multifamily Trust was formed to invest in a portfolio of multifamily (apartment) properties. The Trust elected to be taxed as a Real Estate Investment Trust ("REIT") under Sections 856-860 of the Internal Revenue Code. The Trust's mission is to provide investors the opportunity of long-term ownership in lower risk and well-managed income-producing real estate.

## STERLING MULTIFAMILY PROPERTIES, LLLP

Sterling Multifamily Trust is an Umbrella Partnership Real Estate Investment Trust that holds all of its properties in a separate partnership, Sterling Multifamily Properties, LLLP ("Sterling Multifamily Properties"). The Trust controls Sterling Multifamily Properties and acts as its general partner. The Trust uses Sterling Multifamily Properties to acquire properties, including through the exchange of limited partnership units for properties. These "UPREIT" exchanges can be advantageous, as the seller may be able to defer taxation of gain until the seller later resells the limited partnership units received in the exchange. By offering sellers the ability to defer taxation, the Trust gains an advantage in acquiring quality properties.

## STERLING MANAGEMENT, LLC

Sterling Multifamily Trust operates under the direction of the Board of Trustees. Sterling Multifamily Trust has no employees and therefore it retains Sterling Management, LLC, to manage its owned real estate and business operations. Sterling Management's CEO, President, CIO and CFO serve as executive officers of the Trust.



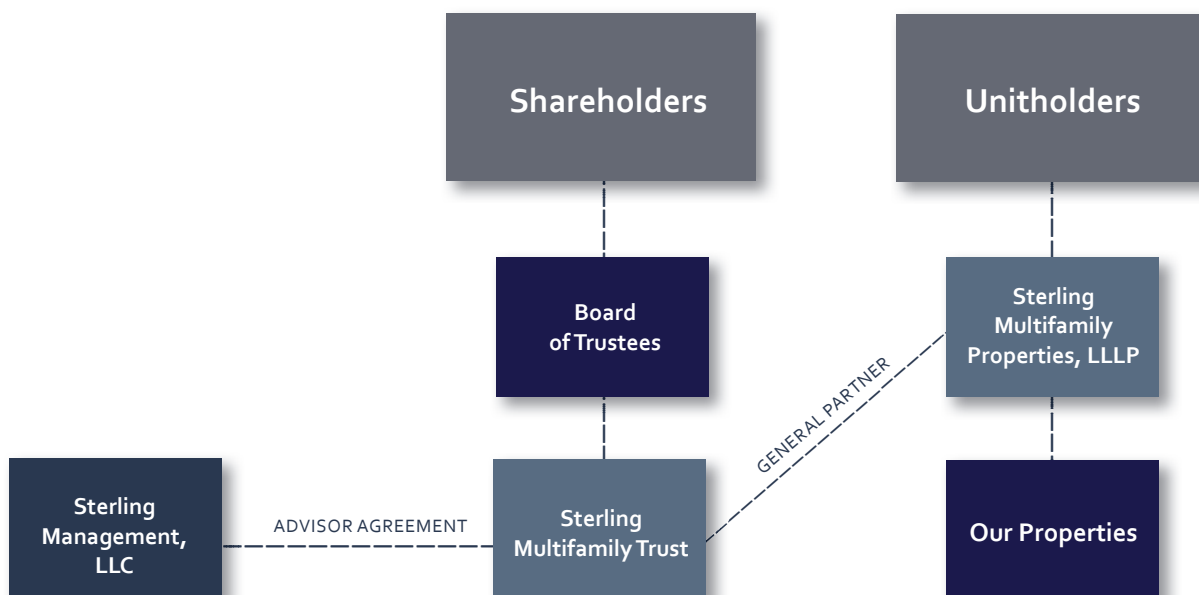
## PUBLIC COMPANY STATUS

From inception through 2010, Sterling Multifamily Trust operated as a private REIT. In 2011, the Trust registered with the Securities and Exchange Commission ("SEC") and became a non-traded public reporting company. The Trust's ongoing growth and success necessitated our registration and transition to public company reporting status.

There are two forms of Public REITs: Traded and Non-Traded. A traded REIT is a public company whose shares are traded on major stock exchanges such as NYSE or NASDAQ. Non-traded REITs may also be public companies, but their shares are not traded on major exchanges and are, instead, offered directly to investors through representatives/broker dealers registered to sell the shares. Sterling Multifamily Trust operates as a public “non-traded” REIT.

The Trust filed its first report on Form 10-Q on May 15, 2011. The Trust's most recent Annual Report on Form 10-K is contained at the end of this document. The Trust's registration and reports are available to the public on the Sterling Multifamily Trust and SEC websites.

## ORGANIZATIONAL STRUCTURE



# NEW DEVELOPMENTS

## Maple Grove Apartments



**ANTICIPATED COMPLETION:** 2021  
**PRICE PER UNIT:** \$198,750  
**ESTIMATED INVESTMENT:** \$32,000,000  
**NUMBER OF UNITS:** 161  
**NUMBER OF BUILDINGS:** 1  
**LOCATION:** MAPLE GROVE, MINNESOTA



# Reside Apartments

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**ANTICIPATED COMPLETION:** 2020  
**PRICE PER UNIT:** \$192,100  
**ESTIMATED INVESTMENT:** \$36,500,000  
**NUMBER OF UNITS:** 190  
**NUMBER OF BUILDINGS:** 4  
**LOCATION:** SAVAGE, MINNESOTA



# Addition to Glen Pond Apartments

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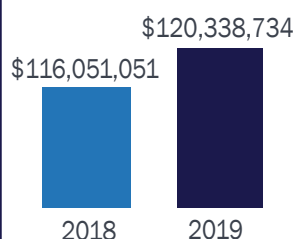
**ANTICIPATED COMPLETION:** 2020  
**PRICE PER UNIT:** \$138,000  
**ESTIMATED INVESTMENT:** \$15,700,000  
**NUMBER OF UNITS:** 114  
**NUMBER OF BUILDINGS:** 2  
**LOCATION:** EAGAN, MINNESOTA



# KEY PERFORMANCE INDICATORS

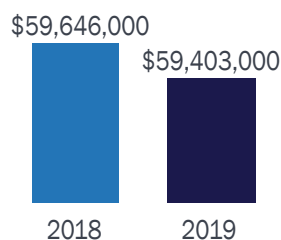
## TOTAL REVENUE

**+3.7%**



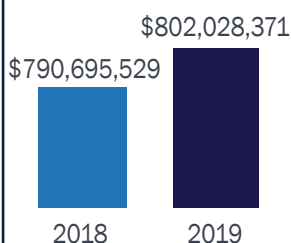
## TOTAL N.O.I.

**(0.4%)**



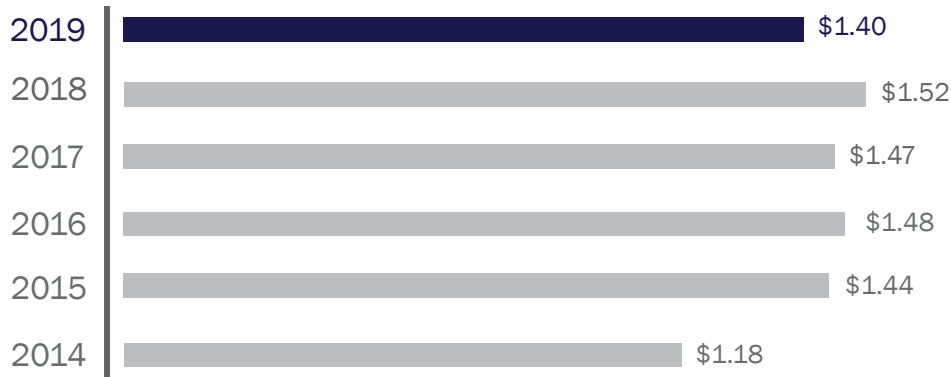
## REAL ESTATE ASSETS

**+1.4%**



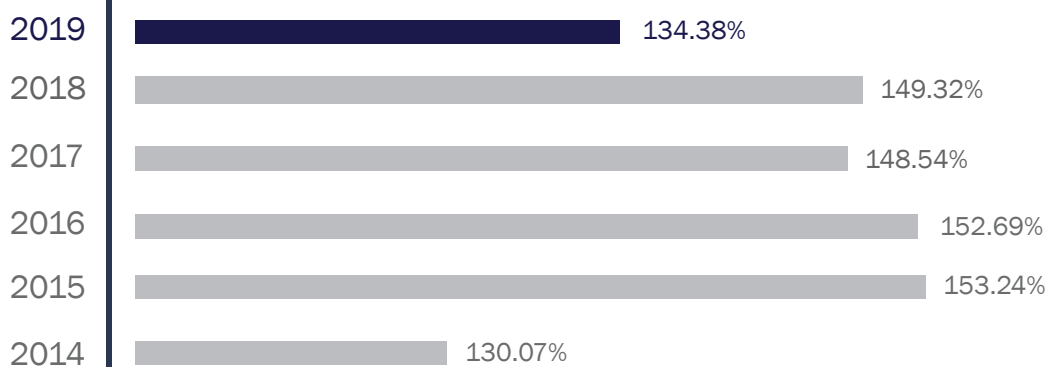
## FUNDS FROM OPERATIONS

Funds from Operations (FFO) is the most commonly accepted and reported measure of REIT operating performance. It is a REIT's net income, excluding gains or losses from sales of property, and adding back real estate depreciation. From 2014 to 2019 Sterling Multifamily Trust experienced an 18.64% increase in FFO per share/unit.



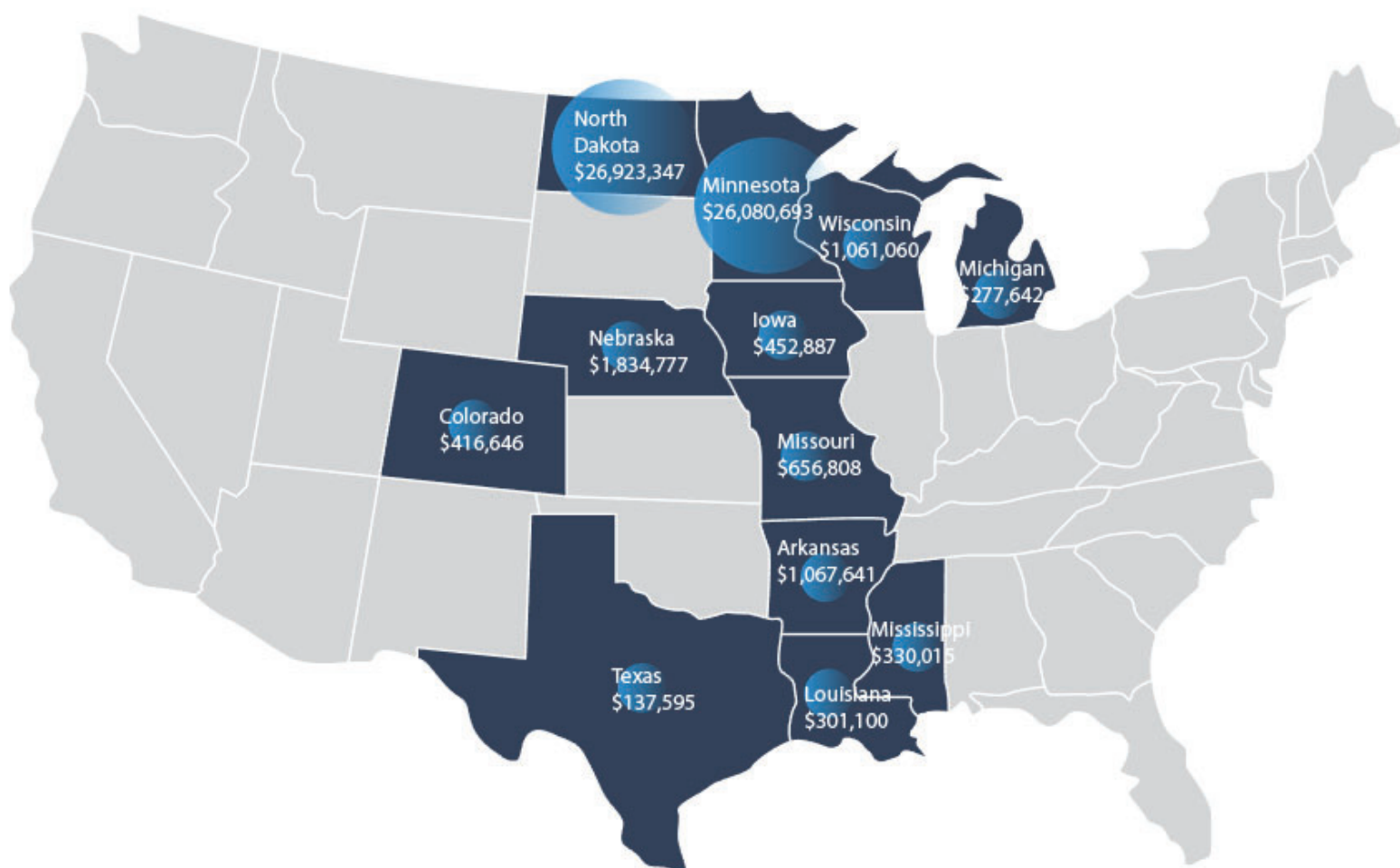
## DIVIDEND COVERAGE RATIO

Dividend Coverage Ratio is Funds from Operations (FFO) divided by dividends paid to share and unit holders.





## NET OPERATING INCOME BY STATE



## TOTAL ANNUAL SHAREHOLDER RETURN

Annualized return is the amount earned by an investment each year over a given time period. These figures show the compounded return throughout the given time frames. The total annualized return calculation includes dividend payments and share price appreciation.

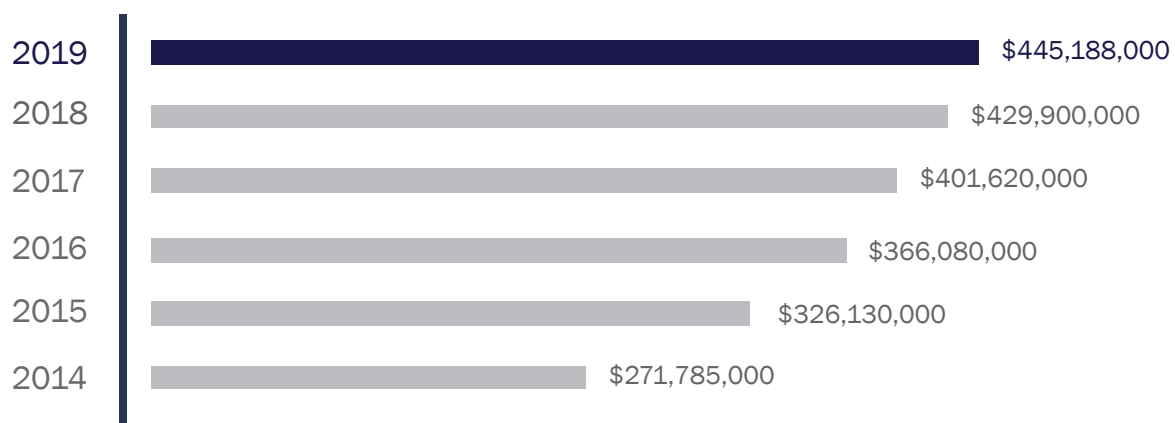


\*This data assumes a 5% dividend reinvestment discount throughout and reinvesting all dividends.

# INVESTOR RETURN

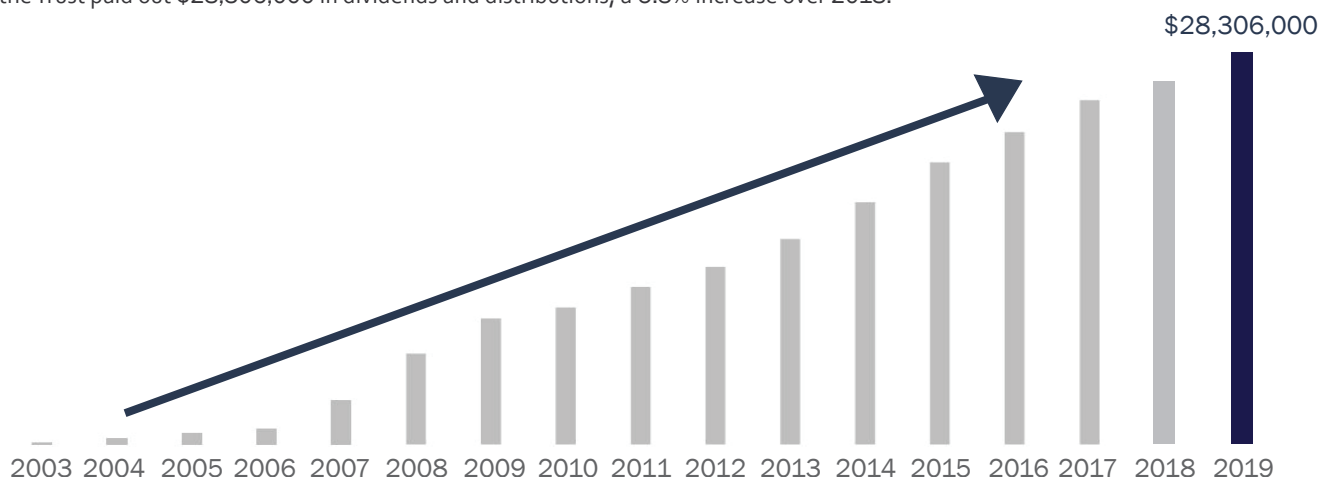
## TOTAL ADJUSTED EQUITY

Total adjusted equity for 2019 is \$445,188,000, which adds back accumulated depreciation and amortization for each respective period of time. From 2014 to 2019 Sterling Multifamily Trust experienced an 63.8% increase.



## TOTAL ANNUAL DIVIDENDS AND DISTRIBUTIONS PAID

Sterling Multifamily Trust has consistently increased the dividends and distributions paid out year after year. In 2019, the Trust paid out \$28,306,000 in dividends and distributions, a 5.3% increase over 2018.



**64.3%**

DIVIDENDS  
REINVESTED

**\$3,293,000**

SHARES PURCHASED  
VIA OPTIONAL CASH

**\$2,023,000**

SHARES/UNITS  
REDEEMED

**1,505**

TOTAL INVESTORS



**5.50%**

DIVIDEND YIELD

DIVIDENDS PER  
SHARE INCREASED  
FROM \$1.0175 IN 2018  
TO

**\$1.045**

IN 2019,  
A 2.7% INCREASE

SHARE PRICE  
INCREASED FROM  
\$18.50 IN 2018 TO

**\$19.00**

IN 2019,  
A 2.7% INCREASE

NET INCOME PER  
SHARE DECREASED  
FROM \$0.84 IN 2018 TO

**\$0.60**

IN 2019,  
A 29% DECREASE

# BOARD OF TRUSTEES

Sterling Multifamily Trust operates under the direction of our Board of Trustees. The Board is responsible for the overall management and control of our affairs. Our Trustees have decades of business, real estate, property management, banking and finance experience. Each board member is also a shareholder. The Board is deeply involved in the Trust's risk management. The Board receives regular reports from Management, which include consideration of operational, financial, legal, regulatory and strategic risks facing the Trust and Partnership.



BRUCE FURNESS



KENNETH REGAN



JAMES HANSEN

## EXECUTIVE COMMITTEE

BRUCE FURNESS\*  
JAMES HANSEN  
TIMOTHY HUNT  
RICHARD SAVAGEAU  
JAMES WIELAND



TIMOTHY HAUGEN



TIMOTHY HUNT



MICHELLE KORSMO

## AUDIT COMMITTEE

JAMES HANSEN  
TIMOTHY HAUGEN  
TIMOTHY HUNT\*  
LANCE WOLF

## DISCLOSURE COMMITTEE

TIMOTHY HAUGEN  
MICHELLE KORSMO  
LANCE WOLF\*



RICHARD SAVAGEAU



JAMES WIELAND



LANCE WOLF

## NOMINATION AND GOVERNANCE COMMITTEE

BRUCE FURNESS  
MICHELLE KORSMO  
RICHARD SAVAGEAU\*  
JAMES WIELAND

\*Indicates Committee Chair



# EXECUTIVE OFFICERS



**KENNETH REGAN**  
Chief Executive Officer



**RYAN DOWNS**  
President & Secretary



**ERICA CHAFFEE**  
Chief Financial Officer



**JOEL THOMSEN**  
Chief Investment Officer



**DELLWOOD ESTATES**



**STONEFIELD APARTMENTS**

# INVESTOR RELATIONS

Sterling Multifamily Trust invests in multifamily (apartment) properties. Our work starts with our Mission: to provide investors the opportunity of long-term ownership in lower risk and well-managed income producing real estate. It declares our purpose and serves as the gold standard against which we weigh our decisions. It is enduring and drives us to consistently look forward.

Sterling Multifamily Trust files periodic and current reports with the Securities and Exchange Commission (SEC). Copies are available on the SEC's website and on Sterling Multifamily Trust's website at [www.smftrust.com](http://www.smftrust.com). To request a hard copy of our financial reports without charge, please call, email or write to:

Sterling Multifamily Trust  
Investor Relations  
1711 Gold Drive South, Suite 100  
Fargo, ND 58103  
(877) 269-1031  
[smftir@sretrust.com](mailto:smftir@sretrust.com)

Communications regarding shareholder address changes, stock transfers, changes of ownership, payment of dividends or other account services can also be directed to the contact information listed above.

## ANNUAL MEETING

We sincerely hope you can join us for this year's annual meeting on June 25, 2020, at 6:00 p.m. at the Holiday Inn, Fargo, North Dakota. Due to Covid-19, our annual meeting may be hosted virtually. Communication regarding any alternative meeting arrangements will be provided to shareholders as promptly as practicable.

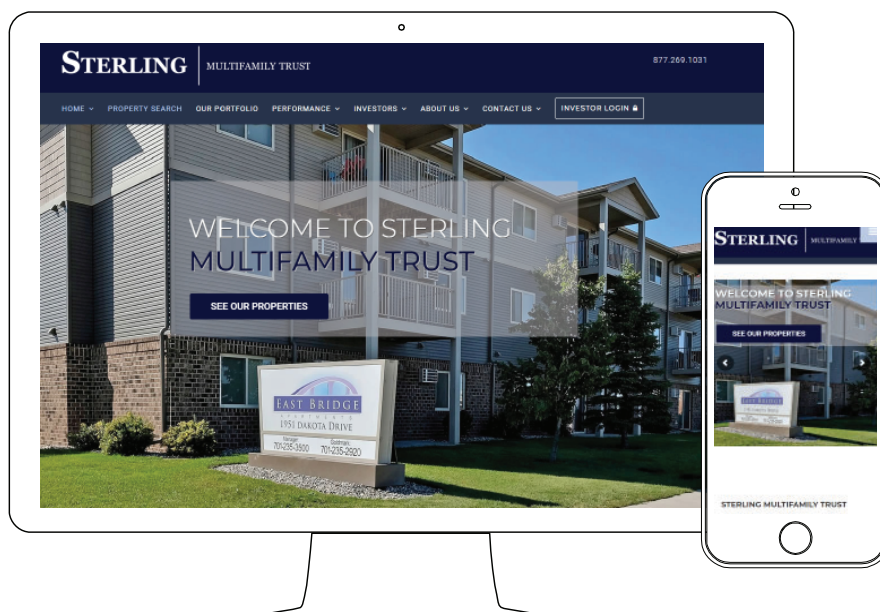
If you have any questions regarding the annual meeting, please contact our office by calling (877) 269-1031.

We look forward to seeing you in June!

## VISIT US ONLINE!

For more information about the Trust, visit us online at:

[www.smftrust.com](http://www.smftrust.com)



# AUDITED FINANCIALS

December 31, 2019

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**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, 2019**
- 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 000-54295

**Sterling Real Estate Trust**

d/b/a Sterling Multifamily Trust

(Exact name of registrant as specified in its charter)

North Dakota  
(State or other jurisdiction of  
incorporation or organization)

1711 Gold Drive South, Suite 100  
Fargo, North Dakota  
(Address of principal executive offices)

90-0115411  
(I.R.S. Employer  
Identification Number)

58103  
(Zip Code)

(701) 353-2720

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:  
Common Shares of Beneficial Interest

(Title of Class)

Title of each class:	Trading Symbol	Name of each exchange on which registered:
Common Shares, par value \$0.01 per share	N/A	N/A

**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 Exchange Act. ☐ Yes ☒ No

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

Indicate by checkmark whether the Registrant has submitted electronically, every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit such files). ☒ Yes ☐ No

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

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input checked="" type="checkbox"/>
Emerging growth company	<input type="checkbox"/>		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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 common shares of beneficial interest held by non-affiliates as of June 30, 2019 was approximately \$153,008,964, computed by reference to the price at which the common shares was last sold as of such date.

Indicate the number of shares outstanding of each of the issuer's classes of common shares, as of the latest practicable date.

Class	Outstanding at March 6, 2020
Common Shares of Beneficial Interest, \$0.01 par value per share	9,562,818

Documents Incorporated by Reference: Portions of Sterling's Proxy Statement for its 2020 Annual Meeting of Shareholders, which Sterling intends to file with the Securities and Exchange Commission within 120 days after the end of Sterling's fiscal year ended December 31, 2019, are incorporated by reference into Part III (Items 10, 11, 12, 13 and 14) of this Annual Report on Form 10-K to the extent described herein. If Sterling does not file its Proxy Statement on or before 120 days after the end of its 2019 fiscal year, Sterling will file the required information in an amendment to this Annual Report on Form 10-K.

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## **Sterling Real Estate Trust**

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## NOTE REGARDING FORWARD-LOOKING STATEMENTS

Certain statements included in this Annual Report on Form 10-K and the documents incorporated into this document by reference contain certain “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended (the “Securities Act”), and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Such forward-looking statements include statements regarding our plans and objectives, including, among other things, our future financial condition, anticipated capital expenditures, anticipated dividends and other matters. Forward-looking statements are typically identified by the use of terms such as “may,” “will,” “should,” “expect,” “intend,” “plan,” “anticipate,” “estimate,” “believe,” “continue,” “predict,” “potential” or the negative of such terms and other comparable terminology. These statements are only predictions and are not historical facts. Actual events or results may differ materially.

The forward-looking statements included herein are based on our current expectations, plans, estimates and beliefs that involve numerous risks and uncertainties. Assumptions relating to the foregoing involve judgments with respect to, among other things, future economic, competitive and market conditions and future business decisions, all of which are difficult or impossible to predict accurately and many of which are beyond our control. Any of the assumptions underlying the forward-looking statements contained herein could be inaccurate. Although we believe the expectations reflected in such forward-looking statements are based on reasonable assumptions, we cannot assure readers that the forward-looking statements included in this filing will prove to be accurate. The accompanying information contained in this Annual Report on Form 10-K, including, without limitation, the information set forth under the section entitled “Risk Factors” in Item 1A, identifies important additional factors that could materially adversely affect actual results and performance. We undertake no obligation to update or revise forward-looking statements to reflect changed assumptions, the occurrence of certain unanticipated events or changes to future operating results.

## PART I

*All dollar amounts in this Form 10-K are stated in thousands with the exception of share and per share amounts, unless otherwise indicated.*

## ITEM 1. BUSINESS

### GENERAL

Sterling Real Estate Trust (“we,” “us,” “our,” “Company,” “Trust” or “Sterling”) is a real estate investment trust (“REIT”). Sterling is registered in North Dakota as an unincorporated business trust in December, 2002. References in this Annual Report on Form 10-K to the “Company,” “Sterling,” “we,” “us,” or “our” include consolidated subsidiaries, unless the context indicates otherwise. As a REIT, we are not subject to U.S. federal income taxation as long as we satisfy certain requirements, principally relating to the nature of our income, the level of our dividends and other factors. At December 31, 2019, we owned directly or through our operating partnership, 173 properties in 11 states.

### UPREIT Structure

We operate as an Umbrella Partnership Real Estate Investment Trust, which is a REIT that holds all or substantially all of its assets through a partnership which the REIT controls as general partner. Therefore, we conduct substantially all of our investment activities and hold all or substantially all of our assets through our operating partnership Sterling Properties, LLLP. We control the operating partnership as the general partner and own approximately 34.63% of the operating partnership as of December 31, 2019. For purposes of satisfying the asset and income tests for qualification as a REIT for tax purposes, our proportionate shares of the assets and income of our operating partnership are deemed to be our assets and income.

We use this UPREIT structure to facilitate acquisitions of real estate properties. A sale of property directly to a REIT is generally a taxable transaction to the property seller. However, in an UPREIT structure, if a property seller exchanges the property for limited partnership units, the seller may defer taxation of gain in such exchange until the seller resells its

limited partnership units or exchanges its limited partnership units for the REIT's common stock. By offering the ability to defer taxation, we may gain a competitive advantage in acquiring desired properties over other buyers who cannot offer this benefit. In addition, investing in our operating partnership, rather than directly in Sterling, may be more attractive to certain institutional or other investors due to their business or tax structure. If an investor is interested in making a substantial investment in our operating partnership, our structure provides us the flexibility to accommodate different terms for each investment, while applicable tax laws generally restrict a REIT from charging different fee rates among its shareholders. Finally, if our shares become publicly traded, the former property seller may be able to achieve liquidity for the investment in order to pay taxes

### **Operating Partnership**

Our operating partnership, Sterling Properties, LLLP, was formed as a North Dakota limited liability limited partnership on April 25, 2003 to acquire, own and operate properties on our behalf. The operating partnership holds a diversified portfolio of multifamily dwellings and commercial properties located principally in the upper and central Midwest United States.

Since our formation, our focus has consisted of owning and operating income-producing real estate properties. In 2006, we held 23 total properties approximating \$56,265 in total assets. Between 2007 and 2019, we focused extensively on strengthening the multifamily component of our portfolio, acquiring properties directly or through UPREIT transactions. A majority of these multifamily properties are located in North Dakota. Our portfolio has grown to 173 properties, approximating \$699,686 in total assets, and book equity, including noncontrolling interests, of approximately \$279,047 as of December 31, 2019. As of December 31, 2019, our portfolio contained approximately 9,852 apartment units and 1,662,000 square feet of leasable commercial space.

### **OUR PEOPLE**

We do not have any employees. Instead, we rely on our external Advisor to conduct our day-to-day affairs.

#### **Our Advisor**

Our external Advisor is Sterling Management, LLC, a North Dakota limited liability company formed on November 14, 2002. Our Advisor is responsible for managing our day-to-day affairs and for identifying, acquiring and disposing investments on our behalf. The Advisor is owned in part by Kenneth Regan, a trustee and our Chief Executive Officer, by an entity controlled by James Wieland, also one of our trustees, by Joel Thomsen, our Chief Investment Officer, and by Ryan M. Downs, our President. In addition, Messrs. Regan, Wieland, Thomsen and Downs serve on the Board of Governors of the Advisor. From 2007 to 2019, our Advisor's staff increased in number and expertise, growing from four to 26 full-time employees. On February 1, 2020, Joel Thomsen was appointed Chief Executive Officer of our Advisor. Kenneth Regan will still serve as Chairman of the Board of Governors for our Advisor.

In September 2019, Sterling Management, LLC onboarded a projects management department that consisted of nine new employees. This team is responsible for overseeing and managing all capital projects that are being completed on the portfolio's 173 properties, oversight and management, that was previously being completed by our third-party property managers. We expect the internal management of capital projects will allow for efficiencies in how capital projects are managed as well as provide better transparency operationally between all departments of Sterling Management. In addition, the services will allow Sterling Management to provide a complete asset management service to the properties. Prior to onboarding, the Trust paid a project management fee to the third-party property managers. Commencing September 1, 2019, the project management fee calculated on projects is paid to Sterling Management, LLC.



## Our Audit Committee

Our Audit Committee was established by the Board of Trustee's to assist the Board in fulfilling its fiduciary responsibilities. The Audit Committee assists the Board by overseeing the integrity of the Trust's financial statements, financial reporting processes, internal accounting and financial controls and the annual independent audit of the Trust's financial statements. The Audit Committee also oversees the establishment and maintenance of processes to assure the Trust's compliance with all applicable laws, regulations and Trust policy. In performing its work, it is the Audit Committee's responsibility to foster free and open means of communication between the Trustees, the independent auditors and the Trust's financial managers. Our Audit Committee is currently comprised of Timothy Hunt (Chairman), Lance Wolf, James Hansen and Timothy Haugen.

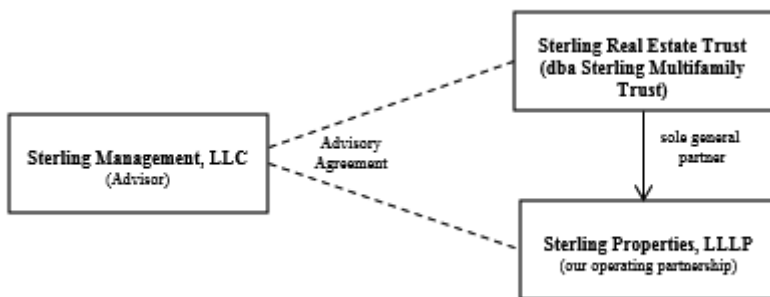
## Our Board of Trustees and Executive Officers

We operate under the direction of our Board of Trustees, the members of which are accountable to us and our shareholders. Our trustees are elected annually by our shareholders. In addition, the Board has a duty to supervise our relationship with the Advisor and evaluates the performance of and fees paid to the Advisor on an annual basis. The Advisory Agreement was approved by the Board of Trustees (including all the independent trustees) on March 28, 2019, effective April 1, 2019 until March 31, 2020. Our Board of Trustees has provided investment guidance for the Advisor to follow and must approve each investment recommended by the Advisor. Currently, we have nine members on our board, seven of whom are independent.

Although we have executive officers, we do not have any paid employees. Our President, Chief Executive Officer, Chief Investment Officer, Chief Financial Officer, Treasurer and Secretary are also officers, employees, owners or governors of our Advisor. Among others, such executive officers oversee our Advisor's day-to-day operations with respect to us. However, when doing so, such executive officers are acting on behalf of our Advisor in performing the Advisor's obligations under the Advisory Agreement. Generally, the only services performed by our executive officers are those required by law or regulation, such as executing documents as required by North Dakota law and providing certifications required by the federal securities laws.

## Organizational Structure

The following chart shows our structure:



- (1) The Advisor is owned in part by our Chief Executive Officer and Trustee Mr. Kenneth P. Regan (36.578%), by Wieland Investments, LLLP, an entity controlled by our Trustee Mr. James S. Wieland (31.578%), by our Chief Investment Officer Joel Thomsen (10.00%) and by our President Ryan M. Downs (3.00%). In addition, Mr. Regan serves as the Chief Executive Officer and Chairman of the Board of the Advisor, and Messrs. Wieland, Thomsen and Downs serve on the Board of Governors of the Advisor.
- (2) The Advisor serves as both our and our operating partnership's advisor. The Advisor does not own any of our shares. Messrs. Regan and Wieland beneficially own approximately 1.57% and 2.47%, respectively, of our shares as of December 31, 2019.

- (3) We control the operating partnership as the general partner and own approximately 34.63% of the operating partnership as of December 31, 2019. Mr. Regan and Mr. Wieland beneficially owned and had voting power over approximately 16.7% and 8.2%, respectively, of the operating partnership as of December 31, 2019.

## **OUR CORE INVESTMENT OBJECTIVES AND STRATEGY**

### **Investment Objectives**

Our primary investment objectives are to:

- acquire quality real estate properties or interests in real estate properties that can provide stable cash flow for distribution to our shareholders, preservation of capital and realization of long-term capital appreciation upon the sale of such properties;
- offer an investment option in which the value of the common shares is correlated to real estate as an asset class rather than traditional asset classes such as stocks and bonds; and
- provide a hedge against inflation through use of month-to-month rentals or short-term and long-term lease arrangements with rental properties tenants.

We may change our investment objectives only with the approval of holders of a majority of the outstanding common shares.

### **Investment Strategy**

Our current investment strategy is to acquire and hold ownership interests in multifamily residential properties primarily located in the central corridor of the contiguous 48 states. There is no current plan for our existing commercial properties (industrial, medical, office and retail) in regard to retention or disposition.

The majority of our acquisitions are located in or near metropolitan areas. However, there is no limitation on the geographic areas in which we may acquire targeted investments.

We may acquire portfolios of real estate properties held by individual owners and real estate properties held by funds, including hedge funds. We anticipate such property owners will primarily sell the properties in exchange for limited partnership interests of the operating partnership.

We may make investments alone or together with other investors, including with affiliates of the Advisor, through holding company structures or joint ventures, real estate partnerships, tenant-in-common deals, REITs or other collective investment vehicles.

### **Investment Guidance**

Our Board of Trustees has provided investment guidance to the Advisor to direct our investment strategy. Changes to our investment guidance must be approved by our Board. The Advisor has been authorized to execute (1) commercial and multifamily real estate property acquisitions and dispositions (2) investments in other real estate related assets, in each case so long as such investments are approved by our Board and (3) acquiring property for the purposes of future development. Our Board will at all times have ultimate oversight over our investments and may change from time to time the scope of authority delegated to our Advisor with respect to acquisition and disposition transactions. Our current investment guidance is that future real estate investments be limited to multifamily apartment properties. We currently have no plans with respect to our commercial properties in regard to retention or disposition.

### ***Investments in Real Estate Properties***

Our investment guidance provides we will primarily invest in existing or newly constructed real estate properties and interests in real estate properties by acquiring direct ownership or ownership interests through equity interests or other joint venture structures. We may also invest in other real estate property types, including undeveloped land or other

development opportunities if the land is acquired for the purpose of producing rental or other operating income and either development or construction is in process or development or construction is planned. We primarily invest in real estate properties with existing rent and expense schedules or newly constructed properties with predictable cash flows. We concentrate our efforts on real estate properties located primarily in North Dakota and Minnesota, the central corridor of the contiguous 48 states and in or near metropolitan areas.

#### ***Investments in Real Estate Related Assets***

Our guidelines provide we may invest in real estate related assets. These assets include securities of other companies engaged in real estate activities, mortgage-backed securities and conventional mortgage loans. To date, our investment in such assets have been nominal. We do not anticipate such investment amounts to be material or long term.

#### ***Receivables***

Receivables consist primarily of amounts due for rent and tenant charges. Accounts receivable are carried at original amounts billed. The operating partnership reviews collectability of charges under its tenant operating leases on a quarterly basis. In the event that collectability is deemed not probable for any tenant charges, beginning with the adoption of ASC 842 as of January 1, 2019, the operating partnership recognizes an adjustment to rental income. Prior to the adoption of ASC 842, the Company recognized a provision for uncollectible amounts or a direct write-off of the specific rent receivable.

Notes receivable are issued periodically and are secured and interest bearing. Receivables are included in “Other assets” in the accompanying consolidated balance sheets.

#### ***Investments in Cash, Cash Equivalents and Other Short-Term Investments***

We may invest in cash, cash equivalents and other short-term investments. Consistent with the rules applicable to qualification as a REIT, such investments may include investments in the following: money market instruments; short-term debt instruments, such as commercial paper, certificates of deposit, bankers’ acceptances, repurchase agreements, interest-bearing time deposits and corporate debt securities; corporate asset-backed securities; and U.S. government or government agency securities. We do not expect to increase such investments in the near future.

### **SEGMENT DATA**

We report our results in two reportable segments: residential and commercial properties. Our residential properties include multifamily. Our commercial properties include retail, office, industrial, restaurant and medical properties. We assess and measure operating results based on net operating income (“NOI”), which we define as total real estate segment revenues less real estate expenses (which consist of real estate taxes, property management fees, utilities, repairs and maintenance, insurance and direct administrative costs). We believe NOI is an important measure of operating performance even though it should not be considered an alternative to net income or cash flow from operating activities. NOI is unaffected by financing, depreciation, amortization, legal and professional fees and certain general and administrative expenses.

### **COMPETITION**

Our properties are located in highly competitive real estate markets. The number of competitive properties in a particular area could have a material adverse effect on our ability to lease space and the amount of rent we can charge at our properties. We compete with many property owners, such as corporations, limited partnerships, individual owners, other real estate investment trusts, insurance companies and pension funds.

Our competition also consists of other owners and developers of multifamily and commercial properties who are trying to attract tenants to their properties. We also compete with other real estate investors such as individuals, partnerships, corporations and other REITs to acquire properties that meet our investment objectives. This competition influences our ability to acquire properties and the prices that we may pay for those properties. We believe, however, that the diversity of

our investments, the experience and abilities of our management and the quality of our assets affords us some competitive advantages that have in the past, and should in the future, allow us to operate our business successfully despite the competitive nature of our business.

