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

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**FORM 8-K**

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**CURRENT REPORT**

**Pursuant to Section 13 or 15(d) of the  
Securities Exchange Act of 1934**

**Date of report (Date of earliest event reported): December 18, 2009**

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**Paladin Realty Income Properties, Inc.**

**(Exact Name of Registrant as Specified in Charter)**

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**Maryland**  
(State or Other Jurisdiction  
of Incorporation)

**000-51860**  
(Commission  
File Number)

**20-0378980**  
(IRS Employer  
Identification No.)

**10880 Wilshire Blvd., Suite 1400, Los Angeles, California 90024**  
(Address of Principal Executive Offices) (Zip Code)

**Registrant's telephone number, including area code: (310) 996-8704**

**Not applicable**  
(Former Name or Former Address, if Changed Since Last Report)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions (*see* General Instruction A.2. below):

- Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)
  - Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)
  - Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))
  - Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))
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## **Item 8.01. Other Events.**

### **Distributions**

On December 18, 2009, the dividend committee of the board of directors of Paladin Realty Income Properties, Inc. (the “Company”) declared cash distributions for the month of January 2010. The declared distributions will be calculated based on stockholders of record each day during such month at a rate of \$0.0016438 per day and will equal a daily amount that, if paid each day for a 365-day period, would equal a 6.0% annualized rate based on a share price of \$10.00. These distributions will be aggregated and paid in cash on February 15, 2010.

### **Revisions to the Consolidated Financial Statements Filed in the 2008 Annual Report on Form 10-K**

In connection with its expected filing of a post-effective amendment on Form S-11, the Company has adjusted its consolidated financial statements and notes thereto that were previously filed in its 2008 Annual Report on Form 10-K in order to retroactively apply a certain new accounting standard that was adopted on January 1, 2009.

On January 1, 2009, the Company adopted Statement of Financial Accounting Standards No. 160 (“FAS 160”), “Noncontrolling Interests in Consolidated Financial Statements.” FAS 160 requires noncontrolling interests (previously referred to as minority interests) to be reported as a component of total equity, which changes the presentation of the noncontrolling interests in the December 31, 2008 and December 31, 2007 consolidated balance sheets and statements of operations and cash flows for the years ended December 31, 2008, 2007 and 2006, from what was previously reported.

Management does not believe that the adjustment in accordance with FAS 160 has a material effect on the Company’s selected financial data or management’s discussion and analysis of financial condition and results of operations for the year ended December 31, 2008, 2007 and 2006 as previously reported in our 2008 Annual Report on Form 10-K. The Company is not revising its selected financial data or management’s discussion and analysis included in its 2008 Annual Report on Form 10-K given the insignificance of the reclassified and revised amounts.

## **Item 9.01 Financial Statements and Exhibits.**

(d) Exhibits

- 99.1 Report of KPMG LLP
- 99.2 Consolidated Financial Statements and Notes to Consolidated Financial Statements as of December 31, 2008 and 2007 and for the Years Ended December 31, 2008, 2007 and 2006



## **EXHIBIT INDEX**

- 99.1 Report of KPMG LLP
- 99.2 Consolidated Financial Statements and Notes to Consolidated Financial Statements as of December 31, 2008 and 2007 and for the Years Ended December 31, 2008, 2007 and 2006

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders  
Paladin Realty Income Properties, Inc.:

We have audited the accompanying consolidated balance sheets of Paladin Realty Income Properties, Inc. and subsidiaries (the Company) as of December 31, 2008 and 2007, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2008. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Paladin Realty Income Properties, Inc. and subsidiaries as of December 31, 2008 and 2007, and the results of their operations, and their cash flows for each of the years in the three-year period ended December 31, 2008, in conformity with U.S. generally accepted accounting principles.

As discussed in note 2 to the consolidated financial statements, the Company has retrospectively applied certain adjustments upon the adoption of an accounting standard related to non-controlling interests.

/s/ KPMG LLP

New York, NY  
March 27, 2009, except for note 2, which is as of December 21, 2009

**PALADIN REALTY INCOME PROPERTIES, INC.**

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**PALADIN REALTY INCOME PROPERTIES, INC. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
**As of December 31, 2008 and 2007**

	<u>2008</u>	<u>2007</u>
<b>ASSETS</b>		
<b>Real Estate:</b>		
Building and improvements	\$ 98,923,969	\$49,726,454
Land	27,320,704	6,131,578
Furniture, fixtures and equipment	3,446,784	1,136,256
In-place leases	1,099,508	1,069,508
Tenant Improvements	17,888	—
	<u>130,808,853</u>	<u>58,063,796</u>
Less: Accumulated depreciation and amortization	(5,062,339)	(2,300,170)
Total real estate, net	125,746,514	55,763,626
Investment in real estate joint venture	1,613,889	1,666,265
Cash and cash equivalents	2,145,506	4,230,937
Restricted Cash	5,024,035	1,328,202
Prepaid insurance and other assets, net	1,536,375	639,417
Due from affiliates	—	926,416
<b>TOTAL ASSETS</b>	<u>\$136,066,319</u>	<u>\$64,554,863</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Mortgages payable	\$ 98,729,308	\$43,879,125
Due to affiliates	832,954	—
Unaccepted subscriptions for common shares	184,500	210,210
Accrued expenses and other liabilities	3,112,268	907,333
Distributions payable	376,626	263,426
Total liabilities	<u>103,235,656</u>	<u>45,260,094</u>
<b>Equity:</b>		
Company's Stockholders' Equity:		
Preferred shares, \$0.01 par value, 100,000,000 shares authorized; none issued or outstanding	—	—
Common shares, \$0.01 par value, 750,000,000 shares authorized; 3,687,656 shares and 2,605,486 shares issued and outstanding, respectively	36,876	26,055
Additional paid-in-capital	32,663,242	22,863,824
Treasury shares, at cost – 30,488 shares and 2,537 shares, respectively	(283,279)	(23,568)
Accumulated deficit and distributions	(7,869,801)	(3,519,900)
Total Company's Stockholders' Equity	<u>24,547,038</u>	<u>19,346,411</u>
Noncontrolling interests	8,283,625	(51,642)
Total Equity	<u>32,830,663</u>	<u>19,294,769</u>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<u>\$136,066,319</u>	<u>\$64,554,863</u>

See notes to consolidated financial statements

**PALADIN REALTY INCOME PROPERTIES, INC. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF OPERATIONS**

**For the years ended December 31, 2008, 2007 and 2006**

	<u>2008</u>	<u>2007</u>	<u>2006</u>
<b>Revenues</b>			
Rental Income	\$10,564,798	\$ 5,072,207	\$1,417,679
Other Income	921,225	416,793	92,999
Interest Income	103,788	106,622	19,824
<b>Total Revenues</b>	<u>11,589,811</u>	<u>5,595,622</u>	<u>1,530,502</u>
<b>Expenses</b>			
Property operating	4,332,542	1,732,394	492,297
Real property taxes	878,813	419,129	78,391
General and administrative	1,873,251	1,036,478	386,249
Interest expense, including amortization of deferred loan costs	4,430,622	2,357,226	812,489
Depreciation and amortization	2,764,030	1,678,196	616,887
<b>Total Expenses</b>	<u>14,279,258</u>	<u>7,223,423</u>	<u>2,386,313</u>
<b>Loss before equity in earnings and noncontrolling interests</b>	<u>(2,689,447)</u>	<u>(1,627,801)</u>	<u>(855,811)</u>
Equity in earnings from real estate joint venture	88,224	83,896	75,226
<b>Net Loss</b>	<u>(2,601,223)</u>	<u>(1,543,905)</u>	<u>(780,585)</u>
Noncontrolling interests	242,673	219,437	127,817
<b>Net loss attributable to Company</b>	<u>\$ (2,358,550)</u>	<u>\$ (1,324,468)</u>	<u>\$ (625,768)</u>
<b>Net Loss per common share</b>			
Basic	<u>\$ (0.73)</u>	<u>\$ (0.75)</u>	<u>\$ (1.42)</u>
Diluted	<u>\$ (0.73)</u>	<u>\$ (0.75)</u>	<u>\$ (1.42)</u>
<b>Weighted average number of common shares outstanding</b>			
Basic	<u>3,219,095</u>	<u>1,758,564</u>	<u>458,658</u>
Diluted	<u>3,219,095</u>	<u>1,758,564</u>	<u>458,658</u>

See notes to consolidated financial statements

**PALADIN REALTY INCOME PROPERTIES, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**  
For the years ended December 31, 2008, 2007 and 2006

	Company Stockholders						
	Common Shares		Treasury Shares	Additional Paid-in Capital	Accumulated Deficit and Dividends	Noncontrolling Interest	Total Equity
	Common shares	Amount	Amount				
<b>BALANCE, December 31, 2005</b>	173,527	\$ 1,735	\$ —	\$ 1,566,911	\$ (79,180)	\$ 192,800	\$ 1,682,266
Issuance of common shares	626,707	6,274	—	6,250,810	—	—	6,257,084
Selling commissions and dealer manager fees	—	—	—	(595,579)	—	—	(595,579)
Offering costs	—	—	—	(192,986)	—	—	(192,986)
Distributions	—	—	—	—	—	(9,960)	(9,960)
Issuance of common shares to directors	12,000	120	—	(120)	—	—	—
Share-based compensation expense	—	—	—	43,178	—	—	43,178
Dividends declared	—	—	—	—	(312,878)	—	(312,878)
Shares issued pursuant to Distribution Reinvestment Plan	18,311	176	—	175,604	—	—	175,780
Net Loss	—	—	—	—	(652,768)	(127,817)	(780,585)
<b>BALANCE, December 31, 2006</b>	<b>830,545</b>	<b>8,305</b>	<b>—</b>	<b>7,247,818</b>	<b>(1,044,826)</b>	<b>55,023</b>	<b>6,266,320</b>
Issuance of common shares	1,714,525	17,148	—	17,088,989	—	—	17,106,137
Treasury share purchased	(2,537)	(25)	(23,568)	—	—	—	(23,593)
Selling commissions and dealer manager fees	—	—	—	(1,604,634)	—	—	(1,604,634)
Offering costs	—	—	—	(534,637)	—	—	(534,637)
Contributions	—	—	—	—	—	129,574	129,574