Generally, there are multifamily and other similar commercial properties within relatively close proximity to each of our properties. Regarding our retail properties, in addition to competitor retail properties, we and our tenants face increasing competition from outlet malls, internet shopping websites, discount shopping clubs, catalog companies, direct mail and telemarketing.

## **ENVIRONMENTAL MATTERS AND GOVERNMENT REGULATION**

As an owner of real estate, we are subject to various environmental laws, rules and regulations adopted by various governmental bodies or agencies. These laws and regulations generally govern wastewater discharges, air emissions, the operation and removal of underground and above-ground storage tanks, the use, storage, treatment, transportation and disposal of solid hazardous materials, the remediation of contaminated property associated with the disposal of solid and hazardous materials and other health and safety-related concerns. Under these laws, a current or previous owner or operator of real estate may be liable for the costs of removal or remediation of certain hazardous or toxic substances released at a property, and may be held liable to a governmental entity or to third parties for property damage or personal injuries and for investigation and clean-up costs incurred in connection with any contamination. We could be subject to liability in the form of fines or damages for noncompliance with these laws and regulations, and some environmental laws create a lien on a contaminated site in favor of the government for damages and costs it incurs in connection with the contamination. Some of these laws and regulations may impose joint and several liability on residents, owners or operators for the costs of investigation or remediation of contaminated properties, regardless of fault or the legality of the original disposal. In addition, the presence of these substances, or the failure to properly remediate these substances, may adversely affect our ability to sell or rent the property or to use the property as collateral for future borrowing. Compliance with new or more stringent laws or regulations or stricter interpretation of existing laws may require material expenditures by us.

In addition we are subject to many other laws and governmental regulations applicable to our properties, and changes in the laws and regulations, or in their interpretation by agencies and the courts, occur frequently. Under the Americans with Disabilities Act of 1990 (the “ADA”), all places of public accommodation are required to meet certain federal requirements related to access and use by disabled persons. The Fair Housing Amendments Act of 1988 (the “FHAA”) requires apartment communities first occupied after March 13, 1991, to be accessible to the handicapped and prohibits housing discrimination based upon familial status. The Housing for Older Persons Act (“HOPA”) provides age-based discrimination exceptions for housing developments qualifying as housing for older persons. Non-compliance with ADA, FHAA or HOPA could result in the imposition of fines, awards of damages to private litigants, payment of attorneys’ fees and other costs to plaintiffs, substantial litigation costs and substantial costs of remediation. We believe our properties which are subject to ADA, FHAA and/or HOPA are substantially in compliance with their present requirements.

Compliance with these laws, rules and regulations has not had a material adverse effect on our business, assets, or results of operations, financial condition or ability to pay dividends. We do not believe our existing portfolio as of December 31, 2019 will require us to incur material expenditures to comply with these laws and regulations. However, we cannot assure that future laws, ordinances or regulations will not impose any material liability, or that the current environmental condition of our properties will not be affected by the operations of tenants, by the existing condition of the land, by operations in the vicinity of the properties, such as the presence of underground storage tanks, or by the activities of unrelated third parties.

## **AVAILABLE INFORMATION**

We electronically file our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, proxy and information statements and all amendments to these filings with the Securities and Exchange Commission (“SEC”). The public may read any materials filed by us with the SEC on the internet site maintained by the SEC at [www.sec.gov](http://www.sec.gov). We also maintain an internet site at [www.sretrust.com](http://www.sretrust.com), which includes the reports and other documents we file with the SEC. These reports are available as soon as reasonably practicable after such material is electronically filed

or furnished to the SEC. This reference to our website is not intended to incorporate information found on the website into this filing.

## **ITEM 1A. RISK FACTORS**

### **Summary of Risk Factors**

#### **Risks Related to Sterling Real Estate Trust**

- Common shares of beneficial interest represent an investment in equity only, and not a direct investment in our assets. Therefore, common shareholders will hold only an indirect interest in our assets.
- Our results are dependent on amounts received from the leasing and resale of investments, which is subject to market and economic changes. If income is insufficient to meet our capital needs, our ability to carry out our business plans could be adversely affected.
- We may raise additional funds in the future to fund our capital needs, which may not be available on acceptable terms if at all.
- Our success is based on continuing to locate and hold suitable real estate investments, and failure of our Advisor to locate additional suitable properties or the unsuccessful operation of our existing real estate investments could adversely affect our operations and our ability to pay dividends.
- Our Board of Trustees may have to make expedited decisions on whether to invest in certain properties or real estate-related assets, including prior to receipt of detailed information on the investment.
- We face competition from other real estate investors for suitable properties, and may not be successful in our attempts to acquire desirable properties
- We may change our investment and operational policies without shareholder consent, and such changes could increase our exposure to additional risks.
- There can be no assurance dividends will be paid or increase over time
- We may pay dividends from sources other than our cash flow from operations, which could subject us to additional risks.
- Dividends may include a return of capital, and shareholders may be required to recognize capital gain on distributions
- We depend on certain executive officers and trustees, and the loss of such persons may delay or hinder our ability to carry out our investment strategies
- Our systems may not be adequate to support our growth, and our failure to successfully oversee our portfolio of real estate investments could adversely affect our results of operation.
- Cybersecurity risks and cyber incidents may adversely affect our business by causing a disruption to our operations, a compromise or corruption of our confidential information, and/or damage to our business relationships, all of which could negatively impact our financial results.

#### **Risks Related to Our Structure**

- There are limitations on ownership of our common shares of beneficial interest, which could discourage a takeover transaction even if it is beneficial to our shareholders.
- Our shareholders may experience dilution if we or our operating partnership issues additional securities
- Our security holders have limited control over our operation, and the Board of Trustees has the sole power to appoint and terminate the Advisor.
- Shareholders have no role in determining our investments and must rely on our Advisor and oversight by the Board of Trustees
- We may issue common shares of beneficial interest with more favorable terms than the outstanding shares without shareholder approval
- Shareholders could incur current tax liability on dividends they elect to reinvest in our shares, and may have to use separate funds to pay their tax liability

- Our trustees, officers, Advisor and its affiliates have limited liability to us and our shareholders and may have the right to be indemnified under certain conditions.
- There may be conflicts of interest between us and our shareholders on one side and our operating partnership and its limited partners on the other side.
- If we are deemed to be an investment company under the Investment Company Act, our shareholders' investment return may be reduced.
- There is no public trading market for our shares, nor do we expect one to develop, which may negatively impact a shareholder's ability to sell their shares and the price at which shares may be sold.
- The estimated value of our common stock is based on a number of assumptions and estimates that may not be accurate and is also subject to a number of limitations
- Shareholders may not be able to have their shares redeemed under the Share Redemption Plan, and if shareholders do redeem their shares, they will not receive the current value of the shares
- There will be transfer restrictions on the shares, and we do not plan to register the shares for resale.

#### **Risks Related to Our Status as a REIT and Related Federal Income Tax Matters**

- If we fail to continue to qualify as a REIT, we would incur additional tax liabilities that would adversely affect our operations and our ability to make distributions and could result in a number of other negative consequences.
- As a REIT, we may be subject to tax liabilities that reduce our cash flow
- We may be forced to borrow funds on a short-term basis, to sell assets or to issue securities to meet the REIT minimum distribution requirement or for working capital purposes.
- If our operating partnership does not qualify as a partnership, its income may be subject to taxation, and we would no longer qualify as a REIT.
- We have transfer restrictions on our shares that may limit offers to acquire substantial amounts of the trust's shares at a premium
- Complying with REIT requirements may restrict our ability to operate in a way to maximize profits
- Complying with REIT requirements may force us to forego or liquidate otherwise attractive investments which could negatively impact shareholder value
- Gains from asset sales may be subject to a 100% prohibited transaction tax, which tax could reduce the trust's available assets and reduce shareholder value.
- Ordinary dividends payable by REITs generally are taxed at the higher ordinary income rate which could reduce the net cash received by shareholders as a result of an investment in the trust and may be detrimental to our ability to raise additional funds through the sale of our common shares.
- Changes in legislative or other actions affecting REITs may adversely affect our status as a REIT.
- Our Board of Trustees may revoke our REIT election without shareholder approval, and we would no longer be required to make distributions of our net income.

#### **Risks Related to Tax-Exempt Investors**

- Common shares may not be a suitable investment for tax-exempt investors.
- Under certain circumstances, tax-exempt shareholders may be subject to unrelated business taxable income, which could adversely affect such shareholders.

#### **Risks Related to Our Relationship with the Advisor and Its Affiliates**

- We depend on our Advisor for the successful operations of the REIT, and if required, we may not be able to find a suitable replacement advisor.
- The termination or replacement of the Advisor could trigger a default or repayment event under financings.
- The Advisor may not be able to retain its key employees, which could adversely affect our ability to carry out our investment strategies.
- Payment of fees and expenses to the Advisor reduces the cash available for dividends.

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

- Our performance could be adversely affected by the general risks involved in real estate investments.



- Market disruptions may significantly and adversely affect our financial condition and results of operations.
- Insufficient geographic diversity of our real estate investments could adversely affect our operating results if economic changes impact those real estate markets where we own significant assets
- We face numerous risks associated with property acquisitions which could adversely affect our operating results.
- We may invest in undeveloped real property, which requires us to pay expenses prior to receiving any income on the property.
- We may acquire multiple properties in a single transaction, which may adversely affect our operations through the inclusion of less desirable investments or financing requirements greater than we would otherwise be willing to incur.
- We may invest in co-ventures, where our co-venture partners, co-tenants or other partners in co-ownership arrangements could take actions that decrease the value of a real estate investment and lower our overall return.
- We could experience difficulties or delays renewing leases or re-leasing space, which will increase our costs to maintain such properties without receiving income.
- We could face potential adverse effects if a commercial tenant is unable to make timely rental payments, declares bankruptcy or become insolvent.
- If our reserves for making capital improvements on our real estate investments are insufficient, we may be required to defer necessary capital improvements which could negatively affect our revenues.
- Properties will face significant competition for tenants, which could limit our profitability
- Increased affordability of single-family homes could limit our ability to retain residents, lease apartment units or increase or maintain rents
- Investments in real estate are illiquid, and we may not be able to resell a property on terms favorable to us
- Valuations and appraisals of our investments may not necessarily correspond to realizable value.
- Uninsured losses related to real estate investments may adversely affect our results of operation
- Discovery of toxic mold on our properties may adversely affect our results of operation
- We may acquire a property or properties “AS IS,” which increases the risk of an investment that requires us to remedy defects or costs without recourse to the prior owner.
- We may engage in leaseback transactions, which involve risks including a failure to qualify as a REIT.
- We rely on affiliated and outside property managers to properly manage and lease our properties

#### **Risks Related with Our Indebtedness and Financing**

- Current market conditions could adversely affect our ability to obtain financing
- We will incur mortgage indebtedness and other borrowings, which will increase our business risks
- We could face difficulties in refinancing loans involving balloon payment obligations.
- The phase out of LIBOR and transition to SOFR as a benchmark interest rate could have adverse effects.
- Derivatives and hedging activity could adversely affect cash flow.
- Lenders may require restrictive covenants relating to our operations, which may adversely affect our flexibility and our ability to achieve our investment objectives.
- Increases in interest rates on variable rate debt incurred by us will reduce cash available for dividends
- Complying with REIT requirements may limit our ability to hedge liabilities through tax-efficient means which could adversely affect our operations
- We may structure acquisitions of property in exchange for limited partnership units in our operating partnership on terms that could limit our liquidity or our flexibility

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

- Investments in real estate related equity assets could involve higher risks than other investments, which could adversely affect our operations and ability to make dividend payments
- There are conflicts of interest in our relationship with the Advisor and its affiliates and several trustees, which could adversely affect our operations and business operations (Allocation of time and effort) (Division of Loyalty) (Allocation of Investment Opportunities)

## **Risks Related to Sterling Real Estate Trust**

***Our common shares of beneficial interest represent an investment in equity only, and not a direct investment in our assets. Therefore, common shareholders will hold only an indirect interest in our assets.***

The common shares of beneficial interest represent an equity interest only in us, not in any of our assets or our operating partnership's real estate or other investments. Our principal asset is our equity interest in the operating partnership. Neither the Advisor nor any of its managers or affiliates have any obligation with respect to the payment of dividends to our shareholders or the return of investments made to us by the shareholders.

***Our results are dependent on amounts received from the leasing and resale of investments, which are subject to market and economic changes. If income is insufficient to meet our capital needs, our ability to carry out our business plans could be adversely affected.***

Our purpose is to acquire and hold real estate investments as long-term investments before we resell the investments to maximize anticipated appreciation for our shareholders. The primary income that will be generated by us will be the profits, if any, from the operation or holding of the real estate and upon the resale of the investments. If circumstances arise which cause an investment to remain at its current value or decrease in value, we may generate less income than anticipated.

***We may seek to raise additional funds in the future to fund our capital needs, and such funds may not be available on acceptable terms if at all.***

We may need to raise additional capital in the future in order to fulfill our business plans. The timing and amount of our future capital needs will depend on a number of factors, including the revenue generated by the operation of our real estate investments, when and if the properties will appreciate in value, the resale price of the properties and other investments, our future operating expenses and required capital outlays. There can be no assurance additional financing will be available when needed on terms favorable to us, if at all.

Further, we may be required to raise additional capital and sell additional securities in the future on terms which are more favorable to those investors than the terms under which our current securityholders acquired their investments. If adequate funds are not available or are not available on acceptable terms, our ability to fund our current business plans and to acquire additional real estate and other investments could be significantly limited. Such limitation could have a material adverse effect on our results.

***Our success is based on continuing to locate and hold suitable real estate investments, and failure of our Advisor to locate additional suitable properties or the unsuccessful operation of our existing real estate investments could adversely affect our operations and our ability to pay dividends.***

Our ability to achieve our investment objectives and to pay dividends to our shareholders and distributions to unitholders is dependent upon the performance of our Advisor in locating suitable investments and appropriate financing arrangements for us as well as on the successful management of our properties after acquisition. We currently own, through the operating partnership, the properties described under Item 2 — Properties. We cannot be sure our Advisor will be successful in locating suitable investments on financially attractive terms, or be certain that operation of the properties will avoid the risks attendant to real estate acquisitions, such as:

- The risk properties may not perform in accordance with expectations, including projected occupancy and rental rates;
- The risk we may have underestimated the cost of improvements or repairs required to bring or keep an acquired property up to or at standards established for its intended use or its intended market position.

***Our Board of Trustees may have to make expedited decisions on whether to invest in certain properties, including prior to receipt of detailed information.***

Our Board of Trustees may be required to make expedited decisions in order to effectively compete for the acquisition of desirable properties and other assets. In such cases, our Advisor and Board of Trustees may not have access to detailed information regarding real estate investments, such as physical characteristics, environmental matters, zoning regulations or other local conditions affecting the real estate investment, at the time of making an investment decision to pay a non-refundable deposit and to proceed with an acquisition. In addition, the actual time period during which our Advisor will be allowed to conduct due diligence may be limited. Therefore, there can be no assurance our Advisor and Board of Trustees will have knowledge of all circumstances that may adversely affect an investment.

***We face competition from other real estate investors for suitable properties, and may not be successful in our attempts to acquire desirable properties.***

The multifamily and commercial real estate industries are highly competitive, and we face competition for investment opportunities. These competitors may be real estate developers, real estate financing entities, real estate investment trusts, mutual funds, hedge funds, investment banking firms, institutional investors and other entities or investors that acquire real estate and may have substantially greater financial resources than we do. These entities or investors may be able to accept more risk than our Board of Trustees believes is in our best interest. This competition may limit the number of suitable investment opportunities offered or available to us. This competition also may increase the bargaining power of property owners seeking to sell to us, making it more difficult for us to acquire properties or interests in properties. In addition, we believe competition from entities organized for purposes similar to ours may increase in the future.

***We may change our investment and operational policies without shareholder consent, and such changes could increase our exposure to additional risks.***

Generally, the Board of Trustees may change our investment and operational policies, including our policies with respect to investments, acquisitions, growth, operations, indebtedness, capitalization and distributions, at any time without the consent of our shareholders, which could result in our making investments different from, and possibly riskier than, investments made in the past. A change in our investment policies may, among other things, increase our exposure to interest rate risk, default risk and commercial real estate market fluctuations, all of which could materially affect our ability to achieve our investment objectives.

***There can be no assurance dividends or distributions will be paid or increase over time.***

There are many factors that can affect the availability and timing of cash dividends to our shareholders and distributions to unitholders. Dividends and distributions will be based principally on cash available from our real estate and other investments. The amount of cash available for dividends will be affected by many factors, such as our ability to acquire profitable real estate investments and successfully manage our real estate properties and our operating expenses. We can give no assurance we will be able to pay or maintain dividends or distributions or that dividends or distributions will increase over time. Our actual results may differ significantly from the assumptions used by our Board of Trustees in establishing the dividend or distribution rate to our securityholders.

***We may pay dividends or distributions from sources other than our cash flow from operations, which could subject us to additional risks.***

We are permitted to pay dividends and distributions from any source. If we fund dividends or distributions from cash flow from operations or working capital, we will have less funds available for investment in real estate and other investments and our securityholders' overall return may be reduced. Actual cash available for dividends and distributions may vary substantially from the estimates of our Board of Trustees. Because we may receive income from interest or rents at various times during our fiscal year, dividends and distributions paid may not reflect our income earned in that particular period. In these instances, we may obtain third party financing to fund our dividends or distributions, causing us to incur additional

interest expense. We may also fund such dividends and distributions from the sale of assets or additional securities. Any of these actions could potentially negatively affect future results of operations.

***Dividends may include a return of capital, and shareholders may be required to recognize capital gain on distributions.***

Dividends payable to shareholders may include a return of capital. To the extent dividends exceed cash flow from operations, a shareholder's basis in our shares will be reduced and, to the extent dividends exceed a shareholder's basis, the shareholder may recognize capital gain and be required to make tax payments.

***We depend on certain executive officers and trustees, and the loss of such persons may delay or hinder our ability to carry out our investment strategies.***

Our future success substantially depends on the active participation of James Wieland, one of our trustees, Kenneth Regan, our Chief Executive Officer and a trustee, Ryan Downs, our President and Joel Thomsen, our Chief Investment Officer. Messrs. Wieland, Regan, Downs and Thomsen are also governors and owners of our Advisor. Messrs. Wieland, and Regan, have over 38 years of extensive experience each in the commercial real estate industry, and have been instrumental in setting our strategic direction, operating our business and arranging necessary financing, and through the Advisor, in locating desirable real estate investments and where serving as property manager, managing our properties. Losing the services of Messrs. Wieland, Regan, Downs or Thomsen could have a material adverse effect on our ability to successfully carry out our investment strategies and achieve our investment objectives. There can be no guarantee they will remain affiliated with us. See "Risks Related to Conflicts of Interest."

***Our systems may not be adequate to support our growth, and our failure to successfully oversee our portfolio of real estate investments could adversely affect our results of operation.***

There can be no assurance we will be able to adapt our management, administrative, accounting and operational systems, or hire and retain sufficient staff, to support any growth we may experience. Our failure to successfully oversee our current and future real estate investments or developments could have a material adverse effect on our results of operation and financial condition and our ability to pay dividends to our shareholders.

***Cybersecurity risks and cyber incidents may adversely affect our business by causing a disruption to our operations, a compromise or corruption of our confidential information, and/or damage to our business relationships, all of which could negatively impact our financial results.***

A cyber incident is considered to be any adverse event that threatens the confidentiality, integrity or availability of our information resources. These incidents may be an intentional attack or an unintentional event and could involve gaining unauthorized access to our information systems for purposes of misappropriating assets, stealing confidential information, corrupting data or causing operational disruption. The result of these incidents may include disrupted operations, misstated or unreliable financial data, liability for stolen assets or information, increased cybersecurity protection and insurance costs, litigation and damage to our investor relationships. As our reliance on technology has increased, so have the risks posed to its information systems, both internal and those provided by Sterling Management and service providers. Our and Sterling Management's processes, procedures and internal controls that are designed to mitigate cybersecurity risks and cyber intrusions do not guarantee that a cyber incident will not occur or that our financial results, operations or confidential information will not be negatively impacted by such an incident.

### **Risks Related to Our Structure**

***There are limitations on ownership of our common shares of beneficial interest, which could discourage a takeover transaction even if it is beneficial to our shareholders.***

Our Amended Declaration of Trust provides no person may own more than 9.9% of our outstanding common shares of beneficial interest. Even if a shareholder did not acquire more than 9.9% of our shares, the shareholder may become subject

to such restrictions if redemptions by other shareholders cause the holdings to exceed 9.9% of our outstanding shares. This limitation may have the effect of delaying, deferring or preventing a transaction or a change in control of us, including an extraordinary transaction (such as a merger, tender offer or sale of all or substantially all of our assets) that might provide a premium price for our shareholders, even if it would be in the best interest of our shareholders. The ownership limits and restrictions on transferability will continue to apply until our Board of Trustees determines it is no longer in our best interest to continue to qualify or seek to qualify as a REIT.

***Our shareholders may experience dilution if we or our operating partnership issues additional securities.***

Our shareholders do not have preemptive rights to any shares issued by us in the future. If we sell additional shares in the future to raise capital, issue additional shares pursuant to a dividend reinvestment plan or issue shares in exchange for limited partnership units pursuant to the Limited Liability Limited Partnership Agreement (“LLLP Agreement”) of our operating partnership, our shareholders will experience dilution of their equity investment in us. In addition, if our operating partnership sells additional securities or issues additional securities in connection with a property acquisition transaction, we would, and indirectly our shareholders would, experience dilution in their equity position in the operating partnership.

***Our securityholders have limited control over our operation, and the Board of Trustees has the sole power to appoint and terminate the Advisor.***

Our Board of Trustees has the sole authority to determine our major policies, including our policies regarding financing, growth, investment strategies, debt capitalization, REIT qualification, distribution, and to take certain actions including acquiring or disposing of real estate and real estate related investments, dividend declaration and the election or removal of the Advisor. Our securityholders do not have the right to remove the Advisor, but have the right to elect and remove trustees. Under the Amended Declaration of Trust, our trustees may not do the following without the approval of the holders of a majority of the outstanding common shares of beneficial interest:

- Amend the Amended Declaration of Trust, except for amendments which do not adversely affect the rights, preference and privileges of shareholders;
- Sell all or substantially all of our assets other than in the ordinary course of business or in connection with a liquidation and dissolution;
- Conduct a merger or other reorganization of the trust; or
- Dissolve or liquidate us.

Our shareholders have the right, without the concurrence of the Board of Trustees, to terminate the trust and liquidate our assets or amend the Amended Declaration of Trust.

***Shareholders have no role in determining our investments and must rely on our Advisor and oversight by the Board of Trustees.***

For future acquisitions or dispositions, the Board of Trustees has the authority to approve investment acquisitions or dispositions without shareholder approval. Therefore, shareholders will not be able to evaluate the terms of future investment acquisitions or dispositions, their economic merit or other relevant financial data before we acquire or sell investments. Shareholders must rely entirely on the oversight of our Board of Trustees, the management ability of our Advisor and the performance of the property managers.

***We may issue securities with more favorable terms than the outstanding shares without shareholder approval.***

Under our Amended Declaration of Trust, our Board of Trustees has the authority to establish more than one class or series of shares and to fix the relative preferences and rights regarding conversion, voting powers, restrictions, limitations as to dividends and other distributions, and terms or conditions of redemption of such different classes or series without shareholder approval. Thus, our Board could authorize the issuance of a class or series of shares with terms and conditions that could have priority as to dividends and amounts payable upon liquidation over the rights of the holders of our

outstanding common shares of beneficial interest. Such class or series of shares could also have the effect of delaying, deferring or preventing a change in control of us, including an extraordinary transaction (such as a merger, tender offer or sale of all or substantially all of our assets) that might otherwise provide a premium price to holders of our shares, even if it would be in the best interest of our shareholders.

***Shareholders could incur current tax liability on dividends they elect to reinvest in our shares, and may have to use separate funds to pay their tax liability.***

Shareholders that participate in our dividend reinvestment plan will be deemed to have received, and for income tax purposes will be taxed on, the amount reinvested in shares to the extent the amount reinvested was not a tax-free return of capital. In addition, our shareholders will be treated for tax purposes as having received an additional dividend to the extent the shares are purchased at a discount to fair market value. As a result, unless shareholders are a tax-exempt entity, they may have to use funds from other sources to pay their tax liability on the value of the shares received.

***Our trustees, officers, Advisor and its affiliates have limited liability to us and our shareholders, and may have the right to be indemnified under certain conditions.***

Our Amended Declaration of Trust provides that our trustees, officers, Advisor and its affiliates will not be held liable for any loss or liability suffered by us if: (1) the trustee, officer, Advisor or its affiliate determines in good faith its actions or inactions were in our best interest, (2) such actions were taken on behalf of us and (3) such liability or loss was not the result of: (a) negligence or misconduct by a trustee (other than an independent trustee), the Advisor or its affiliate or (b) gross negligence or willful misconduct by an independent trustee. Moreover, we are required to indemnify our trustees, officers, the Advisor and its affiliates, subject to limitations stated in the Amended Declaration of Trust. As a result, we and our shareholders have limited rights against our trustees, officers, the Advisor and its affiliates, which could reduce our and our shareholders' recovery from these persons. In addition, we may be obligated to fund the defense costs incurred by such parties in some cases, which would decrease the cash otherwise available for dividends to our shareholders.

***There may be conflicts of interest between us and our shareholders on one side and our operating partnership and its limited partners on the other side.***

Our trustees and officers have duties to us and our shareholders in connection with their management of us. At the same time, we, as general partner will have duties to our operating partnership and its limited partners in connection with the management of the operating partnership. Our duties as general partner of the operating partnership may come into conflict with the duties of our trustees and officers to us and our shareholders. The LLLP Agreement of our operating partnership expressly limits our liability for monetary damages by providing we will not be liable for losses sustained, liabilities incurred or benefits not derived if we acted in good faith. In addition, our operating partnership is required to indemnify us and our trustees and officers from and against any and all claims arising from operations of our operating partnership, unless it is established: (1) the act or omission was material and committed in bad faith or was the result of active and deliberate dishonesty; (2) the indemnified party received an improper personal benefit in money, property or services; or (3) in the case of a criminal proceeding, the indemnified person had reasonable cause to believe the act or omission was unlawful. The LLLP Agreement also provides that we will not be held responsible for any misconduct or negligence on the part of any agent appointed by us in good faith.

***If we are deemed to be an investment company under the Investment Company Act, our shareholders' investment return may be reduced.***

We are not registered as an investment company under the Investment Company Act of 1940, as amended ("Investment Company Act") based on exemptions we believe are available to us. If we were obligated to register as an investment company, we would have to comply with a variety of substantive requirements under the Investment Company Act. Registration as an investment company, which would be costly, would subject us to a host of complex regulations, and would divert the attention of management from the conduct of our business. If the SEC or a court of competent jurisdiction were to find we are required, but in violation of the Investment Company Act had failed, to register as an investment company, possible consequences include, but are not limited to, the following: (i) the SEC could apply to a district court



to enjoin the violation; (ii) our shareholders could sue us and recover any damages caused by the violation; (iii) any contract to which we are party made in, or whose performance involves a violation of the Investment Company Act would be unenforceable by any party to the contract unless a court were to find that under the circumstances enforcement would produce a more equitable result than non-enforcement and would not be inconsistent with the purposes of the Investment Company Act; and (iv) criminal and civil actions could be brought against us. Should we be subjected to any or all of the foregoing, our operations and results of operations would be materially and adversely affected.

***There is no public trading market for our shares, nor do we expect one to develop, which may negatively impact a shareholders ability to sell their shares and the price at which shares may be sold.***

There is no public market for our shares and there is no assurance one may develop. In addition, the price shareholders may receive for the sale of their shares is likely to be less than the proportionate value of our investments. If our shareholders are able to find a buyer for their shares, they may have to sell them at a substantial discount from the price they purchased the shares. Consequently, shareholders may not be able to liquidate their investments in the event of emergency or for any other reason. Therefore, shareholders should consider our securities as illiquid and a long-term investment and should be prepared to hold their shares for an indefinite period of time.

***The estimated value of our common stock is based on a number of assumptions and estimates that may not be accurate and is also subject to a number of limitations.***

The current estimated value of our common stock equals \$19.25 per share. The methodology used by our Board to determine this value was based on estimates of the value of our real estate investments, cash and other assets and debt and other liabilities as of a date certain and certain additional information. No formal valuation has been undertaken by us. Our valuation process involves a number of estimates, assumptions and subjective judgments that may not be accurate and complete. Further, different parties using different assumptions and estimates could derive a different estimated value per share, which could be significantly different from our estimated value per share. The estimated value per share may not represent current market values or fair values as determined in accordance with U.S. generally accepted accounting principles. The estimated value of our real estate assets used in the analysis may not necessarily represent the value we would receive or accept if the assets were marketed for sale. Further, acquisitions and dispositions of properties will have an effect on the value of our estimated price per share, which is not reflected in the current estimated price. Moreover, the estimated per share value of the common stock does not reflect a specific liquidity discount for the fact that the shares are not currently traded on a public market, a discount for the non-assumable or prepayment obligations associated with certain loans and other costs that may be incurred in connection with the sale of assets. A shareholder should not rely on the estimated value per share as being an accurate or precise measure of the then-current value of the shares of our common stock in making a decision to buy or sell shares of our common stock, including whether to reinvest dividends by participating in the dividend reinvestment plan and whether to request redemption pursuant to our share redemption program.

***Shareholders may not be able to have their shares redeemed under the Share Redemption Plan, and if shareholders do redeem their shares, they will not receive the current value of the shares.***

We have adopted a share redemption plan. However, our Board of Trustees can limit, suspend, terminate or amend the plan at any time without shareholder approval, and there is no assurance we will have sufficient funds available at the time of any request to honor a redemption request for cash. Shares redeemed under this plan may be purchased at a discount to the current price of the shares or to the price paid for such shares by the shareholder. Therefore, shareholders may not receive the amount they paid for the shares and may receive less by selling their shares back to us than they would receive if they were to sell their shares to other buyers.

***There are transfer restrictions on the shares, and we do not plan to register the shares for resale.***

Other than shares issued under our dividend reinvestment plan, we have not registered our shares under federal or state securities laws, but rather we have sold the shares in reliance on exemptions under applicable federal and state securities laws. Therefore, the shares may be “restricted securities” and may not be resold unless they are subsequently registered

under the Securities Act and applicable state securities laws or pursuant to exemption from such registration requirements or may have other transfer restrictions based on the exemption relied on for the sale of the shares. We are not obligated to, nor do we currently plan to, register any shares for resale.

### **Risks Related to Our Status as a REIT and Related Federal Income Tax Matters**

***If we fail to continue to qualify as a REIT, we would incur additional tax liabilities that would adversely affect our operations and our ability to make distributions and could result in a number of other negative consequences.***

Although our management believes we are organized, have operated, and will be able to continue to be organized and to operate in such a manner to qualify as a real estate investment trust (REIT), as that term is defined under the Internal Revenue Code, we may not have been organized, may not have operated, or may not be able to continue to be organized or to operate in a manner to have qualified or remain qualified as a REIT. Qualification as a REIT involves the application of highly technical and complex Internal Revenue Code provisions for which there are only limited judicial or administrative interpretations. Even a technical or inadvertent mistake could endanger our REIT status.

The determination that we qualify as a REIT requires an ongoing analysis of various factual matters and circumstances, some of which may not be within our control, regarding our organization and ownership, distributions of our income and the nature and diversification of our income and assets. The fact we hold substantially all of our assets through our operating partnership and our ongoing reliance on factual determinations, such as determinations related to the valuation of our assets, further complicates the application of the REIT requirements for us.

If we lose our REIT qualification, we will face income tax consequences that will reduce substantially our available cash for dividends and investments for each of the years involved because:

- We would be subject to federal corporate income taxation on our taxable income, including any applicable alternative minimum tax, and could be subject to increased state and local taxes;
- We would not be allowed a deduction for dividends paid to shareholders in computing our taxable income; and
- Unless we are entitled to relief under applicable statutory provisions, we could not elect to be taxed as a REIT for four taxable years following the year during which we were disqualified.

The increased taxes could reduce the value of the shares as well as cash available for dividends to shareholders and investments in additional assets. In addition, if we fail to continue to qualify as a REIT, we will not be required to pay dividends to shareholders. Our failure to continue to qualify as a REIT also could impair our ability to expand our business and to raise capital.

***As a REIT, we may be subject to tax liabilities that reduce our cash flow.***

Even if we continue to qualify as a REIT for federal income tax purposes, we may be subject to federal and state taxes on our income or property, including the following:

- To continue to qualify as a REIT, we must distribute annually at least 90% of our REIT taxable income (which is determined without regard to the dividends-paid deduction or net capital gains) to our shareholders. If we satisfy the distribution requirement but distribute less than 100% of our REIT taxable income, we will be subject to corporate income tax on the undistributed income. In such situation, shareholders will be treated as having received the undistributed income and having paid the tax directly, but tax-exempt shareholders, such as charities or qualified pension plans, will receive no benefit from any deemed tax payments.
- We may be subject to state and local taxes on our income or property, either directly or indirectly, because of the taxation of our operating partnership or of other entities through which we indirectly own our assets.
- If we have net income from the sale of foreclosure property we hold primarily for sale to customers in the ordinary course of business or other non-qualifying income from foreclosure property, we must pay a tax on that income at the highest corporate income tax rate.

- If we sell a property, other than foreclosure property, we hold primarily for sale to customers in the ordinary course of business, our gain will be subject to the 100% “prohibited transaction” tax.
- We will be subject to a 4% nondeductible excise tax on the amount, if any, by which the distributions we pay in any calendar year are less than the sum of 85% of our ordinary income, 95% of our capital gain net income, and 100% of our undistributed income from prior years.

***We may be forced to borrow funds on a short-term basis, to sell assets or to issue securities to meet the REIT minimum distribution requirement or for working capital purposes.***

To qualify as a REIT, in general, we must distribute to our shareholders at least 90% of our net taxable income each year, excluding capital gains. However, we could be required to include earnings in our net taxable income before we actually receive the related cash. If we do not have sufficient cash to pay the necessary dividends to preserve our REIT status for any year or to avoid taxation, we may need to borrow funds, to sell assets or to issue additional securities even if the then-prevailing market conditions are not favorable for such actions. In addition, we will require a minimum amount of cash to fund our daily operations. Due to the REIT distribution requirements, we may be forced to make distributions when we otherwise would use the cash to fund our working capital needs. Therefore, we may be forced to borrow funds, to sell assets or to issue additional securities at certain times for our working capital needs.

***If our operating partnership does not qualify as a partnership, its income may be subject to taxation, and we would no longer qualify as a REIT.***

The Internal Revenue Code classifies “publicly traded partnerships” as associations taxable as corporations (rather than as partnerships), unless substantially all of their taxable income consists of specified types of passive income. We structured our operating partnership to be classified as a partnership for federal income tax purposes. However, no assurance can be given the IRS will not challenge our position or will classify our operating partnership as a “publicly traded partnership” for federal income tax purposes. To minimize this risk, we have placed certain restrictions on the transfer and/or redemption of partnership units in the LLLP Agreement. If the IRS would assert successfully our operating partnership should be treated as a “publicly traded partnership” and substantially all of the operating partnership’s gross income did not consist of the specified types of passive income, the Internal Revenue Code would treat the operating partnership as an association taxable as a corporation. In such event, we would cease to qualify as a REIT. In addition, the imposition of a corporate tax on the operating partnership would reduce the amount of distributions the operating partnership could make to us and, in turn, reduce the amount of cash available to us to pay dividends to our shareholders.

***We have transfer restrictions on our shares that may limit offers to acquire substantial amounts of the trust’s shares at a premium.***

To qualify as a REIT, our shares must be beneficially owned by 100 or more persons and no more than 50% of the value of our issued and outstanding shares may be owned directly or indirectly by five or fewer individuals. Currently, our Amended Declaration of Trust prohibits transfers of our shares that would result in: (1) our shares being beneficially owned by fewer than 100 persons, (2) five or fewer individuals, including natural persons, private foundations, specified employee benefit plans and trusts, and charitable trusts, owning more than 50% of our shares, applying broad attribution rules imposed by the federal income tax laws, or (3) before our shares qualify as a class of publicly-offered securities, 25% or more of our shares being owned by ERISA investors. If a shareholder acquires shares in excess of the ownership limits or in violation of the restrictions on transfer, we:

- May consider the transfer to be void ab initio.
- May not reflect the transaction on our books.
- May institute legal action to enjoin the transaction.
- May redeem such excess shares.
- Automatically transfer any excess shares to a charitable trust for the benefit of a charitable beneficiary.

If such excess shares are transferred to a trust for the benefit of a charitable beneficiary, the charitable trustee shall sell the excess shares and the shareholder will be paid the net proceeds from the sale equal to the lesser of: (1) the price paid by the shareholder or the “market price” of our shares if no value was paid or (2) the price per share received by the charitable trustee.

If shares are acquired in violation of the ownership limits or the restrictions on transfer described above:

- Transferee may lose its power to dispose of the shares; and
- Transferee may incur a loss from the sale of such shares if the fair market price decreases.

These limitations may have the effect of preventing a change of control or takeover of us by a third party, even if the change in control or takeover would be in the best interest of our shareholders.

***Complying with REIT requirements may restrict our ability to operate in a way to maximize profits.***

To qualify as a REIT, we must continually satisfy tests concerning, among other things, the sources of our income, the nature and diversification of our assets, the amounts we distribute to our shareholders, and the ownership of our common shares. For example, we may be required to pay dividends to our shareholders at disadvantageous times, including when we do not have readily available funds. Thus, compliance with the REIT requirements may hinder our ability to operate solely on the basis of maximizing profits.

***Complying with REIT requirements may force us to forego or liquidate otherwise attractive investments which could negatively impact shareholder value.***

To qualify as a REIT, at the end of each calendar quarter, at least 75% of our assets must consist of cash, cash items, government securities and qualified real estate assets. The remainder of our investments in securities (other than government securities and qualified real estate assets), in general, cannot include more than 10% of the voting securities of any one issuer or more than 10% of the value of the outstanding securities of any one issuer. In addition, no more than 5% of the value of our assets (other than government securities and qualified real estate assets) can consist of the securities of any one issuer, and no more than 25% of the value of our assets may be represented by securities of one or more taxable REIT subsidiaries. Therefore, we may be required to liquidate otherwise attractive investments or may be forced to forego attractive investments to satisfy these requirements. Such action or inaction could be adverse to our shareholder interests.

***Gains from asset sales may be subject to a 100% prohibited transaction tax, which tax could reduce the trust’s available assets and reduce shareholder value.***

We may have to sell assets from time to time to satisfy our REIT distribution requirements and other REIT requirements or for other purposes. The IRS may posit one or more asset sales may be “prohibited transactions.” If we are deemed to have engaged in a “prohibited transaction,” our gain from such sale would be subject to a 100% tax. The Internal Revenue Code sets forth a safe harbor for REITs that wish to sell property without risking the imposition of the 100% tax, but we cannot assure you we will be able to qualify for the safe harbor. We will use reasonable efforts to avoid the 100% tax by: (1) conducting activities that may otherwise be considered a prohibited transaction through a taxable REIT subsidiary, (2) conducting our operations in such a manner so no sale or other disposition of an asset we own, directly or through any subsidiary other than a taxable REIT subsidiary, will be treated as a prohibited transaction or (3) structuring certain sales of our assets to comply with a safe harbor available under the Internal Revenue Code. We do not intend to hold assets in a manner to cause their dispositions to be treated as “prohibited transactions,” but we cannot assure you the IRS will not challenge our position, especially if we make frequent sales or sales of assets in which we have short holding periods. Payment of a 100% tax would adversely affect our results of operations.

***Ordinary dividends payable by REITs generally are taxed at the higher ordinary income rate which could reduce the net cash received by shareholders as a result of an investment in the trust and may be detrimental to our ability to raise additional funds through the sale of our common shares.***

The maximum U.S. federal income tax rate for “qualified dividends” payable by U.S. corporations to individual U.S. shareholders currently is 20%. In addition, the 3.8% tax on net investment income may apply to such dividends. In general, ordinary dividends payable by REITs to its individual U.S. shareholders, however, are generally not eligible for the reduced rates and generally are taxed at ordinary income rates (for REIT dividends received after December 31, 2017, the maximum individual income tax rate currently is 37%, but the current maximum, effective federal income tax rate as to REIT dividends may be reduced to 29.6% because of a partial deduction that may apply with respect to REIT dividends; in addition, the 3.8% tax on net investment income may apply to REIT dividends). It is possible also that tax legislation enacted in 2019 or subsequent years might increase this rate differential. The differing treatment of dividends received from REITs and other corporations might cause individual investors to view an investment in REITs as less attractive related to other corporations which might be detrimental to our ability to raise additional funds through the sale of our common shares.

***Changes in legislative or other actions affecting REITs may adversely affect our status as a REIT.***

The rules dealing with U.S. federal income taxation are constantly under review by the legislative process, the IRS and the U.S. Treasury Department. Changes to tax laws (which changes may apply retroactively) could adversely affect us or our shareholders. Furthermore, new legislation, regulations, administrative interpretations or court decisions could change the federal income tax laws with respect to our qualification as a REIT or the federal income tax consequences of our qualification. We cannot predict whether, when, in what forms, or with what effective dates, the laws applicable to us or our shareholders may be changed.

***Our Board of Trustees may revoke our REIT election without shareholder approval, and we would no longer be required to make distributions of our net income.***

Our Board of Trustees can revoke or otherwise terminate our REIT election without the approval of our shareholders if our Board determines it is not in our best interest to continue to qualify as a REIT. In such case, we would become subject to U.S. federal income tax on our taxable income, and we no longer would be required to distribute most of our net income to our shareholders, which may reduce the total return to our shareholders and affect the value of the shares.

## **Risks Related to Tax-Exempt Investors**

### ***Common shares may not be a suitable investment for tax-exempt investors.***

There are special considerations that apply to investing in common shares on behalf of a trust, pension, profit sharing or 401(k) plans, health or welfare plans, trusts, individual retirement accounts (IRAs), or Keogh plans. If you are investing the assets of any of the above in common shares, you should satisfy yourself:

- Your investment is consistent with your fiduciary obligations under applicable law, including common law, ERISA and the Internal Revenue Code;
- Your investment is made in accordance with the documents and instruments that govern the trust, plan or IRA, including any investment policy;
- Your investment satisfies the prudence and diversification requirements of Sections 404(a)(1)(B) and 404(a)(1)(C) of ERISA and other applicable provisions of ERISA and the Internal Revenue Code;
- Your investment will not impair the liquidity of the trust, plan or IRA;
- Your investment will not produce “unrelated business taxable income” for the trust, plan or IRA;
- You will be able to value the assets of the trust, plan or IRA annually in accordance with ERISA requirements and applicable provisions of the trust, plan or IRA; and
- Your investment will not constitute a prohibited transaction under Section 406 of ERISA or Section 4975 of the Internal Revenue Code.

We have not evaluated, and will not evaluate, whether an investment in us is suitable for any particular trust, plan, or IRA.

### ***Under certain circumstances, tax-exempt shareholders may be subject to unrelated business taxable income, which could adversely affect such shareholders.***

Neither ordinary nor capital gain distributions with respect to our common shares nor gain from the sale of our common shares, in general, should constitute unrelated business taxable income to tax-exempt shareholders. The following, however, are some exceptions to this rule:

- Under certain circumstances, part of the income and gain recognized by certain qualified employee pension trusts with respect to our common shares may be treated as unrelated business taxable income if our common shares are held predominately by qualified employee pension trusts (which we do not expect to be the case);
- Part of the income and gain recognized by a tax-exempt shareholder with respect to common shares would constitute unrelated business taxable income if the tax-exempt shareholder incurs debt to acquire the common shares; and
- Part or all of the income or gain recognized with respect to our common shares held by social clubs, voluntary employee benefit associations, supplemental unemployment benefit trusts and qualified group legal services plans that are exempt from federal income taxation under Sections 501(c)(7), (9), (17), or (20) of the Internal Revenue Code may be treated as unrelated business taxable income.

Therefore, tax-exempt shareholders are not assured all dividends received from the trust will be tax-exempt.

## **Risks Related to Our Relationship with the Advisor and Its Affiliates**

### ***We depend on our Advisor for the successful operations of the REIT, and if required, we may not be able to find a suitable replacement advisor.***

Our ability to achieve our investment objectives is dependent upon the successful performance of our Advisor in locating attractive acquisitions, advising on dispositions of real estate properties and other real estate related assets, advising on any financing arrangements and other administrative tasks to operate our business. If the Advisor suffers or is distracted by



adverse financial, operational problems in connection with its operations unrelated to us or for any reason, it may be unable to allocate a sufficient amount of time and resources to our operations. If this occurs, our ability to achieve our investment objectives or pay dividends to our shareholders may be adversely affected. Any adversity experienced by the Advisor or problems in our relationship with the Advisor could also adversely impact the operation of our properties and, consequently, our cash flow and ability to pay dividends to shareholders.

Either we or the Advisor can terminate the Advisory Agreement upon 60 days written notice to the other party for any reason, or we can terminate the Advisory Agreement immediately for cause or material breach of the Advisory Agreement. In addition, the Board of Trustees may determine not to renew the Advisory Agreement in any year. If this occurs, we would need to find another advisor to provide us with day-to-day management services or engage employees to provide these services directly to us, which would likely be difficult to do and may be costly. There can be no assurances we would be able to find a suitable replacement advisor or suitable employees or enter into agreements for such services on acceptable terms.

***The termination or replacement of the Advisor could trigger a default or repayment event under financings.***

Lenders providing financing for our acquired properties may include provisions in the mortgage loan documentation that state the termination or replacement of the Advisor is an event of default or an event triggering acceleration of the repayment of the loan in full. Even though we will attempt to have such provisions excluded from the loan documents, the lenders may still require them to be included. In addition, the termination or replacement of the Advisor could trigger an event of default under any credit agreement governing a line of credit we may obtain. If an event of default or repayment event occurs with respect to any of our properties, our ability to achieve our investment objectives could be materially adversely affected.

***The Advisor may not be able to retain its key employees, which could adversely affect our ability to carry out our investment strategies.***

We depend on the retention by the Advisor of its key officers, employees and governors. However, none of these individuals have an employment agreement with the Advisor. The loss of any or all of the services by the Advisor's key officers, employees and governors and the Advisor's inability to find, or any delay in finding, replacements with equivalent skills and experience, could adversely impact our ability to successfully carry out our investment strategies and achieve our investment objectives.

Our future success also depends on the Advisor's and its affiliates' ability to identify, hire, train and retain highly qualified real estate, managerial, financial, marketing and technical personnel to provide the services to us pursuant to the Advisory Agreement and any other written services agreement, including any property management agreements. Competition for such personnel is intense, and the Advisor or its affiliates may not be able to attract, assimilate or retain such personnel in the future. The inability to attract and retain the necessary personnel could have a material adverse effect on our business and results of operations.

***Payment of fees and expenses to the Advisor reduces the cash available for dividends.***

The Advisor performs services for us in connection with the selection, acquisition, financing and disposition of our investments; the management of our assets; and certain administrative services. We pay the Advisor an annual management fee, reimbursement for operating and acquisition expenses as well as acquisition, disposition, financing and development fees. Such fees and payments reduce the amount of cash available for further investments or dividends to our shareholders. Additionally, such fees increase the risk shareholders may receive a lower price when they resell their shares than the purchase price they initially paid for their shares.

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

### ***Our performance could be adversely affected by the general risks involved in real estate investments.***

Our results of operation and financial condition, the value of our real estate assets, and the value of an investment in us are subject to the risks normally associated with the ownership and operation of real estate properties, including, among others:

- Fluctuations in occupancy rates, rent schedules and operating expenses, which can render the sale or refinancing of a real estate investment difficult or unattractive;
- The validity and enforceability of leases, financial resources of the tenants, tenant bankruptcies, rent levels and sales levels in the local areas of the investments;
- Perceptions of the safety, convenience and attractiveness of our properties and the neighborhoods where they are located;
- Ability to provide adequate management, maintenance and insurance on our properties;
- Adverse changes in local population trends, market conditions, neighborhood values, local economic and social conditions;
- Supply and demand for properties such as our real estate investments and competition from properties that could be used in the same manner as our real estate investments;
- Changes in interest rates and availability of permanent mortgage funds;
- Changes in real estate tax rates and other taxes;
- Changes in governmental rules, regulations and fiscal policies, including the effects of inflation and enactment of unfavorable real estate, rent control, environmental or zoning laws; and
- Hazardous material laws, uninsured losses and other risks.

All of these factors are beyond our control. Any negative changes in these factors could affect our ability to meet our obligations, pay dividends to shareholders or achieve our investment objectives.

### ***Market disruptions may significantly and adversely affect our financial condition and results of operations.***

Our results of operations may be sensitive to changes in overall economic conditions impacting tenant leasing practices, such as increased unemployment, weakening of tenant financial condition, large-scale business failures and tight credit markets. Adverse economic conditions affecting tenant income, such as employment levels, business conditions, interest rates, tax rates, fuel and energy costs and other matters, could reduce overall tenant leasing or cause tenants to shift their leasing practices. In addition, periods of economic slowdown or recession, rising interest rates or declining demand for real estate, excessive availability of competing properties or the public perception any of these events may occur, could result in a general decline in rents or an increased incidence of defaults under existing leases. A general reduction in the level of tenant leasing could adversely affect our ability to maintain our current occupancy rates and gain new tenants, affecting our growth and profitability. Accordingly, difficult financial and macroeconomic conditions could have a significant adverse effect on our cash flows, profitability and results of operations.

### ***Insufficient geographic diversity of our real estate investments could adversely affect our operating results if economic changes impact real estate markets where we own significant assets.***

Geographic concentration of our properties may expose us to economic downturns in those areas where our properties are located. A recession in any area where we own several properties or interests in properties could adversely affect our ability to generate or increase operating revenues, locate and retain financially sound tenants or dispose of unproductive properties. In addition, it could have an adverse impact on our tenant's revenues, costs and results of operations and may adversely affect their ability to meet their obligations to us. Likewise, we may be required to lower our rental rates to attract desirable tenants in such an environment. Currently, the majority of our properties are located in North Dakota and Minnesota, and we hold several properties in Fargo, North Dakota and Moorhead, Minnesota. To the extent weak economic or real estate conditions affect North Dakota, Minnesota or other markets in which we own properties more severely than other areas of the country, our financial performance could be negatively impacted.

***We face numerous risks associated with property acquisitions which could adversely affect our operating results.***

Through our operating partnership, we acquire properties and portfolios of properties. Our acquisition activities and their success are subject to the following risks typically encountered in real estate acquisitions:

- We may be unable, or decide it is not in our interests, to complete an acquisition after making a non-refundable deposit and incurring certain other acquisition-related costs or purchasing an option to purchase;
- We may be unable to obtain financing for acquisitions on favorable terms or at all;
- Acquired properties may fail to perform as expected;
- The actual costs of repositioning or redeveloping acquired properties may be greater than our estimates;
- Acquired properties may be located in new markets in which we may face risks associated with a lack of market knowledge or understanding of the local economy, lack of business relationships in the area and unfamiliarity with local governmental and permitting procedures; and
- We may be unable to quickly and efficiently integrate new acquisitions, particularly acquisitions of portfolios of properties, into our existing operations.

These risks could have an adverse effect on our results of operation, our financial condition and the amount available for payment of dividends to our shareholders.

***We may invest in and develop undeveloped real property, which requires us to pay expenses prior to receiving any income on the property.***

We have the discretion to invest up to 10% of our total assets in undeveloped property. If we invest in undeveloped property, such property will not generate operating revenue while costs are incurred to develop the property and may generate other expenses including property taxes and insurance. In addition, construction and development of such properties may not be completed within budget or as scheduled and projected rental levels may not be achieved. In addition to the risks of real estate investments in general, an investment in undeveloped property is subject to additional risks, including the expense and delay which may be associated with rezoning the land for a higher use and the development and environmental concerns of governmental entities and/or community groups. Therefore, we will not generate income on such property until development is completed and we begin leasing the property.

***We may acquire multiple properties in a single transaction, which may adversely affect our operations through the inclusion of less desirable investments or financing requirements greater than we would otherwise be willing to incur.***

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

***We may invest in co-ventures, where our co-venture partners, co-tenants or other partners in co-ownership arrangements could take actions that decrease the value of a real estate investment and lower our overall return.***

We may enter into joint ventures, tenant-in-common investments or other co-ownership arrangements with our Advisor, its affiliates, our trustees, or third parties having investment objectives similar to ours in the acquisition of real estate

investments. In such arrangements, we may be acquiring non-controlling interests in or sharing responsibility for managing the affairs of the joint venture. In such event, we would not be in a position to exercise sole decision-making authority regarding the joint venture. Investments in joint ventures may, under certain circumstances, involve risks not present where another party is not involved, including the possibility partners or co-venturers might become bankrupt or fail to fund their required capital contributions. Co-venturers may have economic or other business interests or goals which are inconsistent with our business interests or goals, and may be in a position to take actions contrary to our policies or objectives. Such investments may also have the potential risk of impasses on decisions, such as a sale, because neither we nor the co-venturer would have full control over the joint venture. Disputes between us and co-venturers may result in litigation or arbitration that would increase our expenses and prevent our management and the Advisor from focusing their time and effort on our business. Consequently, actions by or disputes with co-venturers might result in subjecting properties owned by the joint venture to additional risk. In addition, we may in certain circumstances be liable for the actions of our co-venturers. Any of these risks could subject us to liabilities in excess of those contemplated and reduce our returns on that investment.

***We could experience difficulties or delays renewing leases or re-leasing space, which will increase our costs to maintain such properties without receiving income.***

We derive a significant portion of our net income from rent received from our tenants. Our properties include both residential as well as commercial properties. If a tenant experiences a downturn in its business or other types of financial distress, it may be unable to make timely rental payments. If a significant number of tenants default on lease payments to us, it would cause us to lose the revenue associated with such leases and require us to find alternative sources of revenue to meet mortgage payments and prevent a foreclosure if the property is subject to a mortgage. If lease defaults occur, we may experience delays in enforcing our rights as landlord. Also, if our tenants decide not to renew their leases, terminate early or default on their lease, we may not be able to re-let the space or may experience delays in finding suitable replacement tenants. Even if tenants decide to renew or lease new space, the terms of renewals or new leases, including the cost of required renovations or concessions to tenants, particularly commercial tenants, may be less favorable to us than current lease terms. As a result, our net income and ability to pay dividends to shareholders could be materially adversely affected. Further, if one of our properties cannot be leased on terms and conditions favorable to us, the property may not be marketable at a suitable price without substantial capital improvements, alterations, or at all.

***We could face potential adverse effects if a commercial tenant is unable to make timely rental payments, declares bankruptcy or become insolvent.***

If a tenant experiences a downturn in its business or other types of financial distress, it may be unable to make timely rental payments. Delayed rental payments could adversely affect cash flow available for dividends. If a commercial tenant declares bankruptcy or becomes insolvent, it may adversely affect the income produced by our properties. If a tenant defaults, we may experience delays and incur substantial costs in enforcing our rights as landlord. However, if a tenant files for bankruptcy, we cannot evict the tenant solely because of such bankruptcy. If a court authorizes the commercial tenant to reject and terminate its lease with us, our claim against the tenant for unpaid future rent would be subject to a statutory cap that might be substantially less than the remaining rent actually owed under the lease. In addition, it is unlikely a bankrupt tenant would pay in full amounts it owes us under a lease. Additionally, we may be required to incur additional costs in the form of tenant improvements and leasing commissions in our efforts to lease the space to a new tenant, as well as lower our rental rates to reflect any decline in market rents. This shortfall could adversely affect our cash flow and results of operations.

***If our reserves for making capital improvements on our real estate investments are insufficient, we may be required to defer necessary capital improvements which could negatively affect our revenues.***

We establish capital reserves on a property-by-property basis, as we deem appropriate. If we do not have enough reserves to cover the costs of capital improvements throughout the life of the real estate property and there is insufficient cash available from our operations, we may have to borrow funds or defer necessary improvements to the property. If we delay or do not make necessary capital improvements when needed, there are risks the property may decline in value and may result in fewer tenants maintaining or renewing their leases and attracting new tenants to the property. If this happens, we

may not be able to maintain projected rental rates for affected properties, and our results of operations may be negatively impacted.

***Properties will face significant competition for tenants, which could limit our profitability.***

We face significant competition from owners, operators and developers of similar real estate properties designed and dedicated to serve tenants with the same needs as the tenants that occupy or could occupy our properties in the same market. These competitors may have greater resources than we do, and may have other advantages resulting from lower cost of capital and enhanced operating efficiencies. This competition may affect our ability to attract and retain tenants and may reduce the rents we are able to charge. These competing properties may have vacancy rates higher than our properties, which may result in their owners being willing to lease available space at lower prices than the space in our properties. Due to such competition, the terms and conditions of any lease we enter into with our tenants may vary substantially from those anticipated. Our properties experience competition from existing and planned projects, as well as newer developments located within the market area. We cannot assure competitors will not develop similar properties in the area or not be able to negotiate better leases for existing or new properties which could adversely affect the profitability and viability of our properties.

***Increased affordability of single-family homes could limit our ability to retain residents, lease apartment units or increase or maintain rents.***

The residential properties we own or may acquire can compete with numerous housing alternatives in attracting residents, including other apartment communities and single-family homes, as well as owner occupied single- and multifamily homes available to rent. Competitive housing in a particular area and the increasing affordability of owner occupied single- and multifamily homes available to rent or buy could adversely affect our ability to retain our residents, lease apartment units and increase or maintain rental rates.

***Investments in real estate are illiquid, and we may not be able to resell a property on terms favorable to us.***

We intend to hold real estate properties until such time as our Advisor determines a sale or other disposition appears to be advantageous to achieve our investment objectives or when our shareholders approve our termination and liquidation. Because real estate investments are relatively illiquid, it could be difficult for us to promptly sell one or more of our real estate properties on favorable terms. This may be a result of economic conditions, availability of financing, interest rates and other factors beyond our control. This may limit our ability to change our portfolio promptly in response to adverse changes in the performance of any such property or economic or market trends. We cannot predict the length of time needed to find a willing purchaser and to close the sale of a property. Real estate investments by their nature are often difficult or time consuming to liquidate. In addition, federal tax laws imposing a 100% excise tax on gains from sales of certain types of property sales by a REIT (generally, property viewed as being purchased for resale, rather than investment) could limit our ability to sell properties and may affect our ability to sell properties without adversely affecting returns to our shareholders. These restrictions could adversely affect our ability to achieve our investment objectives.

***Valuations and appraisals of our investments may not necessarily correspond to realizable value.***

We value our real estate properties initially at cost, which we expect to represent fair value at that time. After acquisition, valuations may include appraisals of our properties periodically. The valuation methodologies used to value our real estate properties will involve subjective judgments regarding such factors as comparable sales, rental and operating expense data, the capitalization and/or discount rate and projections of future rent and expenses based on appropriate analysis. Although we believe our valuation procedures are designed to determine the accurate fair value of our assets, appraisals and valuations of our real estate properties and other investments assets will be only estimates of fair value and therefore may not correspond to realizable value upon a sale of those assets.

***Uninsured losses related to real estate investments may adversely affect our results of operation.***

We purchase, and we may be required by lenders of mortgage loans or other financings to obtain, certain insurance coverage on our real estate investments. Either the property manager or the Advisor selects policy specifications and insured limits which it believes to be appropriate and adequate given the risk of loss, the cost of the coverage and industry practice. The nature of the tenants at the properties we hold may expose us and our operations to an increase in liability for personal injuries or other losses. There can be no assurance that such insurance will be sufficient to cover potential liabilities. Some of our policies may be subject to limitations involving large deductibles or co-payments and policy limits which may not be sufficient to cover losses. Furthermore, insurance against certain risks, such as terrorism, flood and toxic mold, may be unavailable or available at commercially unreasonable rates or in amounts less than the full market value or replacement cost of the properties. There can be no assurance particular risks that are currently insurable, will continue to be insurable on an economical basis or current levels of coverage will continue to be available. If a loss occurs that is partially or completely uninsured, we may lose all or part of our investment in a property as well as the anticipated future cash flows from such properties. In addition, if the damaged properties are subject to recourse indebtedness, we would continue to be liable for the indebtedness, even if these properties were irreparably damaged. We may also be liable for any uninsured or underinsured personal injury, death or property damage claims, which could result in decreased dividends to shareholders.

***Discovery of toxic mold in or at our properties may adversely affect our results of operation.***

Litigation and concern about indoor exposure to certain types of toxic molds have been increasing as the public becomes aware exposure to mold can cause a variety of health effects and symptoms, including allergic reactions. Toxic molds can be found almost anywhere; they can grow on virtually any organic substance, as long as moisture and oxygen are present. There are molds that can grow on wood, paper, carpet, foods and insulation. When excessive moisture accumulates in buildings or on building materials, mold growth will often occur, particularly if the moisture problem remains undiscovered or unaddressed. It is impossible to eliminate all mold and mold spores in the indoor environment. The difficulty in discovering indoor toxic mold growth could lead to a risk of lawsuits by affected persons and the risk that the cost to remedy toxic mold could exceed the value of the property. We will attempt to acquire properties where there is no toxic mold or where there has not been any proceeding or litigation with respect to the presence of toxic mold. However, we cannot provide assurances toxic mold will not exist on any of our properties when we acquire the properties or will not subsequently develop on any of our properties.

***We may acquire a property or properties “AS IS,” which increases the risk of an investment that requires us to remedy defects or costs without recourse to the prior owner.***

We may acquire real estate properties “as is” with only limited representations and warranties from the property seller regarding matters affecting the condition, use and ownership of the property. As a result, if defects in the property (including any building on the property) or other matters adversely affecting the property are discovered, we may not be able to pursue a claim for any or all damage against the property seller. Such a situation could negatively affect our results of operations.

***We may engage in leaseback transactions, which involve risks including a failure to qualify as a REIT.***

From time to time we have purchased certain real estate properties and leased them back to the sellers of such properties. While we will use our best efforts to structure any such leaseback transactions to be characterized as a “true lease” so we will be treated as the owner of the property for federal income tax purposes, we cannot assure you the IRS will not challenge such characterization. If any such re-characterization were successful, deductions for depreciation and cost recovery relating to such real property would be disallowed, interest and penalties could be assessed by the IRS and it is possible, under some circumstances, we could fail to qualify as a REIT as a result.



***We rely on affiliated and outside property managers to properly manage and lease our properties.***

The Advisor and an affiliate of the Advisor serve as our principal property managers, and the Advisor has hired and intends to hire other affiliates and/or third parties to serve as additional property managers, to manage our properties and act as leasing agents to lease vacancies in our real estate properties. These property managers will have significant decision-making authority with respect to the management of our properties. Our ability to direct and control how our properties are managed may be limited. We will not, and the Advisor will not as to its affiliates and third party property managers, supervise any of the property managers or any of their respective personnel on a day-to-day basis. Thus, the success of our business may depend in large part on the ability of our property managers to manage the day-to-day operations and their ability to lease vacancies in our properties. Any adversity experienced by our property managers could adversely impact the operation and profitability of our properties and, consequently, our ability to achieve our investment objectives.

**Risks Related with Our Indebtedness and Financing**

***Market conditions could adversely affect our ability to obtain financing.***

As a REIT, we are required to distribute at least 90% of our taxable income (excluding net capital gains) to our shareholders in each taxable year, and thus our ability to retain internally generated cash is limited. Accordingly, our ability to acquire properties or to make capital improvements to or remodel properties can depend on our ability to obtain debt or equity financing from third parties or the sellers of properties or to sell other properties. We have incurred mortgage debt and pledged many of our properties as security for debt in order to obtain funds to acquire additional properties or for working capital. We have also obtained lines of credit to provide a flexible borrowing source of funds.

Market fluctuations and disruptions in the credit markets could significantly affect our ability to access capital. Reductions in our available borrowing capacity, or inability to establish a credit facility when required or when business conditions warrant, could then limit the number, size and quality of properties we could acquire or the amount of improvements we could make on acquired properties, which could materially affect our ability to achieve our investment objectives and may result in price or value decreases of our real estate assets.

***Derivatives and hedging activity could adversely affect cash flow.***

In the normal course of business, we use derivatives to manage our exposure to interest rate volatility on debt instruments, including hedging for future debt issuances. At other times we may utilize derivatives to increase our exposure to floating interest rates. We may also use derivatives to manage commodity prices in the daily operations of our business. There can be no assurance that these hedging arrangements will have the desired beneficial impact. These arrangements, which can include a number of counterparties, may expose us to additional risks, including failure of any of our counterparties to perform under these contracts, and may involve extensive costs, such as transaction fees or breakage costs, if we terminate them. No strategy can completely insulate us from the risks associated with interest rate or commodity pricing fluctuations.

***The phase out of LIBOR and transition to SOFR as a benchmark interest rate could have adverse effects.***

In 2018, the Alternative Reference Rate Committee identified the Secured Overnight Financing Rate (“SOFR”) as the alternative to LIBOR. SOFR is a broad measure of the cost of borrowing cash overnight collateralized by U.S. Treasury securities, published by the Federal Reserve Bank of New York. By the end of 2021, it is expected that no new contracts will reference LIBOR and will instead use SOFR. Due to the broad use of LIBOR as a reference rate, all financial market participants, including the Company, are impacted by the risks associated with this transition and therefore it could adversely affect our operations and cash flows.

***We will incur mortgage indebtedness and other borrowings, which will increase our business risks.***

We have obtained mortgage loans on many of our properties so we can use our capital to acquire additional real estate properties and make improvements on the properties. However, we may not incur indebtedness of more than 300% of our net assets, unless such excess is approved by a majority of our trustees. High debt levels will cause us to incur higher interest charges, which would result in higher debt service payments and could be accompanied by restrictive covenants.

If there is a shortfall between the cash flow from a property and the cash flow needed to service mortgage debt on that property, then the amount available for dividends to shareholders may be reduced. In addition, incurring mortgage debt increases the risk of loss since defaults on indebtedness secured by a property may result in lenders initiating foreclosure actions. In that case, we could lose the property securing the loan in default, thus reducing the value of our shareholders' investment.

For tax purposes, a foreclosure on any of our properties will be treated as: (1) if the foreclosed debt is nonrecourse, a sale of the property for a purchase price equal to the outstanding balance of the debt secured by the mortgage or (2) if the foreclosed debt is recourse, a sale of the property for a purchase price equal to its fair market value and as cancellation of debt income to the extent, if any, the outstanding debt balance exceeds the fair market value. If the outstanding balance of the debt secured by the mortgage exceeds our tax basis in the property, we will recognize taxable income on foreclosure, but we would not receive any cash proceeds. We may give full or partial guarantees to lenders of mortgage debt on behalf of our operating partnership, whereby we will be responsible to the lender for satisfaction of the debt if it is not paid by our operating partnership. If any mortgage contains cross-collateralization or cross-default provisions, a default on a single property could affect multiple properties. If any of our properties are foreclosed upon due to a default, our ability to pay cash dividends to our shareholders could be adversely affected.

***We could face difficulties in refinancing loans involving balloon payment obligations.***

Some of our mortgage loans require us to make a lump-sum or "balloon" payment at maturity. Our ability to make a balloon payment at maturity could be uncertain and may depend upon our ability to obtain additional financing, to refinance the debt or our ability to sell the particular property. If we try and refinance the debt, we may not be able to obtain terms as favorable as the original loan. Based on historical interest rates, current interest rates are low and, as a result, the interest rate obtained upon refinancing in subsequent years may be higher than the original loan. If we are not able to refinance the debt, or obtain acceptable terms, we may be required to sell the mortgaged property at a time which may not permit realization of the maximum return on such property. The effect of a refinancing or sale could affect the rate of return to shareholders and the projected time of disposition of our assets.

***Lenders may require restrictive covenants relating to our operations, which may adversely affect our flexibility and our ability to achieve our investment objectives.***

Mortgage loans obtained by us could impose restrictions that affect our distribution and operating policies, our ability to incur additional debt and our ability to resell interests in the property. Loan documents may contain covenants that limit our ability to further mortgage the property, discontinue insurance coverage, replace the Advisor or the property manager, or terminate certain operating or lease agreements related to the property. Such restrictions may limit our ability to achieve our investment objectives.

***Increases in interest rates on variable rate debt incurred and new financings by us will reduce cash available for dividends.***

Increases in interest rates on any variable rate debt incurred or new financings would increase our interest costs, which could reduce our cash flows and our ability to pay dividends to our shareholders. In addition, if we need to repay existing debt during periods of rising interest rates, we could be required to liquidate one or more of our investments in properties at times which may not permit realization of the maximum return on such investments.

***Complying with REIT requirements may limit our ability to hedge liabilities through tax-efficient means, which may adversely affect our results of operations.***

We have entered into three hedging transactions and may enter into additional such transactions. Hedging transactions could take a variety of forms, including interest rate swaps or cap agreements, options, futures contracts, forward rate agreements, or similar financial instruments. The REIT provisions of the Code substantially limit our ability to hedge liabilities. Because we conduct substantially all of our operations through our operating partnership, any income from a hedging transaction entered into to manage risk of interest rate changes with respect to borrowings made or to be made to

acquire or carry real estate assets will not constitute gross income to us for purposes of the 75% or 95% gross income test. As a result, we may be required to limit the operating partnership's use of advantageous hedging techniques or to implement hedges through certain taxable corporations. This could increase the costs of hedging activities because any taxable corporation would be subject to tax on gains or expose the operating partnership to greater risks associated with changes in interest rates than is otherwise desirable. In addition, losses of a taxable corporation will generally not be deductible by the operating partnership and will generally only be available to offset future taxable income of such corporation. We intend to structure any hedging transaction in a manner that does not jeopardize our ability to qualify as a REIT.

***We may structure acquisitions of property in exchange for limited partnership units in our operating partnership on terms that could limit our liquidity or our flexibility.***

We may acquire properties by issuing limited partnership units in our operating partnership to contributors of property which may include affiliates. If we enter into such transactions, in order to induce the property owners to accept limited partnership units rather than cash, it may be necessary for us to provide them with additional incentives. For instance, our operating partnership's LLLP Agreement provides any holder of limited partnership units may, subject to certain conditions, request redemption of their units and may acquire our shares on a one-for-one exchange basis.

We may, however, enter into additional contractual arrangements with contributors of property under which we would agree to redeem a contributor's units for our shares or cash, at the option of the contributor, at set times. If the contributor required us to redeem units for cash pursuant to such a provision, it would limit our liquidity and thus our ability to use cash to make other investments, satisfy other obligations or pay dividends. Moreover, if we were required to redeem units for cash at a time when we did not have sufficient cash to fund the redemption, we might be required to sell one or more properties to raise funds to satisfy this obligation or seek short-term financing. Furthermore, in order to allow a contributor of a property to defer taxable gains on the contribution of property to our operating partnership, we might agree not to sell a contributed property for a defined period of time or until the contributor exchanged the contributor's units for cash or our shares. Such an agreement would prevent us from selling those properties, even if market conditions made such a sale favorable to us.

#### **Risks Related to Other Investments**

***Investments in other real estate related investments could involve higher risks than investment in real estate properties, which could adversely affect our operations and ability to make dividend payments.***

We are permitted to invest in other real estate assets. We can invest in real estate equity, debt and derivative securities. These assets can be quite risky, illiquid and volatile and the value of these assets could cause the value of our shares to fluctuate and could result in losses that materially adversely affect our results of operations.

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

We are subject to conflicts of interest arising out of our relationships with our affiliates, our Advisor and its affiliates, including the material conflicts discussed below.

***There are conflicts of interest in our relationship with the Advisor and its affiliates and several trustees, which could adversely affect our operations and business operations.***

We are subject to potential conflicts of interest arising out of our relationships with the Advisor, its affiliates and certain trustees. Conflicts of interest may arise among a trustee or the Advisor and its respective affiliates, on the one hand, and us and our shareholders, on the other hand. As a result of these conflicts, the trustee or Advisor may favor its own interests or the interests of its affiliates over the interest of our shareholders.

### *Allocation of time and effort*

We rely on the personnel of the Advisor and its affiliates to manage our assets and daily operations. Two of our trustees are also governors and owners of the Advisor and the primary property manager of a number of our properties, and therefore have conflicts of interest in allocating their time, services and functions among us and other real estate programs or business ventures the Advisor or its affiliates organize or serve.

### *Division of loyalty*

Several of our officers and/or trustees serve as officers, governors and owners of one or more entities (certain of which are affiliated with our Advisor or trustees), property managers, tenants of our properties, brokerage companies and other real estate entities owning real estate investments. As a result, these individuals owe duties to these other entities and their investors, which may conflict with the duties that they owe to us and our shareholders. Their loyalties to these other entities and investors could result in action or inaction detrimental to our business, which could harm implementation of our business strategy and investment and leasing opportunities.

### *Allocation of investment opportunities*

The Advisor and its affiliates are or may become committed to the management of other business ventures. Accordingly, there may be conflicts of interest between our investments and other investments or business ventures in which the Advisor and its affiliates are participants. In addition, the Advisor and its officers will advise other investment programs that invest in commercial real estate properties and real estate related assets in which we may be interested. Therefore, the Advisor could face conflicts of interest in allocating and determining which programs will have the opportunity to acquire and participate in such investments as they become available. As a result, other investment programs advised by the Advisor may compete with us with respect to investors and certain investments we may want to acquire.

## **ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

## **ITEM 2. PROPERTIES**

### **General**

As of December 31, 2019, we owned 173 properties, containing approximately 9,852 apartments and 1,662,000 square feet of leasable commercial space.

It is our policy to acquire assets with an intention to hold these assets as long-term investments seeking income and capital appreciation through an increase in value of our real estate portfolio, as well as increased revenue as a result of higher rent. These types of investments are the core of our strategy of creating shareholder value. We currently own and maintain a portfolio of real estate diversified by geographical location and by type and size. Sterling's current acquisition strategy and focus is on multifamily apartment properties. Our Advisor monitors industry trends and invests in property believed to provide the most favorable return balanced with risk. We attempt to manage our real estate portfolio by evaluating changes or trends in the industries in which our tenants operate, the creditworthiness of our tenants and changes or trends in the area demographics surrounding our properties for evidence that our properties will continue to meet our investment objectives of cash flow, preservation of capital and capital appreciation.

With the exception of single tenant buildings, the majority of our real estate investments are managed by a third party. Property management firms usually receive between 3% and 5% of gross rent collection for their services. Substantially all of our commercial revenues consist of base rents received under leases having terms ranging from month-to-month to over 25 years. More than half of our existing commercial property leases as of December 31, 2019 contain "step up" rental clauses providing for annual increases in the base rental payments of approximately 1.0% to 3.0% each year during the term of the lease.

## Properties

The 173 properties are located in 11 states, primarily in North Dakota and Minnesota with others located in Arkansas, Colorado, Iowa, Louisiana, Michigan, Mississippi, Missouri, Nebraska and Wisconsin. The residential and commercial portfolio of properties includes a diversified mixture of multifamily, single and multi-tenant retail and office buildings as well as industrial properties. The majority of the properties are located in the largest cities in the states of North Dakota and Minnesota. Please see Notes 2 and 3 to the consolidated financials included in this report for more information.

As of December 31, 2019, approximately 73.4% (based on cost) of the properties were apartment communities located primarily in North Dakota and Minnesota with others located in Missouri and Nebraska. Most multifamily dwelling properties are leased to a variety of tenants under short-term leases of less than a year.

As of December 31, 2019, approximately 26.6% (based on cost) of the properties were comprised of industrial, office, retail and medical commercial properties located primarily in North Dakota with others located in Arkansas, Colorado, Iowa, Louisiana, Michigan, Minnesota, Mississippi, Nebraska and Wisconsin. Most commercial properties are leased to a variety of tenants under long-term leases.

The following table sets forth certain information regarding each of our properties owned, including unconsolidated affiliates, as of December 31, 2019 (in thousands, except units or leasable sq. ft.).