Distributions	—	—	—	—	—	(16,802)	(16,802)
Share-based compensation expense	—	—	—	40,000	—	—	40,000
Dividends declared	—	—	—	—	(1,150,606)	—	(1,150,606)
Shares issued pursuant to							
Distribution Reinvestment Plan	62,953	627	—	626,288	—	—	626,915
Net Loss	—	—	—	—	(1,324,468)	(219,437)	(1,543,905)
<b>BALANCE, December 31, 2007</b>	<u>2,605,486</u>	<u>26,055</u>	<u>(23,568)</u>	<u>22,863,824</u>	<u>(3,519,900)</u>	<u>(51,642)</u>	<u>19,294,769</u>
Issuance of common shares	994,881	9,949	—	9,912,818	—	—	9,922,767
Treasury share purchased	(27,951)	(280)	(259,711)	—	—	—	(259,991)
Selling commissions and dealer							
manager fees	—	—	—	(943,952)	—	—	(943,952)
Offering costs	—	—	—	(329,620)	—	—	(329,620)
Contributions	—	—	—	—	—	8,826,659	8,826,659
Distributions	—	—	—	—	—	(248,719)	(248,719)
Share-based compensation expense	—	—	—	36,822	—	—	36,822
Dividends declared	—	—	—	—	(1,991,351)	—	(1,991,351)
Shares issued pursuant to							
Distribution Reinvestment Plan	115,240	1,152	—	1,123,350	—	—	1,124,502
Net Loss	—	—	—	—	(2,358,550)	(242,673)	(2,601,223)
<b>BALANCE, December 31, 2008</b>	<u>3,687,656</u>	<u>\$36,876</u>	<u>\$(283,279)</u>	<u>\$32,663,242</u>	<u>\$(7,869,801)</u>	<u>\$8,283,625</u>	<u>\$32,830,663</u>

See notes to consolidated financial statements.

**PALADIN REALTY INCOME PROPERTIES, INC. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

**For the years ended December 31, 2008, 2007 and 2006**

	<u>2008</u>	<u>2007</u>	<u>2006</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net Loss	\$ (2,601,223)	\$ (1,543,905)	\$ (780,585)
Adjustments to reconcile net loss to net cash provided by operating activities			
Equity in earnings from real estate joint venture	(88,224)	(83,896)	(75,226)
Distributions from real estate joint venture	88,224	83,896	75,226
Depreciation and amortization expense	2,764,030	1,678,196	616,887
Amortization of deferred loan costs	77,995	83,664	20,606
Amortization of deferred compensation	36,822	40,000	43,178
Changes in operating assets and liabilities:			
Increase in restricted cash	(245,763)	(98,445)	(289,797)
Increase in prepaid insurance and other assets	(147,871)	(68,815)	(93,007)
Increase in due to affiliates	890,393	15,727	90,117
Increase in accrued expenses and other liabilities	550,245	118,959	783,889
Net cash provided by operating activities	<u>1,324,628</u>	<u>225,381</u>	<u>391,288</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Expenditures for real estate and improvements	(67,145,384)	(11,581,949)	(24,699,123)
Increase in restricted cash	(3,475,780)	(179,750)	—
Decrease in due to affiliates	—	(578,498)	—
Investment in real estate joint venture	—	—	(40,794)
Distributions from real estate joint venture in excess of equity in earnings	52,376	82,604	89,665
Net cash used in investing activities	<u>(70,568,788)</u>	<u>(12,257,593)</u>	<u>(24,650,252)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Borrowings from mortgages payable	50,667,612	6,250,000	16,350,000
Payments on mortgage payable	(67,429)	(16,638)	—
Borrowings from notes payable to affiliate	—	—	6,200,000
Payments on notes payable to affiliate	—	(3,800,000)	(2,400,000)
Deferred loan costs	(522,935)	(94,833)	(470,500)
Decrease (increase) in restricted cash	25,710	(738,210)	28,000
Proceeds from issuance of common shares	9,922,767	17,106,137	6,257,084
Treasury shares purchased	(259,991)	(23,593)	—
(Decrease) increase in unaccepted subscriptions for common stock	(25,710)	188,210	(28,000)
Selling commissions and dealer manager fees	(943,952)	(1,604,634)	(595,579)
Offering costs	(329,620)	(534,637)	(95,000)
Decrease (increase) in due from affiliates	868,977	(1,217,400)	—
Distributions paid	(753,653)	(343,022)	(71,981)
Contributions from noncontrolling interests	8,826,659	129,574	—
Distributions to noncontrolling interests	(249,706)	(14,036)	(9,960)
Net cash provided by financing activities	<u>67,158,729</u>	<u>15,286,918</u>	<u>25,164,064</u>
Net (decrease) increase in cash and cash equivalents	(2,085,431)	3,254,706	905,100
Cash and cash equivalents – beginning of year	4,230,937	976,231	71,131
Cash and cash equivalents – end of year	<u>\$ 2,145,506</u>	<u>\$ 4,230,937</u>	<u>\$ 976,231</u>

	2008	2007	2006
<b>Supplemental disclosure of non-cash investing and Financing activities</b>			
Mortgage loan assumed in connection with purchase of real estate	\$4,250,000	\$4,795,763	\$16,500,000
Acquisition fees due to affiliate	\$ —	\$ —	\$ 484,506
Offering costs due to affiliate	\$ —	\$ —	\$ 97,986
Expenditures for real estate and improvements accrued but unpaid	\$1,654,690	\$ —	\$ —
Distributions payable	\$ 376,626	\$ 263,426	\$ 82,756
Common stockholders distributions reinvested in accordance with Distribution Reinvestment Plan	\$1,124,502	\$ 626,915	\$ 175,780
Issuance of common stock for compensation plan	\$ —	\$ —	\$ 120,000
<b>Supplemental disclosure of cash flow information</b>			
Cash paid during the year for interest	\$4,119,045	\$2,245,569	\$ 592,483

**See notes to consolidated financial statements**

## **Paladin Realty Income Properties, Inc. and Subsidiaries**

### **Notes to Consolidated Financial Statements**

**December 31, 2008, 2007 and 2006**

#### **1. Organization**

Paladin Realty Income Properties, Inc., a Maryland corporation (“Paladin REIT” or the “Company”), was formed on October 31, 2003 to invest in a diversified portfolio of high quality investments, including investments in real properties and real estate related investments, focusing primarily on investments that produce current income. Paladin REIT owns interests in nine joint ventures that own ten income-producing properties as of December 31, 2008, consisting of 801 Fiber Optic Drive, a 56,336 square foot distribution facility built in 2001 that is 100% leased to FedEx Ground Package System, Inc., a subsidiary of FedEx Corporation; Champion Farms Apartments, a 264-unit luxury multifamily rental community built in 2000; Fieldstone Apartments, a 266-unit multifamily rental community property built in 2001; Pinehurst Apartment Homes, a 146-unit multifamily rental community built in two phases in 1986 and 1988; Pheasant Run Apartments, a 160-unit multifamily rental community built in 1985; Retreat Apartments, a 342-unit multifamily rental community built in 1984; Hilltop Apartments, a 124-unit multifamily rental community built in 1986; Conifer Crossing, a 420-unit multifamily rental community built in 1981; and Two and Five Governor Park, which includes a two-story Class B office building with 22,470 rentable square feet and a three-story Class B+ office building with 53,048 rentable square feet. Paladin REIT intends to invest in a variety of real estate product types, including apartments, office buildings, industrial buildings, shopping centers and hotels. Paladin REIT may also make real estate related investments, which include loans on real property such as first mortgage loans and mezzanine loans. Paladin REIT elected to be taxed as a REIT for U.S. federal income tax purposes beginning with the taxable year ended December 31, 2006. Subject to certain restrictions and limitations, the business of Paladin REIT is managed by Paladin Realty Advisors, LLC (“Paladin Advisors”), an affiliate of Paladin REIT, pursuant to an amended and restated advisory agreement, dated as of July 18, 2008 (the “Advisory Agreement”). Paladin Advisors supervises and manages the day-to-day operations of Paladin REIT and selects the real property investments and real estate related investments it makes, subject to oversight by the board of directors of Paladin REIT. Paladin Advisors also provides marketing, sales and client services on behalf of Paladin REIT.

On February 23, 2005, Paladin REIT’s initial public offering (the “Initial Offering”) was declared effective and Paladin REIT commenced its offering efforts. The Initial Offering terminated on July 28, 2008 in connection with the commencement of Paladin REIT’s follow-on offering (the “Follow-On Offering” and collectively with the Initial Offering, the “Offerings”) on July 28, 2008. As of December 31, 2008 Paladin REIT had received proceeds of \$36,917,400 for 3,705,644 shares in the Offerings.

Paladin REIT owns its assets and conducts its operations through Paladin Realty Income Properties, L.P., its operating partnership (“Paladin OP”). As of December 31, 2008 and 2007, Paladin Advisors held a 0.5% and 0.8% limited partnership interest, respectively, and Paladin REIT held a 99.5% and 99.2% general partnership interest, respectively, in Paladin OP. Management expects Paladin REIT’s ownership percentage in Paladin OP to continue to increase as Paladin REIT invests net proceeds from the Offerings in Paladin OP.

#### **2. Summary of Significant Accounting Policies**

##### ***Basis of Presentation***

The consolidated financial statements include the accounts of Paladin REIT and its wholly-owned and controlled entities (collectively, the “Company”). In accordance with the Financial Accounting Standards Board (“FASB”) Interpretation No. 46(R), “Consolidation of Variable Interest Entities” (“FIN 46R”), the Company also consolidates any variable interest entities (“VIEs”) of which it is the primary beneficiary as defined. When the Company does not have a controlling interest in an entity but exerts a significant influence over the entity, the Company applies the equity method of accounting. All intercompany balances and transactions have been eliminated in consolidation.