Property	Location	Year Acquired	# of Units or Leasable Sq. Ft	Total Investment	Physical Occupancy at December 31, 2019
32nd Avenue Office	Fargo, ND	2004	31,750	\$ 4,230	92.96 %
Aetna	Bismarck, ND	2006	50,000	7,210	100.00 %
Amberwood	Grand Forks, ND	2016	95	4,081	92.29 %
Applebee's Neighborhood Bar & Grill	Apple Valley, MN	2011	4,997	2,523	100.00 %
Applebee's Neighborhood Bar & Grill	Bloomington, MN	2010	5,043	2,208	100.00 %
Applebee's Neighborhood Bar & Grill	Coon Rapids, MN	2010	5,576	2,434	100.00 %
Applebee's Neighborhood Bar & Grill	Savage, MN	2010	4,936	1,518	100.00 %
Arbor	Bismarck, ND	2013	12	696	96.71 %
Arbor II	Bismarck, ND	2013	12	700	97.76 %
Arbor III	Bismarck, ND	2013	12	696	93.06 %
Ashbury	Fargo, ND	2013 & 2016	61	4,139	94.20 %
Auburn II	Fargo, ND	2007	24	1,089	85.77 %
Autumn Ridge	Grand Forks, ND	2004	144	10,381	95.28 %
Barrett Arms	Crookston, MN	2014	24	1,169	93.41 %
Bayview	Fargo, ND	2007	100	4,516	88.51 %
Becker Furniture	Waite Park, MN	2006	30,200	1,578	100.00 %
Bell Plaza* (FKA Northland Plaza)	Bloomington, MN	2015	296,967	52,700	86.85 %
Berkshire	Fargo, ND	2008	12	474	95.12 %
Betty Ann	Fargo, ND	2009	24	928	91.12 %
Biolife Plasma Center	Bismarck, ND	2008	11,671	2,756	100.00 %
Biolife Plasma Center	Grand Forks, ND	2008	13,190	2,909	100.00 %
Biolife Plasma Center	Janesville, WI	2008	12,225	2,282	100.00 %
Biolife Plasma Center	Mankato, MN	2008	13,181	4,073	100.00 %
Biolife Plasma Center	Marquette, MI	2008	11,737	3,196	100.00 %
Biolife Plasma Center	Onalaska, WI	2008	12,180	2,450	100.00 %
Biolife Plasma Center	Oshkosh, WI	2008	12,191	2,187	100.00 %
Biolife Plasma Center	Sheboygan, WI	2008	13,230	2,573	100.00 %
Biolife Plasma Center	Stevens Point, WI	2008	13,190	2,482	100.00 %
Birchwood I	Fargo, ND	2017	18	421	98.36 %
Birchwood II	Fargo, ND	2017	48	2,662	92.83 %
Bradbury	Bismarck, ND	2018	96	6,057	91.28 %
Bridgeport	Fargo, ND	2016	120	8,337	90.14 %
Bristol Park	Grand Forks, ND	2016	80	5,742	89.50 %
Brookfield	Fargo, ND	2008	72	2,620	93.87 %
Cambridge (FKA 44th Street)	Fargo, ND	2013	42	2,416	94.33 %
Candlelight	Fargo, ND	2012	66	2,030	88.02 %

Property	Location	Year Acquired	# of Units or Leasable Sq. Ft	Total Investment	Physical Occupancy at December 31, 2019
Carling Manor	Grand Forks, ND	2008	12	831	91.43 %
Carlton Place	Fargo, ND	2008	213	8,743	90.92 %
Carr	Fargo, ND	2017	18	830	94.64 %
Cedars 4	Fargo, ND	2018	18	1,205	88.47 %
Chandler 1802	Grand Forks, ND	2014	24	1,338	96.96 %
Chandler 1834	Grand Forks, ND	2018	12	670	84.87 %
Chandler 1866	Grand Forks, ND	2005	12	354	99.50 %
Cherry Creek (FKA Village)	Grand Forks, ND	2008	35	1,770	94.96 %
Cityside	Fargo, ND	2018	36	1,328	90.34 %
Columbia West	Grand Forks, ND	2008	70	4,336	90.97 %
Country Club	Fargo, ND	2011	40	1,814	90.83 %
Countryside	Fargo, ND	2011	24	932	89.37 %
Courtyard	St. Louis Park, MN	2013	151	9,179	96.76 %
Dairy Queen	Dickinson, ND	2012	2,811	1,330	100.00 %
Dairy Queen	Moorhead, MN	2011	2,712	1,185	100.00 %
Dairy Queen	Apple Valley, MN	2018	5,348	3,079	100.00 %
Dakota Manor	Fargo, ND	2014	54	2,788	90.44 %
Danbury	Fargo, ND	2007	135	7,510	91.54 %
Dellwood Estates	Anoka, MN	2013	132	11,910	98.41 %
Eagle Run	West Fargo, ND	2010	144	6,985	90.82 %
Eagle Sky I	Bismarck, ND	2016	20	1,573	92.88 %
Eagle Sky II	Bismarck, ND	2016	20	1,645	91.31 %
East Bridge	Fargo, ND	2017	58	6,427	91.57 %
Echo Manor	Hutchinson, MN	2014	30	1,112	97.83 %
Eide Bailly Building***	Fargo, ND	2007	74,646	9,193	100.00 %
Emerald Court	Fargo, ND	2008	24	1,041	91.59 %
Essex	Fargo, ND	2017	18	928	91.56 %
Fairview	Bismarck, ND	2008	84	5,436	90.52 %
Family Dollar Store	Mandan, ND	2010	9,100	820	100.00 %
First International Bank & Trust	Moorhead, MN	2011	3,510	1,014	100.00 %
Flickertail	Fargo, ND	2008	180	7,425	88.42 %
Forest Avenue	Fargo, ND	2013	20	785	94.92 %
Four Points Office Building	Fargo, ND	2007	11,973	1,394	100.00 %
Galleria III	Fargo, ND	2010	18	1,117	96.78 %
Garden Grove	Bismarck, ND	2016	95	7,205	95.83 %
Gate City Bank	Grand Forks, ND	2008	17,406	1,522	100.00 %
Georgetown	Fridley, MN	2014	462	33,837	97.04 %
Glen Pond	Eagan, MN	2011	414	33,968	97.52 %
Goldmark Office Park	Fargo, ND	2007	124,425	17,891	64.85 %
Grand Forks Marketplace**	Grand Forks, ND	2003	182,522	21,484	100.00 %
Granger Court	Fargo, ND	2013	59	3,169	95.24 %
Great American Insurance Building	Fargo, ND	2005	15,000	2,245	73.82 %
Griffin Court	Moorhead, MN	2014	128	5,228	86.43 %
Guardian Building Products	Fargo, ND	2012	100,600	3,754	100.00 %
Hannifin	Bismarck, ND	2013	14	789	96.81 %
Harrison Richfield	Grand Forks, ND	2007	140	7,907	95.14 %
Hartford	Fargo, ND	2018	30	1,407	88.03 %
Highland Meadows	Bismarck, ND	2011	144	10,421	95.60 %
Hunter's Run I	Fargo, ND	2007	12	481	97.05 %
Hunter's Run II	Fargo, ND	2008	12	518	92.61 %
Huntington	Fargo, ND	2015	10	435	92.85 %
Islander	Fargo, ND	2011	24	1,159	90.98 %
Jadestone	Fargo, ND	2017	18	838	90.13 %
Kennedy	Fargo, ND	2013	12	813	90.76 %
Library Lane	Grand Forks, ND	2007	60	2,999	94.19 %
Madison (FKA Columbine)	Grand Forks, ND	2015	12	681	88.44 %
Maple Ridge	Omaha, NE	2008	168	10,659	95.32 %
Maplewood	Maplewood, MN	2014	240	16,370	95.10 %
Maplewood Bend	Fargo, ND	2009 and 2010	182	7,326	88.87 %
Martha Alice	Fargo, ND	2009	24	951	91.57 %
Mayfair (FKA Colony Manor)	Grand Forks, ND	2008	24	1,316	90.24 %
Midtown Plaza	Minot, ND	2004	17,797	1,296	97.81 %

Property	Location	Year Acquired	# of Units or Leasable Sq. Ft	Total Investment	Physical Occupancy at December 31, 2019
Monticello	Fargo, ND	2013	18	903	89.12 %
Montreal Courts	Little Canada, MN	2013	444	28,120	96.73 %
Morningside	Fargo, ND	2018	17	761	87.41 %
Oak Court	Fargo, ND	2008	81	2,995	91.98 %
Oakview Townhomes (FKA Arrowhead)	Grand Forks, ND	2017	82	5,909	96.31 %
O'Reilly Auto Store	Mandan, ND	2010	6,300	679	100.00 %
Pacific Park I	Fargo, ND	2013	30	999	93.27 %
Pacific Park II	Fargo, ND	2013	39	1,089	93.52 %
Pacific South	Fargo, ND	2013	15	553	80.58 %
Park Circle	Fargo, ND	2017	18	937	94.23 %
Parkview Arms	Bismarck, ND	2015	62	4,596	94.49 %
Parkway Office (FKA Echelon Building)	Fargo, ND	2006	17,000	1,938	100.00 %
Parkwest Gardens	West Fargo, ND	2014	142	7,849	86.80 %
Parkwood	Fargo, ND	2008	40	1,389	91.21 %
Pebble Creek	Bismarck, ND	2008	70	4,014	95.16 %
Plumtree	Fargo, ND	2017	18	939	89.28 %
Prairiewood Court I & II	Fargo, ND	2006 and 2007	60	2,335	81.69 %
Prairiewood Meadows	Fargo, ND	2012	85	3,537	88.21 %
Quail Creek	Springfield, MO	2015	164	10,996	94.23 %
Redpath	White Bear Lake, MN	2016	25,817	4,017	100.00 %
Regis Building	Edina, MN	2009	102,448	13,131	100.00 %
Robinwood	Coon Rapids, MN	2014	120	8,284	98.34 %
Rosedale Estates	Roseville, MN	2014	360	26,286	95.17 %
Rosegate	Fargo, ND	2008	90	3,560	84.70 %
Roughrider	Grand Forks, ND	2016	12	699	94.11 %
Saddlebrook	West Fargo, ND	2008	60	1,804	88.63 %
Sage Park (FKA Brighton Village)	New Brighton, MN	2014	240	17,636	96.99 %
Sargent	Fargo, ND	2017	36	1,734	90.32 %
Schrock	Fargo, ND	2013	18	751	94.10 %
Sheridan Pointe	Fargo, ND	2013	48	2,884	95.23 %
Sierra Ridge	Bismarck, ND	2006 and 2011	136	10,430	95.30 %
Social Security Building	St. Cloud, MN	2007	10,810	2,912	100.00 %
Somerset	Fargo, ND	2008	75	3,999	92.09 %
Southgate	Fargo, ND	2007	162	6,472	90.93 %
Southview III	Grand Forks, ND	2011	18	738	92.96 %
Southview Village	Fargo, ND	2007	72	3,112	95.44 %
Spring	Fargo, ND	2013	25	975	88.69 %
Stanford Court	Grand Forks, ND	2013	96	4,508	86.96 %
Stonefield	Bismarck, ND	2014	192	31,126	97.33 %
Stony Brook	Omaha, NE	2009	148	11,617	96.40 %
Summerfield	Fargo, ND	2015	18	825	95.01 %
Summit Point	Fargo, ND	2015	87	6,596	94.00 %
Sunchase	Fargo, ND	2017	36	1,878	94.41 %
Sunset Ridge	Bismarck, ND	2008 and 2010	180	13,826	93.79 %
Sunview	Grand Forks, ND	2008	36	1,955	92.65 %
Sunwood Estates	Fargo, ND	2007	81	4,197	91.14 %
Terrace on the Green	Moorhead, MN	2012	116	3,757	85.98 %
Thunder Creek	Fargo, ND	2018	57	4,954	90.24 %
Titan Machinery	Bismarck, ND	2015	22,293	3,423	100.00 %
Titan Machinery	Dickinson, ND	2012	17,760	1,790	100.00 %
Titan Machinery	Fargo, ND	2012	29,800	3,336	100.00 %
Titan Machinery	Marshall, MN	2011	42,000	5,081	100.00 %
Titan Machinery	Minot, ND	2012	23,690	2,630	100.00 %
Titan Machinery	North Platte, NE	2016	16,480	1,769	100.00 %
Titan Machinery	Sioux City, IA	2013	32,532	4,567	100.00 %
Twin Oaks	Hutchinson, MN	2014	80	4,442	97.99 %
Twin Parks	Fargo, ND	2008	66	2,500	91.64 %
Valley Homes Duplexes	Grand Forks, ND	2015	24	2,463	89.22 %
Valley View	Golden Valley, MN	2014	72	7,566	99.03 %
Village Park	Fargo, ND	2008	60	2,368	94.33 %
Village West	Fargo, ND	2008	80	2,980	87.99 %
Walgreens	Alexandria, LA	2009	14,560	4,296	100.00 %

Property	Location	Year Acquired	# of Units or Leasable Sq. Ft	Total Investment	Physical Occupancy at December 31, 2019
Walgreens	Batesville, AR	2009	14,820	7,616	100.00 %
Walgreens	Denver, CO	2011	13,390	5,210	100.00 %
Walgreens	Fayetteville, AR	2009	14,550	5,810	100.00 %
Walgreens	Laurel, MS	2010	14,820	4,542	100.00 %
Washington	Grand Forks, ND	2016	17	745	92.63 %
Wells Fargo Building	Duluth, MN	2007	95,961	10,182	82.13 %
West Oak	Fargo, ND	2017	18	820	87.66 %
Westcourt	Fargo, ND	2014	64	3,580	84.40 %
Westside	Hawley, MN	2010	14	507	89.09 %
Westwind	Fargo, ND	2008	18	620	91.53 %
Westwood Estates	Fargo, ND	2008	200	7,930	87.75 %
Willow Park	Fargo, ND	2008	102	6,668	91.08 %
Woodland Pines (FKA Fredericksburg)	Omaha, NE	2018	173	12,458	94.17 %

\* 70.00% ownership interest

\*\* 66.67% ownership interest

\*\*\* 50.00% ownership interest

The following information applies to all of our operating properties:

- We believe all of our properties are adequately covered by insurance and suitable for their intended purposes;
- Our properties are located in markets where we are subject to competition in attracting new tenants and retaining current tenants; and
- Depreciation is provided on a straight-line basis over the estimated useful lives of the buildings.

## Geography

Of our 173 properties, 125 are located in North Dakota, with 82 being located in the greater Fargo, North Dakota and Moorhead, Minnesota metropolitan statistical area. The North Dakota region generated approximately 48.7% of our rental revenue for the year ended December 31, 2019.

The following table presents the total real estate investment amount by state and annual rental revenue by state, as of and for the years ended December 31, 2019 (in thousands):

State	Real Estate Investment	%	Rental Revenue	%
North Dakota	\$ 408,936	51.0 %	\$ 58,657	48.7 %
Minnesota	302,219	37.7 %	50,756	42.2 %
Other	90,873	11.3 %	10,926	9.1 %
	\$ 802,028	100.0 %	\$ 120,339	100.0 %

## Economy

The North Dakota workforce is concentrated in agricultural, energy, information technology, aerospace sciences and medical sciences. According to the U.S. Census Bureau, the 2018 estimated combined population of the Fargo, West Fargo and Moorhead metro area was 204,759 people.



The following chart depicts the difference in unemployment rates between North Dakota and the national average for 2019:

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
National <sup>(1)</sup>	4.0 %	3.8 %	3.8 %	3.6 %	3.6 %	3.7 %	3.7 %	3.7 %	3.5 %	3.6 %	3.5 %	3.5 %
North Dakota <sup>(1)</sup>	2.5 %	2.4 %	2.3 %	2.3 %	2.3 %	2.3 %	2.4 %	2.4 %	2.5 %	2.5 %	2.5 %	2.4 %

(1) Seasonally adjusted

Source: Bureau of Labor Statistics

## Tenants

Our tenants are varied and consist of individuals and national, regional, and local businesses. Our commercial/retail properties generally attract a mix of tenants. In 2019, 2018 and 2017, no single tenant represented more than 10% of our revenues. We have investments in several types of real estate, including multifamily, retail, office, industrial, restaurant, and medical. Within our office, retail and industrial properties, we have over 100 tenants who operate in numerous industries, including restaurants, pharmacy, medical, financing, banking, insurance, professional services, technology, wholesale and direct retail.

## Lease Expirations

The vast majority of residential leases are for one year periods. The following table lists a summary, as of December 31, 2019, of lease expirations on non-residential properties scheduled to occur during each of the ten calendar years from 2020 to 2029 and thereafter, assuming that tenants exercise no renewal options or early termination rights. Base rents do not include CAM (common area maintenance).

The table is based on leases at December 31, 2019 for our non-residential properties including our unconsolidated affiliates (in thousands, except leasable area data).

Lease Expiration Year	# of Leases Expiring	Gross Leasable Area	% of Gross Leasable Area	Expiring Base Rent	% of Total Base Rent
Month-to-Month	5	35,422	2.33 %	\$ 623	2.79 %
2020	14	212,655	13.97 %	1,117	5.00 %
2021	28	370,306	24.32 %	2,866	12.82 %
2022	20	277,721	18.24 %	2,130	9.52 %
2023	12	65,563	4.31 %	528	2.36 %
2024	9	45,108	2.96 %	287	1.28 %
2025	10	53,991	3.55 %	680	3.04 %
2026	2	97,559	6.41 %	633	2.83 %
2027	3	52,474	3.45 %	375	1.68 %
2028	9	118,386	7.78 %	1,174	5.25 %
2029	3	59,180	3.89 %	683	3.05 %
Thereafter	10	134,051	8.79 %	11,264	50.38 %
Leased Total	125	1,522,416	100.00 %	\$ 22,360	100.00 %

## Mortgage Notes Secured by the Properties

At December 31, 2019, we had \$395,038 in mortgage notes payable with respect to our properties. Principal payments on these notes are payable as follows (in thousands):

Years ending December 31,	Amount
2020	\$ 24,862
2021	38,756
2022	26,458
2023	49,220
2024	19,054
Thereafter	236,688
	<u>\$ 395,038</u>

## Acquisitions and Dispositions

We had no acquisitions or dispositions during the year ended December 31, 2019. Capitalization rates are a key decision-making item used by the Board. In making acquisitions, the Board currently targets capitalization rates between 6.0 to 10.0%, depending on the amount of risk involved. For those properties with greater risk, the Board targets greater capitalization rates (9.0% or greater). For those properties exhibiting less risk, a lower capitalization risk is acceptable. For potential acquisitions, the Board also requires an adequate spread between the financing on the property and the capitalization rate. Capitalization rates for acquisitions are calculated using projected net operating income divided by the investment. Net operating income is calculated by taking GAAP net income and adding back depreciation, amortization and interest expense. Capitalization rates for dispositions are calculated in the same way with the exception of using historical, rather than projected, net operating income. The market has seen an increase in investors, driving up overall acquisition prices, thus lowering capitalization rates below the target thresholds set by the board.

We use historical occupancy, rental income, and expenses to calculate projected net operating income for potential real estate investments. For residential properties, we make various assumptions about future rents, occupancy levels, and expenses based on historical financial information and our assessment of the property's future potential. The projected NOI for residential acquisitions is typically based on historical occupancy and expenses over a three to five year period. When historical information is unavailable, market vacancy and credit loss factors are estimated. We normally do not assign a value to residential tenant leases already in place due to the short-term duration of twelve months or less of these leases and the uncertainty of retaining all tenants due to a change in ownership and in some cases property management companies.

For commercial properties, assumptions regarding rental income and expenses are based on the terms of the in-place leases and available historical financial information which is then used to generate projected net operating income.

Numerous estimates and assumptions are necessary to generate projected net operating income for potential commercial and residential acquisitions, and there is no guarantee actual net operating income will equal projected net operating income.

See financial statement notes 17 and 18 for additional details regarding acquisitions and dispositions.

## Insurance

We believe we have adequate property damage, fire loss and liability insurance on all of our properties with reputable, commercially rated companies. We also believe our insurance policies contain commercially reasonable deductibles and limits, adequate to cover our properties. We expect to maintain this type of insurance coverage and to obtain similar coverage with respect to any additional properties we acquire in the near future. Further, we have title insurance relating to our properties in an aggregate amount we believe to be adequate. In 2019, the operating partnership decided to self-

insure a portion of their habitation insurance policy. The change was due to the evolving insurance market and the rising cost of insurance premiums for the habitation market.

### **Regulations**

Our properties, as well as any other properties we may acquire in the future, are subject to various federal, state and local laws, ordinances and regulations. They include, among other things, zoning regulations, land use controls, environmental controls relating to air and water quality, noise pollution and indirect environmental impacts such as increased motor vehicle activity. We believe we have all permits and approvals necessary under current law to operate our properties.

### **ITEM 3. LEGAL PROCEEDINGS**

The Company is subject, from time to time, to various legal proceedings and claims that arise in the ordinary course of business. While the resolution of such matters cannot be predicted with certainty, management believes, based on currently available information, that the final outcome of such matters will not have a material effect on the financial statements of the Company.

### **ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

## **PART II**

### **ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED SHAREHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

#### **Market Information**

Our common shares of beneficial interest are not listed on any national exchange or over-the-counter market or quoted on any national securities market, and we currently do not have plans to list or have our common shares quoted.

#### **Shareholders and Unit Holders**

As of March 6, 2020, we had 9,562,818, common shares of beneficial interests outstanding, held by a total of 983 common shareholders and no outstanding options or warrants to purchase our common shares.

In addition, as of March 6, 2020, there were approximately 17,917,440 limited partnership units of our operating partnership outstanding held by approximately 513 limited partners. Pursuant to the exchange rights under the LLLP Agreement of the operating partnership, we have the option, upon redemption requests by the holders of the limited partnership units, to acquire the limited partnership units by paying the holders with our common shares of beneficial interest on a one-for-one exchange basis. The numbers of common shareholders and limited partners is based on the Company's records.

#### **Quarterly Dividend Data**

We have declared and intend to continue to declare regular quarterly dividends to our common shareholders. Because all of our operations are conducted through our operating partnership, our ability to pay dividends depends on the operating partnership's ability to make distributions to us and its other limited partners. We pay declared dividends quarterly, whereby the dividend attributable to a calendar quarter would be paid during the first month of the next quarter. Dividends will be paid to common shareholders as of the record dates selected by the Board of Trustees. We intend to make dividends sufficient to satisfy the requirements for qualification as a REIT for federal tax purposes.

The following tables show the dividends we have declared (including the total amount paid on a per share basis, paid in cash, reinvested in shares of our common stock pursuant to the Dividend Reinvestment Plan, and the total amount paid) during the last two fiscal years (in thousands, except per share data).

<b>2019 Quarter Ended</b>	<b>Dividends Per Common Share</b>	<b>Cash</b>	<b>Reinvested via DRP</b>	<b>Total Dividends</b>
December 31	\$ 0.261250	\$ 880	\$ 1,585	\$ 2,465 <sup>(a)</sup>
September 30	\$ 0.261250	881	1,554	2,435
June 30	\$ 0.261250	849	1,558	2,407
March 31	\$ 0.261250	818	1,556	2,374
		\$ 3,428	\$ 6,253	\$ 9,681

<b>2018 Quarter Ended</b>	<b>Dividends Per Common Share</b>	<b>Cash</b>	<b>Reinvested via DRP</b>	<b>Total Dividends</b>
December 31	\$ 0.254375	\$ 802	\$ 1,479	\$ 2,281 <sup>(a)</sup>
September 30	\$ 0.254375	793	1,455	2,248
June 30	\$ 0.254375	759	1,458	2,217
March 31	\$ 0.254375	765	1,425	2,190
		\$ 3,119	\$ 5,817	\$ 8,936

(a) Fourth quarter dividends paid on January 15<sup>th</sup> of the following year.

We expect that future dividends will be maintained at least at the present rate, unless there are changes in our results of operations, our general financial condition, general economic conditions or the Board determines other action prudent.

#### **Sale of Securities**

Neither Sterling nor the operating partnership issued any unregistered securities during the three months ended December 31, 2019.

#### *Other Sales*

During the year ended December 31, 2019, there were 1,475 limited partnership units or \$28,033 exchanged for common shares on a one-for-one basis pursuant to redemption requests made by accredited investors.

## Redemptions of Securities

Set forth below is information regarding common shares and limited partnership units redeemed during the year ended December 31, 2019:

Period	Total Number of Common Shares Redeemed	Total Number of Limited Partner Units Redeemed	Average Price Paid per Common Share/Unit	Total Number of Shares Redeemed as Part of Publicly Announced Plans or Programs	Total Number of Units Redeemed as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares (or Units) that May Yet Be Redeemed Under Publicly Announced Plans or Programs
January 1-31, 2019	3,000	5,000	\$ 18.00	1,190,000	774,000	\$ 7,743
February 1-28, 2019	2,000	3,000	\$ 18.00	1,192,000	777,000	\$ 7,655
March 1-31, 2019	6,000	27,000	\$ 18.00	1,198,000	804,000	\$ 7,059
Total	11,000	35,000				
April 1-30, 2019	4,000	5,000	\$ 18.00	1,202,000	809,000	\$ 6,905
May 1-31, 2019	2,000	8,000	\$ 18.00	1,204,000	817,000	\$ 6,728
June 1-30, 2019	3,000	3,000	\$ 18.00	1,207,000	820,000	\$ 6,632
Total	9,000	16,000				
July 1-31, 2019	5,000	2,000	\$ 18.00	1,212,000	822,000	\$ 6,506
August 1-31, 2019	8,000	2,000	\$ 18.00	1,220,000	824,000	\$ 6,335
September 1-30, 2019	—	1,000	\$ 18.00	1,220,000	825,000	\$ 6,312
Total	13,000	5,000				
October 1-31, 2019	4,000	1,000	\$ 18.00	1,224,000	826,000	\$ 6,219
November 1-30, 2019	1,000	6,000	\$ 18.00	1,225,000	832,000	\$ 6,088
December 1-31, 2019	12,000	1,000	\$ 18.00	1,237,000	833,000	\$ 5,861
Total	17,000	8,000				

For the year ended December 31, 2019, we redeemed all shares or units for which we received redemption requests. In addition, for the year ended December 31, 2019, all common shares and units redeemed were redeemed as part of the publicly announced plans.

The Amended and Restated Share Redemption Plan permits us to repurchase common shares held by our shareholders and limited partnership units held by partners of our operating partnership, up to a maximum amount of \$35,000 worth of shares and units, upon request by the holders after they have held them for at least one year and subject to other conditions and limitations described in the plan. The amount remaining to be redeemed as of December 31, 2019 was \$5,861. The redemption price for such shares and units redeemed under the plan was fixed at \$18.00 per share or unit effective January 1, 2019. Subsequently the redemption price was increased to \$18.25 effective January 1, 2020 and is the current redemption price. The redemption plan will terminate in the event the shares become listed on any national securities exchange, the subject of bona fide quotes on any inter-dealer quotation system or electronic communications network or are the subject of bona fide quotes in the pink sheets. Additionally, the Board, in its sole discretion, may terminate, amend or suspend the redemption plan at any time if it determines to do so is in our best interest.

## ITEM 6. SELECTED FINANCIAL DATA

The following table sets forth our selected consolidated financial information and should be read in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and our audited consolidated financial statements and the notes thereto, both of which appear elsewhere in this Form 10-K.

	December 31,				
	2019	2018	2017	2016	2015
BALANCE SHEET DATA:	(in thousands, except per share data)				
Total assets	\$ 699,686	\$ 714,467	\$ 691,605	\$ 670,513	\$ 642,375
Mortgage loans payable, net	\$ 393,164	\$ 406,017	\$ 394,843	\$ 390,479	\$ 379,911
Total liabilities	\$ 420,639	\$ 430,716	\$ 417,830	\$ 411,858	\$ 401,948
Stockholders' equity	\$ 279,047	\$ 283,751	\$ 273,775	\$ 258,655	\$ 240,427
	Year Ended December 31,				
	2019	2018	2017	2016	2015
STATEMENT OF OPERATIONS DATA:					
Rental income	\$ 120,339	\$ 116,051	\$ 114,280	\$ 108,063	\$ 97,182
Operating expenses	100,713	96,062	95,044	91,500	81,834
Interest	18,282	18,329	18,630	18,366	17,141
Depreciation and amortization	21,495	21,350	21,544	22,145	19,574
Total expenses	104,825	100,162	100,188	97,100	87,481
Total other income (expense)	545	6,089	5,791	1,894	1,683
Loss on impairment of property	—	—	—	—	412
Net income	16,059	21,978	19,883	12,857	11,384
Noncontrolling interest in income	10,525	14,604	13,369	8,432	7,098
Net income attributable to Sterling	\$ 5,534	\$ 7,374	\$ 6,514	\$ 4,425	\$ 4,286
Net income per common share	\$ 0.60	\$ 0.84	\$ 0.78	\$ 0.56	\$ 0.59
Weighted average shares outstanding	9,268	8,791	8,300	7,844	7,223
STATEMENT OF CASH FLOWS DATA:					
Cash flows provided by operating activities	\$ 41,326	\$ 38,422	\$ 37,478	\$ 34,999	\$ 28,315
Cash flows used in investing activities	(19,373)	(17,017)	(13,019)	(15,127)	(25,766)
Cash flows provided by (used in) financing activities	(34,636)	(11,893)	(23,176)	(13,178)	3,269
OTHER DATA					
Dividends declared (a)	\$ 9,681	\$ 8,936	\$ 8,212	\$ 7,527	\$ 6,885
Dividends declared per share	\$ 1.0450	\$ 1.0175	\$ 0.9900	\$ 0.9600	\$ 0.9300

(a) Consists of dividends paid by the Trust on its common shares of beneficial interest.

## ITEM 7. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

### Safe Harbor Statement Under the Private Securities Litigation Reform Act of 1995

Certain statements contained in this section and elsewhere in this Form 10-K constitute “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements involve a number of known and unknown risks, uncertainties and other factors which may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Please see “Note Regarding Forward-Looking Statements” and “Risk Factors” for more information. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date the statements were made and are not guarantees of future performance.

## Executive Summary

Our real estate portfolio as of December 31, 2019 consists of 173 properties in 11 states. Our properties are primarily located in North Dakota and Minnesota and contain 9,852 apartment units and approximately 1,662,000 square feet of leasable commercial space. The portfolio has a net book value of real estate investments (cost less accumulated depreciation) of approximately \$655,712, which includes construction in progress. Our portfolio of properties currently includes a diversified mixture of multifamily, single and multi-tenant retail and office buildings. The Trust's current investment strategy is to focus on multifamily real estate properties located primarily in the central corridor of the contiguous forty-eight (48) states. There is no current plan for the existing commercial properties (industrial, medical, office, and retail) in regards to retention or disposition.

## Specific Achievements

- Increased revenues from rental operations by \$4,288 or 3.7% for the year ended December 31, 2019, compared to the year ended December 31, 2018.
- Declared and paid dividends aggregating \$1.045 per common share for the year ended December 31, 2019.

## Results of Operations for the Years Year Ended December 31, 2019 and 2018

	Year ended December 31, 2019			Year ended December 31, 2018		
	Residential	Commercial (unaudited) (in thousands)	Total	Residential	Commercial (unaudited) (in thousands)	Total
Real Estate Revenues	\$ 94,763	\$ 25,576	\$ 120,339	\$ 89,783	\$ 26,268	\$ 116,051
Real Estate Expenses						
Real Estate Taxes	9,372	2,706	12,078	8,870	2,754	11,624
Property Management	12,470	975	13,445	11,761	904	12,665
Utilities	8,198	1,174	9,372	7,746	1,460	9,206
Repairs and Maintenance	21,030	2,235	23,265	18,533	2,141	20,674
Insurance	2,684	92	2,776	2,138	98	2,236
Total Real Estate Expenses	53,754	7,182	60,936	49,048	7,357	56,405
Net Operating Income	<u>\$ 41,009</u>	<u>\$ 18,394</u>	<u>59,403</u>	<u>\$ 40,735</u>	<u>\$ 18,911</u>	<u>59,646</u>
Interest			18,282			18,329
Depreciation and amortization			21,495			21,350
Administration of REIT			4,112			4,100
Loss on lease terminations			—			(22)
Other (income)/expense			(545)			(6,089)
Net Income			<u>\$ 16,059</u>			<u>\$ 21,978</u>
Net Income Attributed to:						
Noncontrolling Interest			\$ 10,525			\$ 14,604
Sterling Real Estate Trust			\$ 5,534			\$ 7,374
Dividends per share <sup>(1)</sup>			\$ 1.0450			\$ 1.0175
Earnings per share			\$ 0.6000			\$ 0.8400
Weighted average number of common shares			9,268			8,791

(1) Does not take into consideration the amounts distributed by the operating partnership to limited partners.

## Revenues

Property revenues totaled approximately \$120,339 for the year ended December 31, 2019 which constituted an increase of approximately \$4,288 or 3.7% compared to the same period in 2018. Residential property revenues increased approximately \$4,980 and commercial property revenues decreased approximately \$692.

The following table illustrates the occupancy percentage for the periods ended indicated:

	December 31, 2019	December 31, 2018
Residential occupancy	93.7 %	93.6 %
Commercial occupancy	91.8 %	90.2 %

Residential revenues for the year ended December 31, 2019 increased \$4,980 in comparison to the same period for 2018. Residential properties acquired since January 1, 2018 contributed approximately \$2,308 to the increase in total residential revenues in the twelve months ended December 31, 2019. The remaining increase is due to increased rent charges at our stabilized properties, decreased vacancy, as well as increased collection efforts on receivable balances written off. Income related to Ratio Utility Billing System (RUBS) income in our Minneapolis market also contributed to the overall residential income increase. Residential revenues comprised 78.7% of total revenues for the year ended December 31, 2019 compared to 77.3% of total revenues for the year ended December 31, 2018. Residential occupancy year-over-year has remained comparable increasing 0.1%, during the year ended December 31, 2019.

For the year ended December 31, 2019, total commercial revenues decreased \$692 in comparison to the same period for 2018. The decrease was primarily attributable to the sale of three commercial properties in 2018, as well as rental incentives recorded in 2019 for an office building in Minneapolis, Minnesota. Commercial revenues comprised 21.3% of the total revenues for the year ended December 31, 2019 compared to 22.7% of total revenues for the year ended December 31, 2018. Commercial occupancy year-over-year has remained comparable, increasing 1.6%, during the year ended December 31, 2019. The increase is primarily due to fourth quarter leasing activity that occurred in properties located in Minnesota.

### ***Expenses***

Residential expenses from operations of \$53,754 during the year ended December 31, 2019 increased \$4,706 or 9.6% in comparison to the same period in 2018. The increase was attributed to an increase in repairs and maintenance expense of \$2,497 or 13.5%, related to upgrades occurring on properties in the North Dakota region. Increases in real estate taxes of \$502 or 5.7% and property insurance of \$546 or 25.5% also contributed to the overall operational expense increase. Actual property management fees increased \$709 or 6%, during the year ended December 31, 2019 and continue to approximate 5% of net collected rents; however, other property management related expenses have increased due to increased competition for labor.

Commercial expenses from operations of \$7,182 during the year ended December 31, 2019 decreased \$175 or 2.4% in comparison to the same period in 2018. The decrease was attributed to a decrease in utilities expense of \$286 or 19.59%. The utility decrease was offset by an increase to repairs and maintenance expense of \$94 or 4.4%, during the year ended December 31, 2019. These operational expense variances primarily relate to the demolition and disposition of a commercial property in Fargo, North Dakota. Property management expense increased by \$71 or 7.9%, during the year ended December 31, 2019 which offset the decrease in utility expense.

Interest expense of \$18,282 during the year ended December 31, 2019 decreased \$47 or 0.3% in comparison to the same period in 2018. Interest expense was approximately 15.19% and 15.79% of rental income for the year ended December 31, 2019 and 2018, respectively. The decrease of interest expense primarily relates to increased construction in progress. Interest expense for construction in progress is classified as a contra-expense account, offsetting interest expense. Pay offs of higher interest rate loans during the year end 2019 decreased the overall rated average interest rate on our consolidated mortgage debt. Interest expense on mortgages for the years ended December 31, 2019 and 2018 as a percentage of revenue was 14.7% and 14.9% respectively.

Depreciation and amortization expense of \$21,495 during the year ended December 31, 2019 increased \$145 or 0.7% in comparison to the same period in 2018. The increase is primarily due to normal increases in monthly amortization expense.

Other income (expense) of \$545 for the year ended December 31, 2019 decreased \$5,544 or 91% in comparison to the same period in 2018. The decrease was primarily attributed to disposition activity in the prior period that did not occur in



the current period. In addition, during the year ended December 31, 2018 we recognized a gain on involuntary conversion of \$1,467 and a gain on sale of real estate investments of \$3,715, where no such capital transaction occurred during the year ended December 31, 2019. Furthermore, during the year ended December 31, 2019, we incurred a \$816 loss on involuntary conversion due to the evaluation and analysis of a commercial property in Fargo, ND, where the future economic benefit of a portion of the property was determined to be non-recoverable. Based on the facts and circumstances surrounding the demolition, we will not be recognizing insurance proceeds related to the loss.

REIT administration expenses of \$4,112 for the year ended December 31, 2019 increased \$12 or 0.3% in comparison to the same period in 2018.

### ***Net Operating Income***

We measure the performance of our segments based on net operating income (“NOI”), which we define as total revenue from rental operations less expenses from rental operations and real estate taxes (excluding depreciation and amortization related to real estate investments and impairment of real estate investments). We believe that NOI is an important supplemental measure of operating performance for a REIT because it provides a measure of core operations unaffected by depreciation, amortization, financing, and administration expense. NOI does not represent cash generated by operating activities in accordance with GAAP and should not be considered an alternative to net income, net income available for non-controlling interests and shareholders of the Trust or cash flow from operating activities as a measure of financial performance. See Note 3 to the Consolidated Financial Statements included herein, as well as the above table for more information on NOI performance by segment.

### ***Net Income***

Net income for the year ended December 31, 2019 was \$16,059 compared to \$21,978 for the year ended December 31, 2018. During the year ended December 31, 2018, the Company recognized gains in other income totaling \$5,181, as discussed above, which resulted in higher net income in the prior period than the current period.

## Results of Operations for the Years Ended December 31, 2018 and 2017

	Year ended December 31, 2018			Year ended December 31, 2017		
	Residential	Commercial (unaudited) (in thousands)	Total	Residential	Commercial (unaudited) (in thousands)	Total
Real Estate Revenues	\$ 89,783	\$ 26,268	\$ 116,051	\$ 86,858	\$ 27,422	\$ 114,280
Real Estate Expenses						
Real Estate Taxes	8,870	2,754	11,624	8,118	2,934	11,052
Property Management	11,761	904	12,665	11,363	872	12,235
Utilities	7,746	1,460	9,206	7,103	1,423	8,526
Repairs and Maintenance	18,533	2,141	20,674	19,293	2,120	21,413
Insurance	2,138	98	2,236	1,406	92	1,498
Total Real Estate Expenses	49,048	7,357	56,405	47,283	7,441	54,724
Net Operating Income	<u>\$ 40,735</u>	<u>\$ 18,911</u>	<u>59,646</u>	<u>\$ 39,575</u>	<u>\$ 19,981</u>	<u>59,556</u>
Interest			18,329			18,630
Depreciation and amortization			21,350			21,544
Administration of REIT			4,100			5,144
Loss on lease terminations			(22)			146
Other (income)/expense			(6,089)			(5,791)
Net Income			<u>\$ 21,978</u>			<u>\$ 19,883</u>
Net Income Attributed to:						
Noncontrolling Interest			\$ 14,604			\$ 13,369
Sterling Real Estate Trust			\$ 7,374			\$ 6,514
Dividends per share <sup>(1)</sup>			\$ 1.01750			\$ 0.9900
Earnings per share			\$ 0.8400			\$ 0.7800
Weighted average number of common shares			8,791			8,300

(1) Does not take into consideration the amounts distributed by the operating partnership to limited partners.

### Revenues

Property revenues totaled approximately \$116,051 for the year ended December 31, 2018 which constituted an increase of approximately \$1,771 or 1.5% compared to the same period in 2017. Residential property revenues increased approximately \$2,925 and commercial property revenues decreased approximately \$1,154.

The following table illustrates changes the occupancy percentage for the twelve month periods indicated:

	December 31, 2018	December 31, 2017
Residential occupancy	93.6 %	94.7 %
Commercial occupancy	90.2 %	95.6 %

Residential revenues for the year ended December 31, 2018 increased \$2,925 in comparison to the same period for 2017. Residential properties acquired since January 1, 2017 contributed approximately \$2,576 to the increase in total residential revenues in the year ended December 31, 2018. Residential revenues comprised 77.3% of total revenues for the year ended December 31, 2018 compared to 76.0% of total revenues for the year ended December 31, 2017. Residential occupancy year-over-year decreased 1.1% due to increased competition from development of new properties.

For the year ended December 31, 2018 total commercial revenues decreased \$1,154 in comparison to the same period for 2017. Rental income from commercial properties acquired since January 1, 2017 decreased approximately \$1,255 in comparison to the year ended December 31, 2017. The decrease was primarily attributed to the sale of three commercial

properties in the second and third quarters of 2018 offset by the acquisition of one retail property in September 2018. Commercial revenues comprised 22.7% of total revenue for the year ended December 31, 2018 compared to 24.0% of total revenues for the year ended December 31, 2017. Commercial physical occupancy decreased 5.4% due to increased development of new commercial properties, primarily in the North Dakota region.

### ***Expenses***

Residential expenses from operations of \$49,048 during the year ended December 31, 2018 increased \$1,765 or 3.7% in comparison to the same period in 2017. Expenses driving this increase were real estate tax expenses, which increased \$752 or 9.3% primarily due to real estate tax law changes in North Dakota and property insurance which increased \$733 or \$52.1% due to higher premiums, and additional property through acquisition purchases. Actual property management fees remained relatively unchanged and continued to approximate 5% of net collected rents; however, other property management related expenses increased due to increased competition for labor.

Commercial expenses from operations of \$7,357 during the year ended December 31, 2018 decreased \$84 or 1.13% in comparison to the same period in 2017. The decrease was primarily driven by the decrease in real estate tax expense of \$180 of 6.1%, relating to the sale of commercial properties during the year ended December 31, 2018.

Interest expense of \$18,329 during the year ended December 31, 2018 decreased \$301 or 1.62% in comparison to the same period in 2017 due to decreased financing activity during the year. At year end there were several new loans issued that minimally impacted interest expense. Interest expense was approximately 15.8% and 16.3% of rental income for the years ended December 31, 2018 and 2017, respectively.

Depreciation and amortization expense of \$21,350 decreased \$194 or 0.9% for the year ended December 31, 2018 in comparison to the same period in 2017. Amortization expense will continue to decrease as lease intangibles become fully amortized. Depreciation and amortization expense as a percentage of rental income for the years ended December 31, 2018 and 2017 was relatively consistent at 18.4% and 18.9%, respectively.

Other income (expense) during the year ended December 31, 2018 was \$6,089. During the year ended December 31, 2018, the Company recognized a net gain of \$3,715 on the sale of real estate investments (three properties) and a gain on involuntary conversion of \$1,467. In comparison, the Company's other income (expense) during the year ended December 31, 2017 included a net gain of \$2,049 incurred in connection with the sale of a retail property in June 2017 and the sale of vehicles in January 2017. In addition, other income in the year ended December 31, 2017 included a \$2,186 gain on a change in control over a real estate investment.

REIT administration expenses decreased from \$5,144 for the year ended December 31, 2017 to \$4,100 for the year ended December 31, 2018 due to a decrease in acquisition expenses. The acquisitions completed after July 1, 2017 were considered asset acquisitions and as such, transaction costs were capitalized upon closing.

### ***Net Income***

Net income for the year ended December 31, 2018 was \$21,978 compared to \$19,883 for the year ended December 31, 2017, an increase of \$2,095. During the year ended December 31, 2018, the Company recognized a net gain of \$3,715 on the sale of real estate investments and a gain on involuntary conversion of \$1,467. In comparison, the Company's other income (expense) during the year ended December 31, 2017 included a net gain of \$2,049 incurred in connection with the sale of a retail property in June 2017 and the sale of vehicles in January 2017. In addition, the prior period other income included a \$2,186 gain on change in control over a real estate investment in 2017.

### ***Property Acquisitions and Dispositions***

#### *Property Acquisitions and Dispositions during the year ended December 31, 2019*

During the year ended December 31, 2019, there were no acquisitions or dispositions. The market has seen an increase in investors, driving up overall acquisition prices, thus lowering capitalization rates below the target thresholds set by the board.

#### *Property Acquisitions and Dispositions during the year ended December 31, 2018*

We acquired nine properties for a total of \$31,501 during the year ended December 31, 2018. Total consideration for the acquisitions was the issuance of approximately \$7,819 in limited partnership units of the operating partnership, 1031 tax-deferred exchange funds of \$11,326, assumed loans of \$2,104, assumed liabilities of \$576 and cash of \$9,676.

During the year ended December 31, 2018, the operating partnership sold three properties. We sold an industrial property located in Redwood Falls, Minnesota for \$5,200 and recognized a gain of \$935 in April 2018. We sold a retail property located in Austin, Texas for \$3,615 and recognized a gain of \$1,266 in July 2018. We sold one of two buildings included in an office property located in Bismarck, North Dakota for \$4,250 and recognized a gain of \$1,514 in July 2018.

#### *Property Acquisitions and Dispositions during the year ended December 31, 2017*

We acquired 12 properties for a total of \$23,195 during the year ended December 31, 2017. Total consideration for the acquisitions was the issuance of approximately \$10,006 in limited partnership units of the operating partnership, 1031 tax-deferred exchange funds of \$4,278, new loans of \$4,180, assumed liabilities of \$132 and cash of \$4,599. In addition, there was a change in control over a real estate investment, with the operating partnership acquiring the other tenant in common's 59.74% ownership interest in the property (see Notes 2 and 18 of the consolidated financial statements). We estimated the property had a fair value of \$10,080. The operating partnership assumed a loan of \$1,295 and issued \$4,727 of limited partnership units for a total purchase price of approximately \$6,022. The Company accounted for this as a business combination and recognized a gain on change in control of real estate investment of \$2,186 in the second quarter of 2017 as a result of remeasuring the carrying value to fair value.

During the year ended December 31, 2017, the operating partnership sold a retail property in Fargo, North Dakota for approximately \$4,400 and recognized a gain of \$2,072.

See Notes 17 and 18 to the Consolidated Financial Statements included herein for more information regarding our acquisitions and dispositions during the years ended December 31, 2019 and 2018 and 2017.

### ***Joint Venture***

During the year ended December 31, 2019, the operating partnership invested in two joint ventures.

The operating partnership owns a 60% interest in a joint venture ("SE Savage") that is currently developing a 190 unit multifamily property. The operating partnership has contributed \$3,277 in cash to SE Savage during 2019. SE Savage holds land located in Savage, Minnesota, total assets of \$5,464, and no mortgage payable.

The operating partnership owns a 60% interest in a joint venture ("SE Maple Grove") that intends to develop a 160 unit multifamily property. The operating partnership has contributed \$2,073 in cash to SE Maple Grove during 2019. SE Maple Grove holds land located in Maple Grove, Minnesota, total assets of \$3,455, and no mortgage payable.

## **Funds From Operations (FFO)**

Funds From Operations (FFO) applicable to common shares and limited partnership units means net income (computed in accordance with GAAP), excluding gains (or losses) from sales of property, plus depreciation and amortization, and after adjustments for unconsolidated partnerships and joint ventures. Adjustments for unconsolidated partnerships and joint ventures will be calculated to reflect funds from operations on the same basis.

Historical cost accounting for real estate assets implicitly assumes the value of real estate assets diminishes predictably over time. Since real estate values have historically risen or fallen with market conditions, many industry investors have considered presentations of operating results for real estate companies that use historical cost accounting to be insufficient by themselves. The term Funds From Operations (FFO) was created to address this problem. It was intended to be a standard supplemental measure of REIT operating performance that excluded historical cost depreciation from — or “added back” to — GAAP net income.

Our management believes this non-GAAP measure is useful to investors because it provides supplemental information that facilitates comparisons to prior periods and for the evaluation of financial results. Management uses this non-GAAP measure to evaluate our financial results, develop budgets and manage expenditures. The method used to produce non-GAAP results is not computed according to GAAP, is likely to differ from the methods used by other companies and should not be regarded as a replacement for corresponding GAAP measures. Management encourages the review of the reconciliation of this non-GAAP financial measure to the comparable GAAP results.

Since the introduction of the definition of FFO, the term has come to be widely used by REITs. In the view of National Association of Real Estate Investment Trusts (“NAREIT”), the use of the definition of FFO (combined with the primary GAAP presentations required by the Securities and Exchange Commission) has been fundamentally beneficial, improving the understanding of operating results of REITs among the investing public and making it easier than before to compare the results of one REIT with another.

While FFO applicable to common shares and limited partnership units are widely used by REITs as performance metrics, all REITs do not use the same definition of FFO or calculate FFO in the same way. The FFO reconciliation presented here is not necessarily comparable to FFO presented by other real estate investment trusts. FFO should also not be considered as an alternative to net income as determined in accordance with GAAP as a measure of a real estate investment trust’s performance, but rather should be considered as an additional, supplemental measure, and should be viewed in conjunction with net income as presented in the consolidated financial statements included in this report. FFO applicable to common shares and limited partnership units does not represent cash generated from operating activities in accordance with GAAP, and is not necessarily indicative of sufficient cash flow to fund a real estate investment trust’s needs or its ability to service indebtedness or to pay dividends to shareholders.

The following tables include calculations of FFO, and the reconciliations to net income, for the years ended December 31, 2019, 2018 and 2017, respectively. We believe these calculations are the most comparable GAAP financial measure (in thousands):

*Reconciliation of Net Income Attributable to Sterling to FFO Applicable to Common Shares and Limited Partnership Units*

	Year ended December 31, 2019			Year ended December 31, 2018			Year ended December 31, 2017		
	Amount	Weighted Avg Shares and Units(1)	Per Share and Unit (2)	Amount	Weighted Avg Shares and Units(1)	Per Share and Unit (2)	Amount	Weighted Avg Shares and Units(1)	Per Share and Unit (2)
	(in thousands, except per share data)								
Net Income attributable to Sterling Real Estate Trust	\$ 5,534	9,268	\$ 0.60	\$ 7,374	8,791	\$ 0.84	\$ 6,514	8,300	\$ 0.78
Add back:									
Noncontrolling Interest - OPU	10,647	17,831		14,768	17,607		13,634	17,375	
Depreciation & Amortization from continuing operations	21,495			21,350			21,544		
Pro rata share of unconsolidated affiliate depreciation & amortization	378			377			382		
Subtract:									
Gain on sale of land, depreciable real estate, investment in equity method investee, and change in control of real estate investments	—			(3,715)			(4,261)		
Funds from operations applicable to common shares and limited partnership units (FFO)	\$ 38,054	27,099	\$ 1.40	\$ 40,154	26,398	\$ 1.52	\$ 37,813	25,675	\$ 1.47

(1) Please see Note 10 and Note 12 to the consolidated financial statements included above for more information.

(2) Net Income is calculated on a per share basis. FFO is calculated on a per share and unit basis.

## Liquidity and Capital Resources

Our principal demands for funds will be for the: (i) acquisition of real estate and real estate-related investments, (ii) payment of acquisition related expenses and operating expenses, (iii) payment of dividends/distributions, (iv) payment of principal and interest on current and any future outstanding indebtedness, (v) redemptions of our securities under our redemption plans and (vi) capital improvements and property related expenditures. Generally, we expect to meet cash needs for the payment of operating expenses and interest on outstanding indebtedness from cash flow from operations. We expect to pay dividends/distributions and fund any repurchase requests from our shareholders and the unit holders of our operating partnership from cash flow from operations; however, we may use other sources to fund dividends/distributions and repurchases, as necessary. We expect to meet cash needs for acquisitions and other real-estate investments from cash flow from operations, net proceeds of share offerings, UPREIT issuance of partnership units and debt proceeds.

### *Evaluation of Liquidity*

We continually evaluate our liquidity and ability to fund future operations, debt obligations and any repurchase requests. As part of our analysis, we consider among other items, credit quality of tenants and lease expirations.

### *Credit Quality of Tenants*

We are exposed to credit risk within our tenant portfolio, which can reduce our results of operations and cash flow from operations if our tenants are unable to pay their rent. Tenants experiencing financial difficulties may become delinquent on their rent or default on their leases and, if they file for bankruptcy protection, may reject our lease in bankruptcy court, resulting in reduced cash flow. This may negatively impact net asset values and require us to incur impairment charges. Even if a default has not occurred and a tenant is continuing to make the required lease payments, we may restructure or renew leases on less favorable terms, or the tenant's credit profile may deteriorate, which could affect the value of the leased asset and could in turn require us to incur impairment charges.

Historically, the geographic location of our properties and credit-worthiness of our tenants have resulted in minimal to no property impairments. We currently anticipate the trend to continue. It is possible, however, that tenants may file for bankruptcy or default on their leases in the future and that economic conditions may deteriorate. In addition, occupancy levels in markets may decline.

To mitigate credit risk on commercial properties, we have historically looked to invest in assets that we believe are critically important to our tenant's operations and have attempted to diversify our portfolio by tenant, tenant industry and geography. We also monitor all of our properties' performance through review of rent delinquencies as a precursor to a potential default, meetings with tenant management and review of tenants' financial statements and compliance with financial covenants. When necessary, our asset management process includes restructuring transactions to meet the evolving needs of tenants, refinancing debt and selling properties, as well as protecting our rights when tenants default or enter into bankruptcy.

### *Lease Expirations and Occupancy*

There is one material commercial triple net lease is scheduled to expire in the next twelve months. The Advisor, with the assistance of our property managers, actively manages our real estate portfolio and begins discussing options with tenants in advance of scheduled lease expirations. In certain cases, we may obtain lease renewals from our tenants; however, tenants may elect to move out at the end of their term. In the cases where tenants elect not to renew, we may seek replacement tenants or try to sell the property.

### *Cash Flow Analysis*

Our objectives are to generate sufficient cash flow over time to provide shareholders with increasing dividends and to seek investments with potential for strong returns and capital appreciation throughout varying economic cycles. We have funded 100% of dividends paid from operating cash flows. In setting a dividend rate, we focus primarily on expected returns from investments we have already made to assess the sustainability of a particular dividend rate over time.

	Year Ended December 31,	
	2019	2018
	(in thousands)	
Net cash flows provided by operating activities	\$ 41,326	\$ 38,422
Net cash flows used in investing activities	\$ (19,373)	\$ (17,017)
Net cash flows used in financing activities	\$ (34,636)	\$ (11,893)

### *Operating Activities*

Our real estate properties generate cash flow in the form of rental revenues, which is reduced by interest payments, direct lease costs and property-level operating expenses. Property-level operating expenses consist primarily of property management fees including salaries and wages of property management personnel, utilities, cleaning, repairs, insurance, security and building maintenance cost, and real estate taxes. Additionally, we incur general and administrative expenses, advisory fees, acquisition and disposition expenses and financing fees.

Net cash provided by operating activities was \$41,326 and \$38,422 for the years ended December 31, 2019 and 2018, respectively, which consists primarily of net income from property operations adjusted for non-cash depreciation and amortization. The funds generated for the years ended December 31, 2019 and 2018 were primarily from property operations of our real estate portfolio.

#### *Investing Activities*

Our investing activities generally consist of real estate-related transactions (purchases and sales of properties) and payments of capitalized property-related costs such as intangible assets and reserve escrows.

Net cash used in investing activities was \$19,373 and \$17,017 for the years ended December 31, 2019 and 2018, respectively (this does not include the value of UPREIT units issued in connection with investing activities). For the years ended December 31, 2019 and 2018, cash flows used in investing activities related primarily to 2019 and 2018 capital expenditures of \$15,445 and \$10,273, respectively, as well as 2019 investment in unconsolidated affiliates of \$5,350 and 2018 acquisition activity of \$20,419. In addition, during the year ended December 31, 2019, a \$1,300 revolving line of credit was made to an unrelated third party. The line bears an interest rate of Prime Plus 2% or 6.75% as of December 31, 2019. In addition, during the years ended December 31, 2019 and 2018, proceeds of \$2,596 and \$1,112 were received from involuntary conversions.

#### *Financing Activities*

Our financing activities generally consist of funding property purchases by raising capital, issuing UPREIT units, using excess cash and/or securing mortgage notes payable as well as paying dividends, paying syndication costs and making principal payments on mortgage notes payable.

Net cash used in financing activities was \$34,636 and \$11,893 for the years ended December 31, 2019 and 2018, respectively. During the year ended December 31, 2019, we paid \$21,872 in dividends and distributions, redeemed \$2,023 of shares and units, received proceeds of \$3,293 from optional cash purchases, \$15,087 from new mortgage notes payable, and made mortgage principal payments of \$28,388. For the year ended December 31, 2018, we paid \$21,265 in dividends and distributions, redeemed \$2,431 of shares and units, received proceeds of \$4,176 from optional cash purchases, new mortgage notes payable of \$23,728, and made mortgage principal payments of \$15,060.

#### *Dividends*

##### *Common Stock*

We declared cash dividends to our shareholders during the period from January 1, 2019 to December 31, 2019 totaling \$9,681 or \$1.045 per share, of which \$3,426 was cash dividends and \$6,253 were reinvested through the dividend reinvestment plan.

We declared cash dividends to our shareholders during the period from January 1, 2018 to December 31, 2018 totaling \$8,936 or \$1.0175 per share, of which \$3,119 was cash dividends and \$5,817 were reinvested through the dividend reinvestment plan.

We continue to provide cash dividends to our shareholders from cash generated by our operations. The following chart summarizes the sources of our cash used to pay dividends. Our primary source of cash is cash flow provided by operating activities from our investments as presented in our cash flow statement. We also include distributions from unconsolidated affiliates to the extent that the underlying real estate operations in these entities generate these cash flows and the gain on sale of properties relates to net profits from the sale of certain properties. Our presentation is not intended to be an alternative to our consolidated statement of cash flows and does not present all sources and uses of our cash.



The following table presents certain information regarding our dividend coverage:

	Year Ended December 31,	
	2019	2018
	(in thousands)	
Cash flows provided by operations (includes net income of \$16,059 and \$21,978, respectively)	\$ 41,326	\$ 38,422
Distributions in excess of earnings received from unconsolidated affiliates	126	162
Gain (Loss) on sales of real estate and non-real estate investments	—	3,715
Dividends declared	(9,681)	(8,936)
Excess	<u>\$ 31,771</u>	<u>\$ 33,363</u>

#### *Limited Partnership Units*

The operating partnership agreement provides that our operating partnership will distribute to the partners (subject to certain limitations) cash from operations on a quarterly basis (or more frequently, if we so elect) in accordance with the percentage interests of the partners. We determine the amounts of such distributions in our sole discretion.

For the year ended December 31, 2019, we declared quarterly distributions totaling \$18,627 to holders of limited partnership units in our operating partnership, which we paid on April 15, July 15, and October 15, 2019 and January 15, 2020. Distributions were paid at a rate of \$0.26125 per unit per quarter, which is equal to the per share distribution rate paid to the common shareholders.

For the year ended December 31, 2018, we declared quarterly distributions totaling \$17,955 to holders of limited partnership units in our operating partnership, which we paid on April 16, July 16, October 16, 2018 and January 15, 2019. Distributions were paid at a rate of \$0.254375 per unit per quarter, which is equal to the per share distribution rate paid to the common shareholders.

#### *Sources of Dividends*

For the year ended December 31, 2019, we declared aggregate dividends of \$9,681, which were paid with cash flows provided by operating activities and distributions from unconsolidated affiliates. Our funds from operations, or FFO, was \$38,054, therefore, our management believes our distribution policy is sustainable over time. For the year ended December 31, 2018, we declared aggregate dividends of \$8,936 which were paid with cash flows provided by operating activities and distributions from unconsolidated affiliates. Our FFO was \$40,154 for the year ended December 31, 2018. For a further discussion of FFO, including a reconciliation of FFO to net income, see “Funds from Operations” above.

#### *Cash Resources*

At December 31, 2019, our cash resources consisted of cash and cash equivalents totaling approximately \$9,002. Our cash reserves can be used for working capital needs and other commitments. In addition, we had unencumbered properties with a gross book value of \$70,180, which could potentially be used as collateral to secure additional financing in future periods.

At December 31, 2019, there was no balance outstanding on the lines of credit totaling \$32,815. Of the \$32,815 available as of December 31, 2019, one variable rate line of credit secured two letters of credit totaling \$1,216, leaving \$31,599 available and unused under the agreements. See Note 6 to the accompanying consolidated financial statements for additional details regarding our line of credit agreements.

The sale of our securities and issuance of limited partnership units of the operating partnership in exchange for property acquisitions and sale of additional common or preferred shares is also expected to be a source of long-term capital for us. During the year ended December 31, 2019, we did not sell any common shares in private placements. During the year ended December 31, 2019, we issued 340,000 and 173,000 common shares under the dividend reinvestment plan and optional share purchases, respectively which raised gross proceeds of \$9,438. During the year ended December 31, 2018,

we did not sell any common shares in private placements. During the year ended December 31, 2018, we issued 325,000 and 226,000 common shares under the dividend reinvestment plan and as optional share purchases, respectively which raised gross proceeds of \$9,887.

At December 31, 2019, our restricted deposits of \$8,380 consisted of lenders' escrows and funds restricted through lender or other agreements.

During the year ended December 31, 2019, no partnership units were issued in relation to property acquisitions.

During the year ended December 31, 2018, we issued limited partnership units valued at approximately \$7,819 in connection with the acquisition of nine properties.

### Off-Balance Sheet Arrangements

As of December 31, 2019, and 2018, we had no off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

### Contractual Obligations

The table below presents our obligations and commitments to make future payments under our debt obligations as of December 31, 2019.

	Payments Due by Year (in thousands)						Total
	2020	2021	2022	2023	2024	Thereafter	
Long-term debt (a):							
Fixed rate (b)	\$ 24,862	\$ 38,756	\$ 26,458	\$ 49,220	\$ 19,054	\$ 236,688	\$ 395,038
Interest (c)	15,129	13,845	12,721	10,748	9,184	26,866	88,493
Special assessments	74	44	44	44	45	437	688
	<u>\$ 40,065</u>	<u>\$ 52,645</u>	<u>\$ 39,223</u>	<u>\$ 60,012</u>	<u>\$ 28,283</u>	<u>\$ 263,991</u>	<u>\$ 484,219</u>

- (a) Amounts exclude capitalized loan fees of \$1,874, net of accumulated amortization, as of December 31, 2019. Fixed rate amounts for each year include scheduled principal amortization payments.
- (b) Included in fixed rate debt is \$12,960 of variable rate mortgage debts that have been swapped to fixed rate through their maturities on April 2020 and November 2029.
- (c) Represents expected interest payments on our consolidated debt obligations as of December 31, 2019.

### Inflation

Substantially all of our multifamily property leases are for a term of one year or less. In an inflationary environment, this may allow us to realize increased rents upon renewal of existing leases or the beginning of new leases. Short-term leases generally will minimize our risk from the adverse effects of inflation, although these leases generally permit residents to leave at the end of the lease term and therefore will expose us to the effect of a decline in market rents. In a deflationary rent environment, we may be exposed to declining rents more quickly under these shorter-term leases.

As of December 31, 2019, most of our commercial leases require tenants to reimburse us for a share of our operating expenses. As a result, we are able to pass on much of any increases to our property operating expenses that might occur due to inflation by correspondingly increasing our expense reimbursement revenues. During the year-ended December 31, 2019, inflation did not have a material impact on our revenues or net income.

### Critical Accounting Policies and Estimates

The following discloses accounting policies and estimates we believe are most "critical" to the portrayal of our financial condition and results of operations and require our most difficult, subjective or complex judgments. These judgments often result from the need to make estimates about the effect of matters that are inherently uncertain. GAAP requires

information in financial statements about accounting principles, methods used and disclosures pertaining to significant estimates. This discussion addresses our judgment pertaining to trends, events or uncertainties known which were taken into consideration upon the application of those policies and the likelihood that materially different amounts would be reported upon taking into consideration different conditions and assumptions. See also Note 2 to the consolidated financial statements.

### ***Acquisition of Real Estate Investments***

The Company allocates the purchase price of properties that meet the definition of an asset acquisition to net tangible and identified intangible assets acquired based on their relative fair values. In making estimates of relative fair values for purposes of allocating purchase price, the Company utilizes a number of sources, including independent appraisals that may be obtained in connection with the acquisition or financing of the respective property, our own analysis of recently acquired and existing comparable properties in our portfolio and other market data. The Company also considers information obtained about each property as a result of its pre-acquisition due diligence, marketing and leasing activities in estimating the relative fair value of the tangible and intangible assets acquired.

### ***Impairment of Long-Lived Assets***

The Company periodically evaluates its long-lived assets, including its investments in real estate, for indicators of impairment. The judgments regarding the existence of impairment indicators are based on factors such as operational performance, market conditions and legal and environmental concerns, as well as the Company's ability to hold and its intent with regard to each asset. Future events could occur which would cause the Company to conclude that impairment indicators exist and an impairment loss is warranted.

### ***Business Interruption Proceeds***

Insurance recoveries for business interruption was recognized during the year ended December 31, 2019, for \$879. The event that resulted in these recoveries during the year ending December 31, 2019, was caused by a roof collapse at one of our commercial properties in Fargo, North Dakota. The insurance proceeds are reflected in the statement of operations included in real estate rental income.

### ***REIT Status***

We operate in a manner intended to enable us to continue to qualify as a REIT under Sections 856-860 of the Internal Revenue Code. Under those sections, a REIT which distributes at least 90% of its REIT taxable income, excluding net capital gains, as a distribution to its shareholders each year and which meets certain other conditions will not be taxed on that portion of its taxable income which is distributed to its shareholders. We intend to distribute to our shareholders 100% of our taxable income. Therefore, no provision for Federal income taxes is required. If we fail to distribute the required amount of income to our shareholders, we would fail to qualify as a REIT and substantial adverse tax consequences may result.

### ***Estimated Value of Units/Shares***

The Board of Trustees determined an estimate of fair value for the trust shares in 2019 and 2018. In addition, the Board of Trustees, acting as general partner for the operating partnership, determined an estimate of fair value for the limited partnership units in 2019 and 2018. In determining this value, the Board relied upon their experience with, and knowledge about, the Trust's real estate portfolio and debt obligations. The Board typically determines the share price on an annual basis. The trustees determine the price in their discretion and use data points to guide their determination which is typically based on a consensus of opinion. In addition, the Board considers how the price chosen will affect existing share and unit values, redemption prices, dividend coverage ratios, yield percentages, dividend reinvestment factors, and future UPREIT transactions, among other considerations and information. The fair value was not determined based on, nor intended to comply with, fair value standards under US GAAP and the value may not be indicative of the price we would get for selling our assets in their condition.

Determination of price is a matter within the Board's sole discretion. The Trust does not determine price based on any rote formula or specific factors. At this time, no shares are held in street name accounts and the Trust is not subject to FINRA's specific pricing requirements set out in Rule 2231 or otherwise. Thus, the Trust does not employ any specific valuation methodology or formula. Rather, the Board looks to available data and information, which is often adjusted and weighted, or discounts are applied to comport more closely with the assets held by the Trust at the time of valuation. The principal valuation methodology utilized is the NAV calculation/direct capitalization method. The information made available to the Board is assembled by the Trust's Advisor.

As with any valuation methodology, the methodologies utilized by the Board in reaching an estimate of the value of the shares and limited partnership units are based upon a number of estimates, assumptions, judgments or opinions that may, or may not, prove to be correct. The use of different estimates, assumptions, judgments, or opinions would likely have resulted in significantly different estimates of the value of the shares and limited partnership units. In addition, the Board's estimate of share and limited partnership unit value is not based on the book values of our real estate, as determined by GAAP, as our book value for most real estate is based on the amortized cost of the property, subject to certain adjustments.

Furthermore, in reaching an estimate of the value of the shares and limited partnership units, the Board applied a liquidity discount to one valuation scenario in order to reflect the fact that the shares and limited partnership units are not currently traded on a national securities exchange, but did not apply a discount for debt that may include a prepayment obligation or a provision precluding assumption of the debt by a third party, or reflect the costs that are likely to be incurred in connection with an appropriate exit strategy, whether that strategy might be a listing of the limited partnership units or common shares on a national securities exchange or a merger or sale of our portfolio.

There have been no material changes in our Significant Accounting Policies as disclosed in Note 2 to our consolidated financial statements for the year ended December 31, 2019 included elsewhere in this report.

### **Recently Issued Accounting Pronouncements**

For a discussion of recently issued accounting pronouncements, see Note 2, Principal Activity and Significant Accounting Policies— Recently Issued Accounting Pronouncements, to the consolidated financial statements that are a part of this Annual Report on Form 10-K.

### **Recent Developments**

*Common Share Dividends.* On January 15, 2020, we paid a dividend or distribution of \$0.26125 per share on our common shares of beneficial interest, to common shareholders and limited unit holders of record on December 31, 2019. All future dividends remain subject to the discretion of our Board of Trustees.

*Share and Unit Price Increase.* The Board of Trustees approved an increase in the common share price from \$19.00 per share to \$19.25 per share effective January 1, 2020.

*Acquisitions:* On January 10, 2020, we acquired a 54-unit apartment complex in Fargo, North Dakota for \$4,968. Total consideration given for the acquisition was approximately 104,000 limited partnership units of the operating partnership valued at \$19.00 per unit for an aggregate consideration of \$1,971 and cash of \$2,997.

On January 31, 2020, we acquired a 12-unit apartment complex in Fargo, North Dakota for \$612. Total consideration given for the acquisition was approximately 29,000 limited partnership units of the operating partnership valued at \$19.25 per unit for an aggregate consideration of \$557 and cash of \$55.

On March 1, 2020, we acquired 74 units in 6 apartment complexes located in Bismarck, North Dakota for \$4,077. Total consideration given for the acquisition was approximately 211,800 limited partnership units of the operating partnership valued at \$19.25 per unit for an aggregate consideration of \$4,077.

On March 1, 2020, we acquired 48 units in 2 apartment complexes located in Fargo, North Dakota for \$2,400. Total consideration given for the acquisition was approximately 124,700 limited partnership units of the operating partnership valued at \$19.25 per unit for an aggregate consideration of \$2,400.

*Financing:* On January 27, 2020, a joint venture we have a 60% interest, closed on a \$26,000 construction loan to fund the development of a multi-family property located in Savage, Minnesota. The Trust is jointly and severally liable for the full mortgage balance. In addition, on the same date, we entered into a loan facility with the joint venture to provide an additional \$5,007 in financing for the project.

On March 6, 2020, we paid off 2 mortgage notes totaling approximately \$5,890.

*Litigation:* On February 10, 2020, the Trust settled a tenant dispute with a tenant of a Minneapolis, Minnesota property. The settlement did not lead to a material change in the consolidated financial statements.

*Disposition:* On March 1, 2020, we disposed of a retail location in Apple Valley, Minnesota for \$3,670.

Pending acquisitions and dispositions are subject to numerous conditions and contingencies and there are no assurances that the transactions will be completed.

#### ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The principal material financial market risk to which we are exposed is interest-rate risk. Our exposure to market risk for changes in interest rates relates primarily to refinancing long-term fixed rate obligations, the opportunity cost of fixed rate obligations in a falling interest rate environment and our variable rate lines of credit.

The following table shows the scheduled maturities and principal amortization of our indebtedness as of December 31, 2019 for each of the next five years and thereafter and the weighted average interest rates by year.

	2020	2021	2022	2023	2024	Thereafter	Total
<b>Debt:</b>							
Fixed rate debt:							
Mortgage notes payable (a)	\$ 24,862	\$ 38,756	\$ 26,458	\$ 49,220	\$ 19,054	\$ 236,688	\$ 395,038
<b>Weighted average interest rate on debt:</b>							
Fixed rate debt							
Mortgage notes payable (a)	4.48%	4.50%	4.30%	4.46%	4.31%	4.24%	4.31%

(a) Amounts exclude capitalized loan fees of \$1,875, net of accumulated amortization, as of December 31, 2019. Fixed rate amounts for each year include scheduled principal amortization payments.

The table incorporates only those interest rate exposures that existed as of December 31, 2019. It does not consider those interest rate exposures or positions that could arise after that date. The information presented herein is merely an estimate and has limited predictive value. As a result, the ultimate realized gain or loss with respect to interest rate fluctuations will depend on the interest rate exposures that arise during future periods, our hedging strategies at that time and future changes in interest rates.

#### ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Our consolidated financial statements included in this Annual Report are listed in Item 15 and begin immediately after the signature pages.

## **ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

### **ITEM 9A. CONTROLS AND PROCEDURES**

#### **Disclosure Controls and Procedures**

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this Annual Report on Form 10-K (the “Evaluation Date”). Based upon the evaluation, our Chief Executive Officer and Chief Financial Officer concluded as of the Evaluation Date that our disclosure controls and procedures were effective to ensure that information required to be disclosed in our reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Commission’s rules and forms, and is accumulated and communicated to management, including our principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

#### **Report of Management on Internal Control Over Financial Reporting**

Our management is responsible for establishing and maintaining a comprehensive system of internal control over financial reporting to provide reasonable assurance of the proper authorization of transactions, the safeguarding of assets and the reliability of the financial records. Our internal control system was designed to provide reasonable assurance to our management and Board of Trustees regarding the preparation and fair presentation of published financial statements. The system of internal control over financial reporting provides for appropriate division of responsibility and is documented by written policies and procedures that are communicated to employees. The framework upon which management relied in evaluating the effectiveness of our internal control over financial reporting was set forth in *Internal Controls – Integrated Framework* (2013) published by the Committee of Sponsoring Organization of the Treadway Commission.

Our internal control system was designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles in the U.S. Our internal control over financial reporting includes those policies and procedures that:

- i. pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and
- ii. disposition of our assets;
- iii. provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the U.S., and that our receipts and expenditures are being made only in accordance with authorization of our management and trustees; and
- iv. provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the consolidated financial statements.

Based on the results of our evaluation, our management concluded that our internal control over financial reporting was effective as of December 31, 2019. However, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in our business or other conditions, or that the degree of compliance with our policies or procedures may deteriorate.

The effectiveness of the Company’s internal controls over financial reporting as of December 31, 2019 has been audited by Baker Tilly Virchow Krause, LLP, an independent registered public accounting firm, as stated in their report which is included herein.

### **Inherent Limitations of Disclosure Controls and Procedures and Internal Control over Financial Reporting**

There are inherent limitations to the effectiveness of any control system. A control system, no matter how well conceived and operated, can provide only reasonable assurance that its objectives are met. No evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within us have been detected. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or because the degree of compliance with the policies and procedures may deteriorate.

### **Changes in Internal Control Over Financial Reporting**

There have been no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) and Rule 15d-15(f) under the Exchange Act) during the fourth quarter ended December 31, 2019 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

### **ITEM 9B. OTHER INFORMATION**

None.

## **PART III**

The information required in Item 10 (Directors, Executive Officers and Corporate Governance), Item 11 (Executive Compensation), Item 12 (Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters), Item 13 (Certain Relationships and Related Transactions, and Director Independence), and Item 14 (Principal Accountant Fees and Services) is incorporated by reference to our definitive proxy statement for the 2020 Annual Meeting of Shareholders to be filed with the SEC or filed by amendment to this Annual Report on or before April 30, 2020.

**PART IV**

**ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

**(a)(1) The financial statements listed below are included in this report**

**Report of Independent Registered Public Accounting Firm**

**Consolidated Financial Statements**

**Consolidated Balance Sheets at December 31, 2019 and 2018**

**Consolidated Statements of Operations and Other Comprehensive Income for the Years Ended December 31, 2019, 2018 and 2017**

**Consolidated Statements of Stockholders' Equity for the Years Ended December 31, 2019, 2018 and 2017**

**Consolidated Statements of Cash Flows for the Years Ended December 31, 2019, 2018 and 2017**

**Notes to Consolidated Financial Statements**

**Real Estate and Accumulated Depreciation (Schedule III)**

**(a)(3) Exhibits**

**See the Exhibit Index filed as part of this Annual Report on Form 10-K.**





**STERLING REAL ESTATE TRUST AND SUBSIDIARIES**

CONSOLIDATED BALANCE SHEETS AS OF *DECEMBER 31, 2019* AND *2018*,  
AND THE RELATED CONSOLIDATED STATEMENTS OF OPERATIONS AND  
OTHER COMPREHENSIVE INCOME, SHAREHOLDERS' EQUITY AND CASH FLOWS  
FOR THE YEARS ENDED  
*DECEMBER 31, 2019, 2018* AND *2017*,  
INCLUDING NOTES

and

REPORTS OF INDEPENDENT REGISTERED  
PUBLIC ACCOUNTING FIRM

## STERLING REAL ESTATE TRUST AND SUBSIDIARIES

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## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders, the Audit Committee, and the Board of Directors of Sterling Real Estate Trust:

### **Opinions on the Financial Statements and Internal Control over Financial Reporting**

We have audited the accompanying consolidated balance sheets of Sterling Real Estate Trust (the "Company") as of December 31, 2019 and 2018, the related consolidated statements of operations and other comprehensive income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2019, and the related notes and financial statement schedules (collectively referred to as the "consolidated financial statements"). We also have audited the Company's internal control over financial reporting as of December 31, 2019, based on criteria established in *Internal Control – Integrated Framework: (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2019 and 2018, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2019, in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2019, based on criteria established in *Internal Control – Integrated Framework: (2013)* issued by COSO.

### **Basis for Opinions**

The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Report of Management on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's consolidated financial statements and an opinion on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the financial statements included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other

procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

### **Definition and Limitations of Internal Control Over Financial Reporting**

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Baker Tilly Virchow Krause, LLP

We have served as the Company's auditor since 2013.

Chicago, Illinois

March 13, 2020

## PART I – FINANCIAL INFORMATION

### Item 1. Financial Statements

#### STERLING REAL ESTATE TRUST AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS AS OF DECEMBER 31, 2019 AND 2018

	December 31, 2019	December 31, 2018
	(in thousands)	
<b>ASSETS</b>		
Real estate investments		
Land and land improvements	\$ 114,666	\$ 114,027
Building and improvements	676,228	675,308
Construction in progress	11,134	1,361
Real estate investments	802,028	790,696
Less accumulated depreciation	(146,316)	(128,112)
Real estate investments, net	655,712	662,584
Cash and cash equivalents	9,002	21,212
Restricted deposits	8,380	8,853
Investment in unconsolidated affiliates	7,915	2,691
Note receivable	1,300	—
Lease intangible assets, less accumulated amortization of \$15,558 in 2019 and \$13,715 in 2018	9,133	10,976
Other assets, net	8,244	8,151
Total Assets	\$ 699,686	\$ 714,467
<b>LIABILITIES</b>		
Mortgage notes payable, net	\$ 393,164	\$ 406,017
Dividends payable	7,118	6,828
Tenant security deposits payable	4,439	4,286
Lease intangible liabilities, less accumulated amortization of \$1,881 in 2019 and \$1,621 in 2018	1,207	1,468
Accrued expenses and other liabilities	14,711	12,117
Total Liabilities	420,639	430,716
<b>COMMITMENTS and CONTINGENCIES - Note 16</b>		
<b>SHAREHOLDERS' EQUITY</b>		
Beneficial interest	102,373	97,883
Noncontrolling interest		
Operating partnership	174,221	183,360
Partially owned properties	2,416	2,538
Accumulated other comprehensive loss	37	(30)
Total Shareholders' Equity	279,047	283,751
	\$ 699,686	\$ 714,467

See Notes to Consolidated Financial Statements

**STERLING REAL ESTATE TRUST AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF OPERATIONS AND OTHER COMPREHENSIVE INCOME**  
**FOR THE YEARS ENDED DECEMBER 31, 2019, 2018 AND 2017**

	Year Ended December 31,		
	2019	2018	2017
	(in thousands, except per share data)		
Income from rental operations			
Real estate rental income	\$ 120,339	\$ 109,933	\$ 108,118
Tenant reimbursements	—	6,118	6,162
	120,339	116,051	114,280
Expenses			
Expenses from rental operations			
Operating expenses, excluding real estate taxes	48,858	44,781	43,672
Real estate taxes	12,078	11,624	11,052
Depreciation and amortization	21,495	21,350	21,544
Interest	18,282	18,329	18,630
(Gain)/loss on lease terminations	—	(22)	146
	100,713	96,062	95,044
Administration of REIT	4,112	4,100	5,144
Total expenses	104,825	100,162	100,188
Income from operations	15,514	15,889	14,092
Other income			
Equity in income of unconsolidated affiliates	759	634	1,016
Other income	301	273	85
Gain on sale of real estate and non-real estate investments	—	3,715	2,049
Gain on change in control of real estate investments	—	—	2,186
Gain on sale of investment in equity method investee	—	—	3
(Loss)/gain on involuntary conversion	(515)	1,467	452
	545	6,089	5,791
Net income	\$ 16,059	\$ 21,978	\$ 19,883
Net income attributable to noncontrolling interest:			
Operating Partnership	10,647	14,768	13,634
Partially owned properties	(122)	(164)	(265)
Net income attributable to Sterling Real Estate Trust	\$ 5,534	\$ 7,374	\$ 6,514
Net income per common share, basic and diluted	\$ 0.60	\$ 0.84	\$ 0.78
Comprehensive income:			
Net income	\$ 16,059	\$ 21,978	\$ 19,883
Other comprehensive gain - change in fair value of interest rate swaps	67	35	80
Comprehensive income	16,126	22,013	19,963
Comprehensive income attributable to noncontrolling interest	10,569	14,628	13,423
Comprehensive income attributable to Sterling Real Estate Trust	\$ 5,557	\$ 7,385	\$ 6,540

See Notes to Consolidated Financial Statements

**STERLING REAL ESTATE TRUST AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY**  
**FOR THE YEARS ENDED DECEMBER 31, 2019, 2018 AND 2017**

	Common Shares	Paid-in Capital	Accumulated Distributions in Excess of Earnings	Total Beneficial Interest	Noncontrolling Interest			Accumulated Comprehensive Income (Loss)	Total
					Operating Partnership	Partially Owned Properties			
BALANCE AT DECEMBER 31, 2016	8,001	\$ 106,207	\$ (21,480)	\$ 84,727	\$ 170,138	\$ 3,935	\$ (145)	\$ 258,655	
Shares issued under trustee compensation plan	4	59	—	59	—	—	—	59	
Contribution of assets in exchange for the issuance of noncontrolling interest shares	—	—	—	—	14,733	—	—	14,733	
Shares/units redeemed	(72)	(1,110)	—	(1,110)	(1,284)	—	—	(2,394)	
Dividends declared	—	—	(8,212)	(8,212)	(17,244)	—	—	(25,456)	
Dividends reinvested - stock dividend	331	5,163	—	5,163	—	—	—	5,163	
Issuance of shares under optional purchase plan	216	3,543	—	3,543	—	—	—	3,543	
UPREIT units converted to REIT common shares	8	133	—	133	(133)	—	—	—	
Change in fair value of interest rate swaps	—	—	—	—	—	—	80	80	
Distributions paid to consolidated real estate entity noncontrolling interests	—	—	—	—	—	(490)	—	(490)	
Net income	—	—	6,514	6,514	13,634	(265)	—	19,883	
BALANCE AT DECEMBER 31, 2017	8,488	\$ 113,995	\$ (23,179)	\$ 90,816	\$ 179,844	\$ 3,180	\$ (65)	\$ 273,775	
Shares issued pursuant to trustee compensation plan	3	57	—	57	—	—	—	57	
Contribution of assets in exchange for the issuance of noncontrolling interest shares	—	—	—	—	7,819	—	—	7,819	
Shares/units redeemed	(75)	(1,315)	—	(1,315)	(1,116)	—	—	(2,431)	
Dividends declared	—	—	(8,936)	(8,936)	(17,955)	—	—	(26,891)	
Dividends reinvested - stock dividend	325	5,711	—	5,711	—	—	—	5,711	
Issuance of shares under optional purchase plan	226	4,176	—	4,176	—	—	—	4,176	
Change in fair value of interest rate swaps	—	—	—	—	—	—	35	35	
Distributions paid to consolidated real estate entity noncontrolling interests	—	—	—	—	—	(478)	—	(478)	
Net income	—	—	7,374	7,374	14,768	(164)	—	21,978	
BALANCE AT DECEMBER 31, 2018	8,967	\$ 122,624	\$ (24,741)	\$ 97,883	\$ 183,360	\$ 2,538	\$ (30)	\$ 283,751	
Shares issued pursuant to trustee compensation plan	3	62	—	62	—	—	—	62	
Shares/units redeemed	(50)	(891)	—	(891)	(1,132)	—	—	(2,023)	
Dividends declared	—	—	(9,681)	(9,681)	(18,626)	—	—	(28,307)	
Dividends reinvested - stock dividend	342	6,145	—	6,145	—	—	—	6,145	
Issuance of shares under optional purchase plan	173	3,293	—	3,293	—	—	—	3,293	
UPREIT units converted to REIT common shares	1	28	—	28	(28)	—	—	—	
Change in fair value of interest rate swaps	—	—	—	—	—	—	67	67	
Net income	—	—	5,534	5,534	10,647	(122)	—	16,059	
BALANCE AT DECEMBER 31, 2019	9,436	\$ 131,261	\$ (28,888)	\$ 102,373	\$ 174,221	\$ 2,416	\$ 37	\$ 279,047	

See Notes to Consolidated Financial Statements

**STERLING REAL ESTATE TRUST AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED DECEMBER 31, 2019, 2018 AND 2017**

	Year Ended December 31,		
	2019	2018	2017
	(in thousands)		
OPERATING ACTIVITIES			
Net income	\$ 16,059	\$ 21,978	\$ 19,883
Adjustments to reconcile net income to net cash from operating activities			
Gain on sale of real estate investments	—	(3,715)	(2,072)
Loss on sale of non-real estate investments	—	—	23
Gain on change in control of real estate investment	—	—	(2,186)
Loss/(Gain) on involuntary conversion	515	(1,467)	(452)
Loss on lease terminations	—	—	146
Equity in income of unconsolidated affiliates	(759)	(634)	(1,016)
Distributions of earnings of unconsolidated affiliates	759	634	1,016
Allowance for uncollectible accounts receivable	203	560	—
Depreciation	19,644	19,165	19,057
Amortization	1,805	2,127	2,429
Amortization of debt issuance costs	636	708	769
Effects on operating cash flows due to changes in			
Other assets	(234)	(2,980)	(441)
Tenant security deposits payable	153	85	149
Accrued expenses and other liabilities	2,545	1,961	173
NET CASH PROVIDED BY OPERATING ACTIVITIES	41,326	38,422	37,478
INVESTING ACTIVITIES			
Purchase of real estate investment properties	—	(20,419)	(8,794)
Capital expenditures and tenant improvements	(15,445)	(10,273)	(11,047)
Proceeds from sale of real estate investments and non-real estate investments	—	12,482	4,442
Proceeds from involuntary conversion	2,596	1,112	1,940
Investment in unconsolidated affiliates	(5,350)	(81)	(294)
Distributions in excess of earnings received from unconsolidated affiliates	126	162	92
Notes receivable issued	(1,300)	—	642
NET CASH USED IN INVESTING ACTIVITIES	(19,373)	(17,017)	(13,019)
FINANCING ACTIVITIES			
Payments for financing, debt issuance and lease costs	(136)	(707)	(486)
Payments on investment certificates and subordinated debt	—	(50)	—
Principal payments on special assessments payable	(597)	(284)	(1,275)
Proceeds from issuance of mortgage notes payable and subordinated debt	15,087	23,728	23,916
Principal payments on mortgage notes payable	(28,388)	(15,060)	(26,208)
Advances on lines of credit	—	3,811	—
Payments on lines of credit	—	(3,811)	—
Proceeds from issuance of shares under optional purchase plan	3,293	4,176	3,543
Shares/units redeemed	(2,023)	(2,431)	(2,394)
Dividends/distributions paid	(21,872)	(21,265)	(20,272)
NET CASH USED IN FINANCING ACTIVITIES	(34,636)	(11,893)	(23,176)
NET CHANGE IN CASH AND CASH EQUIVALENTS AND RESTRICTED DEPOSITS	(12,683)	9,512	1,283
CASH AND CASH EQUIVALENTS AND RESTRICTED DEPOSITS AT BEGINNING OF YEAR	30,065	20,553	19,270
CASH AND CASH EQUIVALENTS AND RESTRICTED DEPOSITS AT END OF YEAR	\$ 17,382	\$ 30,065	\$ 20,553
CASH AND CASH EQUIVALENTS AND RESTRICTED DEPOSITS AT END OF YEAR			
Cash and cash equivalents	\$ 9,002	\$ 21,212	\$ 12,490
Restricted deposits	8,380	8,853	8,063
TOTAL CASH AND CASH EQUIVALENTS AND RESTRICTED DEPOSITS, END OF YEAR	\$ 17,382	\$ 30,065	\$ 20,553

See Notes to Consolidated Financial Statements



**STERLING REAL ESTATE TRUST AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED DECEMBER 31, 2019, 2018 AND 2017 (Continued)**

	Year Ended December 31,		
	2019	2018	2017
	(in thousands)		
SCHEDULE OF CASH FLOW INFORMATION			
Cash paid during the period for interest, net of capitalized interest	\$ 17,684	\$ 17,575	\$ 17,847
SUPPLEMENTARY SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES			
Dividends reinvested	\$ 6,145	\$ 5,711	\$ 5,163
Dividends declared and not paid	2,465	2,281	2,101
UPREIT distributions declared and not paid	4,653	4,547	4,335
UPREIT units converted to REIT common shares	28	—	133
Shares issued pursuant to trustee compensation plan	62	57	59
Acquisition of assets in exchange for the issuance of noncontrolling interest units in UPREIT	—	7,819	14,733
Increase in land improvements due to increase in special assessments payable	639	447	1,300
Unrealized gain on interest rate swaps	67	35	80
Acquisition of assets with new financing	—	—	5,052
Acquisition of assets through assumption of debt and liabilities	—	2,680	1,427
Capitalized interest and real estate taxes related to construction in progress	138	—	142
Acquisition of assets with accounts payable	—	—	416

See Notes to Consolidated Financial Statements

**STERLING REAL ESTATE TRUST AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2019, 2018 AND 2017**

(Dollar amounts in thousands, except share and per share data)

**NOTE 1 – ORGANIZATION**

Sterling Real Estate Trust (“Sterling”, “the Trust” or “the Company”) is a registered, but unincorporated business trust organized in North Dakota in December 2002. Sterling has elected to be taxed as a Real Estate Investment Trust (“REIT”) under Sections 856-860 of the Internal Revenue Code, which requires that 75% of the assets of a REIT must consist of real estate assets and that 75% of its gross income must be derived from real estate. The net income of the REIT is allocated in accordance with the stock ownership in the same fashion as a regular corporation.