##### ***Noncontrolling Interest***

In December 2007, the FASB issued Statement of Financial Accounting Standards (“SFAS”) No. 160, “Noncontrolling Interests in Consolidated Financial Statements” (“FAS 160”), effective for fiscal years beginning on or after December 15, 2008. FAS 160 establishes requirements for ownership interests in subsidiaries held by parties other than the Company (previously referred to as a minority interest). Noncontrolling interest is presented and disclosed as a separate component of equity (not as a liability or other item outside of permanent equity). Consolidated net income includes the noncontrolling interest’s share of income. The calculation of earnings per share continues to be based on income amounts attributable to the parent. All changes in the parent’s ownership interest in a subsidiary are accounted for as equity transactions if the parent retains its controlling financial interest in the

subsidiary.

The Company has adopted FAS 160 effective January 1, 2009. As a result, the financial statements included in Exhibit 99.2 of this Form 8-K have been revised to give effect to the adoption of FAS 160 for all periods presented. The Company's noncontrolling interests are comprised of the ownership interests of the noncontrolling interests in joint ventures controlled by the Company through ownership or contractual arrangements. Balances attributable to these noncontrolling interests, including amounts previously included in Prepaid Insurance and Other Assets, were reclassified to become a separate component of equity as of all dates presented. Also, consolidated net income was reclassified to include the amounts attributable to the noncontrolling interests. These noncontrolling interests reported in equity are not subject to any mandatory redemption requirements or other redemption features outside of the Company's control that would result in presentation outside of permanent equity.

### ***Real Estate and Depreciation***

Real estate is stated at cost, less accumulated depreciation. The Company allocates the cost of newly acquired properties between net tangible and identifiable intangible assets. The primary intangible asset associated with an apartment or office building property acquisition is the value of the existing lease agreements. When allocating cost to an acquired property, the Company allocates costs to the estimated value of the land, building and fixtures assuming the property is vacant and to the estimated intangible value of the existing lease agreements. The Company estimates the intangible value of the lease agreements by determining the lost revenue associated with a hypothetical lease-up. The Company depreciates the buildings and fixtures based on the expected useful life of the asset, which ranges from 27 to 45 years for the buildings and improvements and from five to seven years for furniture, fixtures and equipment. The intangible value of the lease agreements is amortized over the average remaining life of the existing leases, which ranges from three to 24 months. This amortization is included in depreciation and amortization expense on the accompanying consolidated statements of operations. Improvements and betterments are capitalized when they extend the useful life of the asset. Expenditures for repairs and maintenance are expensed as incurred.

The Company reviews long-lived assets and related identifiable intangibles for impairment whenever events or changes in circumstances indicate the carrying amount of the assets may not be recoverable. When such events or changes in circumstances occur, recoverability of the asset to be held and used is measured by a comparison of the carrying amount of the asset to future cash flows, undiscounted and without interest, expected to be generated by the asset. If the sum of the expected future cash flows (undiscounted and without interest) is less than the Company's carrying amount for the asset, an impairment loss is recognized based upon the asset's fair value.

### ***Investments***

The Company follows the provisions of FIN 46R and the Company is required to evaluate whether it has a controlling financial interest in an entity through means other than voting rights. If the Company determines that the joint venture is a "variable interest entity" ("VIE") and that the Company is the "primary beneficiary" as defined in FIN 46R, it will account for such investment as if it were a consolidated subsidiary. For a joint venture investment which is not a VIE, the Company considers other relevant accounting literature including Accounting Principles Board Opinion 18 — "The Equity Method of Accounting for Investments in Common Stock," Statement of Position ("SOP") 78-9 — "Accounting for Investments in Real Estate Ventures," and Emerging Issues Task Force Issue ("EITF") 04-5 — "Determining whether a General Partner or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights" to determine the method of accounting for each of the partially-owned entities. In accordance with the above pronouncements, the Company determines whether it should consolidate the entity or account for it on the equity method or cost method. Factors considered in determining whether or not the Company exercises control include substantive participating rights of partners on significant business decisions, including dispositions and acquisitions of assets, financing and operating and capital budgets, board and management representatives and authority and other contractual rights of the Company's partners. To the extent that the Company is deemed to control these entities, these entities will be consolidated.

As of December 31, 2008, Paladin OP held a 70% ownership interest in Springhurst Housing Partners, LLC ("Springhurst"), an 83% ownership interest in Glenwood Housing Partners I, LLC ("Glenwood"), a 97.5% ownership interest in KC Pinehurst Associates, LLC ("KC Pinehurst"), a 97.5% ownership interest in KC Pheasant Associates, LLC ("KC Pheasant"), a 97.5% interest in KC Retreat Associates, LLC ("KC Retreat"), a 49% interest in Park Hill Partners I, LLC ("Park Hill Partners"), a 42.5% ownership interest in FPA/PRIP Conifer, LLC ("FPA/PRIP Conifer"), a 47.65% ownership interest in FPA/PRIP Governor Park, LLC ("FPA/PRIP Governor Park") and a 74% ownership interest in PRIP 801, LLC, as described in Note 3. Paladin REIT has determined that Paladin OP and the entities in which it has invested are not VIEs. Paladin REIT consolidates Paladin OP, Springhurst, Glenwood, KC Pinehurst, KC Pheasant, and KC Retreat, as it is the

majority owner and exercises control over all significant decisions. Paladin REIT also consolidates Park Hill Partners, FPA/PRIP Conifer and FPA/PRIP Governor Park because it holds a significant ownership interest and exercises control over all significant decisions. Paladin REIT accounts for its investment in PRIP 801, LLC, under the equity method of accounting, as the other member has substantive participating rights as defined in EITF 04-5 and SOP 78-9. This investment is recorded initially at cost, and subsequently adjusted for equity in earnings or losses and cash contributions and distributions. Distributions received up to the amount of earnings are considered as distributions from operations and any excess amount of distributions are considered a return of capital.

On a periodic basis the Company will evaluate whether there are any indicators that the value of its investments in partially-owned entities accounted for by the equity method are impaired. An investment is impaired if the Company's estimate of the value of the investment is less than the carrying amount. The ultimate realization of the Company's investment in partially-owned entities is dependent on a number of factors including the performance of that entity and market conditions. If the Company determines that a decline in the value of a partially-owned entity is other than temporary, then the Company would record an impairment charge.

#### ***Deferred Loan Costs***

Loan costs are capitalized and amortized using the effective interest method over the life of the related loan. The amortization is recorded as a component of interest expense.

#### ***Revenue Recognition***

The Company primarily leases residential apartments to tenants under non-cancellable operating leases with terms ranging from three to 24 months. The Company also leases commercial space to tenants with lease terms extending to 2013. Rental income related to leases is recognized in the period earned over the lease term in accordance with SFAS No. 13, "Accounting for Leases."

Other income consists of various tenant-related charges and is recognized as revenue in the period in which the applicable charge is incurred.

#### ***Accounts Receivable***

Accounts receivable is included in prepaid insurance and other assets, net in the consolidated balance sheets. Bad debts are recorded under the specific identification method, whereby, uncollectible receivables are directly written off when identified.

#### ***Use of Estimates***

The presentation of the consolidated financial statements in accordance with U.S. generally accepted accounting principles requires management to make estimates and assumptions relating to the reported amount of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the period. Significant items subject to such estimates and assumptions include the carrying amount of the property, plant and equipment, and valuation allowances for receivables. Actual results could differ from those estimates.

#### ***Cash Equivalents***

Cash equivalents represent highly liquid investments with maturities at the date of purchase of three months or less.

#### ***Restricted Cash***

Restricted cash includes subscription proceeds that are held in escrow until investors are admitted as stockholders. Upon acceptance of stockholders, shares of stock are issued, and Paladin REIT receives the subscription proceeds. Restricted cash included \$184,500 and \$210,210 as of December 31, 2008 and 2007, respectively, for subscription proceeds that were held in escrow. At December 31, 2008 and 2007, restricted cash also included \$4,289,535 and \$567,992 held in restricted accounts for building and tenant improvements, repairs, property taxes and insurance as required by lenders. At December 31, 2008 and 2007, restricted cash also included \$550,000 held in a restricted account as collateral for a letter of credit as described in Note 3.

#### ***Income Taxes***

The Company elected to be taxed as a REIT for U.S. federal income tax purposes beginning with the taxable year

ended December 31, 2006, under Sections 856 through 860 of the Internal Revenue Code of 1986, as amended. The Company believes it operates in such a manner as to qualify for treatment as a REIT for federal income tax purposes. Accordingly, the Company generally will not be subject to federal income tax, provided that distributions to its stockholders equal at least the amount of its taxable income. If the Company fails to qualify as a REIT in any taxable year without the benefit of certain relief provisions, it will be subject to federal and state income taxes on its taxable income at regular corporate income tax rates. Even if the Company qualifies for taxation as a REIT, the Company may be subject to certain state or local taxes on its income, property or net worth and federal income and excise taxes on its undistributed income. No provision has been made for federal income taxes for the years ended December 31, 2008, 2007 and 2006 in the accompanying consolidated financial statements.

In July 2006, the FASB issued Interpretation No. 48 (“FIN 48”), “Accounting for Uncertainty in Income Taxes — An Interpretation of FASB Statement No. 109.” FIN 48 increases the relevancy and comparability of financial reporting by clarifying the way companies account for uncertainty in measuring income taxes. FIN 48 prescribes a comprehensive model for how a company should recognize, measure, present, and disclose in its financial statements uncertain tax positions that the company has taken or expects to take on a tax return. FIN 48 only allows a favorable tax position to be included in the calculation of tax liabilities and expenses if a company concludes that it is more likely than not that its adopted tax position will be sustained. The Company adopted FIN 48 as required effective January 1, 2007. The adoption of FIN 48 did not have a material impact on its consolidated financial position, results of operations and cash flows. All of the Company’s tax years are subject to examination by tax jurisdictions.