Sterling previously established an operating partnership (“Sterling Properties, LLLP”) and transferred all of its assets and liabilities to the operating partnership in exchange for general partnership units. As the general partner, Sterling has management responsibility for all activities of the operating partnership. As of December 31, 2019 and 2018, Sterling owned approximately 34.63% and 33.41%, respectively, of the operating partnership.

**NOTE 2 – PRINCIPAL ACTIVITY AND SIGNIFICANT ACCOUNTING POLICIES**

*Basis of Presentation*

The accompanying consolidated financial statements include the accounts of Sterling and all subsidiaries for which we maintain a controlling interest.

The accompanying consolidated financial statements have been prepared in accordance with United States Generally Accepted Accounting Principles (“U.S. GAAP”) and require management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of income and expenses during the reporting periods. Actual results could differ from those estimates.

*Principles of Consolidation*

The consolidated financial statements include the accounts of Sterling, Sterling Properties, LLLP, wholly-owned limited liability companies and partially-owned limited liability companies where we maintain a controlling interest. All significant intercompany transactions and balances have been eliminated in consolidation.

Additionally, we evaluate the need to consolidate affiliates based on standards set forth in the Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 810, Consolidation (“ASC 810”). In determining whether we have a requirement to consolidate the accounts of an entity, management considers factors such as our ownership interest, our authority to make decisions and contractual and substantive participating rights of the limited partners and shareholders, as well as whether the entity is a variable interest entity (“VIE”) for which we have both: a) the power to direct the activities of the VIE that most significantly impact the entity’s economic performance, and b) the obligation to absorb losses or the right to receive benefits from the VIE that could be potentially significant to the VIE.

**STERLING REAL ESTATE TRUST AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
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(Dollar amounts in thousands, except share and per share data)

*Principal Business Activity*

Sterling currently owns directly and indirectly, 173 properties. The Trust's 125 residential properties are located in North Dakota, Minnesota, Missouri and Nebraska and are principally multifamily apartment buildings. The Trust owns 48 commercial properties primarily located in North Dakota with others located in Arkansas, Colorado, Iowa, Louisiana, Michigan, Minnesota, Mississippi, Nebraska and Wisconsin. The commercial properties include retail, office, industrial, restaurant and medical properties. The Trust's mix of properties is 73.4% residential and 26.6% commercial (based on cost) at December 31, 2019. Currently our focus is limited to multifamily apartment properties. We currently have no plans with respect to our non-multifamily apartment properties. We will consider unsolicited offers for purchase of non-multifamily properties on a case by case basis.

<b>Residential Property</b>	<b>Location</b>	<b>No. of Properties</b>	<b>Units</b>
	North Dakota	105	6,160
	Minnesota	16	3,033
	Missouri	1	164
	Nebraska	3	495
		<u>125</u>	<u>9,852</u>

<b>Commercial Property</b>	<b>Location</b>	<b>No. of Properties</b>	<b>Sq. Ft</b>
	North Dakota	20	780,000
	Arkansas	2	28,000
	Colorado	1	17,000
	Iowa	1	33,000
	Louisiana	1	15,000
	Michigan	1	12,000
	Minnesota	15	680,000
	Mississippi	1	15,000
	Nebraska	1	19,000
	Wisconsin	5	63,000
		<u>48</u>	<u>1,662,000</u>

*Concentration of Credit Risk*

Our cash balances are maintained in various bank deposit accounts. The bank deposit amounts in these accounts may exceed federally insured limits at various times throughout the year.

*Real Estate Investments*

Real estate investments are recorded at cost less accumulated depreciation. Ordinary repairs and maintenance are expensed as incurred.

The Company allocates the purchase price of each acquired investment property accounted for as an asset acquisition based upon the estimated acquisition date fair value of the individual assets acquired and liabilities assumed, which generally include (i) land, (ii) building and other improvements, (iii) in-place lease intangibles, (iv) acquired above and below market lease intangibles, (v) any assumed financing that is determined to be above or below market, (vi) goodwill, if any. Transaction costs related to acquisitions accounted for as asset acquisitions are capitalized as a cost of the property.

For tangible assets acquired, including land, building and other improvements, the Company considers available comparable market and industry information in estimating acquisition date fair value. Key factors considered in the calculation of fair value of both real property and intangible assets include the current market rent values, "dark" periods (building in vacant status), direct costs estimated with

**STERLING REAL ESTATE TRUST AND SUBSIDIARIES**  
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obtaining a new tenant, discount rates, escalation factors, standard lease terms, and tenant improvement costs. The Company allocates a portion of the purchase price to the estimated acquired in-place lease intangibles based on factors available in third party appraisals or cash flow estimates of the property prepared by our internal analysis. These estimates are based upon cash flow projections for the property, existing leases, lease origination costs for similar leases as well as lost rental payments during an assumed lease-up period. The Company also evaluates each acquired lease as compared to current market rates. If an acquired lease is determined to be above or below market, the Company allocates a portion of the purchase price to such above or below market leases based upon the present value of the difference between the contractual lease payments and estimated market rent payments over the remaining lease term. Renewal periods are included within the lease term in the calculation of above and below market lease values if, based upon factors known at the acquisition date, market participants would consider it reasonably assured that the lessee would exercise such options. Fair value estimates used in acquisition accounting, including the discount rate used, require the Company to consider various factors, including, but not limited to, market knowledge, demographics, age and physical condition of the property, geographic location, and size and location of tenant spaces within the acquired investment property.

The portion of the purchase price allocated to acquired in-place lease value intangibles is amortized on a straight-line basis over the life of the related lease as amortization expense. The Company incurred amortization expense pertaining to acquired in-place lease value intangibles of \$1,629, \$2,021 and \$2,253 for the years ended December 31, 2019, 2018 and 2017, respectively.

The portion of the purchase price allocated to acquired above and below market lease intangibles is amortized on a straight-line basis over the life of the related lease as an adjustment to rental income. Amortization pertaining to above market lease intangibles of \$214, \$222 and \$226 for the years ended December 31, 2019, 2018 and 2017, respectively, was recorded as a reduction to income from rental operations. Amortization pertaining to below market lease intangibles of \$261, \$280 and \$284 for the years ended December 31, 2019, 2018 and 2017, respectively, was recorded as an increase to income from rental operations.

Furniture and fixtures are stated at cost less accumulated depreciation. All costs associated with the development and construction of real estate investments, including acquisition fees and interest, are capitalized as a cost of the property. Expenditures for renewals and improvements that significantly add to the productive capacity or extend the useful life of an asset are capitalized. Expenditures for routine maintenance and repairs, which do not add to the value or extend useful lives, are charged to expense as incurred.

Depreciation is provided for over the estimated useful lives of the individual assets using the straight-line method over the following estimated useful lives:

Buildings and improvements	40 years
Furniture, fixtures and equipment	5-9 years

Depreciation expense for the years ended December 31, 2019, 2018 and 2017 totaled \$19,644, \$19,165 and \$19,057 respectively.

The Company's real estate investments are reviewed for potential impairment at the end of each reporting period whenever events or changes in circumstances indicate that the carrying value may not be recoverable. At the end of each reporting period, the Company separately determines whether impairment indicators exist for each property.

Examples of situations considered to be impairment indicators include, but are not limited to:

- a substantial decline or continued low occupancy rate;
- continued difficulty in leasing space;
- significant financially troubled tenants;
- a change in plan to sell a property prior to the end of its useful life or holding period;
- a significant decrease in market price not in line with general market trends; and

**STERLING REAL ESTATE TRUST AND SUBSIDIARIES**  
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(Dollar amounts in thousands, except share and per share data)

- any other quantitative or qualitative events or factors deemed significant by the Company's management or board of trustees.

If the presence of one or more impairment indicators as described above is identified at the end of the reporting period or throughout the year with respect to a real estate investment, the asset is tested for recoverability by comparing its carrying value to the estimated future undiscounted cash flows. A real estate investment is considered to be impaired when the estimated future undiscounted cash flows are less than its current carrying value. When performing a test for recoverability or estimating the fair value of an impaired real estate investment, the Company makes complex or subjective assumptions which include, but are not limited to:

- projected operating cash flows considering factors such as vacancy rates, rental rates, lease terms, tenant financial strength, demographics, holding period and property location;
- projected capital expenditures and lease origination costs;
- projected cash flows from the eventual disposition of an operating property using a property specific capitalization rate;
- comparable selling prices; and
- property specific discount rates for fair value estimates as necessary.

To the extent impairment has occurred, the Company will record an impairment charge calculated as the excess of the carrying value of the asset over its fair value for impairment of real estate investments. There were no impairment losses during the years ended December 31, 2019, 2018 or 2017.

*Properties Held for Sale*

We account for our properties held for sale in accordance with ASC 360, Property, Plant and Equipment ("ASC 360"), which addresses financial accounting and reporting in a period in which a component or group of components of an entity either has been disposed of or is classified as held for sale.

In accordance with ASC 360, at such time as a property is held for sale, such property is carried at the lower of (1) its carrying amount or (2) fair value less costs to sell. In addition, a property being held for sale ceases to be depreciated. We classify operating properties as properties held for sale in the period in which all of the following criteria are met:

- management, having the authority to approve the action, commits to a plan to sell the asset;
- the asset is available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets;
- an active program to locate a buyer and other actions required to complete the plan to sell the asset has been initiated;
- the sale of the asset is probable and the transfer of the asset is expected to qualify for recognition as a completed sale within one year;
- the asset is being actively marketed for sale at a price that is reasonable in relation to its current fair value; and
- given the actions required to complete the plan to sell the asset, it is unlikely that significant changes to the plan would be made or that the plan would be withdrawn.

The results of operations of a component of an entity that either has been disposed of or is classified as held-for-sale under the requirements of ASC 360 is reported in discontinued operations in accordance with ASC 205, Presentation of Financial Statements ("ASC 205") if such disposal or classification represents a strategic shift that has (or will have) a major effect on our operations and financial results.

There were no properties classified as held for sale at December 31, 2019 and 2018. See Note 17.

**STERLING REAL ESTATE TRUST AND SUBSIDIARIES**  
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(Dollar amounts in thousands, except share and per share data)

*Construction in Progress*

The Company capitalizes direct and certain indirect project costs incurred during the development period such as construction, insurance, architectural, legal, interest and other financing costs, and real estate taxes. At such time as the development is considered substantially complete, the capitalization of certain indirect costs such as real estate taxes and interest and financing costs cease and all project-related costs included in construction in process are reclassified to land and building and other improvements.

Construction in progress as of December 31, 2019 consists primarily of construction, development and planning costs associated with Glen Pond developments in Eagan, Minnesota and Goldmark Office Park 1715 building located in Fargo, North Dakota. The Glen Pond development consists of 114 units of multifamily property. Current expectations are that the project will be completed in the second or third quarter of calendar year 2020 and the current project budget approximates \$15,598. The Goldmark Office Park 1715 is a commercial office building. Current expectations are that the project will be completed in the first quarter 2020 and the current project budget is approximately \$2,000.

*Cash and Cash Equivalents and Restricted Deposits*

We classify highly liquid investments with a maturity of three months or less when purchased as cash equivalents. Restricted cash includes funds escrowed for tenant security deposits, real estate tax, insurance and mortgage escrows and escrow deposits required by lenders on certain properties to be used for future building renovations or tenant improvements and potential Internal Revenue Code Section 1031 tax deferred exchanges (1031 Exchange).

*Investment in Unconsolidated Affiliates*

We account for unconsolidated affiliates using the equity method of accounting per guidance established under ASC 323, Investments – Equity Method and Joint Ventures (“ASC 323”). The equity method of accounting requires the investment to be initially recorded at cost and subsequently adjusted for our share of equity in the affiliates’ earnings and distributions. We evaluate the carrying amount of the investments for impairment in accordance with ASC 323. Unconsolidated affiliates are reviewed for potential impairment if the carrying amount of the investment exceeds its fair value. An impairment charge is recorded when an impairment is deemed to be other-than-temporary. To determine whether impairment is other-than-temporary, we consider whether we have the ability and intent to hold the investment until the carrying amount is fully recovered. The evaluation of an investment in an affiliate for potential impairment can require our management to exercise significant judgments. No impairment losses were recorded related to the unconsolidated affiliates for the years ended December 31, 2019, 2018 and 2017.

We use the equity method to account for investments that qualify as variable interest entities where we are not the primary beneficiary and entities that we do not control or where we do not own a majority of the economic interest but have the ability to exercise significant influence over the operations and financial policies of the investee. We will also use the equity method for investments that do not qualify as variable interest entities and do not meet the control requirements for consolidation, as defined in ASC 810. For a joint venture accounted for under the equity method, our share of net earnings and losses is reflected in income when earned and distributions are credited against our investment in the joint venture as received.

In determining whether an investment in a limited liability company or tenant in common is a variable interest entity, we consider: the form of our ownership interest and legal structure; the size of our investment; the financing structure of the entity, including the necessity of subordinated debt; estimates of future cash flows; our and our partner’s ability to participate in the decision making related to acquisitions, dispositions, budgeting and financing on the entity; and obligation to absorb losses and preferential returns. We determined that our tenant in common arrangements and our investments in joint ventures do not qualify as variable interest entities and do not meet the control requirements for consolidation, as defined in ASC 810 at each reporting period.

**STERLING REAL ESTATE TRUST AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
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(Dollar amounts in thousands, except share and per share data)

As of December 31, 2019 and 2018, the unconsolidated affiliates held total assets of \$31,261 and \$22,954 and mortgage notes payable of \$16,690 and \$17,091, respectively.

The operating partnership previously owned a 40.26% interest as a tenant in common in a single asset limited liability company which owns a 144 unit residential, multifamily apartment complex in Bismarck, North Dakota. As of May 1, 2017, there was a change in control over the real estate investment, with the operating partnership acquiring the other tenant in common's 59.74% ownership interest in the property (see Note 18).

The operating partnership is a 50% owner of Grand Forks Marketplace Retail Center through 100% ownership in a limited liability company. Grand Forks Marketplace Retail Center has approximately 183,000 square feet of commercial space in Grand Forks, North Dakota. The property is encumbered by a non-recourse first mortgage with a balance at December 31, 2019 and 2018 of \$10,264 and \$10,483, respectively. The Company is jointly and severally liable for the full mortgage balance.

The operating partnership owns a 66.67% interest as tenant in common in an office building with approximately 75,000 square feet of commercial rental space in Fargo, North Dakota. The property is encumbered by a first mortgage with a balance at December 31, 2019 and 2018 of \$6,426 and \$6,608 respectively. The Company is jointly and severally liable for the full mortgage balance.

The operating partnership owns a 60% interest in a joint venture ("SE Savage") that is currently developing a 190-unit multifamily property. As of December 31, 2019, the operating partnership has contributed \$3,277 in cash to SE Savage. SE Savage holds land located in Savage, Minnesota, total assets of \$5,464, no mortgage payable.

The operating partnership owns a 60% interest in a joint venture ("SE Maple Grove") that intends to develop a 160-unit multifamily property. As of December 31, 2019, The operating partnership has contributed \$2,073 in cash to SE Maple Grove. SE Maple Grove holds land located in Maple Grove, Minnesota, total assets of \$3,455, no mortgage payable.

*Receivables*

Receivables consist primarily of amounts due for rent and tenant charges. Accounts receivable are carried at original amounts billed. The operating partnership reviews collectability of charges under its tenant operating leases on a quarterly basis. In the event that collectability is deemed not probable for any tenant charges, beginning with the adoption of ASC 842 as of January 1, 2019, the operating partnership recognizes an adjustment to rental income. Prior to adoption of ASC 842, the Company recognized a provision uncollectible amounts or direct write-off of the specific rent receivable. Receivables are included in Other assets in the accompanying consolidated balance sheets.

Notes receivable are issued periodically and are secured and interest bearing.

*Financing and Lease Costs*

Financing costs have been capitalized and are being amortized over the life of the financing (line of credit) using the effective interest method. Unamortized financing costs are written off when debt is retired before the maturity date and included in interest expense at that time.

Lease costs incurred in connection with new leases have been capitalized and are being amortized over the life of the lease using the straight-line method. We record the amortization of leasing costs in depreciation and amortization on the consolidated statements of operations and comprehensive income. If an applicable lease terminates prior to the expiration of its initial lease term, we write off the carrying amount of the costs to amortization expense. Financing and lease cost are included in other assets in the accompanying consolidated balance sheets.

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*Debt Issuance Costs*

We amortize external debt issuance costs related to notes and mortgage notes using the effective interest rate method, over the estimated life of the related debt. We record debt issuance costs net of amortization, on our consolidated balance sheets as an offset to their related debt. We record debt issuance costs related to revolving lines of credit on our consolidated balance sheets as financing fees, regardless of whether a balance on the line of credit is outstanding. We record the amortization of all debt issuance costs as interest expense.

*Intangible Assets and Liabilities*

Lease intangibles are a purchase price allocation recorded on property acquisition. The lease intangibles represent the estimated value of in-place leases and the value of leases with above or below market lease terms. Lease intangibles are amortized over the term of the related lease.

The carrying amount of intangible assets is regularly reviewed for indicators of impairments in value. Impairment is recognized only if the carrying amount of the intangible asset is considered to be unrecoverable from its undiscounted cash flows and is measured as the difference between the carrying amount and the estimated fair value of the asset. Based on the review, management determined no impairment charges were necessary for the years ended December 31, 2019, 2018 and 2017.

*Noncontrolling Interest*

A noncontrolling interest in a subsidiary is in most cases an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements and separate from the parent company's equity. In addition, consolidated net income is required to be reported at amounts that include the amounts attributable to both the parent and the noncontrolling interest, and the amount of consolidated net income attributable to the parent and the noncontrolling interest are required to be disclosed on the face of the consolidated statements of operations and comprehensive income.

**Operating Partnership:** Interests in Sterling Properties, LLLP held by limited partners are represented by operating partnership units. Sterling Properties, LLLP's income is allocated to holders of units based upon the ratio of their holdings to the total units outstanding during the period. Capital contributions, distributions, syndication costs, and profits and losses are allocated to noncontrolling interests in accordance with the terms of the operating partnership agreement.

**Partially Owned Properties:** The Company reflects noncontrolling interests in partially owned properties on the balance sheet for the portion of properties consolidated by the Company that are not wholly owned by the Company. The earnings or losses from those properties attributable to the noncontrolling interests are reflected as noncontrolling interest in partially owned properties in the consolidated statement of operations and comprehensive income.

*Syndication Costs*

Syndication costs consist of costs paid to attorneys, accountants, and selling agents, related to the raising of capital. Syndication costs are recorded as a reduction to beneficial and noncontrolling interest.

*Federal Income Taxes*

We have elected to be taxed as a REIT under the Internal Revenue Code, as amended. A REIT calculates taxable income similar to other domestic corporations, with the major difference being a REIT is entitled to a deduction for dividends paid. A REIT is generally required



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to distribute each year at least 90% of its taxable income. If it chooses to retain the remaining 10% of taxable income, it may do so, but it will be subject to a corporate tax on such income. REIT shareholders are taxed on REIT distributions similar to corporate distributions.

A summary of the tax characterization of the dividends paid to shareholders of the Company's common stock for the years ended December 31, 2019, 2018 and 2017 follows:

	Tax Year Ended December 31,					
	Dividend	%	Dividend	%	Dividend	%
	2019	2019	2018	2018	2017	2017
Tax status						
Ordinary income	\$ 0.8791	84.12 %	\$ 0.7258	71.33 %	\$ 0.8124	82.05 %
Capital gain	0.0048	0.46 %	—	— %	0.0015	0.16 %
Return of capital	0.1611	15.42 %	0.2917	28.67 %	0.1761	17.79 %
	<u>\$ 1.0450</u>	<u>100.00 %</u>	<u>\$ 1.0175</u>	<u>100.00 %</u>	<u>\$ 0.9900</u>	<u>100.00 %</u>

We intend to continue to qualify as a REIT and, provided we maintain such status, will not be taxed on the portion of the income that is distributed to shareholders. In addition, we intend to distribute all of our taxable income; therefore, no provisions or liabilities for income taxes have been recorded in the consolidated financial statements.

Sterling conducts its business activity as an Umbrella Partnership Real Estate Investment Trust ("UPREIT") through its Operating Partnership – Sterling Properties, LLLP. The Operating Partnership is organized as a limited liability limited partnership. Income or loss is allocated to the partners in accordance with the provisions of the Internal Revenue Code 704(b) and 704(c). UPREIT status allows non-recognition of gain by an owner of appreciated real estate if that owner contributes the real estate to a partnership in exchange for a partnership interest. The conversion of a partnership interest to shares of beneficial interest in the REIT will be a taxable event to the limited partner.

We follow ASC Topic 740, *Income Taxes*, to recognize, measure, present and disclose in our consolidated financial statements uncertain tax positions that we have taken or expect to take on a tax return. As of December 31, 2019 and 2018 we did not have any liabilities for uncertain tax positions that we believe should be recognized in our consolidated financial statements. We are no longer subject to Federal and State tax examinations by tax authorities for years before 2016.

The operating partnership has elected to record related interest and penalties, if any, as income tax expense on the consolidated statements of operations and other comprehensive income.

*Revenue Recognition*

We are the lessor for our residential and commercial leases and these leases will continue to be accounted for as operating leases under the new standard as described under recent accounting pronouncements. Therefore, the Company did not have significant changes in accounting for lease revenues.

As of December 31, 2019, we derived 79% of our revenues from residential leases that are generally for terms of one-year or less. The residential leases may include lease income related to such items as parking, storage and non-refundable deposits that we treat as a single lease component because amenities cannot be leased on their own and the timing and pattern of revenue recognition are the same. The collection of lease payments at lease commencement is probable and therefore we subsequently recognize lease income over the lease term on a straight-line basis. Residential leases are renewable upon consent of both parties on an annual or monthly basis.

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As of December 31, 2019, we derived 21% of our revenues from commercial leases primarily under long-term lease agreements. We elected to apply the package of practical expedients for the commercial leases and these leases will continue to be accounted for as operating leases as of January 1, 2019. Substantially all commercial leases contain fixed escalations or, in some instances, changes based on the Consumer Price Index, which occur at specified times during the term of the lease. In certain commercial leases, variable lease income, such as percentage rent, is recognized when rents are earned. We recognize rental income and rental abatements from our commercial leases when earned on a straight-line basis over the lease term. Recognition of rental income commences when control of the leased space has been transferred to the tenant.

We recognize variable income from pass-through expenses on an accrual basis over the periods in which the expenses were incurred. Pass-through expenses are comprised of real estate taxes, operating expenses and common area maintenance costs which are reimbursed by tenants in accordance with specific allowable costs per tenant lease agreements. When we pay pass-through expenses, subject to reimbursement by the tenant, they are included within Operating expenses, excluding real estate taxes and Real estate taxes, and reimbursements are included within "Real estate rental income" along with the associated base rent in the accompanying consolidated financial statements.

We record base rents on a straight-line basis. The monthly base rent income according to the terms of our leases is adjusted so that an average monthly rent is recorded for each tenant over the term of its lease. The straight-line rent adjustment decreased revenue by \$44 for the year ended December 31, 2019 and increased revenue by \$99 and \$246 for the years ended December 31, 2018 and 2017, respectively. The straight-line receivable balance included in other assets on the consolidated balance sheets as of December 31, 2019 and 2018 was \$3,331 and \$3,374 respectively. We receive payments for expense reimbursements from substantially all our multi-tenant commercial tenants throughout the year based on estimates. Differences between estimated recoveries and the final billed amounts, which are immaterial, are recognized in the subsequent year.

Upon adoption of ASU 2016-02 on January 1, 2019, we elected not to bifurcate lease contracts into lease and non-lease components, since the timing and pattern of revenue is not materially different, and the non-lease component is not the primary component of the lease. Accordingly, both lease and non-lease components are presented in Real estate rental income beginning January 1, 2019 in our consolidated financial statements. The adoption of ASU 2016-02 did not result in a material change to our recognition of real estate rental income.

Lease income related to the Company's operating leases is comprised of the following:

	Year ended December 31, 2019		
	Residential	Commercial	Total
	(in thousands)		
Lease income related to fixed lease payments	\$ 91,930	\$ 19,578	\$ 111,508
Lease income related to variable lease payments	—	6,077	6,077
Other (a)	(934)	(176)	(1,110)
Lease Income (b)	<u>\$ 90,996</u>	<u>\$ 25,479</u>	<u>\$ 116,475</u>

- (a) For the year ended December 31, 2019, "Other" is comprised of revenue adjustments related to changes in collectability and amortization of above and below market lease intangibles and lease inducements.
- (b) Excludes other rental income for the year ended December 31, 2019 of \$3,864, which is accounted for under the revenue recognition standard.

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As of December 31, 2019, non-cancelable commercial operating leases provide for future minimum rental income as follows (in thousands). Apartment leases are not included as the terms are generally for one year or less.

<b>Years ending December 31,</b>	<b>Amount</b>
	<b>(in thousands)</b>
2020	\$ 17,956
2021	14,979
2022	11,595
2023	9,663
2024	9,244
Thereafter	43,453
	<u>\$ 106,890</u>

*Business Interruption Proceeds*

Insurance recoveries for business interruption were recognized during the year ended December 31, 2019 of \$879. The event that resulted in these recoveries during the year ending December 31, 2019, was caused by a roof collapse at one of our commercial properties in Fargo, North Dakota. The insurance proceeds are reflected in the statement of operations as real estate rental income.

*Earnings per Common Share*

Basic earnings per common share is computed by dividing net income available to common shareholders (the “numerator”) by the weighted average number of common shares outstanding (the “denominator”) during the period. Sterling had no dilutive potential common shares as of December 31, 2019, 2018 and 2017 and therefore, basic earnings per common share was equal to diluted earnings per common share for both periods.

For the years ended December 31, 2019, 2018 and 2017, Sterling’s denominators for the basic and diluted earnings per common share were approximately 9,268,000, 8,791,000, and 8,300,000, respectively.

*Incurred but Not Reported Insurance Liability*

The Company maintains business insurance programs with deductible limits, which cover property, business automobile and general liability claims. The Company accrues estimated losses using a reserve for known claims and estimates based on historical loss experience. The calculations used to estimate property claim reserves are based on numerous assumptions, some of which are subjective. The Company will adjust its property claim reserves, if necessary, in the event future loss experience differs from historical loss patterns. Property claim reserves is \$204 as of December 31, 2019 and is included in other liabilities on the consolidated balance sheet.

*Reclassifications*

Certain reclassifications considered necessary for a fair presentation have been made to the prior period financial statements in order to conform to the current year presentation. These reclassifications have not changed the results of operations or equity.

*Recent Accounting Pronouncements*

In May 2014, the FASB issued their final standard on revenue from contracts with customers, as Accounting Standards Update 2014-09, *Revenue from Contracts with Customers*, or ASU 2014-09. ASU 2014-09, which establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers, supersedes most current GAAP applicable to revenue recognition and converges U.S. and international accounting standards in this area. The core principle of the new guidance is that revenue shall only be recognized when an entity has transferred control of goods or services to a customer and for an amount reflecting the

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consideration to which the entity expects to be entitled for such exchange. Additionally, lease contracts are specifically excluded from ASU 2014-09. We adopted this standard effective as of January 1, 2018 and have concluded that the adoption of this guidance did not have an impact on our financial position or results of operations.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*, which superseded FASB ASC Topic 840. The standard for operating leases as lessor is largely unchanged under ASU 2016-02. However, the standard requires lessees to recognize lease assets and lease liabilities for leases classified as operating and finance leases on the balance sheet. Lessees will recognize in the statement of financial position a liability to make lease payments and a right-of-use asset representing its right to use the underlying asset for the lease term. For leases with a term of 12 months or less, a lessee is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and lease liabilities. If a lessee makes this election, it will recognize lease expense for such leases generally on a straight-line basis over the lease term.

We adopted this standard effective as of January 1, 2019, using the optional transition method to apply the standard as of the effective date. The Company elected to apply the package of practical expedients for the leases as lessor for its residential and commercial leases and these leases will continue to be accounted for as operating leases as of the effective date. Further, the Company elected the practical expedient to combine lease and non-lease components for leases as lessor. Finally, the Company evaluated taxes collected from lessees, lessor costs paid directly by lessees, and initial direct costs and determined that the guidance was consistent with existing practice. Based on these evaluations, the Company determined that for leases as lessor, as of January 1, 2019, there was no impact on lease revenue or related expenses.

In November 2016, the FASB issued ASU No. 2016-18 to require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents will be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. ASU 2016-18 was effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years and early adoption was permitted. The pronouncement requires a retrospective transition method of adoption. We adopted this standard effective January 1, 2018. Upon adoption, the Company included amounts generally described as restricted cash within the beginning-of-period, change and end-of-period total amounts on the statement of cash flows rather than within an activity on the statement of cash flows.

In August 2016, the FASB issued ASU No. 2016-15 to provide guidance for areas where there is diversity in practice in how certain cash receipts and cash payments are presented and classified in the statement of cash flows. ASU 2016-15 is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. We adopted this standard effective January 1, 2018 and have concluded that the adoption of this guidance did not have an impact on our financial position or results of operations, since the cumulative earnings approach for distributions received from equity method investees would continue to be utilized.

The new standards must be applied retrospectively to all periods presented in the financial statements. The Company adopted the new standard effective January 1, 2018 and will continue to apply the cumulative earnings approach for distributions received from equity method investees. While overall cash flows did not change, there were changes between cash flow classifications due primarily to restricted deposits.

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As of December 31, 2017, the following cash flows were reclassified:

	Year Ended December 31, 2017		
	As Originally Presented	Reclassification Adjustments (in thousands)	As Presented Herein
Cash Flows from Operating Activities:			
Restricted deposits - tenant security deposits	\$ (137)	\$ 137	\$ —
Restricted deposits - real estate tax and insurance escrow	\$ 256	\$ (256)	\$ —
Net cash provided by operating activities	\$ 37,597	\$ (119)	\$ 37,478
Cash Flows from Investing Activities			
Purchase of real estate investment properties	\$ (4,599)	\$ (4,195)	\$ (8,794)
Restricted deposits - exchange escrow	\$ (4,278)	\$ 4,278	\$ —
Restricted deposits - replacement reserves	\$ (863)	\$ 863	\$ —
Net cash provided by Investing activities	\$ (13,965)	\$ 946	\$ (13,019)
Cash and cash equivalents, beginning of period	\$ 12,034		
(adjustments for restricted deposits, beginning of period)		\$ 7,236	
Cash and cash equivalents and restricted deposits, beginning of period			\$ 19,270
Cash and cash equivalents, end of period	\$ 12,490		
(adjustments for restricted deposits, end of period)		\$ 8,063	
Cash and cash equivalents and restricted deposits, end of period			\$ 20,553

Management does not believe that any other recently issued, but not yet effective accounting pronouncements, if adopted, would have a material effect on the accompanying Consolidated Financial Statements.

**NOTE 3 – SEGMENT REPORTING**

We report our results in two reportable segments: residential and commercial properties. Our residential properties include multifamily properties. Our commercial properties include retail, office, industrial, restaurant and medical properties. We assess and measure operating results based on net operating income (“NOI”), which we define as total real estate revenues less real estate expenses (which consist of real estate taxes, property management fees, utilities, repairs and maintenance, insurance and direct administrative costs). We believe NOI is an important measure of operating performance even though it should not be considered an alternative to net income or cash flow from operating activities. NOI is unaffected by financing, depreciation, amortization, legal and professional fees and certain general and administrative expenses. The accounting policies of each segment are consistent with those described in Note 2 of this report.

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**Segment Revenues and Net Operating Income**

The revenues and net operating income for the reportable segments (residential and commercial) are summarized as follows for the years ended December 31, 2019, 2018 and 2017, along with reconciliations to the consolidated financial statements. Segment assets are also reconciled to Total Assets as reported in the consolidated financial statements for the years ended December 31, 2019, 2018 and 2017.

	Year ended December 31, 2019			Year ended December 31, 2018			Year ended December 31, 2017		
	Residential	Commercial	Total	Residential	Commercial	Total	Residential	Commercial	Total
	(in thousands)			(in thousands)			(in thousands)		
Income from rental operations	\$ 94,763	\$ 25,576	\$ 120,339	\$ 89,783	\$ 26,268	\$ 116,051	\$ 86,858	\$ 27,422	\$ 114,280
Expenses from rental operations	53,754	7,182	60,936	49,048	7,357	56,405	47,284	7,440	54,724
Net operating income	<u>\$ 41,009</u>	<u>\$ 18,394</u>	<u>\$ 59,403</u>	<u>\$ 40,735</u>	<u>\$ 18,911</u>	<u>\$ 59,646</u>	<u>\$ 39,574</u>	<u>\$ 19,982</u>	<u>\$ 59,556</u>
Depreciation and amortization			21,495			21,350			21,544
Interest			18,282			18,329			18,630
Administration of REIT			4,112			4,100			5,144
(Gain)/loss on lease terminations			—			(22)			146
Other (income)/expense			(545)			(6,089)			(5,791)
Net income			<u>\$ 16,059</u>			<u>\$ 21,978</u>			<u>\$ 19,883</u>

**Segment Assets and Accumulated Depreciation**

As of December 31, 2019	Residential	Commercial	Total
		(in thousands)	
Real estate investments	\$ 605,813	\$ 196,215	\$ 802,028
Accumulated depreciation	(104,170)	(42,146)	(146,316)
	<u>\$ 501,643</u>	<u>\$ 154,069</u>	<u>655,712</u>
Cash and cash equivalents			9,002
Restricted deposits and funded reserves			8,380
Investment in unconsolidated affiliates			7,915
Other assets			8,244
Note receivable			1,300
Intangible assets, less accumulated amortization			9,133
Total Assets			<u>\$ 699,686</u>

As of December 31, 2018	Residential	Commercial	Total
		(in thousands)	
Real estate investments	\$ 595,006	\$ 195,690	\$ 790,696
Accumulated depreciation	(90,143)	(37,969)	(128,112)
	<u>\$ 504,863</u>	<u>\$ 157,721</u>	<u>662,584</u>
Cash and cash equivalents			21,212
Restricted deposits and funded reserves			8,853
Investment in unconsolidated affiliates			2,691
Other assets			8,151
Intangible assets, less accumulated amortization			10,976
Total Assets			<u>\$ 714,467</u>

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**NOTE 4 - RESTRICTED DEPOSITS AND FUNDED RESERVES**

	<b>At December 31,</b>	
	<b>2019</b>	<b>2018</b>
	<b>(in thousands)</b>	
Tenant security deposits	\$ 4,325	\$ 4,156
Real estate tax and insurance escrows	2,058	2,225
Replacement reserves	1,997	2,472
	<u>\$ 8,380</u>	<u>\$ 8,853</u>

*Tenant Security Deposits*

We have set aside funds to repay tenant security deposits upon tenant move-out.

*Real Estate Tax and Insurance Escrows*

Pursuant to the terms of certain mortgages, we have established and maintain real estate tax escrows and insurance escrows to pay real estate taxes and insurance. We are required to contribute to the account monthly an amount equal to 1/12 of the estimated real estate taxes and insurance premiums.

*Replacement Reserves*

Pursuant to the terms of certain mortgages, we have established and maintain several replacement reserve accounts. We make monthly deposits into the replacement reserve accounts to be used for repairs and replacements on the property. Certain replacement reserve accounts require authorization from the mortgage company for withdrawals.