In accordance with FIN 48, the Company has assessed its tax positions for all open tax years as of January 1, 2007 and concluded that there were no material FIN 48 uncertainties to be recognized. The Company’s accounting policy with respect to interest and penalties related to tax uncertainties is to classify these amounts as provision for income taxes. The Company has not recognized any interest and penalties related to tax uncertainties for the years ended December 31, 2008, 2007 and 2006.

### ***Organization and Offering Costs***

Organization costs are expensed as incurred and offering costs are charged to stockholders’ equity. These costs are subject to a 3.0% limitation of the gross proceeds from the Offerings pursuant to the Company’s Advisory Agreement with Paladin Advisors, as described in Note 6.

### ***Expense Reimbursement***

Pursuant to the Advisory Agreement, Paladin Advisors is entitled to reimbursement of actual expenses incurred for administrative and other services provided to the Company by Paladin Advisors and its affiliates, including reimbursement of personnel costs and overhead for which they do not otherwise receive a fee. The Company will not reimburse Paladin Advisors for operating expenses that in the fiscal year then ended exceed the greater of (1) 2% of the average invested assets of Paladin REIT or (2) 25% of the net income as described below of the Company (the “2%/25% Rule”), and Paladin Advisors must reimburse Paladin REIT quarterly for any amounts by which the operating expenses of Paladin REIT exceeds the 2%/25% Rule in the previous four consecutive fiscal quarters (the “Expense Period”).

The average invested assets of the Company for any period are equal to the average book value of the Company’s assets invested in equity interests in, and loans secured by, real estate before reserves for depreciation or bad debts or other similar non-cash reserves computed by taking the average of such values at the end of each month during the period. The net income of the Company for any period is equal to the Company’s total revenue less total expenses other than additions to reserves for depreciation, bad debts or other similar non-cash reserves for such period. Operating expenses include all expenses incurred by the Company under U.S. generally accepted accounting principles (including the asset management fee), but excluding organization and offering expenses, interest payments, taxes, non-cash expenditures such as depreciation, amortization and bad debt reserves, the subordinated disposition fee, acquisition fees and expenses and distributions pursuant to Paladin Advisors’ subordinated participation interest in Paladin OP.

Paladin Advisors must reimburse the excess expenses to the Company within 60 days after the end of each fiscal quarter unless the independent directors determine that the excess expenses were justified based on unusual and nonrecurring factors which they deem sufficient. Within 60 days after the end of any Expense Period for which total operating expenses exceed the 2%/25% Rule, Paladin REIT will send its stockholders a written disclosure, together with an explanation of the factors the independent directors considered in arriving at the conclusion that the excess expenses were justified. However, at Paladin Advisors’ option, Paladin Advisors or its affiliate, as applicable may defer the reimbursement of expenses and elect to receive such payments, without interest, in any subsequent fiscal year that Paladin Advisors designates.

### ***Per Share Data***

The Company presents both basic and diluted loss per share, or EPS. Basic EPS excludes potentially dilutive securities and is computed by dividing net loss available to common stockholders by the weighted average number of common shares outstanding during the period. Dilutive EPS reflects the potential dilution that could occur if securities or other contracts to issue common shares were exercised, where such exercise would result in a lower EPS amount. The diluted EPS would include weighted average unvested restricted shares issued to independent directors totaling 0, 4,000 and 8,000 shares for the years ended December 31, 2008, 2007 and 2006, respectively, but are excluded from the calculation as their effect would be antidilutive. All shares have fully vested as of December 2, 2008.

### ***Unaccepted Subscriptions for Common Shares***

Unaccepted subscriptions for shares of our common stock include proceeds related to subscriptions that were held in escrow but had not been accepted by the Company as of December 31, 2008 and 2007.

### ***Fair Value of Financial Instruments***

The fair values of the Company's cash and cash equivalents, restricted cash, other assets, distributions payable and other liabilities approximate the carrying values due to the short-term nature of these financial instruments. As of December 31, 2008, the mortgage loans payable had an estimated fair value of approximately \$97.9 million compared to the carrying value of \$98.7 million. As of December 31, 2007, the mortgage loans payable had an estimated fair value of approximately \$44.1 million compared to the carrying value of \$43.9 million. To determine fair value, the fixed rate debt is discounted at a rate based on an estimate of current lending rates as of December 31, 2008 and 2007.

### ***Stock-based Compensation***

Under the terms of the Independent Director Incentive Stock Plan, the Company granted 3,000 shares at fair value of \$10 of restricted common stock to each of the four independent directors on June 30, 2006. One-third of the restricted common stock vested on each of the first three anniversaries of December 2, 2005, the date the Company reached its minimum offering. There are 60,000 shares in total authorized under the Independent Director Incentive Stock Plan, which expires on February 28, 2015.

The Company records compensation expense for restricted common stock as required by SFAS No. 123(R), "Share-Based Payment, revised 2004." Compensation expense for common stock unvested at March 21, 2006 was based on the grant date fair value of the common shares calculated under SFAS No. 123(R) and was recognized using the straight-line attribution method, assuming no forfeitures. For the years ended December 31, 2008 and 2007, the Company recorded \$36,822 and \$40,000, respectively, of related compensation expense which amounts are included in general and administrative expenses in the accompanying consolidated statements of operations. Total unamortized compensation costs on non-vested shares at December 31, 2008 and 2007 is \$0 and \$36,822, respectively.

As of December 31, 2008, all 12,000 shares have vested. There have been no forfeitures as of December 31, 2008. As of December 31, 2007, 8,000 shares have vested. There were 4,000 shares unvested and there were no forfeitures as of December 31, 2007.

### ***Reportable Segments***

SFAS No. 131, "Disclosures About Segments of Enterprise and Related Information," establishes standards for reporting financial and descriptive information about an enterprise's reportable segments. Management has determined that the Company has one reportable segment, which owns interests in real estate investments.

### ***Environmental Matters***

Under various federal, state and local environmental laws, statutes, ordinances, rules and regulations, an owner of real property may be liable for the costs of removal or remediation of certain hazardous or toxic substances at, on, in or under such property as well as certain other potential costs relating to hazardous or toxic substances. These liabilities may include government fines and penalties and damages for injuries to persons and adjacent property. Such laws often impose liability without regard to whether the owner knew of, or was responsible for, the presence of or disposal of such substances. As of December 31, 2008, the Company is not aware of any environmental matter that could have a material impact on the consolidated financial statements.

### ***Reclassifications***

Certain amounts in the prior year consolidated financial statements have been reclassified in order to conform to the current year presentation.

### ***Risk and Uncertainties***

The Company and the properties in which it has an interest are operating in a challenging and uncertain economic environment. Financial and real estate companies continue to be affected by the lack of liquidity in financial markets, declines in real estate values and the reduction in the willingness of financial institutions to make new loans and refinance or extend existing loans on the same terms and conditions. Should the market conditions continue to deteriorate, there is no assurance that such conditions will not result in decreased property value, or cash flows, or impact the ability to repay, refinance or extend the Company's mortgages payable.

### ***Recent Accounting Pronouncements***

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" which defines fair value, establishes a framework for measuring fair value and expands the related disclosure requirements. This statement was effective for fiscal years beginning after November 15, 2007 and for interim periods within those years. The Company's adoption of SFAS No. 157, as of January 1, 2008, did not have a material impact on its consolidated financial position, results of operations or cash flows. FASB Staff Position ("FSP") FAS 157-2, "Effective Date of FASB Statement No. 157," delays the effective date of SFAS No. 157 until fiscal years beginning after November 15, 2008 for all nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. In accordance with FSP FAS 157-2, the Company has not applied the provisions of SFAS No. 157 to the initial measurement of intangible assets acquired in business combinations during the year ended December 31, 2008.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities—Including an amendment of FASB Statement No. 115." The fair value option established by SFAS No. 159 permits all entities to choose to measure eligible items at fair value at specified election dates. A business entity will report unrealized gains and losses on items for which the fair value option has been elected in earnings (or another performance indicator if the business entity does not report earnings) at each subsequent reporting date. This statement was effective for fiscal years beginning after November 15, 2007 and for interim periods within those years. The Company has adopted SFAS No. 159 effective January 1, 2008 and has elected not to measure any of our current eligible financial assets or liabilities at fair value upon adoption. However, the Company does reserve the right to elect to measure future eligible financial assets or liabilities at fair value.

In September 2007, the FASB ratified Emerging Issues Task Force ("EITF") Issue 07-6, "Accounting for the Sale of Real Estate Subject to the Requirements of FASB Statement No. 66 When the Agreement Includes a Buy-Sell Clause," which clarifies that a buy-sell clause, in and of itself, does not constitute a prohibited form of continuing involvement that would preclude partial sale treatment under Statement 66. EITF 07-6 applies prospectively to new arrangements entered into in fiscal years beginning after December 15, 2007. The adoption of EITF 07-6 on January 1, 2008 did not have a material impact on the Company's consolidated financial position, results of operations and cash flows.

In December 2007, the FASB issued SFAS No. 141R, "Business Combinations" which requires most identifiable assets, liabilities, noncontrolling interests and goodwill acquired in a business combination to be recorded at full fair value. Under SFAS No. 141R, all business combinations will be accounted for by applying the acquisition method. SFAS No. 141R is effective for the periods beginning on or after December 15, 2008. Earlier application is prohibited and will be applied to business combinations occurring after the effective date. The adoption of SFAS No. 141R could materially impact the Company's future financial results to the extent that the Company acquires significant amounts of real estate, as related acquisition costs will be expensed as incurred compared to the current practice of capitalizing such costs and amortizing them over the estimated useful life of the assets acquired.

On November 13, 2008, the FASB ratified EITF consensus on EITF Issue No. 08-06, "Equity Method Investment Accounting Considerations" ("EITF 08-06"). EITF 08-06 addresses questions about the potential effect of FASB Statement No. 141R, Business Combinations, and FASB Statement No. 160, Noncontrolling Interests in Consolidated Financial Statements—an amendment of ARB No. 51, on equity-method accounting under Accounting Principles Board ("APB 18"). EITF 08-06 generally continues existing practices under APB 18 including the use of a cost-accumulation approach to initial measurement of the investment. EITF 08-06 does not require the investor to perform a separate impairment test on the underlying assets of an equity method investment. However, an equity-method investor is required to recognize its proportionate share of impairment charges recognized by the investee, adjusted for basis differences, if any, between the investee's carrying amount for the impaired assets and the cost allocated to such assets by the investor. The investor is also required to perform an overall other than temporary impairment test of its investment in accordance with APB 18. EITF 08-06

is effective for fiscal years beginning on or after December 15, 2008 and interim periods within those fiscal years and shall be applied prospectively. The Company is currently evaluating the impact of adopting this pronouncement on its consolidated financial position, results of operations and cash flows.

On December 11, 2008, the FASB issued FSP FAS 140-4 and FIN 46(R)-8, Disclosures about Transfers of Financial Assets and Interests in Variable Interest Entities (“FSP FAS 140-4 and FIN 46R-8”). This FSP includes disclosure objectives and requires public entities to provide additional year-end and interim disclosures about transferors, sponsors, servicers, primary beneficiaries, and holders of significant variable interests in a variable-interest entity or qualifying special purpose entity. FSP FAS 140-4 and FIN 46R-8 is effective for the first interim period or fiscal year ending after December 15, 2008. The Company does not believe that the adoption of FSP FAS 140-4 and FIN 46R-8 will have an impact on the Company’s financial statements as the Company does not have significant variable interests.

### **3. Investments**

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

##### *Retreat Apartments*

On January 14, 2008, a wholly-owned subsidiary of Paladin OP, PRIP 11128, LLC purchased a 97.5% interest in KC Retreat, a joint venture between PRIP 11128, LLC, JTL Holdings, LLC and JTL Asset Management, Inc., which owns the Retreat Apartments. The Retreat Apartments is a 342-unit multifamily rental community built in 1984. The apartment complex is located in Shawnee, Kansas. The total purchase price of Retreat Apartments was \$15.9 million, plus closing costs of \$200,000 and approximately \$350,000 for capital expenditures. KC Retreat secured a mortgage loan of \$13.6 million to finance the acquisition. Paladin OP’s investment in KC Retreat was \$2,850,000. The Company also paid an acquisition fee payable to Paladin Advisors of \$156,750 in connection with the acquisition of Retreat Apartments.

The operating agreement for KC Retreat provides that the Company will receive priority in distributions of operating cash flow until it has received at least 12.0% on its invested equity, after which its co-venture partners will receive distributions until they have reached the same 12.0% on their invested equity. Thereafter, operating cash flow will be distributed 50% to the Company and 50% to its co-venture partners. The operating agreement for KC Retreat also provides for priority distributions of sale proceeds, if any. First, the Company will receive a priority distribution equal to a return of its invested capital plus an amount that when added to all distributions of cash flow made to the Company during the life of its investment, is sufficient to generate a 12.0% internal rate of return on its invested capital. Second, the Company’s co-venture partners will receive distributions that when added to all distributions of cash flow made to its co-venture partners during the life of their investment, is sufficient to generate a 12.0% internal rate of return on their invested capital. Third, any further sale proceeds will be distributed 50% to the Company and 50% to its co-venture partners.

##### *Hilltop Apartments*

On April 7, 2008, a wholly-owned subsidiary of Paladin OP, PRIP 6700, LLC purchased a 49% interest in Park Hill Partners, a joint venture between PRIP 6700, LLC and JTL Properties, LLC, which owns Hilltop Apartments. Hilltop Apartments is a 124-unit multifamily rental community built in 1986. The apartment complex is located in Kansas City, Missouri. The total acquisition cost for PRIP 6700, LLC’s interest in Park Hill Partners was \$1,050,000, including approximately \$50,000 for capital expenditures reserve and \$50,000 for closing costs and working capital. The property was encumbered by an existing first mortgage in the amount of \$4,250,000. The Company paid an acquisition fee payable to Paladin Advisors of \$57,750 in connection with the acquisition of Hilltop Apartments.

The operating agreement for Park Hill Partners provides that the Company will receive priority in distributions of operating cash flow until it has received at least 12.0% on its invested equity, after which its co-venture partners will receive distributions until they have reached the same 12.0% on their invested equity. Thereafter, operating cash flow will be distributed 49% to the Company and 51% to its co-venture partners. The operating agreement for Park Hill Partners also provides for priority distributions of sale proceeds, if any. First, the Company will receive a priority distribution equal to a return of its invested capital plus an amount that when added to all distributions of cash flow made to the Company during the life of its investment, is sufficient to generate a 12.0% internal rate of return on its invested capital. Second, the Company’s co-venture partners will receive distributions that when added to all distributions of cash flow made to the co-venture partners during the life of their investment, is sufficient to generate a 12.0% internal rate of return on their invested capital. Third, any further sale proceeds will be distributed 49% to the Company and 51% to its co-venture partners.

##### *Conifer Crossing*

On August 4, 2008, a wholly-owned subsidiary of Paladin OP, PRIP 3383, LLC purchased a 42.5% interest in FPA/PRIP Conifer, a joint venture between PRIP 3383, LLC and FPA Conifer Investors, LLC. On August 5, 2008, FPA/PRIP Conifer purchased Conifer Crossing. Conifer Crossing is a 420-unit multifamily rental community developed in



1981. The apartment complex is located in Norcross, Georgia. Including funds earmarked for renovation and closing costs, the total capitalization for this investment was approximately \$39,385,000. FPA/PRIP Conifer secured a mortgage loan of \$28.7 million to finance the acquisition. As a condition to the loan, FPA/PRIP Conifer was required to fund an escrow account with approximately \$6,613,500 for the payment for such repairs and improvements pursuant to a Repair Escrow Agreement dated August 5, 2008. Paladin OP's investment in FPA/PRIP Conifer was \$4.5 million. The Company paid an acquisition fee payable to Paladin Advisors in the amount of \$251,268 in connection with the acquisition of Conifer Crossing.

The operating agreement for FPA/PRIP provides that the Company will receive priority in distributions of operating cash flow until the Company has received at least 8.5% on its invested equity, after which the Company's co-venture partner will receive distributions until the co-venture partner has reached the same 8.5% on its invested equity. If the Company's pro rata distribution exceeds 9.0% in a calendar year, the Company will share 20% of its excess distributions with its co-venture partner as a cash flow bonus.

The operating agreement also provides for distributions of sale proceeds, if any, as follows. First, the Company and the co-venture partner will receive a 100% return of our equity investments. Second, the Company and the co-venture partner will receive pro rata distributions until the Company and the co-venture partner each have received a 12.0% internal rate of return on their invested capital. Third, the Company will share its pro rata portion of fifty percent of the remaining distributions with the co-venture partner and the co-venture partner will receive all of the other fifty percent of the remaining distributions as incentive compensation.

#### *Two and Five Governor Park*

On December 19, 2008, PRIP 5060/6310, LLC, a Delaware limited liability company and a subsidiary of Paladin OP, formed a joint venture with FPA Governor Park Investors, LLC ("FPA Governor Park Investors"), a Delaware limited liability company and an affiliate of Fowler Property Acquisitions, LLC, a California limited liability company ("Fowler Property Acquisitions"), to acquire Two and Five Governor Park located at 6310 Greenwich Drive, San Diego, California 92122 and 5060 Shoreham Place, San Diego, California 92122 ("Two and Five Governor Park"), two office properties located in suburban San Diego.

The joint venture, FPA/PRIP Governor Park, is the sole member of FPA Governor Park Associates, LLC, a Delaware limited liability company ("FPA Governor Park Associates"). FPA Governor Park Associates is the borrower and holds title to Two and Five Governor Park.

The acquisition of Two and Five Governor Park by FPA Governor Park, which was completed on December 19, 2008, was made pursuant to a Purchase and Sale Agreement, dated as of September 9, 2008 (the "Purchase Agreement"), between the Seller and Fowler Property Acquisitions, as amended by the First Amendment to Real Estate Purchase and Sale Agreement, dated as of October 23, 2008. Fowler Property Acquisitions assigned the Purchase Agreement to FPA Governor Park Associates pursuant to an Assignment and Assumption of Agreement of Purchase and Sale, dated as of September 25, 2008.

Including funds earmarked for renovation and closing costs, the total capitalization for this investment was approximately \$16,686,350, which was comprised of a mortgage loan from an affiliate of the seller in the amount of \$11,440,000 and \$5,246,350 in capital contributions, of which the Company contributed \$2,500,000 with proceeds from the Company's Follow-On Offering. Of the \$11,440,000 in loan proceeds, approximately \$8,330,000 was funded at closing. The remaining \$3,110,000 is available to fund future costs and expenses consisting of \$811,000 for operating deficits including interest expense, \$880,000 for capital expenditures and \$1,419,000 for tenant improvements and leasing commissions. Closing costs equaled \$351,350. In addition, FPA/PRIP Governor Park set aside a reserve of \$225,000 to be used as needed to cover the 9.0% preferred return to the Company until depleted.

Pursuant to the operating agreement for FPA/PRIP Governor Park, dated as of December 19, 2008 as amended on March 25, 2009, between PRIP 5060/6310, LLC and FPA Governor Park Investors, the Company owns a 47.65% interest in FPA/PRIP Governor Park and FPA Governor Park Investors owns the remaining interest. The operating agreement provides that the Company's investment will be treated as preferred equity, and the Company will receive a priority preferred return of 9.0% on its invested equity and a fixed, priority 15.0% internal rate of return upon a capital event. The operating agreement also provides the Company with super-majority voting rights with respect to all major decisions by FPA/PRIP Governor Park. Fowler Property Acquisitions is not affiliated with the Company or any of its affiliates, except that an affiliate of Fowler Property Acquisitions participates in another joint venture with the Company relating to Conifer Crossing located at 3383 Holcomb Bridge Road NW, Norcross, Georgia.