**NOTE 5 - LEASE INTANGIBLES**

The following table summarizes the net value of other intangible assets and liabilities and the accumulated amortization for each class of intangible:

<b>As of December 31, 2019</b>	<b>Lease Intangibles</b>	<b>Accumulated Amortization</b>	<b>Lease Intangibles, net</b>
Lease Intangible Assets		(in thousands)	
In-place leases	\$ 21,480	\$ (14,051)	\$ 7,429
Above-market leases	3,211	(1,507)	1,704
	<u>\$ 24,691</u>	<u>\$ (15,558)</u>	<u>\$ 9,133</u>
Lease Intangible Liabilities			
Below-market leases	\$ (3,088)	\$ 1,881	\$ (1,207)

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<u>As of December 31, 2018</u>	<u>Lease Intangibles</u>	<u>Accumulated Amortization</u>	<u>Lease Intangibles, net</u>
Lease Intangible Assets		(in thousands)	
In-place leases	\$ 21,480	\$ (12,422)	\$ 9,058
Above-market leases	3,211	(1,293)	1,918
	<u>\$ 24,691</u>	<u>\$ (13,715)</u>	<u>\$ 10,976</u>
Lease Intangible Liabilities			
Below-market leases	<u>\$ (3,089)</u>	<u>\$ 1,621</u>	<u>\$ (1,468)</u>

The estimated aggregate amortization expense for each of the five succeeding fiscal years and thereafter is as follows:

<u>Years ending December 31,</u>	<u>Intangible Assets</u>	<u>Intangible Liabilities</u>
	(in thousands)	
2020	\$ 1,456	\$ 213
2021	1,163	184
2022	1,028	164
2023	891	151
2024	891	151
Thereafter	3,704	344
	<u>\$ 9,133</u>	<u>\$ 1,207</u>

The weighted average amortization period for the intangible assets (in-place leases, above-market leases) and intangible liabilities (below-market leases) acquired as of December 31, 2019 was 6.7 years.

**NOTE 6 – LINES OF CREDIT**

We have a \$18,300 variable rate (1-month LIBOR plus 2.25%) line of credit agreement with Wells Fargo Bank, which expires in June 2021; a \$6,315 variable rate (floating LIBOR plus 2.00%) line of credit agreement with Bremer Bank, which expires in June 2022; a \$5,000 variable rate (floating LIBOR plus 2.00%) line of credit agreement with Bremer Bank, which expires June 2022; and a \$3,200 variable rate (LIBOR plus 2.04%) line of credit agreement with Bank of the West, which expires November 2020. The lines of credit are secured by properties in Duluth, Edina, Moorhead and St. Cloud, Minnesota; and Bismarck, Dickinson, Grand Forks and Fargo, North Dakota. At December 31, 2019, the \$6,315 variable rate line of credit with Bremer Bank secured two letters of credit totaling \$1,216, leaving \$31,599 available and unused under the agreements.

Certain line of credit agreements include covenants that, in part, impose maintenance of certain debt service coverage and debt to net worth ratios. As of December 31, 2019, three residential properties were out of compliance with Bremer's debt service coverage ratio requirement on an individual property basis. An annual waiver was received from the lender. As of December 31, 2018, three residential properties were out of compliance with Bremer's debt service coverage ratio requirement on an individual property basis and the pooled property debt yield was out of compliance with Wells Fargo's requirement. An annual waiver was received from the lender.



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**NOTE 7 - MORTGAGE NOTES PAYABLE**

The following table summarizes the Company's mortgage notes payable.

	Principal Balance At	
	December 31, 2019	December 31, 2018
	(in thousands)	
Fixed rate mortgage notes payable (a)	\$ 395,038	\$ 408,339
Less unamortized debt issuance costs	1,874	2,322
	<u>\$ 393,164</u>	<u>\$ 406,017</u>

(a) Includes \$12,960 and \$865 of variable rate mortgage debt that was swapped to a fixed rate as of December 31, 2019 and 2018, respectively.

As of December 31, 2019, we had 121 fixed rate and no variable rate mortgage loans with effective interest rates ranging from 3.15% to 7.25% per annum and a weighted average effective interest rate of 4.31% per annum.

As of December 31, 2018, we had 127 fixed rate and no variable rate mortgage loans with effective interest rates ranging from 3.44% to 7.25% per annum, and a weighted average effective interest rate of 4.42% per annum.

The majority of the Company's mortgages payable require monthly payments of principal and interest. Certain mortgages require reserves for real estate taxes and certain other costs. Mortgages are secured by the respective properties, assignment of rents, business assets, deeds to secure debt, deeds of trust and/or cash deposits with the lender.

Certain mortgage note agreements include covenants that, in part, impose maintenance of certain debt service coverage and debt to worth ratios. As of December 31, 2019, ten loans on residential properties were out of compliance due to various unit renovation and parking lot repair and maintenance costs, bad debts and increased vacancies in the North Dakota markets. The loans were secured by properties located in Bismarck, Fargo and Grand Forks, North Dakota with a total outstanding balance of \$16,361 at December 31, 2019. Annual waivers have been received from the lenders on \$10,435 of the loans out of compliance. Annual waivers were not received from one lender on loans with a balance of \$5,926. As of December 31, 2018, nine loans on residential properties were out of compliance due to various unit renovation, parking lot repair and maintenance costs, and increased vacancies in the North Dakota markets. The loans were secured by properties located in Bismarck, Fargo and Grand Forks, North Dakota with a total outstanding balance of \$13,128 at December 31, 2018. Annual waivers have been received from the lenders

We are required to make the following principal payments on our outstanding mortgage notes payable for each of the five succeeding fiscal years and thereafter as follows:

Years ending December 31,	Amount (in thousands)
2020	\$ 24,862
2021	38,756
2022	26,458
2023	49,220
2024	19,054
Thereafter	236,688
Total payments	<u>\$ 395,038</u>

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**NOTE 8 – DERIVATIVES AND HEDGING ACTIVITIES**

As part of our interest rate risk management strategy, we have used interest rate derivatives to manage our exposure to interest rate movements and add stability to interest expense. Interest rate swaps designated as cash flow hedges involve the receipt of variable rate amounts from a counterparty in exchange for the Trust making fixed rate payments over the life of the agreement without exchange of the underlying notional amount.

As of December 31, 2019, the Trust used three interest rate swaps to hedge the variable cash flows associated with variable rate debt. Changes in fair value of the derivatives that are designated and that qualify as cash flow hedges are recorded in “Accumulated other comprehensive (loss) income” and are reclassified into interest expense as interest payments are made on the Company’s variable rate debt. Over the next 12 months, the Company estimates that an additional \$30 will be reclassified as a \$30 decrease to interest expense.

The following table summarizes the Trust’s interest rate swaps as of December 31, 2019, which effectively convert one-month floating rate LIBOR to a fixed rate:

<b>Effective Date</b>		<b>Notional</b>	<b>Fixed Interest Rate</b>	<b>Maturity Date</b>
April 15, 2005	\$	814	7.25%	April 15, 2020
November 1, 2019	\$	7,168	3.15%	November 1, 2029
November 1, 2019	\$	4,978	3.28%	November 1, 2029

The following table summarizes the Company’s interest rate swaps that were designated as cash flow hedges of interest rate risk:

<b>Interest Rate Derivatives</b>	<b>Number of Instruments</b>		<b>Notional</b>	
	<b>December 31, 2019</b>	<b>December 31, 2018</b>	<b>December 31, 2019</b>	<b>December 31, 2018</b>
Interest rate swaps	3	1	\$ 12,960	\$ 865

The table below presents the estimated fair value of the Company’s derivative financial instruments as well as their classification in the accompanying consolidated balance sheets. The valuation techniques are described in Note 9 to the consolidated financial statements.

<b>Derivatives designated as cash flow hedges:</b>	<b>Derivatives</b>			
	<b>December 31, 2019</b>		<b>December 31, 2018</b>	
	<b>Balance Sheet Location</b>	<b>Fair Value</b>	<b>Balance Sheet Location</b>	<b>Fair Value</b>
Interest rate swaps	Other assets, net	\$ 58	N/A	\$ —
Interest rate swaps	Accrued expenses and other liabilities	\$ 21	Accrued expenses and other liabilities	\$ 30

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The carrying amount of the swaps have been adjusted to their fair value at the end of the quarter, which because of changes in forecasted levels of LIBOR, resulted in reporting an asset and liability for the fair value of the future net payments forecasted under the swap. The interest rate swap is accounted for as an effective hedge in accordance with ASC 815-20 whereby it is recorded at fair value and changes in fair value are recorded to comprehensive income. The following table presents the effect of the Company's derivative financial instruments on the accompanying consolidated statements of operations and other comprehensive (loss) income for the years ended December 31, 2019 and 2018:

Derivatives in Cash Flow Hedging Relationships		Amount of (Gain)/Loss Recognized in Other Comprehensive Income on Derivatives	Location of Gain Reclassified from Accumulated other Comprehensive Income (AOCI) into Income		Amount of (Gain)/Loss Reclassified from AOCI into income
		2019			2019
Interest rate swaps	\$	67	Interest expense	\$	28
		2018			2018
Interest rate swaps	\$	35	Interest expense	\$	30

*Credit-risk-related Contingent Features*

The Trust has agreements with each of its derivative counterparties that contain a provision whereby if the Trust defaults on the related indebtedness, including default where repayment of the indebtedness has not been accelerated by the lender, then the Trust could also be declared in default on its corresponding derivative obligation.

The Trust's agreements with each of its derivative counterparties also contain a provision whereby if the Trust consolidates with, merges with or into, or transfers all or substantially all of its assets to another entity and the creditworthiness of the resulting, surviving or transferee entity is materially weaker than the Trust's, the counterparty has the right to terminate the derivative obligations. As of December 31, 2019, the termination value of derivatives in a liability position, which includes accrued interest but excludes any adjustment for non-performance risk, which the Trust has deemed not significant, was \$21. As of December 31, 2019, the Trust has pledged the properties related to the loans which are hedged as collateral. If the Trust had breached any of these provisions as of December 31, 2019, it could have been required to settle its obligations under the agreements at their termination value of \$21.

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**NOTE 9 - FAIR VALUE MEASUREMENT**

The following table presents the carrying value and estimated fair value of the Company's financial instruments:

	December 31, 2019		December 31, 2018	
	Carrying Value	Fair Value	Carrying Value	Fair Value
(in thousands)				
<b>Financial assets:</b>				
Note receivable	\$ 1,300	\$ 1,389	\$ —	\$ —
Derivative assets	\$ 58	\$ 58	\$ —	\$ —
<b>Financial liabilities:</b>				
Mortgage notes payable, net	\$ 393,164	\$ 415,183	\$ 406,017	\$ 400,192
Derivative liabilities	\$ 21	\$ 21	\$ 30	\$ 30

The carrying values shown in the table are included in the consolidated balance sheets under the captions indicated in Note 8. ASC 820-10 established a three-level valuation hierarchy for fair value measurement. Management uses these valuation techniques to establish the fair value of the assets at the measurement date. These valuation techniques are based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect management's assumptions.

These two types of inputs create the following fair value hierarchy:

- Level 1 – Quoted prices for identical instruments in active markets;
- Level 2 – Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose significant inputs are observable;
- Level 3 – Instruments whose significant inputs are unobservable.

The guidance requires the use of observable market data, when available, in making fair value measurements. When inputs used to measure fair value fall within different levels of the hierarchy, the level within which the fair value measurement is categorized is based on the lowest level input that is significant to the fair value measurement.

***Recurring Fair Value Measurements***

The following table presents the Company's financial instruments, which are measured at fair value on a recurring basis, by the level in the fair value hierarchy within which those measurements fall. Methods and assumptions used to estimate the fair value of these instruments are described after the table.

	Level 1	Level 2	Level 3	Total
	(in thousands)			
<b>December 31, 2019</b>				
Derivative assets	\$ —	\$ 58	\$ —	\$ 58
Derivative liabilities	\$ —	\$ 21	\$ —	\$ 21
<b>December 31, 2018</b>				
Derivative liabilities	\$ —	\$ 30	\$ —	\$ 30

*Derivatives:* The fair value of interest rate swaps is determined using a discounted cash flow analysis on the expected future cash flows of the derivative. This analysis utilizes observable market data including forward yield curves and implied volatilities to determine the

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market's expectation of the future cash flows of the variable component. The fixed and variable components of the derivative are then discounted using calculated discount factors developed based on the LIBOR swap rate and are aggregated to arrive at a single valuation for the period. The Company also incorporates credit valuation adjustments to appropriately reflect both its own nonperformance risk and the respective counterparty's nonperformance risk in the fair value measurements.

Although the Company has determined that the majority of the inputs used to value its derivatives fall within Level 2 of the fair value hierarchy, the credit valuation adjustments associated with its derivatives utilize Level 3 inputs, such as estimates of current credit spreads to evaluate the likelihood of default by itself and its counterparties. However, as of December 31, 2019 and 2018, the Company has assessed the significance of the impact of the credit valuation adjustments on the overall valuation of its derivative positions and has determined that the credit valuation adjustments are not significant to the overall valuation. As a result, the Company has determined that its derivative valuations in their entirety are classified within Level 2 of the fair value hierarchy. In adjusting the fair value of its derivative contracts for the effect of nonperformance risk, the Company has considered any applicable credit enhancements. The Company's derivative instruments are further described in Note 8.

***Fair Value Disclosures***

The following table presents the Company's financial assets and liabilities, which are measured at fair value for disclosure purposes, by the level in the fair value hierarchy within which they fall. Methods and assumptions used to estimate the fair value of these instruments are described after the table.

	Level 1	Level 2	Level 3	Total
	(in thousands)			
<b>December 31, 2019</b>				
Mortgage notes payable, net	\$ —	\$ —	\$ 415,183	\$ 415,183
<b>December 31, 2018</b>				
Mortgage notes payable, net	\$ —	\$ —	\$ 400,192	\$ 400,192

*Mortgage notes payable:* The Company estimates the fair value of its mortgage notes payable by discounting the future cash flows of each instrument at rates currently offered to the Company for similar debt instruments of comparable maturities by the Company's lenders. Judgment is used in determining the appropriate rate for each of the Company's individual mortgages and notes payable based upon the specific terms of the agreement, including the term to maturity, the quality and nature of the underlying property and its leverage ratio. The rates used range from 3.75% to 3.80% and from 4.82% to 4.83% at December 31, 2019 and 2018, respectively. The fair value of the Company's matured mortgage notes payable were determined to be equal to the carrying value of the properties because there is no market for similar debt instruments and the properties' carrying value was determined to be the best estimate of fair value. The Company's mortgage notes payable are further described in Note 7.

**NOTE 10 – NONCONTROLLING INTEREST OF UNITHOLDERS IN OPERATING PARTNERSHIP**

As of December 31, 2019 and 2018, outstanding limited partnership units totaled 17,811,000 and 17,876,000, respectively. Total aggregate distributions per unit for the years ended December 31, 2019, 2018, and 2017 were \$1.0450, \$1.0175 and \$0.9900, respectively. The operating partnership declared fourth quarter distributions of \$4,653 and \$4,547, to limited partners payable in January 2020 and 2019, respectively.

During the year ended December 31, 2019, there were 1,000 limited partnership units of the operating partnership exchanged for 1,000 common shares of the Trust, pursuant to redemption requests. The aggregate value of these transactions was \$28. During the year ended December 31, 2018, there were no common shares exchanged for limited partnership units of the operating partnership. During the year ended December 31, 2017, Sterling exchanged 8,000 limited partnership units for 8,000 common shares held by the Trust, pursuant to redemption requests. The aggregate value of these transactions was \$133.

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At the sole and absolute discretion of the limited partnership, and so long our redemption plans exist, and applicable holding periods are met, Limited Partners may request the operating partnership redeem their limited partnership units. The operating partnership may choose to offer the Limited Partner: (i) cash for the redemption or, at the request of the Limited Partner, (ii) offer shares in lieu of cash for the redemption on a basis of one limited partnership unit for one Sterling common share (the "Exchange Request"). The Exchange Request shall be exercised pursuant to a Notice of Exchange. If the issuance of Sterling common shares pursuant to an Exchange Request will cause the shareholder to exceed the ownership limitations, among other reasons, payment will be made to the Limited Partner in cash. No Limited Partner may exercise an Exchange Request more than twice during any calendar year, and Exchange Requests may not be made for less than 1,000 limited partnership units. If a Limited Partner owns fewer than 1,000 limited partnership units, all of the limited partnership units held by the Limited Partner must be exchanged pursuant to the Exchange Request.

**NOTE 11 – REDEMPTION PLANS**

Our Board of Trustees has approved redemption plans that enable our shareholders to sell their common shares and the partners of our operating partnership to sell their limited partnership units to us, after they have held the securities for at least one year and subject to other conditions and limitations described in the plans.

Our redemption plans currently provide that the maximum amount that can be redeemed under the plan is \$35,000 worth of securities. As of December 31, 2019, there were \$5,900 worth of securities left to be redeemed under the redemption plan. Currently, the fixed redemption price is \$18.25 per share or unit under the plans which price became effective January 1, 2020. Prior to January 1, 2020, the redemption price was \$18.00 per share or unit under the plan. Prior to January 1, 2019, the redemption price was \$17.50 per share or unit under the plan.

We may redeem securities under the plans provided the aggregate total has not been exceeded if we have sufficient funds to do so. The plans will terminate in the event the shares become listed on any national securities exchange, the subject of bona fide quotes on any inter-dealer quotation system or electronic communications network or are the subject of bona fide quotes in the pink sheets. Additionally, the Board, in its sole discretion, may terminate, amend or suspend the redemption plans, either or both of them, if it determines to do so in its sole discretion.

During the years ended December 31, 2019, 2018 and 2017, the Company redeemed 50,000, 75,000 and 72,000 common shares valued at \$891, \$1,315 and \$1,110, respectively. In addition, during the years ended December 31, 2019, 2018 and 2017, the Company redeemed 64,000, 64,000 and 83,000 units valued at \$1,132, \$1,116 and \$1,284, respectively.

**NOTE 12 – BENEFICIAL INTEREST**

We are authorized to issue 100,000,000 common shares of beneficial interest with \$0.01 par value and 50,000,000 preferred shares with \$0.01 par value, which collectively represent the beneficial interest of Sterling. As of December 31, 2019 and 2018, there were 9,436,000 and 8,967,000 common shares outstanding. We had no preferred shares outstanding as of either date.

Dividends paid to holders of common shares were \$1.0450 per share, \$1.0175 per share and \$0.9900 per share for the years ended December 31, 2019, 2018 and 2017, respectively.

**NOTE 13 – DIVIDEND REINVESTMENT PLAN**

Our Board of Trustees approved a dividend reinvestment plan to provide existing holders of our common shares with a convenient method to purchase additional common shares without payment of brokerage commissions, fees or service charges. On July 20, 2012, we registered with the Securities Exchange Commission 2,000,000 common shares to be issued under the plan on Form S-3D, which automatically became effective on July 20, 2012. On July 11, 2017, we registered with the Securities Exchange Commission an additional 2,000,000 common shares to be issued under the plan on Form S-3D, which automatically became effective on July 11, 2017.

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Under this plan, eligible shareholders may elect to have all or a portion (but not less than 25%) of the cash dividends they receive automatically reinvested in our common shares. If an eligible shareholder elects to reinvest cash dividends under the plan, the shareholder may also make additional optional cash purchases of our common shares, not to exceed \$10 per fiscal quarter without our prior approval. The purchase price per common share under the plan equals 95% of the estimated value per common share for dividend reinvestments and equals 100% of the estimated value per common share for additional optional cash purchases, as determined by our Board of Trustees. In addition, eligible shareholders may not in any calendar year purchase or receive via transfer more than \$40 additional optional cash purchases of Common Shares.

The estimated value per common share was \$19.00 and \$18.50 at December 31, 2019 and 2018, respectively. See discussion of determination of estimated value in Note 18.

Therefore, the purchase price per common share for dividend reinvestments was \$18.05 and \$17.58 and for additional optional cash purchases was \$19.00 and \$18.50 at December 31, 2019 and 2018, respectively. The Board, in its sole discretion, may amend, suspend or terminate the plan at any time, without the consent of shareholders, upon a ten day notice to participants.

In the year ended December 31, 2019, 342,000 shares were issued pursuant to dividend reinvestments and 173,000 shares were issued pursuant to additional optional cash purchases under the plan. In the year ended December 31, 2018, 325,000 shares were issued pursuant to dividend reinvestments and 226,000 shares were issued pursuant to additional optional cash purchases under the plan. In the year ended December 31, 2017, 331,000 shares were issued pursuant to dividend reinvestments and 216,000 shares were issued pursuant to additional optional cash purchases under the plan.

**NOTE 14 – RELATED PARTY TRANSACTIONS**

*Property Management Fee*

During the years ended December 31, 2019, 2018 and 2017, we paid property management fees to GOLDMARK Property Management in an amount equal to approximately 5% of rents of the properties managed. GOLDMARK Property Management is owned in part by Kenneth Regan, James Wieland and Joel Thompson. For the years ended December 31, 2019, 2018 and 2017, we paid management fees of \$12,486, \$11,827, and \$11,359 respectively, to GOLDMARK Property Management. In addition, during the years ended December 31, 2019, 2018 and 2017, we paid repair and maintenance related payroll and payroll related expenses to GOLDMARK Property Management totaling \$6,076, \$5,217 and \$5,030, respectively.

*Board of Trustee Fees*

We incurred Trustee fees of \$57, \$68 and \$56 during the years ended December 31, 2019, 2018 and 2017, respectively. As of December 31, 2019, and 2018 we owed our Trustees \$29 and \$34 for unpaid board of trustee fees, respectively. There is no cash retainer paid to Trustees. Instead, we pay Trustees specific amounts of shares for meetings attended. Our Trustee Compensation Plan provides:

Board Chairman – Board Meeting	105 shares/meeting
Trustee – Board Meeting	75 shares/meeting
Committee Chair – Committee Meeting	30 shares/meeting
Trustee – Committee Meeting	30 shares/meeting

Common shares earned in accordance with the plan are calculated on an annual basis. Shares earned pursuant to the Trustee Compensation Plan are issued on or about July 15 for Trustees' prior year of service. Non-independent Trustees are not compensated for their service on the Board or Committees.

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*Advisory Agreement*

We are an externally managed trust and as such, although we have a Board of Trustees and executive officers responsible for our management, we have no paid employees. The following is a brief description of the current fees and compensation that may be received by the Advisor under the Advisory Agreement, which must be renewed on an annual basis and approved by a majority of the independent trustees. The Advisory Agreement was approved by the Board of Trustees (including all the independent Trustees) on March 29, 2019, effective April 1, 2019.

**Management Fee:** 0.35% of our total assets (before depreciation and amortization), annually. Total assets are our gross assets (before depreciation and amortization) as reflected on our consolidated financial statements, taken as of the end of the fiscal quarter last preceding the date of computation. The management fee will be payable monthly in cash or our common shares, at the option of the Advisor, not to exceed one-twelfth of 0.35% of the total assets as of the last day of the immediately preceding month. The management fee calculation is subject to quarterly and annual reconciliations. The management fee may be deferred at the option of the Advisor, without interest.

During the years ended December 31, 2019, 2018 and 2017, we incurred advisory management fees of \$2,996, \$2,909 and \$2,830 with Sterling Management, LLC, our Advisor. As of December 31, 2019 and 2018, we owed our Advisor \$503 and \$242, respectively, for unpaid advisory management fees. These fees cover the office facilities, equipment, supplies, and staff required to manage our day-to-day operations.

**Acquisition Fee:** For its services in investigating and negotiating acquisitions of investments for us, the Advisor receives an acquisition fee of 2.5% of the purchase price of each property acquired, capped at \$375 per acquisition. The total of all acquisition fees and acquisition expenses cannot exceed 6% of the purchase price of the investment, unless approved by a majority of the trustees, including a majority of the independent trustees, if they determine the transaction to be commercially competitive, fair and reasonable to us.

During the year ended December 31, 2019, we incurred no acquisition fees. During the years ended December 31, 2018 and 2017, we incurred acquisition fees of \$740 and \$727, respectively, with our Advisor. There were no acquisition fees owed to our Advisor as of December 31, 2019. As of December 31, 2018, we owed our Advisor \$32 for unpaid acquisition fees.

**Disposition Fee:** For its services in the effort to sell any investment for us, the Advisor receives a disposition fee of 2.5% of the sales price of each property disposition, capped at \$375 per disposition.

During the year ended December 31, 2019, we incurred no disposition fees. During the years ended December 31, 2018 and 2017, we incurred disposition fees of \$327 and \$110 with our Advisor. See Note 17. There were no disposition fees owed to our Advisor as of December 31, 2019 and 2018, respectively.

**Financing Fee:** 0.25% of all amounts made available to us pursuant to any loan, refinance (excluding rate and/or term modifications of an existing loan with the same lender), line of credit or other credit facility. The finance fee shall be capped at \$38 per loan, refinance, line of credit or other credit facility.

During the years ended December 31, 2019, 2018 and 2017, we incurred financing fees of \$11, \$77 and \$114 with our Advisor for loan financing and refinancing activities. There were no financing fees owed to our Advisor as of December 31, 2019. As of December 31, 2018, we owed our Advisor \$8 for unpaid financing fees.



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**Development Fee:** Based on regressive sliding scale (starting at 5% and declining to 3%) of total project costs, excluding cost of land, for development services requested by us.

Total Cost	Fee	Range of Fee	Formula
0 – 10M	5.0 %	0 – .5M	$0M - 5.0\% \times (TC - 0M)$
10M - 20M	4.5 %	.5 M – .95M	$.50M - 4.5\% \times (TC - 10M)$
20M – 30M	4.0 %	.95 M – 1.35M	$.95M - 4.0\% \times (TC - 20M)$
30M – 40M	3.5 %	1.35 M – 1.70M	$1.35M - 3.5\% \times (TC - 30M)$
40M – 50M	3.0 %	1.70 M – 2.00M	$1.70M - 3.0\% \times (TC - 40M)$

TC = Total Project Cost

During the years ended December 31, 2019, 2018 and 2017, there were no development fees incurred with our Advisor. As of December 31, 2019 and 2018, we owed our Advisor a total of \$104 for unpaid development fees as part of a 10% hold back, respectively.

**Project Management Fee:** 6% of all completed capital improvement projects on real estate investments owned by the Trust are paid to the Advisor.

Our Advisor began completing our capital improvement projects in September 2019. These projects were previously performed by our property managers. During the year ended December 31, 2019, there were \$67 in project management fees incurred with our Advisor for capital improvement projects, which we owed to our advisor as of December 31, 2019.

*Operating Partnership Units Issued in Connection with Acquisitions*

During the year ended December 31, 2019, we issued no operating partnership (OP) units to entities affiliated with any related parties.

During the year ended December 31, 2018, we issued directly or indirectly, 234,000 operating partnership (OP) units to entities affiliated with Messrs. Regan, and Wieland, two of our trustees, in connection with the acquisition of various properties. The aggregate value of these units was \$4,327.

During the year ended December 31, 2017, we issued directly or indirectly, 408,000 operating partnership (OP) units to entities affiliated with Messrs. Regan, and Wieland, two of our trustees, in connection with the acquisition of various properties. The aggregate value of these units was \$6,536.

*Commissions*

During the year ended December 31, 2019 there were no commissions incurred. During the years ended December 31, 2018 and 2017, we incurred real estate commissions of \$384, and \$572, respectively, to GOLDMARK Commercial Real Estate Services, Inc., which is controlled by Messrs. Regan and Wieland. There were no outstanding commissions owed as of December 31, 2019 or 2018.

*Rental Income*

During the years ended December 31, 2019, 2018 and 2017, we received rental income of \$56, \$55 and \$54, respectively, under an operating lease agreement with GOLDMARK Commercial Real Estate Services, Inc..

During the years ended December 31, 2019, 2018 and 2017, we paid our Advisor \$61, \$50 and \$45, respectively, under an operating lease agreement.

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During the years ended December 31, 2019, 2018 and 2017, we received rental income of \$262, \$230 and \$215, respectively, under operating lease agreements with GOLDMARK Property Management.

*Construction Costs*

There were no construction costs incurred during the years ended December 31, 2019 and 2018 to GOLDMARK Development, which is controlled by Messrs. Regan and Wieland. As of December 31, 2017, we incurred total costs of \$8,997 related to the construction of a clubhouse and six 6-plex two-story townhomes to GOLDMARK Development. There was no retainage or unpaid construction fees owed to GOLDMARK Development as of December 31, 2019 and 2018. Phase II of the Bismarck, North Dakota development project was completed in August 2017.

*Insurance*

Our Advisor manages insurance claims for the Trusts as well as a related party. The Advisor handles filing, processing, disputing and closing all insurance claims. During June 2019, the Trust and a related party incurred damage from a large windstorm. The claim is currently still open and funds were received from the insurance company to begin rehabilitation on our properties. As this was an aggregate property claim, funds will be disbursed when all disputes of the claim are completed. The Trust currently holds a related party receivable from our Advisor for these insurance funds totaling \$892.

**NOTE 15 - RENTALS UNDER OPERATING LEASES / RENTAL INCOME**

Residential apartment units are rented to individual tenants with lease terms of one year or less. Gross revenues from residential rentals totaled \$94,763, \$89,783 and \$86,858 for the years ended December 31, 2019, 2018 and 2017, respectively.

Commercial properties are leased to tenants under terms expiring at various dates through 2038. Lease terms often include renewal options. For the years ended December 31, 2019, 2018 and 2017, gross revenues from commercial property rentals, including CAM income (common area maintenance) of \$6,077, \$6,118 and \$6,162, respectively, totaled \$25,576, \$26,268 and \$27,422, respectively.

Commercial space is rented under long-term agreements. Minimum future rentals on non-cancelable operating leases as of December 31, 2019 are as follows:

<u>Years ending December 31,</u>	<u>Amount</u> <u>(in thousands)</u>
2020	\$ 17,956
2021	14,979
2022	11,595
2023	9,663
2024	9,244
Thereafter	43,453
	<u>\$ 106,890</u>

**NOTE 16 - COMMITMENTS AND CONTINGENCIES**

*Environmental Matters*

Federal law (and the laws of some states in which we own or may acquire properties) imposes liability on a landowner for the presence on the premises of hazardous substances or wastes (as defined by present and future federal and state laws and regulations). This liability is without regard to fault or knowledge of the presence of such substances and may be imposed jointly and severally upon all succeeding

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landowners. If such hazardous substance is discovered on a property acquired by us, we could incur liability for the removal of the substances and the cleanup of the property.

There can be no assurance that we would have effective remedies against prior owners of the property. In addition, we may be liable to tenants and may find it difficult or impossible to sell the property either prior to or following such a cleanup.

*Risk of Uninsured Property Losses*

We maintain property damage, fire loss, and liability insurance. However, there are certain types of losses (generally of a catastrophic nature) which may be either uninsurable or not economically insurable. Such excluded risks may include war, earthquakes, tornados, certain environmental hazards, and floods. Should such events occur, (i) we might suffer a loss of capital invested, (ii) tenants may suffer losses and may be unable to pay rent for the spaces, and (iii) we may suffer a loss of profits which might be anticipated from one or more properties.

*Litigation*

The Company is subject, from time to time, to various legal proceedings and claims that arise in the ordinary course of business. While the resolution of such matters cannot be predicted with certainty, management believes, based on currently available information, that the final outcome of such matters will not have a material effect on the consolidated financial statements of the Company.

**NOTE 17 – DISPOSITIONS**

During the year ended December 31, 2019, the operating partnership had no dispositions.

During the year ended December 31, 2018, the operating partnership sold three properties. We sold an industrial property located in Redwood Falls, Minnesota for \$5,200 and recognized a gain of \$935 in April 2018. We sold a retail property located in Austin, Texas for \$3,615 and recognized a gain of \$1,266 in July 2018. We sold one of two buildings included in an office property located in Bismarck, North Dakota for \$4,250 and recognized a gain of \$1,514 in July 2018.

During the year ended December 31, 2017, the operating partnership sold a Fargo, North Dakota retail property for approximately \$4,400 and recognized a gain of \$2,072.

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**NOTE 18 – BUSINESS COMBINATIONS AND ACQUISITIONS**

The Company did not acquire any properties during the year ended December 31, 2019.

The Company closed on the following acquisitions during the year ended December 31, 2018:

<u>Date</u>	<u>Property Name</u>	<u>Location</u>	<u>Property Type</u>	<u>Units/ Square Footage/ Acres</u>	<u>Acquisition Price</u>
3/1/18	Thunder Creek Apartments	Fargo, ND	Apartment complex	57 units	\$ 4,460
9/1/18	Chandler 1834	Grand Forks, ND	Apartment complex	12 units	630
9/17/18	Dairy Queen (a)	Apple Valley, MN	Retail building	5,348 sq. ft.	3,000
10/1/18	Hartford Apartments	Fargo, ND	Apartment complex	30 units	1,350
10/24/18	Bradbury Apartments	Bismarck, ND	Apartment complex	96 units	5,826
11/1/18	Cityside Apartments	Fargo, ND	Apartment complex	31 units	1,054
11/1/18	Morningside Apartments	Fargo, ND	Apartment complex	17 units	714
11/1/18	Fredericksburg Apartments	Omaha, NE	Apartment complex	173 units	11,319
12/31/18	Cityside Apartments (c)	Fargo, ND	Apartment complex	5 units	153
12/31/18	Cedars 4	Fargo, ND	Apartment complex	18 units	1,151
					<u>\$ 29,657 (b)</u>

(a) This property was acquired utilizing Internal Revenue Code 1031 tax-deferred exchange funds.

(b) Acquisition price does not include capitalized closing costs and adjustments of \$1,156 and special assessments of \$105.

(c) Subsequent purchase of additional units on adjacent property; consolidated with property acquired on November 1, 2018 for management purposes.

Total consideration given for acquisitions through December 31, 2018 was completed through issuing approximately 423,000 limited partnership units of the operating partnership valued at \$18.50 per unit for an aggregate consideration of approximately \$7,819, 1031 tax-deferred exchange funds of \$11,326 assumed loans of \$2,104, assumed liabilities \$576, and cash of \$9,093. The value of units issued in exchange for property is determined through a value established annually by our Board of Trustees, and reflects the fair value at the time of issuance.

The Company closed on the following acquisitions during the year ended December 31, 2017:

<u>Date</u>	<u>Property Name</u>	<u>Location</u>	<u>Property Type</u>	<u>Units/ Square Footage/ Acres</u>	<u>Acquisition Price</u>
1/10/17	Sargent Apartments	Fargo, ND	Apartment complex	36 units	\$ 1,710
1/11/17	Arrowhead Apartments	Grand Forks, ND	Apartment complex	82 units	5,494
1/17/17	West Oak Apartments	Fargo, ND	Apartment complex	18 units	777
1/17/17	Carr Apartments	Fargo, ND	Apartment complex	18 units	828
5/1/17	Plumtree Apartments	Fargo, ND	Apartment complex	18 units	907
5/1/17	Sunchase Apartments	Fargo, ND	Apartment complex	36 units	1,765
6/1/17	Essex Apartments	Fargo, ND	Apartment complex	18 units	858
6/1/17	Jadestone Apartments	Fargo, ND	Apartment complex	18 units	809
6/1/17	Park Circle Apartments	Fargo, ND	Apartment complex	18 units	903
7/3/17	East Bridge Apartments (a)	Fargo, ND	Apartment complex	58 units	6,060
12/1/17	Birchwood I Apartments	Fargo, ND	Apartment complex	18 units	401
12/1/17	Birchwood II Apartments	Fargo, ND	Apartment complex	48 units	2,425
					<u>\$ 22,937 (b)</u>

(a) This property was acquired utilizing Internal Revenue Code 1031 tax-deferred exchange.

(b) Acquisition price does not include capitalized closing costs and adjustments totaling \$258.

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Total consideration given for acquisitions through December 31, 2017 was completed through issuing approximately 118,000 limited partnership units of the operating partnership valued at \$16.00 per unit and \$16.50 per unit for an aggregate consideration of approximately \$10,006, 1031 exchange funds of \$4,278, new loans of \$4,180, assumed liabilities \$132, and cash of \$4,599. The value of units issued in exchange for property is determined through a value established annually by our Board of Trustees and reflects the fair value at the time of issuance.

In addition, as of May 1, 2017, the operating partnership acquired the remaining 59.74% ownership interest in a 144 unit property which was previously held as tenant in common (See Note 2). We estimated the property had a fair value of approximately \$10,080. The operating partnership assumed a loan of \$1,295 and issued \$4,727 of limited partnership units for a total purchase price of approximately \$6,022. The Company accounted for this as a business combination and recognized a gain on change in control of real estate investment of \$2,186 in the second quarter of 2017 as a result of remeasuring the carrying value to fair value. The total loan on this property was \$2,167, thus in addition to the portion of the loan assumed from the other tenant in common, the Company also recorded an additional \$872 in new financing related to this acquisition.

The following table summarizes the acquisition date fair values, before prorations, the Company recorded in conjunction with the acquisitions discussed above:

	Year Ended December 31,		
	2019	2018	2017
Land, building, tenant improvements and FF&E	\$ -	\$ 30,918	\$ 23,195
Mortgages notes payable assumed	-	(2,104)	-
Other liabilities	-	(576)	(132)
Net assets acquired	-	28,238	23,063
Equity/limited partnership unit consideration	-	(7,819)	(10,006)
Restricted cash proceeds related to IRC Section 1031 tax-deferred exchange	-	(11,326)	(4,278)
New loans	-	-	(4,180)
Net cash consideration	\$ -	\$ 9,093	\$ 4,599

The acquisitions completed after July 1, 2017 were considered asset acquisitions and, as such, transaction costs were capitalized upon closing. For acquisitions prior to July 1, 2017, which were accounted for as business combinations, the transaction costs totaled \$1,131 for the year ended December 31, 2017, are included in "Administration of REIT expenses" in the accompanying consolidated statements of operations and other comprehensive (loss) income.

***Estimated Value of Units/Shares***

The Board of Trustees determined an estimate of fair value for the trust shares in 2019, 2018 and 2017. In addition, the Board of Trustees, acting as general partner for the operating partnership, determined an estimate of fair value for the limited partnership units in 2019, 2018 and 2017. In determining this value, the Board relied upon their experience with, and knowledge about, the Trust's real estate portfolio and debt obligations. The Board typically determines the share price on an annual basis. The trustees determine the price in their discretion and use data points to guide their determination which is typically based on a consensus of opinion. In addition, the Board considers how the price chosen will affect existing share and unit values, redemption prices, dividend coverage ratios, yield percentages, dividend reinvestment factors, and future UPREIT transactions, among other considerations and information. The fair value was not determined based on, nor intended to comply with, fair value standards under US GAAP and the value may not be indicative of the price we would get for selling our assets in their current condition.

Based on the results of the methodologies, the Board determined the fair value of the shares and limited partnership units to be \$16.50 per share/unit effective March 29, 2017. The Board determined the fair value of the shares and limited partnership units to be \$18.50

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per share/unit effective January 1, 2018. The Board determined the fair value of the shares and limited partnership units to be \$19.00 per share/unit effective January 1, 2019. The Board determined the fair value of the shares and limited partnership units to be \$19.25 per share/unit effective January 1, 2020.

Determination of price is a matter within the Board's sole discretion. The Trust does not determine price based on any rote formula or specific factors. At this time, no shares are held in street name accounts and the Trust is not subject to FINRA's specific pricing requirements set out in Rule 2231 or otherwise. Thus, the Trust does not employ any specific valuation methodology or formula. Rather, the Board looks to available data and information, which is often adjusted and weighted to comport more closely with the assets held by the Trust at the time of valuation. The principal valuation methodology utilized is the NAV calculation/direct capitalization method. The information made available to the Board is assembled by the Trust's Advisor.

As with any valuation methodology, the methodologies utilized by the Board in reaching an estimate of the value of the shares and limited partnership units are based upon a number of estimates, assumptions, judgments or opinions that may, or may not, prove to be correct. The use of different estimates, assumptions, judgments, or opinions would likely have resulted in significantly different estimates of the value of the shares and limited partnership units. In addition, the Board's estimate of share and limited partnership unit value is not based on the book values of our real estate, as determined by GAAP, as our book value for most real estate is based on the amortized cost of the property, subject to certain adjustments.

Furthermore, in reaching an estimate of the value of the shares and limited partnership units, the Board applied a liquidity discount to one valuation scenario in order to reflect the fact that the shares and limited partnership units are not currently traded on a national securities exchange and did not consider: a discount for debt that may include a prepayment obligation or a provision precluding assumption of the debt by a third party or the costs that are likely to be incurred in connection with an appropriate exit strategy, whether that strategy might be a listing of the limited partnership units or common shares on a national securities exchange or a merger or sale of our portfolio.