### *Fieldstone Apartments*

In connection with Paladin OP's acquisition of its interest in Glenwood, which owns Fieldstone Apartments, Shiloh Crossing Partners II, LLC ("Shiloh II") was granted the right to require Paladin OP to purchase up to an additional 25% ownership interest in Glenwood from Shiloh II upon the occurrence of certain events and the achievement of certain financial benchmarks at Fieldstone Apartments at a cost of \$62,500 per 1% of ownership interest. On July 1, 2008, Paladin OP purchased an additional 18% interest in Glenwood from Shiloh II for \$1,125,000. Paladin OP now holds an 83% ownership interest in Glenwood. Fieldstone Apartments is a 266-unit luxury multifamily rental community built in 2001. The Company also paid an acquisition fee payable to Paladin Advisors of \$61,875 in connection with the purchase of the additional ownership interest in Glenwood.

Also in connection with Paladin OP's initial acquisition of its interest in Glenwood, a wholly owned subsidiary of Paladin OP, PRIP 10637, LLC, entered into a Phase II Option Agreement ("Option Agreement") with Glenwood Housing Partners II, LLC, an Indiana limited liability company ("Glenwood II"). Glenwood II owns a parcel of land adjacent to Fieldstone Apartments upon which it may construct 88 apartment units with an aggregate of 97,640 square feet of rentable space to be leased, managed and operated as Phase II of the Fieldstone Apartments. The Option Agreement grants PRIP 10637, LLC an ongoing option to purchase at least a 70% but not more than 90% beneficial ownership interest in Glenwood II or any affiliated entity that owns the parcel and developments thereon. PRIP 10637 may exercise the option at any time after the completion of development and stabilization of the project. If exercised, the purchase price for the option interest will be determined by a formula that utilizes market-rate variables as of that future date.

### *Other*

In addition, Paladin OP holds a 70% ownership interest in Springhurst, which owns Champion Farms Apartments. Champion Farms Apartments is a 264-unit luxury multifamily rental community built in 2000. Paladin OP also holds a 97.5% ownership interest in KC Pinehurst, which owns Pinehurst Apartment Homes a 146-unit multifamily rental community built in two phases in 1986 and 1988. Also, Paladin OP holds a 97.5% ownership interest in KC Pheasant, which owns Pheasant Run Apartments, a 160-unit multifamily rental community built in 1985.

In connection with Paladin OP's acquisition of its interest in Springhurst, Buckingham Springhurst, LLC was granted the right to require Paladin OP to purchase up to an additional 20% ownership interest in Springhurst from Buckingham Springhurst, LLC upon the occurrence of certain events and the achievement of certain financial benchmarks at Champion Farms Apartments at a cost of \$67,500 per 1% of ownership interest. As of September 30, 2008, Paladin OP has not been required to purchase additional interests in Springhurst by Buckingham Springhurst, LLC.

The operating agreements for both Springhurst and Glenwood provide that the Company will receive priority in distributions of operating cash flow until it has received at least 8.25% on its invested equity, after which its co-venture partners will receive distributions until they have reached the same 8.25% on their invested equity. Thereafter, operating cash flow will be distributed 50% to the Company and 50% to its co-venture partners. The operating agreements for both Springhurst and Glenwood also provide for priority distributions of sale proceeds, if any. First, the Company will receive a priority distribution equal to a return of its invested capital. Second, its co-venture partners will receive a distribution equal to their invested capital. Third, the Company will receive an amount that when added to all distributions of cash flow made to the Company during the life of its investment, is sufficient to generate an 11.5% internal rate of return on its invested capital. Fourth, the Company's co-venture partners will receive an amount, that when added to all distributions of cash flow made to its co-venture partners during the life of their investment, is sufficient to generate an 11.5% internal rate of return on their invested capital. Fifth, any further sale proceeds will be distributed 50% to the Company and 50% to its co-venture partners.

The operating agreements for both KC Pinehurst and KC Pheasant provide that the Company will receive priority in distributions of operating cash flow until it has received at least 9.0% on its invested equity, after which its co-venture partners will receive distributions until they have reached the same 9.0% on their invested equity. Thereafter, operating cash flow will be distributed 75% to the Company and 25% to its co-venture partners. The operating agreements for both KC Pinehurst and KC Pheasant also provide for priority distributions of sale proceeds, if any. First, the Company will receive a priority distribution equal to a return of its invested capital plus an amount that when added to all distributions of cash flow made to the Company during the life of its investment, is sufficient to generate a 12.0% internal rate of return on its invested capital. Second, the Company's co-venture partners will receive distributions that when added to all distributions of cash flow made to its co-venture partners during the life of their investment, is sufficient to generate a 12.0% internal rate of return on their invested capital. Third, any further sale proceeds will be distributed 50% to the Company and 50% to its co-venture partners.

The Company consolidates FPA/PRIP Governor Park, FPA/PRIP Conifer, Park Hill Partners, KC Retreat, KC Pinehurst, KC Pheasant, Springhurst and Glenwood.

The following table summarizes certain information related to the Company's investments in real estate as of December 31, 2008:

Property	Encumbrances	Initial Costs		Costs Capitalized Subsequent to Acquisition		Total Costs		Accumulated Depreciation	Year Built	Year Acquired
		Land Acquired	Building & Improvements	Land Additions	Improvements	Land Acquired	Building & Improvements			
Champion Farms Apartments	\$ 16,350,000	\$ 2,335,545	\$ 17,856,281	\$ —	\$ 61,029	\$ 2,335,545	\$ 17,917,310	\$(1,028,753)	2000	2006
Fieldstone Apartments	16,500,000	1,446,033	18,548,780	78,750	1,159,128	1,524,783	19,707,908	(870,757)	2001	2006
Pinehurst Apartment Homes	4,711,696	1,230,000	5,865,966	—	—	1,230,000	5,865,966	(236,834)	1986	2007
Pheasant Run Apartments	6,250,000	1,120,000	7,393,945	—	154,162	1,120,000	7,548,107	(292,996)	1985	2007
Retreat Apartments	13,600,000	1,860,000	13,913,549	—	338,312	1,860,000	14,251,861	(528,941)	1984	2008
Hilltop Apartments	4,250,000	430,000	4,475,196	—	59,734	430,000	4,534,930	(98,448)	1986	2008
Conifer Apartments	28,700,000	13,721,349	17,154,149	—	3,803,704	13,721,349	20,957,853	(199,022)	1981	2008
Two and Five Governor Park (1)									1985	
	8,367,612	5,099,027	8,107,703	—	32,331	5,099,027	8,140,034	(7,978)	& 1989	2008
<b>Total</b>	<b>\$98,729,308</b>	<b>\$27,241,954</b>	<b>\$93,315,569</b>	<b>\$78,750</b>	<b>\$ 5,608,400</b>	<b>\$27,320,704</b>	<b>\$98,923,969</b>	<b>\$(3,263,729)</b>		

The aggregate cost of the Company's investments in real estate for federal income tax purposes is approximately \$126.1 million (unaudited) as of December 31, 2008 and \$55.8 million (unaudited) as of December 31, 2007.

Note (1) This investment consists of 2 office buildings.



Condensed financial information of PRIP 801, LLC, is summarized as follows:

**Condensed Balance Sheets  
December 31, 2008 and 2007  
(unaudited)**

	<u>2008</u>	<u>2007</u>
<b>ASSETS</b>		
Investment in real estate, net	\$3,853,956	\$3,934,812
Other Assets, net	145,686	141,911
Total Assets	<u>\$3,999,642</u>	<u>\$4,076,723</u>
<b>LIABILITIES AND MEMBERS' EQUITY</b>		
Mortgage loan payable	\$1,950,000	\$1,950,000
Other Liabilities	28,180	38,116
Members' equity	2,021,642	2,088,607
Total Liabilities and Members' Equity	<u>\$3,999,642</u>	<u>\$4,076,723</u>
Company's share of Members' Equity*	<u>\$1,495,968</u>	<u>\$1,545,655</u>

**Condensed Statements of Income  
For the years ended December 31, 2007 and 2006  
(unaudited)**

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Revenues and interest income	\$ 338,554	\$ 338,791	\$ 339,112
Expenses	(215,669)	(221,786)	(233,823)
Net Income	<u>\$ 122,855</u>	<u>\$ 117,005</u>	<u>\$ 105,289</u>
Company's share of net income*	<u>\$ 90,912</u>	<u>\$ 86,584</u>	<u>\$ 77,914</u>

\* The difference in the Company's share of Members' Equity and the Company's share of net income reflected above compared to the Company's balance sheets and statements of operations is attributed to the depreciation expense of the acquisition costs incurred by the Company.

The mortgage loan requires payments of interest only at a fixed interest rate of 5.498% through November 1, 2010, the anticipated repayment date. If the mortgage loan is not repaid or refinanced as of the anticipated repayment date, interest will accrue at a rate per annum equal to the greater of (a) 8.498% and (b) the treasury rate plus three percentage points. Pursuant to the terms of a cash management agreement, the borrower was required to post a \$550,000 letter of credit by December 1, 2007, or the lender would sweep and retain all cash flow from 801 Fiber Optic Drive. On November 29, 2007, Paladin OP posted a \$550,000 irrevocable standby letter of credit with Wachovia Bank, N.A. secured by \$550,000 cash deposited in a certificate of deposit with Wachovia Bank, N.A. If the borrower does not pay off the loan on November 1, 2010, the lender can apply the letter of credit (or retained cash flow) and will continue to sweep all cash flow to repay the loan. In the event of a default under the loan documents, the cash management agreement further provides that the lender may sweep cash from all accounts maintained by the borrower with the lender (including rent accounts from the property). The estimated principal balance to be due at the anticipated repayment date is \$1,950,000.

In general, the mortgage loan may not be prepaid until January 31, 2008 and as of December 31, 2008 it has not been prepaid. In general, no sale, encumbrance or other transfer of an interest in the property is permitted without the lender's prior written consent.

Alex Gilbert, the managing member of 801 FO, LLC has guaranteed the non-recourse standard loan carve outs, and in exchange for his guarantee, Paladin Realty has agreed to fully indemnify Mr. Gilbert against any defaults caused by the borrower through standard default provisions such as bankruptcy, fraud, misapplication of proceeds and certain environmental violations. The loan agreement obligation is secured by a mortgage on the property and an assignment of rents and personal property. In addition PRIP 801, LLC, has entered into an environmental and hazardous substance indemnification agreement.

The agreements contain various covenants, which among other things, limit the ability of the borrowers to incur indebtedness, engage in certain business activities, enter into material leases on the property and transfer its interest in the property among others. The loan agreements also contain customary events of default, including, without limitation, payment defaults, cross-defaults to certain other agreements with respect to the property and bankruptcy-related defaults. In the event of a default, the loan may be accelerated and all amounts due under the loan will become immediately due and payable.

#### 4. Mortgages Payable

##### Mortgages Payable

Mortgage loans payable consisted of the following:

	December 31, 2008	December 31, 2007
Mortgage loan payable—interest only at a fixed rate of 6.14% payable monthly until the loan matures on July 1, 2016, secured by the Champion Farms Apartments property (1)	\$16,350,000	\$16,350,000
Mortgage loan payable—interest only at 6.05% payable monthly until July 1, 2011, after which principal and interest are due until the loan matures on July 1, 2014, secured by the Fieldstone Apartments property (1)	16,500,000	16,500,000
Mortgage loan payable—principal and interest at 5.58% payable monthly until the loan matures January 1, 2016, secured by the Pinehurst Apartment Homes property (2)	4,711,696	4,779,125
Mortgage loan payable—interest only at 5.95% payable monthly until the loan matures on October 1, 2017, secured by the Pheasant Run Apartments property (3)	6,250,000	6,250,000
Mortgage loan payable—interest only at 5.58% payable monthly until February 1, 2013, after which principal and interest are due until the loan matures on February 1, 2018, secured by the Retreat Apartments property (4)	13,600,000	—
Mortgage loan payable—interest only at 5.81% payable monthly until December 1, 2012, after which principal and interest are due until the loan matures on December 1, 2017, secured by the Hilltop Apartments property (5)	4,250,000	—
Mortgage loan payable—interest only at 5.96% payable monthly until September 1, 2011, after which principal and interest are due until the loan matures on September 1, 2015, secured by the Conifer Crossing property (6)	28,700,000	—
Mortgage loan payable—interest only at 7.00% payable monthly until the loan matures on December 19, 2010, secured by the Two and Five Governor Park properties (7)	8,367,612	—
<b>Total mortgage loans payable</b>	<b>\$98,729,308</b>	<b>\$43,879,125</b>

- (1) In general, the mortgage loan may be voluntarily or involuntarily prepaid subject to certain prepayment penalties. The loan agreement obligation is secured by a mortgage on the property and an assignment of rents and personal property.
- (2) The loan is prepayable at any time prior to its maturity, subject to a prepayment penalty equal to the greater of (1) one percent of the outstanding balance or (2) an amount calculated pursuant to a formula based on the remaining life of the loan and then-current interest rates. In addition the loan is guaranteed by James E. Lippert, an affiliate of JTL Holdings, LLC and JTL Asset Management, Inc., pursuant to a guaranty dated September 13, 2007, but only upon the occurrence of certain limited events.
- (3) Assuming no event of default occurs before the initial maturity date, the loan will automatically be extended until October 1, 2018 with an adjustable interest rate based on the Federal Home Loan Mortgage Corporation Reference Bill Index. The loan is prepayable at any time prior to its maturity, subject to a prepayment penalty equal to the greater of (1) one percent of the outstanding balance or (2) an amount calculated pursuant to a formula based on the remaining life of the loan and then-current interest rates. In the event of default, the entire unpaid principal balance, any accrued interest, any prepayment penalty and all other amounts payable under the Promissory Note will be due and payable.
- (4) Assuming no event of default occurs before the initial maturity date, the loan will automatically be extended until February 1, 2019 with an adjustable interest rate based on the Freddie Mac Reference Bill Index. The loan is prepayable at any time prior to its maturity, subject to a prepayment penalty equal to the greater of (1) one percent of the outstanding balance or (2) an amount calculated pursuant to a formula based on the remaining life of the loan and then-current interest rates. The loan is secured by a multifamily mortgage on the property pursuant to a Multifamily Deed of Trust, Assignment of Rents and Security Agreement. In addition, the loan is guaranteed by James E. Lippert, but only upon the occurrence of certain limited events.
- (5) Assuming no event of default occurs before the initial maturity date, the loan will automatically be extended until December 1, 2018 with an adjustable interest rate based on the Freddie Mac Reference Bill Index. The loan is prepayable at any time prior to its maturity, subject to a prepayment penalty equal to the greater of (1) one percent of the outstanding balance or (2) an amount calculated pursuant to a formula based on the remaining life of the loan and then-current interest rates. The loan is secured by a multifamily mortgage on the property pursuant to a Multifamily Deed of Trust, Assignment of Rents and Security Agreement. In addition, the loan is guaranteed by James E. Lippert, but only upon the occurrence of certain limited events.
- (6) Assuming no event of default occurs before the initial maturity date, the loan will automatically be extended until September 1, 2016 with an adjustable interest rate based on the Freddie Mac Reference Bill Index. The loan is prepayable at any time prior to its maturity, subject to a prepayment penalty equal to the greater of (1) one percent of the outstanding balance or (2) an amount calculated pursuant to a formula based on the remaining life of the loan and then-current interest rates. The loan is secured by a multifamily mortgage on the property pursuant to a Multifamily Deed of Trust, Assignment of Rents and Security Agreement. In addition, the loan is guaranteed by Gregory A. Fowler, a management committee representative of FPA Conifer Investors, LLC, but only upon the occurrence of certain limited events.
- (7) The loan has two, one-year extensions which may be exercised if, among other things, the properties have (1) a debt service coverage ratio of 1.2 or better, and (2) a loan to value ratio of no more than 70.0% based on an appraisal. Each extension is subject to an extension fee equal to 1.5% of the outstanding principal balance. The loan is prepayable at any time prior to its maturity, subject to an exit fee equal to 1.0% of the principal being repaid. The loan is secured by a mortgage on the property pursuant to a Deed of Trust and Absolute Assignment of Rents and Leases and Security Agreement. In addition, the loan is guaranteed by Gregory A. Fowler but only upon the occurrence of certain limited events.

The loan agreements contain various covenants, which among other things, limit the ability of the borrower to incur indebtedness, engage in certain business activities, enter into material leases on the property and transfer their interest in the property among others. The loan agreements also contain certain customary events of default, including, without limitation, payment defaults, cross-defaults to certain other agreements with respect to the property and bankruptcy-related defaults. In the event of default, the loan may be accelerated and all amounts due under the loan will become immediately due and payable.

Principal payments due on the mortgage loans payable as of December 31, 2008 are as follows:

2009	\$ 72,115
2010	8,443,915
2011	277,041
2012	609,710
2013	855,700
Thereafter	88,470,827
Total	<u>\$98,729,308</u>

Paladin REIT's charter provides that its independent directors must approve any borrowing in excess of 300% of the value of its net assets and the justification for such excess borrowing must be disclosed to its stockholders in its next quarterly report. Net assets for purposes of this calculation are defined to be Paladin REIT's total assets (other than intangibles), valued at cost prior to deducting depreciation, reserves for bad debts and other non-cash reserves, less total liabilities. The preceding calculation is generally expected to approximate 75% of the aggregate cost of Paladin REIT's assets before non-cash reserves and depreciation. As of December 31, 2008, Paladin REIT's borrowings did not exceed 300% of the value of its net assets.

## 5. Stockholders' Equity

### *Preferred Shares*

Paladin REIT's board of directors, through Paladin REIT's charter, has the authority to authorize the issuance of 100,000,000 preferred shares in one or more classes or series. The rights and terms of such preferred shares will be determined by the board of directors. However, the voting rights of the preferred shares sold in a private offering shall not exceed voting rights which bear the same relationship to the voting rights of common shares as the consideration paid for each such preferred share bears to the book value of each outstanding common share. As of December 31, 2008 and 2007, Paladin REIT had not issued any preferred shares.

### *Redemptions*

As of August 28, 2008, Paladin REIT's Share Redemption Program was amended as follows. Paladin REIT now waives the one-year holding period in the event of the death or qualifying disability of a stockholder. During any 12-month period, Paladin REIT will not redeem in excess of 10.0% of the number of shares of common stock that were outstanding as of the beginning of such 12-month period. Previously, Paladin REIT was limited to redemptions not in excess of 3.0% of the number of shares of common stock outstanding at the beginning of such 12-month period. Finally, certain fees charged by Paladin REIT's registrar and transfer agent, Phoenix American Financial Services, Inc., for share redemptions are now charged to investors seeking to redeem shares of common stock pursuant to the program.

We fund redemption requests received during a quarter with proceeds received from our distribution reinvestment plan in the month following such quarter. If we do not receive sufficient funds in such month to fulfill all redemption requests from the previous quarter, the remaining amounts will be funded with proceeds received from the distribution reinvestment plan in the subsequent months.

During the year ended December 31, 2008, 18 stockholders redeemed 27,951 shares for \$259,991. During the year ended December 31, 2007, three stockholders redeemed 2,537 shares for \$23,593. As of December 31, 2008, a total of 21 stockholders have redeemed 30,488 shares for \$283,584 since the beginning of the Initial Offering. The redemptions have been recorded as treasury shares.