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**NOTE 19 – QUARTERLY FINANCIAL INFORMATION (unaudited)**

The following table sets forth selected quarterly consolidated financial data for the Company:

2019	Quarter <sup>(1)</sup>			
	First	Second	Third	Fourth
	(in thousands, except per share data)			
Income from rental operations	\$ 29,831	\$ 30,270	\$ 30,173	\$ 30,065
Net Income	\$ 3,790	\$ 4,821	\$ 3,470	\$ 3,978
Net Income attributable to Sterling Real Estate Trust	\$ 1,288	\$ 1,647	\$ 1,213	\$ 1,386
Net Income per common share, basic and diluted	\$ 0.14	\$ 0.18	\$ 0.13	\$ 0.15
Weighted average common shares outstanding	9,091,000	9,209,000	9,322,000	9,444,000

2018	Quarter <sup>(1)</sup>			
	First	Second	Third	Fourth
	(in thousands, except per share data)			
Income from rental operations	\$ 29,099	\$ 28,646	\$ 29,055	\$ 29,251
Net Income	\$ 5,258	\$ 4,977	\$ 7,084	\$ 4,659
Net Income attributable to Sterling Real Estate Trust	\$ 1,740	\$ 1,675	\$ 2,379	\$ 1,580
Net Income per common share, basic and diluted	\$ 0.20	\$ 0.19	\$ 0.27	\$ 0.18
Weighted average common shares outstanding	8,627,000	8,720,000	8,840,000	8,971,000

(1) With regard to per share calculations, the sum of the quarterly results may not equal full year results due to rounding.

**NOTE 20 - SUBSEQUENT EVENTS**

On January 10, 2020, we acquired a 54-unit apartment complex in Fargo, North Dakota for \$4,968. Total consideration given for the acquisition was approximately 104,000 limited partnership units of the operating partnership valued at \$19.00 per unit for an aggregate consideration of \$1,971 and cash of \$2,997.

On January 15, 2020, we paid a dividend or distribution of \$0.26125 per share on our common shares of beneficial interest or limited partnership units, to common shareholders and limited unit holders of record on December 31, 2019.

On January 27, 2020, a joint venture we have a 60% interest, closed on a \$26,000 construction loan to fund the development of a multi-family property located in Savage, Minnesota. The Trust is jointly and severally liable for the full mortgage balance. In addition, on the same date, we entered into a loan facility with the joint venture to provide an additional \$5,007 in financing for the project.

On January 31, 2020, we acquired a 12-unit apartment complex in Fargo, North Dakota for \$612. Total consideration given for the acquisition was approximately 29,000 limited partnership units of the operating partnership valued at \$19.25 per unit for an aggregate consideration of \$557 and cash of \$55.

On February 10, 2020, the Trust settled a tenant dispute with a tenant of a Minneapolis, Minnesota property. The settlement did not lead to a material change in the consolidated financial statements.

On March 1, 2020, we disposed of a retail location in Apple Valley, Minnesota for \$3,670.

On March 1, 2020, we acquired 74 units in 6 apartment complexes located in Bismarck, North Dakota for \$4,077. Total consideration given for the acquisition was approximately 211,800 limited partnership units of the operating partnership valued at \$19.25 per unit for an aggregate consideration of \$4,077.

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On March 1, 2020, we acquired 48 units in 2 apartment complexes located in Fargo, North Dakota for \$2,400. Total consideration given for the acquisition was approximately 124,700 limited partnership units of the operating partnership valued at \$19.25 per unit for an aggregate consideration of \$2,400.

On March 6, 2020, we paid off 2 mortgage notes totaling approximately \$5,890.

Pending acquisitions and dispositions are subject to numerous conditions and contingencies and there are no assurances that the transactions will be completed.

We have evaluated subsequent events through the date of this filing. We are not aware of any other subsequent events which would require recognition or disclosure in the consolidated financial statements.



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Industrial Property	Physical Location	Encumbrances	Initial cost to company		Costs capitalized subsequent to acquisition (a)				Gross Amount at which carried at close of period			Date of Construction or Acquisition	Life on which depreciation on latest income statement is computed
			Land	Buildings	Land	Buildings	Buildings	Land	Buildings	Total			
Guardian Building Products	Fargo, ND	\$ 2,711	\$ 820	\$ 2,554	\$ 55	\$ (94)	\$ 875	\$ 2,460	\$ 3,335	\$ 457	8/29/12	40	
Titan Machinery	Bismarck, ND	2,158	950	1,395	7	—	957	1,395	2,352	174	1/28/15	40	
Titan Machinery	Dickinson, ND	782	354	1,096	400	—	754	1,096	1,850	215	7/30/12	40	
Titan Machinery	Fargo, ND	—	781	1,947	515	—	1,296	1,947	3,243	353	10/30/12	40	
Titan Machinery	Marshall, MN	1,804	300	3,648	81	—	381	3,648	4,029	752	11/1/11	40	
Titan Machinery	Minot, ND	—	618	1,654	—	—	618	1,654	2,272	307	8/1/12	40	
Titan Machinery	North Platte, NE	—	325	1,269	—	—	325	1,269	1,594	128	1/29/16	40	
Titan Machinery	Sioux City, IA	1,171	315	2,472	—	—	315	2,472	2,787	386	10/25/13	40	
Total		\$ 8,626	\$ 4,463	\$ 16,035	\$ 1,058	\$ (94)	\$ 5,521	\$ 15,941	\$ 21,462	\$ 2,772			

Land	Physical Location	Encumbrances	Initial cost to company		Costs capitalized subsequent to acquisition (a)		Gross Amount at which carried at close of period			Date of Construction or Acquisition	Life on which depreciation on latest income statement is computed
			Land	Buildings	Land	Buildings	Land	Buildings	Total		
Property											
Taco Bell	Denver, CO	\$ 419	\$ 669	\$ —	\$ —	\$ —	\$ 669	\$ —	\$ 669	6/14/11	
West 80	Rochester, MN	—	1,364	—	—	—	1,364	—	1,364	8/29/16	
Total		\$ 419	\$ 2,033	\$ —	\$ —	\$ —	\$ 2,033	\$ —	\$ 2,033		

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Medical Property	Physical Location	Initial cost to company				Costs capitalized subsequent to acquisition (a)				Gross Amount at which carried at close of period				Date of Construction or Acquisition	Life on which depreciation on latest income statement is computed									
		Encumbrances		Land		Buildings		Land		Buildings		Land				Buildings								
		\$		\$		\$		\$		\$		\$				\$								
Bio-Life	Bismarck, ND	1,138		306		2,255		11		123		317		2,378		2,695		781		1/3/08	9	-	40	
Bio-Life	Grand Forks, ND	1,137		457		2,230		1		158		458		2,388		2,846		806		1/3/08	10	-	40	
Bio-Life	Janesville, WI	1,138		250		1,857		—		123		250		1,980		2,230		657		1/3/08	9	-	40	
Bio-Life	Mankato, MN	1,137		390		2,111		280		1,154		670		3,265		3,935		988		1/3/08	11	-	40	
Bio-Life	Marquette, MI	—		213		2,793		—		123		213		2,916		3,129		935		1/3/08	9	-	40	
Bio-Life	Onalaska, WI	1,138		208		1,853		—		323		208		2,176		2,384		691		1/3/08	11	-	40	
Bio-Life	Oshkosh, WI	1,137		293		1,705		—		146		293		1,851		2,144		638		1/3/08	10	-	40	
Bio-Life	Sheboygan, WI	1,138		645		1,611		—		248		645		1,859		2,504		604		1/3/08	10	-	40	
Bio-Life	Stevens Point, WI	1,137		119		2,184		—		123		119		2,307		2,426		754		1/3/08	9	-	40	
Total		\$ 9,100		\$ 2,881		\$ 18,599		\$ 292		\$ 2,521		\$ 3,173		\$ 21,120		\$ 24,293		\$ 6,854						

Residential Property	Physical Location	Encumbrances	Initial cost to company			Costs capitalized subsequent to acquisition (a)				Gross Amount at which carried at close of period				Date of Construction or Acquisition	Life on which depreciation on latest income statement is computed					
			Land	Buildings	Total	Land	Buildings	Total	Land	Buildings	Total									
Amberwood	Grand Forks, ND	2,401	\$	426	\$	3,304	\$	3	\$	113	\$	429	\$	3,417	\$	3,846	\$	287	9/13/16	20 - 40
Arbor I/400	Bismarck, ND	394		73		516		4		65		77		581		658		93	6/4/13	40
Arbor II/404	Bismarck, ND	402		73		538		6		43		79		581		660		85	11/1/13	40
Arbor III/406	Bismarck, ND	400		71		536		7		43		78		579		657		84	11/1/13	40
Ashbury	Fargo, ND	2,487		314		3,774		26		25		340		3,799		4,139		291	12/19/16	40
Auburn II	Fargo, ND	923		105		883		12		64		117		947		1,064		299	3/23/07	20 - 40
Autumn Ridge	Grand Forks, ND	5,546		1,072		8,875		44		30		1,116		8,905		10,021		3,018	8/16/04	9 - 40
Barrett Arms	Crookston, MN	842		37		1,001		—		63		37		1,064		1,101		154	1/2/14	40
Bayview	Fargo, ND	2,818		284		3,817		59		65		343		3,882		4,225		1,166	12/31/07	20 - 40
Berkshire	Fargo, ND	458		31		406		4		6		35		412		447		122	3/31/08	20 - 40
Betty Ann	Fargo, ND	488		74		738		2		60		76		798		874		202	8/31/09	40
Birchwood 1	Fargo, ND	248		72		342		—		—		72		342		414		18	12/1/17	40
Birchwood 2	Fargo, ND	1,465		234		2,266		25		120		259		2,386		2,645		123	12/1/17	40
Bradbury Apartments	Bismarck, ND	2,024		1,049		4,922		—		46		1,049		4,968		6,017		154	10/24/18	40
Bridgeport	Fargo, ND	5,134		613		7,676		3		46		616		7,722		8,338		594	12/19/16	40
Bristol Park	Grand Forks, ND	3,089		985		3,976		—		684		985		4,660		5,645		438	2/1/16	40

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			Land	Buildings	Land	Buildings	Land	Buildings	Total			
Brookfield	Fargo, ND	345	228	1,958	30	258	258	2,216	2,474	590	8/1/08	20 - 40
Cambridge (FKA 44th Street)	Fargo, ND	1,585	333	1,845	4	95	337	1,940	2,277	326	2/6/13	40
Candlelight	Fargo, ND	1,854	613	1,221	(337)	416	276	1,637	1,913	287	11/30/12	40
Carling Manor	Grand Forks, ND	442	69	656	1	55	70	711	781	196	3/31/08	40
Carlton Place	Fargo, ND	6,596	703	7,070	96	365	799	7,435	8,234	2,002	9/1/08	20 - 40
Carr	Fargo, ND	544	66	759	1	—	67	759	826	57	1/17/17	40
Cedars 4	Fargo, ND	—	134	1,068	—	(10)	134	1,058	1,192	29	12/31/18	40
Chandler 1802	Grand Forks, ND	642	133	1,114	—	12	133	1,126	1,259	169	1/2/14	40
Chandler 1834	Grand Forks, ND	426	112	552	—	—	112	552	664	18	9/1/18	40
Chandler 1866	Grand Forks, ND	321	31	270	—	28	31	298	329	107	1/3/05	20 - 40
Cherry Creek (FKA Village)	Grand Forks, ND	—	173	1,435	1	60	174	1,495	1,669	413	11/1/08	40
Cityside Apartments	Fargo, ND	722	192	1,129	—	—	192	1,129	1,321	33	11/30/18	40
Columbia West	Grand Forks, ND	2,810	294	3,367	1	440	295	3,807	4,102	1,000	9/1/08	20 - 40
Country Club	Fargo, ND	195	252	1,252	2	211	254	1,463	1,717	294	5/2/11	20 - 40
Countryside	Fargo, ND	119	135	677	—	68	135	745	880	147	5/2/11	40
Courtyard	St. Louis Park, MN	3,466	2,270	5,681	—	721	2,270	6,402	8,672	968	9/3/13	5 - 40
Dakota Manor	Fargo, ND	1,621	249	2,236	20	124	269	2,360	2,629	308	8/7/14	40
Danbury	Fargo, ND	4,978	381	5,922	211	591	592	6,513	7,105	1,815	12/31/07	20 - 40
Dellwood Estates	Anoka, MN	6,924	844	9,924	—	452	844	10,376	11,220	1,679	5/31/13	40
Eagle Run	West Fargo, ND	4,011	576	5,787	128	97	704	5,884	6,588	1,373	8/12/10	40
Eagle Sky I	Bismarck, ND	886	115	1,292	—	74	115	1,366	1,481	136	3/1/16	40
Eagle Sky II	Bismarck, ND	886	135	1,279	—	138	135	1,417	1,552	132	3/1/16	40
East Bridge	Fargo, ND	3,437	792	5,477	—	158	792	5,635	6,427	352	7/3/17	40
Echo Manor	Hutchinson, MN	909	141	875	—	32	141	907	1,048	137	1/2/14	20 - 40
Emerald Court	Fargo, ND	—	66	830	2	87	68	917	985	263	3/31/08	20 - 40
Essex	Fargo, ND	539	212	642	—	68	212	710	922	45	6/1/17	40
Fairview	Bismarck, ND	2,780	267	3,978	39	887	306	4,865	5,171	1,158	12/31/08	20 - 40
Flickertail	Fargo, ND	5,226	426	5,590	76	202	502	5,792	6,294	1,567	12/31/08	40
Forest Avenue	Fargo, ND	366	61	637	4	39	65	676	741	112	2/6/13	40
Galleria III	Fargo, ND	517	118	681	1	267	119	948	1,067	164	11/9/10	40
Garden Grove	Bismarck, ND	4,383	606	6,073	—	99	606	6,172	6,778	575	5/4/16	5 - 40
Georgetown on the River	Fridley, MN	17,839	4,620	25,012	8	3,594	4,628	28,606	33,234	3,439	12/19/14	5 - 40
Glen Pond	Eagan, MN	14,520	3,761	20,569	38	633	3,799	21,202	25,001	4,223	12/2/11	20 - 40
Granger Court I	Fargo, ND	2,200	279	2,619	25	58	304	2,677	2,981	432	6/4/13	20 - 40

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**DECEMBER 31, 2019**  
(Dollar amounts in thousands)

Residential Property	Physical Location	Encumbrances	Initial cost to company		Costs capitalized subsequent to acquisition (a)		Gross Amount at which carried at close of period			Depreciation	Acquisition or Construction	Date of construction or Acquisition	Life on which depreciation on latest income statement is computed
			Land	Buildings	Land	Buildings	Land	Buildings	Total				
Griffin Court	Moorhead, MN	3,067	652	3,858	35	379	687	4,237	4,924	601	6/9/14	5 - 40	
Hannifin	Bismarck, ND	453	81	607	5	52	86	659	745	98	11/1/13	40	
Harrison and Richfield	Grand Forks, ND	5,503	756	6,346	4	316	760	6,662	7,422	2,070	7/1/07	5 - 40	
Hartford Apartments	Fargo, ND	904	154	1,233	—	—	154	1,233	1,387	39	10/1/18	40	
Highland Meadows	Bismarck, ND	5,716	1,532	8,513	—	250	1,532	8,763	10,295	590	5/1/17	5 - 40	
Hunters Run I	Fargo, ND	517	50	419	2	(2)	52	417	469	132	3/23/07	40	
Hunters Run II	Fargo, ND	504	44	441	2	—	46	441	487	127	7/1/08	40	
Huntington	Fargo, ND	358	86	309	—	15	86	324	410	35	8/4/15	40	
Islander	Fargo, ND	821	98	884	—	115	98	999	1,097	195	7/1/11	40	
Jadestone	Fargo, ND	512	212	554	—	67	212	621	833	39	6/1/17	40	
Kennedy	Fargo, ND	399	84	588	7	91	91	679	770	107	2/6/13	20 - 40	
Library Lane	Grand Forks, ND	2,192	301	2,401	12	121	313	2,522	2,835	768	10/1/07	20 - 40	
Madison	Grand Forks, ND	237	95	497	—	52	95	549	644	58	9/1/15	40	
Maple Ridge	Omaha, NE	3,911	766	5,608	59	3,576	825	9,184	10,009	1,829	8/1/08	20 - 40	
Maplewood	Maplewood, MN	9,239	3,120	11,955	—	1,021	3,120	12,976	16,096	1,570	12/19/14	5 - 40	
Maplewood Bend I, II, III, IV, V, VI, VII, VIII & Royale	Fargo, ND	4,746	783	5,839	1	271	784	6,110	6,894	1,419	1/1/09	20 - 40	
Martha Alice	Fargo, ND	488	74	738	2	83	76	821	897	213	8/31/09	20 - 40	
Mayfair	Grand Forks, ND	—	80	1,043	—	123	80	1,166	1,246	306	7/1/08	20 - 40	
Monticello	Fargo, ND	638	60	752	7	32	67	784	851	121	11/8/13	20 - 40	
Montreal Courts	Little Canada, MN	18,020	5,809	19,565	15	1,056	5,824	20,621	26,445	3,254	10/2/13	5 - 40	
Morningside Apartments	Fargo, ND	489	85	673	—	—	85	673	758	20	11/30/18	40	
Oak Court	Fargo, ND	2,720	270	2,210	14	328	284	2,538	2,822	699	4/30/08	28 - 40	
Oakview Townhomes	Grand Forks, ND	3,455	822	4,698	—	378	822	5,076	5,898	374	1/1/17	40	
Pacific Park I	Fargo, ND	594	95	777	3	65	98	842	940	141	2/6/13	40	
Pacific Park II	Fargo, ND	509	111	865	4	47	115	912	1,027	156	2/6/13	40	
Pacific South	Fargo, ND	314	58	459	2	—	60	459	519	79	2/6/13	40	
Park Circle	Fargo, ND	561	196	716	7	17	203	733	936	47	6/1/17	40	
Parkview Arms	Bismarck, ND	—	373	3,845	—	110	373	3,955	4,328	475	5/13/15	5 - 40	
Parkwest Gardens	West Fargo, ND	3,544	713	5,712	—	1,012	713	6,724	7,437	861	6/30/14	20 - 40	
Parkwood	Fargo, ND	—	126	1,143	7	16	133	1,159	1,292	319	8/1/08	40	
Pebble Creek	Bismarck, ND	4,011	260	3,704	—	(300)	260	3,404	3,664	1,015	3/19/08	20 - 40	
Plumtree	Fargo, ND	561	100	782	—	29	100	811	911	54	5/1/17	40	
Prairiewood Courts	Fargo, ND	—	308	1,730	28	80	336	1,810	2,146	582	9/1/06	20 - 40	
Prairiewood Meadows	Fargo, ND	2,067	736	2,514	11	16	747	2,530	3,277	462	9/30/12	40	

**STERLING REAL ESTATE TRUST AND SUBSIDIARIES**  
**SCHEDULE III – REAL ESTATE AND ACCUMULATED DEPRECIATION**  
**DECEMBER 31, 2019**  
(Dollar amounts in thousands)

Residential Property	Physical Location	Encumbrances	Initial cost to company		Costs capitalized subsequent to acquisition (a)		Gross Amount at which carried at close of period			Date of Construction or Acquisition		Life on which depreciation on latest income statement is computed
			Land	Buildings	Land	Buildings	Land	Buildings	Total			
Quail Creek	Springfield, MO	6,292	1,529	8,717	—	96	1,529	8,813	10,342	1,094	2/3/15	5 - 40
Robinwood	Coon Rapids, MN	4,459	1,138	6,133	242	567	1,380	6,700	8,080	809	12/19/14	40
Rosedale Estates	Roseville, MN	15,070	4,680	20,591	—	614	4,680	21,205	25,885	2,681	12/19/14	5 - 40
Rosegate	Fargo, ND	2,836	251	2,978	49	84	300	3,062	3,362	905	4/30/08	20 - 40
Roughrider	Grand Forks, ND	377	100	448	—	117	100	565	665	48	8/1/16	5 - 40
Saddlebrook	West Fargo, ND	909	148	1,262	203	105	351	1,367	1,718	358	12/31/08	40
Sage Park	New Brighton, MN	10,050	2,520	13,985	—	857	2,520	14,842	17,362	1,874	12/19/14	5 - 40
Sargent	Fargo, ND	1,034	164	1,529	4	17	168	1,546	1,714	116	1/10/17	40
Schrock	Fargo, ND	485	71	626	3	6	74	632	706	104	6/4/13	40
Sheridan Pointe	Fargo, ND	1,923	292	2,387	21	11	313	2,398	2,711	365	10/1/13	40
Sierra Ridge	Bismarck, ND	7,168	754	8,795	151	128	905	8,923	9,828	2,295	9/1/06	40
Somerset	Fargo, ND	2,920	300	3,400	43	30	343	3,430	3,773	973	7/1/08	40
Southgate	Fargo, ND	2,562	803	5,267	20	(45)	823	5,222	6,045	1,618	7/1/07	20 - 40
Southview III	Grand Forks, ND	195	99	522	—	79	99	601	700	124	8/1/11	40
Southview Villages	Fargo, ND	2,599	268	2,483	16	174	284	2,657	2,941	797	10/1/07	20 - 40
Spring	Fargo, ND	485	76	822	6	15	82	837	919	145	2/6/13	20 - 40
Stanford Court	Grand Forks, ND	—	291	3,866	—	83	291	3,949	4,240	681	2/6/13	20 - 40
Stonefield-Clubhouse	Bismarck, ND	—	34	1,147	—	50	34	1,197	1,231	103	7/31/16	40
Stonefield-Phase I	Bismarck, ND	8,296	2,804	13,138	227	246	3,031	13,384	16,415	1,675	8/1/14	20 - 40
Stonefield-Phase II	Bismarck, ND	—	1,167	2,566	486	5,129	1,653	7,695	9,348	550	10/23/14	40
Stonefield-Phase III	Bismarck, ND	—	1,079	—	238	—	1,317	—	1,317	—	10/23/14	n/a
Stonybrook	Omaha, NE	6,843	1,439	8,003	—	1,565	1,439	9,568	11,007	2,349	1/20/09	20 - 40
Summerfield	Fargo, ND	681	129	599	1	50	130	649	779	70	8/4/15	40
Summit Point	Fargo, ND	3,621	681	5,434	22	63	703	5,497	6,200	586	10/1/15	20 - 40
Sunchase	Fargo, ND	1,100	181	1,563	14	86	195	1,649	1,844	108	5/1/17	40
Sunset Ridge	Bismarck, ND	8,062	1,759	11,012	36	48	1,795	11,060	12,855	2,928	6/6/08	9 - 40
Sunview	Grand Forks, ND	—	144	1,578	1	124	145	1,702	1,847	450	12/31/08	20 - 40
Sunwood	Fargo, ND	2,695	358	3,376	38	163	396	3,539	3,935	1,065	7/1/07	20 - 40
Terrace on the Green	Moorhead, MN	—	697	2,588	—	265	697	2,853	3,550	489	9/30/12	40
Thunder Creek	Fargo, ND	2,862	633	4,063	—	177	633	4,240	4,873	193	3/1/18	25 - 40
Twin Oaks	Hutchinson, MN	3,144	816	3,245	—	122	816	3,367	4,183	437	10/1/14	40
Twin Parks	Fargo, ND	2,076	119	2,072	43	131	162	2,203	2,365	586	10/1/08	20 - 40
Valley Homes Duplexes	Grand Forks, ND	986	356	1,668	—	310	356	1,978	2,334	228	1/22/15	40
Valley View	Golden Valley, MN	4,440	1,190	6,118	—	166	1,190	6,284	7,474	798	12/19/14	5 - 40

**STERLING REAL ESTATE TRUST AND SUBSIDIARIES**  
**SCHEDULE III – REAL ESTATE AND ACCUMULATED DEPRECIATION**  
**DECEMBER 31, 2019**  
(Dollar amounts in thousands)

Residential Property	Physical Location	Encumbrances	Initial cost to company		Costs capitalized subsequent to acquisition (a)		Gross Amount at which carried at close of period		Depreciation	Date of Construction or Acquisition	Life on which depreciation on latest income statement is computed
			Land	Buildings	Land	Buildings	Land	Buildings			
Village Park	Fargo, ND	710	219	1,932	51	34	270	1,966	572	4/30/08	40
Village West	Fargo, ND	2,389	357	2,274	61	121	418	2,395	654	4/30/08	40
Washington	Grand Forks, ND	408	74	592	—	76	74	668	58	5/4/16	40
Westcourt	Fargo, ND	2,232	287	3,000	28	53	315	3,053	485	1/2/14	5 - 40
West Oak	Fargo, ND	556	85	692	—	37	85	729	58	1/17/17	40
Westside	Hawley, MN	518	59	360	—	63	59	423	94	2/1/10	40
Westwind	Fargo, ND	642	49	455	1	83	50	538	161	4/30/08	20 - 40
Westwood	Fargo, ND	3,782	597	6,341	91	352	688	6,693	1,850	6/5/08	20 - 40
Willow Park	Fargo, ND	3,674	288	5,286	39	707	327	5,993	1,489	12/31/08	40
Woodland Pines	Omaha, NE	6,396	842	10,596	—	477	842	11,073	316	11/30/18	40
Total		\$ 323,735	\$ 73,917	\$ 458,534	\$ 2,908	\$ 34,844	\$ 76,825	\$ 493,378	\$ 83,868		

**STERLING REAL ESTATE TRUST AND SUBSIDIARIES**  
**SCHEDULE III – REAL ESTATE AND ACCUMULATED DEPRECIATION**  
**DECEMBER 31, 2019**  
(Dollar amounts in thousands)

Office Property	Physical Location	Encumbrances	Initial cost to company		Costs capitalized subsequent to acquisition (a)			Gross Amount at which carried at close of period			Date of Construction or Acquisition	Life on which depreciation on latest income statement is computed			
			Land	Buildings	Land	Buildings	Total	Land	Buildings	Total					
32nd Avenue	Fargo, ND	\$ —	\$ 635	\$ 3,300	\$ 87	\$ 100	\$ 4,122	\$ 722	\$ 3,400	\$ 4,122	\$ 1,321	3/16/04	3	-	40
Aetna	Bismarck, ND	—	841	4,915	120	1,283	7,159	961	6,198	7,159	1,996	12/6/06	5	-	40
Bell Plaza	Bloomington, MN	32,894	6,912	36,520	—	1,610	45,042	6,912	38,130	45,042	8,475	8/13/15	3	-	40
First International Bank & Trust	Moorhead, MN	—	210	712	3	88	1,013	213	800	1,013	215	5/13/11	10	-	40
Four Points	Fargo, ND	—	70	1,238	—	78	1,386	70	1,316	1,386	384	10/18/07	5	-	40
Gate City	Grand Forks, ND	—	382	893	1	176	1,452	383	1,069	1,452	280	3/31/08			40
Goldmark Office Park	Fargo, ND	—	1,160	12,446	65	958	14,629	1,225	13,404	14,629	4,217	7/1/07	1	-	40
Great American Bldg	Fargo, ND	814	511	1,290	20	359	2,180	531	1,649	2,180	559	2/1/05	28	-	40
Midtown Plaza	Minot, ND	1,139	30	1,213	—	33	1,276	30	1,246	1,276	452	1/1/04	5	-	40
Parkway office building (FKA Echelon)	Fargo, ND	850	278	1,491	42	66	1,877	320	1,557	1,877	484	5/15/07	9	-	40
Redpath	White Bear Lake, MN	2,537	1,195	1,787	—	—	2,982	1,195	1,787	2,982	175	2/1/16			40
Regis	Edina, MN	—	2,991	7,633	—	—	10,624	2,991	7,633	10,624	2,104	1/1/09			40
SSA	St Cloud, MN	—	100	2,793	—	18	2,911	100	2,811	2,911	898	3/20/07	20	-	40
Wells Fargo Center	Duluth, MN	—	600	7,270	(115)	2,089	9,844	485	9,359	9,844	2,712	7/11/07	4	-	40
Total		\$ 38,234	\$ 15,915	\$ 83,501	\$ 223	\$ 6,858	\$ 106,497	\$ 16,138	\$ 90,359	\$ 24,272					

**STERLING REAL ESTATE TRUST AND SUBSIDIARIES**  
**SCHEDULE III – REAL ESTATE AND ACCUMULATED DEPRECIATION**  
**DECEMBER 31, 2019**  
(Dollar amounts in thousands)

Retail Property	Physical Location	Initial cost to company		Costs capitalized subsequent to acquisition (a)		Gross Amount at which carried at close of period			Date of Construction or Acquisition		Life on which depreciation on latest income statement is computed
		Land	Buildings	Land	Buildings	Land	Buildings	Total	Depreciation	Acquisition	
Applebees	Apple Valley, MN	\$ —	\$ 1,235	\$ —	\$ —	\$ 560	\$ 1,235	\$ 1,795	\$ 278	1/27/11	40
Applebees	Bloomington, MN	—	1,000	11	—	1,011	474	1,485	117	3/22/10	40
Applebees	Coon Rapids, MN	—	750	—	—	750	875	1,625	215	3/9/10	40
Applebees	Savage, MN	—	690	—	—	690	424	1,114	104	1/1/10	40
Becker Furniture	Waite Park, MN	—	150	—	(637)	150	1,428	1,578	697	7/12/06	40
Dairy Queen	Apple Valley, MN	—	1,128	—	—	1,128	1,345	2,473	52	9/17/18	40
Dairy Queen	Dickinson, ND	—	329	—	—	329	658	987	132	1/19/12	40
Dairy Queen	Moorhead, MN	—	243	1	—	244	787	1,031	171	5/13/11	20
Family Dollar	Mandan, ND	—	167	—	—	167	649	816	147	12/14/10	40
O'Reilly	Mandan, ND	—	115	—	—	115	449	564	102	12/14/10	40
Walgreens	Alexandria, LA	1,139	1,090	—	—	1,090	2,973	4,063	745	12/18/09	28
Walgreens	Batesville, AR	5,364	473	—	—	473	6,405	6,878	1,682	7/9/09	40
Walgreens	Denver, CO	3,216	2,349	—	—	2,349	2,358	4,707	506	6/14/11	40
Walgreens	Fayetteville, AR	4,074	636	—	—	636	4,732	5,368	1,242	7/9/09	40
Walgreens	Laurel, MS	1,131	2,984	—	—	1,280	2,984	4,264	709	7/30/10	40
Total		\$ 14,924	\$ 10,960	\$ 12	\$ (637)	\$ 10,972	\$ 27,776	\$ 38,748	\$ 6,899		
Grand Totals		\$ 395,038	\$ 110,169	\$ 4,493	\$ 43,492	\$ 114,662	\$ 648,574	\$ 763,236	\$ 124,665		

**Investments in Unconsolidated Affiliates:**

Property	Physical Location	Initial cost to company		Costs capitalized subsequent to acquisition (a)		Gross Amount at which carried at close of period			Date of Construction or Acquisition	Life on which depreciation on latest income statement is computed
		Land	Buildings	Land	Buildings	Land	Buildings	Total		
Banner	Fargo, ND	\$ 750	\$ 8,016	\$ 203	\$ 224	\$ 953	\$ 8,240	\$ 9,193	3/15/07	40
GF Marketplace	Grand Forks, ND	4,259	15,801	208	1,194	4,467	16,995	21,462	7/1/03	25
										40



**STERLING REAL ESTATE TRUST AND SUBSIDIARIES**  
**SCHEDULE III – REAL ESTATE AND ACCUMULATED DEPRECIATION**  
**DECEMBER 31, 2019**  
(Dollar amounts in thousands)

**Notes:**

- (a) The costs capitalized subsequent to acquisition is net of dispositions.  
(b) The changes in total real estate investments for the years ended December 31, 2019, 2018 and 2017 are as follows (in thousands):

	2019	2018	2017
Balance at January 1,	\$ 790,696	\$ 759,703	\$ 715,300
Purchase of real estate investments	5,981	41,230	47,279
Sale and disposal of real estate investment	(4,422)	(10,222)	(1,267)
Property held for sale	—	—	—
Provision for asset impairment	—	—	—
Construction in progress not yet placed in service	9,773	(15)	(1,609)
Reallocation to intangible assets	—	—	—
Balance at December 31,	\$ 802,028	\$ 790,696	\$ 759,703

- (c) The changes in accumulated depreciation for the years ended December 31, 2019, 2018 and 2017 are as follows (in thousands):

	2019	2018	2017
Balance at January 1,	\$ 128,112	\$ 111,026	\$ 92,325
Depreciation expense	19,644	19,165	19,057
Property held for sale	—	—	—
Sale and disposal of real estate investment	(1,440)	(2,079)	(356)
Balance at December 31,	\$ 146,316	\$ 128,112	\$ 111,026

- (d) The aggregate cost of our real estate for federal income tax purposes is \$680,591.

## Exhibit Index

Exhibit number	Exhibit Description	Filed here with	Incorporated by reference		
			Form	Period ending	Filing date
3.1	Articles of Organization of Sterling Real Estate Trust filed December 3, 2002		10-12G		03/10/11
3.2	Amendment to Articles of Organization of Sterling Real Estate Trust dated August 1, 2014		8-K		06/24/14
3.3	Amended and Restated Bylaws dated June 23, 2011		10-12G		03/10/11
3.4	Amended and Restated Bylaws dated June 23, 2016		8-K		06/29/16
3.5	Amended and Restated Bylaws effective December 12, 2019		8-K		12/16/19
4.1	Declaration of Trust Sterling Real Estate Trust dated July 21, 2004		10-12G		03/10/11
4.2	Addendum to Declaration of Trust dated July 25, 2007		10-12G		03/10/11
4.3	Sterling Third Amended and Restated Declaration of Trust dated March 27, 2014		8-K		04/02/14
4.4	Sterling Third Amended and Restated Declaration of Trust dated June 23, 2016		8-K		06/29/16
4.5	First Amended and Restated Declaration of Trust dated February 9, 2011		10-12G		03/10/11
4.6	Amendment No. 1 to First Amended and Restated Declaration of Trust dated August 1, 2014		8-K		06/24/14
4.7	Amended and Restated Share Repurchase Plan dated December 13, 2018		8-K		12/19/18
4.8	Amended and Restated Share Repurchase Plan effective January 1, 2020		8-K		12/16/19
4.9	Amended and Restated Unit Repurchase Plan dated December 13, 2018		8-K		12/19/18
4.10	Amended and Restated Unit Repurchase Plan, effective January 1, 2020		8-K		12/16/19
4.11	Description of Registrant's Securities	X			
10.1	First Amendment and Complete Restatement of Agreement of Limited Liability Limited Partnership of Sterling Properties, LLLP dated April 25, 2003		10-12G		03/10/11
10.2	Second Amendment to the Agreement of Limited Liability Limited Partnership of Sterling Properties, LLLP dated December 19, 2008		10-12G		03/10/11
10.3	Third Amendment to the Agreement of Limited Liability Limited Partnership of Sterling Properties, LLLP dated August 5, 2009		10-12G		03/10/11
10.4	Fourth Amendment to the Agreement of Limited Liability Limited Partnership of Sterling Properties, LLLP dated February 9, 2011		10-12G		03/10/11
10.5	Fifth Amendment to the Agreement of Limited Liability Limited Partnership of Sterling Properties, LLLP dated June 23, 2011		10-K	12/31/2011	03/30/12
10.6	Seventh Amended and Restated Advisory Agreement dated January 1, 2018		8-K		04/04/18
10.7	Amendment No. 1 to Seventh Amended and Restated Advisory Agreement dated June 21, 2018		8-K		06/26/18
10.8	Eighth Amended and Restated Advisory Agreement dated April 1, 2019		8-K		04/02/19
10.9	Amendment No. 1 to the Eighth Amended and Restated Advisory Agreement effective September 1, 2019		8-K		09/25/19
10.10	Second Amended and Restated Agreement of Limited Liability Limited Partnership of Sterling Properties, LLLP dated January 1, 2013		8-K		12/27/12
10.11	Third Amended and Restated Agreement of Limited Liability Limited Partnership of Sterling Properties LLLP dated August 1, 2104		8-K		06/24/14
10.12	Dividend Reinvestment Plan dated July 20, 2012		S-3D		07/20/12
10.13	First Amendment to Dividend Reinvestment Plan dated September 26, 2013		8-K		10/02/13
10.14	Second Amendment to Dividend Reinvestment Plan dated December 14, 2016		8-K		12/20/16
10.15	Amended and Restated Dividend Reinvestment Plan dated July 11, 2017		S-3D		07/12/17
10.16	Amendment to Certificate of Limited Liability Partnership of Sterling Properties, LLLP dated August 1, 2014		8-K		06/24/14
10.17	Form of Secured Promissory Note (15-Year Note) dated as of December 19, 2014		8-K		12/23/14
10.18	Form of Secured Promissory Note (10-Year Note) dated as of December 19, 2014		8-K		12/23/14
10.19	Form of Mortgage, Security Agreement and Fixture Filing dated as of December 19, 2014		8-K		12/23/14
10.20	Form of Promissory Note dated as of December 19, 2014		8-K		12/23/14
10.21	Form of Mortgage dated as of December 19, 2014		8-K		12/23/14
10.22	Form of Commercial Security Agreement dated as of December 19, 2014		8-K		12/23/14
10.23	Amended and Restated Sterling Real Estate Trust Independent Trustee Common Shares Plan approved June 18, 2015		8-K		06/23/15
10.24	Form of Promissory Note dated as of August 13, 2015		8-K		08/18/15
10.25	Form of Mortgage, Security Agreement and Fixture Filing dated as of August 13, 2015		8-K		08/18/15
10.26	Amendment No. 1 to Amended and Restated Independent Trustee Stock Plan		8-K		04/04/18
21.1	Subsidiaries of Registrant	X			
23.1	Consent of Independent Registered Public Accounting Firm - Baker Tilly Virchow Krause, LLP	X			
31.1	Section 302 Certification of Chief Executive Officer	X			
31.2	Section 302 Certification of Chief Financial Officer	X			
32.1	Section 906 Certification of Chief Executive Officer and Chief Financial Officer	X			

The following materials from Sterling Real Estate Trust's Annual Report on Form 10-K for the year ended December 31, 2019, formatted in XBRL (eXtensible Business Reporting Language): (i) Consolidated Balance Sheets at December 31, 2019 and 2018; (ii) Consolidated Statements of Operations and Comprehensive Income for years ended December 31, 2019, 2018 and 2017; (iii) Consolidated Statements of Shareholders' Equity for the years ended December 31, 2019, 2018 and 2017; (iv) Consolidated Statements of Cash Flows for the years ended December 31, 2019, 2018 and 2017, and; (v) Notes to Consolidated Financial Statements.

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused the report to be signed on its behalf by the undersigned, thereunto duly authorized.

Dated: March 13, 2020

### STERLING REAL ESTATE TRUST

By: /s/ KENNETH P. REGAN

**Kenneth P. Regan**  
Chief Executive Officer  
(Principal Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<u>/s/ KENNETH P. REGAN</u> (Kenneth P. Regan)	Chief Executive Officer and Trustee (principal executive officer)	March 13, 2020
<u>/s/ Erica J. Chaffee</u> (Erica J. Chaffee)	Chief Financial Officer and Treasurer (principal financial officer)	March 13, 2020
<u>/s/ BRUCE W. FURNESS</u> (Bruce W. Furness)	Chairman of the Board of Trustees	March 13, 2020
<u>/s/ JAMES R. HANSEN</u> (James R. Hansen)	Trustee	March 13, 2020
<u>/s/ TIMOTHY HUNT</u> (Timothy Hunt)	Trustee	March 13, 2020
<u>/s/ TIMOTHY HAUGEN</u> (Timothy Haugen)	Trustee	March 13, 2020
<u>/s/ MICHELLE KORSMO</u> (Michelle Korsmo)	Trustee	March 13, 2020
<u>/s/ RICHARD SAVAGEAU</u> (Richard Savageau)	Trustee	March 13, 2020
<u>/s/ JAMES S. WIELAND</u> (James S. Wieland)	Trustee	March 13, 2020
<u>/s/ LANCE R. WOLF</u> (Lance R. Wolf)	Trustee	March 13, 2020

XBRL-Only Content Section

Element	Value
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dei:CurrentFiscalYearEndDate	--12-31
dei:DocumentFiscalYearFocus	2019
Dei:DocumentFiscalPeriodFocus	FY
dei:AmendmentFlag	true/false







## STERLING MULTIFAMILY TRUST

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1711 Gold Drive South Suite 100, Fargo, ND  
58103  
701-353-2720  
[www.smftrust.com](http://www.smftrust.com)