### *Distributions*

The board of directors has declared distributions since December 2005 in the amount of \$0.0016438 per share per day, representing an annualized rate of return of 6.0% on an investment of \$10.00 per share if paid each day over a 365-day period. Distributions have been declared on a monthly basis to stockholders of record as of the close of business each day during the applicable month and paid generally on the 15<sup>th</sup> day of the following month, unless the 15<sup>th</sup> day of the month is not a business day. For federal income tax purposes, distributions may consist of ordinary dividend income, non-taxable return of capital, capital gains or a combination thereof. Distributions to the extent of the Company's current and accumulated earnings and profits are taxable to the recipient as ordinary dividend income. Distributions in excess of these earnings and profits will constitute a non-taxable return of capital rather than an ordinary dividend and will reduce the recipient's basis in the shares to the extent thereof, and thereafter a

taxable gain. All of Paladin REIT's distributions declared and paid to date constitute a return of capital.

## 6. Related Party Transactions

Paladin Realty Securities, LLC ("Paladin Securities"), a wholly owned subsidiary of Paladin Advisors, began serving as the dealer manager for the Initial Offering pursuant to a dealer manager agreement dated June 5, 2007, as amended by the amendment to the dealer manager agreement dated February 23, 2008 (the "IPO Dealer Manager Agreement"). Pursuant to the terms of the IPO Dealer Manager Agreement, Paladin REIT paid Paladin Securities selling commissions of 7.0% of the gross offering proceeds from the sale of shares of Paladin REIT's common stock in its primary offering and 4.0% of the gross offering proceeds from the sale of shares of its common stock pursuant to its distribution reinvestment plan. Paladin REIT also paid Paladin Securities a dealer manager fee of up to 2.5% of gross offering proceeds from the sale of shares of Paladin REIT's common stock in its primary offering.

In connection with the Follow-On Offering, Paladin REIT entered into dealer manager agreement dated February 6, 2008 (the "Follow-On Dealer Manager Agreement"). Pursuant to the terms of the Follow-On Dealer Manager Agreement Paladin REIT pays Paladin Securities selling commissions of 6.0% of the gross offering proceeds from the sale of shares of Paladin REIT's common stock in its primary offering and Paladin REIT does not pay any commission from the sale of shares of its common stock pursuant to its distribution reinvestment plan. Paladin REIT also pays Paladin Securities a dealer manager fee of up to 3.5% of gross offering proceeds from the sale of shares of Paladin REIT's common stock in its primary offering. Paladin Securities may pay all or a portion of these selling commissions and dealer manager fees to participating broker-dealers.

For the year ended December 31, 2008, Paladin REIT incurred \$943,952 in selling commissions and dealer manager fees to Paladin Securities. For the year ended December 31, 2007, Paladin REIT paid \$667,153 in selling commissions and dealer manager fees to Paladin Securities.

The Advisory Agreement entitles Paladin Advisors to specified fees upon the provision of certain services with regard to the Offerings and investment of funds in real properties and real estate related investments, among other services, as well as reimbursement for organization and offering costs incurred by Paladin Advisors on behalf of the Company and certain costs incurred by Paladin Advisors and its affiliates in providing services to the Company.

### Amounts due (from) to Affiliates

	December 31, 2008	December 31, 2007
General and administrative expenses due to affiliates (1)	\$ 1,032,304	\$ 141,731
Organization and offering costs due (from) to affiliates (2)	\$ (199,350)	\$ (1,068,147)
Acquisition fees due to affiliates (3)	\$ —	\$ —
Total due to (from) affiliates	\$ 832,954	\$ (926,416)
Deferred general and administrative expenses (4)	\$ 900,667	\$ 1,499,043
Deferred organization and offering costs (5)	\$ 6,893,824	\$ 4,354,293

- (1) Pursuant to the Advisory Agreement, the Company will not reimburse Paladin Advisors for operating expenses that in the fiscal year then ended exceed the greater of (1) 2% of the Company's average invested assets or (2) 25% of the Company's net income (the "2%/25% Rule"). Paladin Advisors must reimburse the Company for any amounts by which its operating expenses exceed the 2%/25% Rule in the previous four consecutive fiscal quarters within 60 days after the end of each fiscal quarter unless a majority of the independent directors determine that the excess expenses were justified based on unusual and nonrecurring factors which they deem sufficient. Within 60 days after the end of any Expense Period for which total operating expenses exceed the 2%/25% Rule, the Company must send its stockholders written disclosure, together with an explanation of the factors the independent directors considered in arriving at the conclusion that the excess expenses were justified. However, at Paladin Advisors' option, Paladin Advisors or its affiliate, as applicable may defer the reimbursement of expenses and elect to receive such payments, without interest, in any subsequent fiscal year that Paladin Advisors designates. During the year ended December 31, 2008, the Company incurred \$982,678 of general and administrative expenses, which is the equivalent of operating expenses under the Advisory Agreement. Due to the application of the 2%/25% Rule, the Company was able to recognize a total of \$1,873,251 of general and administrative expenses in its consolidated statement of operations with the additional amount of \$890,573, which was incurred in previous years, recorded as due to affiliate. Pursuant to the Advisory Agreement, the Company paid Paladin Advisors \$256,336 in asset management fees for its ten properties during the year ended December 31, 2008. For each of these ten properties from the respective dates of acquisition through the period that the

Company owns the properties, Paladin Advisors has elected to receive a monthly asset management fee equal to one-twelfth of 0.3% of the Company's allocable cost of the real property acquired. Paladin Advisors acknowledges that it has waived its right to receive any additional amounts due under the Advisory Agreement for such properties. Paladin Advisors has elected to defer (without interest) the net balance of \$900,667 in general and administrative expenses. The board of directors (including the independent directors) has approved reimbursing Paladin Advisors for this amount in the future to the extent that reimbursement of this amount, together with all operating expenses paid or reimbursed for the then-current Expense Period, would not result in payment or reimbursement of operating expenses in excess of the 2%/25% Rule in that period. In making this determination, the board of directors (including the independent directors) noted that these were operating expenses necessary for the operation of the Company's business, as the Company is in the early stages of operations and has limited operations to cover its operating expenses and because such amounts will only be reimbursed in the future to the extent described above.

- (2) Organization and offering costs of the Company are paid by Paladin Advisors or its affiliates, including Paladin Realty, on behalf of the Company and directly by the Company. Organization and offering costs consist of actual marketing, legal, accounting, printing and other offering expenses, including amounts to reimburse Paladin Advisors, its affiliates or its dealer manager, for all marketing related costs and expenses, including, but not limited to, expenses relating to registering and marketing the shares and other marketing and organization costs, technology costs and expenses attributable to the Offerings, and payment or reimbursement of bona fide due diligence expenses of the dealer manager and broker-dealers participating in the Offerings. Pursuant to the Advisory Agreement, the Company is obligated to reimburse Paladin Advisors or its affiliates for amounts advanced for organization and offering costs, provided that Paladin Advisors and its affiliates are responsible for the payment of organization and offering costs to the extent they exceed 3.0% of gross proceeds from the Offerings and will be required to return to the Company any amount the Company reimburses them in excess of 3.0% of the gross proceeds from the Offerings. Such costs only become a liability of the Company to the extent they do not exceed 3.0% of the gross proceeds of the Offerings. For the year ended December 31, 2008, the Company paid \$687,009 of offering costs. Due to the application of the 3.0% limitation, the Company was only able to recognize \$329,620, which was charged to stockholders' equity with the additional amount of \$357,389 recorded as due from affiliate. On March 28, 2008 Paladin Advisors reimbursed the Company \$1,226,186. Paladin Advisors is required to reimburse the balance of \$199,350 within 60 days after the end of the Offerings.
- (3) Pursuant to the Advisory Agreement, Paladin Advisors was entitled to acquisition fees related to all acquisitions. During the year ended December 31, 2008, the Company paid \$646,914 of acquisition fees to Paladin Advisors for these acquisitions.
- (4) Not reflected in the consolidated financial statements at December 31, 2008 and 2007 as these amounts have exceeded the limitations imposed by the 2%/25% Rule as described above in footnote 1 and only become due to affiliates when this amount, together with all operating expenses paid or reimbursed for the then-current Expense Period, would not result in payment or reimbursement of operating expenses in excess of the 2%/25% Rule in that period.
- (5) Not reflected in the consolidated financial statements at December 31, 2008 and 2007 as these amounts have exceeded the 3.0% limitation as described above in footnote 2 and only become due to affiliates when they do not exceed such limitation.

#### **7. Quarterly Financial Data (Unaudited)**

The following table presents selected unaudited quarterly financial data for each quarter during the years ended December 31, 2008 and 2007:

	<b>For the Quarter Ended</b>			
	<b>March 31, 2008</b>	<b>June 30, 2008</b>	<b>September 30, 2008</b>	<b>December 31, 2008</b>
Revenues	\$2,294,137	\$2,592,841	\$3,239,901	\$3,462,932
Equity in earnings from real estate joint venture	\$ 21,227	\$ 21,384	\$ 17,594	\$ 28,019
Net loss attributable to Company	\$ (368,301)	\$ (486,185)	\$ (666,148)	\$ (837,916)
Loss per common share:				
Basic	\$ (0.13)	\$ (0.16)	\$ (0.20)	\$ (0.23)
Diluted	\$ (0.13)	\$ (0.16)	\$ (0.20)	\$ (0.23)

	<b>For the Quarter Ended</b>			
	<b>March 31, 2007</b>	<b>June 30, 2007</b>	<b>September 30, 2007</b>	<b>December 31, 2007</b>
Revenues	\$1,186,408	\$1,238,470	\$1,329,419	\$1,841,325
Equity in earnings from real estate joint venture	\$ 21,233	\$ 20,986	\$ 20,998	\$ 20,679
Net loss attributable to Company	\$ (372,045)	\$ (361,766)	\$ (230,227)	\$ (360,430)
Loss per common share:				
Basic	\$ (0.38)	\$ (0.24)	\$ (0.11)	\$ (0.15)
Diluted	\$ (0.38)	\$ (0.24)	\$ (0.11)	\$ (0.15)

## **8. Subsequent Events**

### ***Redemptions***

From January 1 to March 20, 2009, twelve stockholders redeemed 34,111 shares for \$317,239.