AMERICAN REALTY INVESTORS INC
Form 10-K/A
April 07, 2005

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K/A

(Amendment No. 1)

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

For the Year Ended December 31, 2004

¨ **TRANSITION REPORT PURSUANT TO SECTIONS 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Commission File Number 001-15663

American Realty Investors, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Nevada	**75-2847135**

(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**
1800 Valley View Lane, Suite 300,	
Dallas, Texas	**75234**
(Address of Principal Executive Offices)	**(Zip Code)**

(469) 522-4200

(Registrant s Telephone Number, Including Area Code)

Securities Registered Pursuant to Section 12(b) of the Act:

Title of each class	*Name of each exchange on which registered*
Common Stock, $.01 par value	New York Stock Exchange

Securities Registered Pursuant to Section 12(g) of the Act:

NONE

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

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes ¨ No x

The aggregate market value of the shares of voting and non-voting common equity held by non-affiliates of the Registrant, computed by reference to the closing sales price of the Common Stock on the New York Stock Exchange as of June 30, 2004 (the last business day of the Registrant s most recently completed second fiscal quarter) was $19,911,105 based upon a total of 2,204,995 shares held as of June 30, 2004 by persons believed to be non-affiliates of the Registrant. The basis of the calculation does not constitute a determination by the Registrant as defined in Rule 405 of the Securities Act of 1933, as amended, such calculation, if made as of a date within sixty days of this filing would yield a different value. As of March 24, 2005, there were 10,895,972 shares of common stock outstanding, including 746,972 shares issued to and owned by Transcontinental Realty Investors, Inc.

Documents Incorporated by Reference:

Consolidated Financial Statements of Income Opportunity Realty Investors, Inc.; Commission File No. 001-14784

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AMENDMENT #1 FOR ANNUAL REPORT ON 10-K FOR

AMERICAN REALTY INVESTORS, INC.

The undersigned registrant hereby amends the following items, exhibits, or other portions of its Annual Report on Form 10-K for the fiscal year ended 12/31/2004 as set forth below and as reflected in the substituted pages attached hereto, which replace the same numbered pages in the original filing:

*Page 39, 3rd paragraph from the bottom, 1st line, changed translation to transaction and 3rd line, changed TCI to ARI.

*Page 44, 1st full paragraph, 3rd line, changed TCI to ARI.

*Page 71, 1st line, removed Related Party.

*Page 85, 1st line below table, changed ARI owed $1.4 to ARI owed $1.1.

*Page 115, ITEM 9, last paragraph, 1st line, changed March 30 to April 15.

*Page 131, ITEM 14 table, far right column (1) was changed to superscript.

*Page 133, ITEM 15(a) **1.** 1st line, Report of Independent Certified Public Accountants changed to Reports of Independent Registered Public Accounting Firms and the last line of the page changed 2003 to 2004.

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this Amendment to be signed on its behalf by the undersigned, thereunto duly authorized.

American Realty Investors, Inc.

Dated: April 6, 2005

By: /s/ Scott T. Lewis

Scott T. Lewis

Executive Vice President and

Chief Financial Officer

(Principal Financial and Accounting

Officer and Acting Principal

Executive Officer)

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ANNUAL REPORT ON FORM 10-K

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FORWARD LOOKING STATEMENTS

Certain Statements in this Form 10-K are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, and Section 21E of the Securities Exchange Act of 1934. The words estimate, plan, intend, expect, anticipate, believe, and similar expressions are intended to identify forward-looking statements. The forward-looking statements are found at various places throughout this Report and in the documents incorporated herein by reference. The Company disclaims any intention or obligations to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Although we believe that our expectations are based upon reasonable assumptions, we can give no assurance that our goals will be achieved. Important factors that could cause our actual results to differ from estimates or projections contained in any forward-looking statements are described under Risk Factors Related to ARI s Business beginning on page 5.

PART I

ITEM 1. *BUSINESS*

The predecessor to American Realty Investors, Inc. (ARI or the Company or we or us) was organized in 1961 to provide investors with a professionally managed, diversified portfolio of equity real estate and mortgage loan investments selected to provide opportunities for capital appreciation as well as current income.

On October 23, 2001, ARI, Transcontinental Realty Investors, Inc. (TCI), and Income Opportunity Realty Investors, Inc. (IORI) jointly announced a preliminary agreement with the plaintiff s legal counsel of the derivative action entitled *Olive et al. V. National Income Realty Trust, et al.* for a complete settlement of all disputes in the lawsuit (the Olive Litigation). In February 2002, the court granted final approval of the proposed settlement (the Olive Settlement). Under the Olive Settlement, ARI agreed to either (i) acquire all of the outstanding shares of IORI and TCI not currently owned by ARI for a cash payment or shares of ARI preferred stock or (ii) make a tender offer for all of the outstanding shares of IORI and TCI not currently owned by ARI. On November 15, 2002, ARI commenced the tender offers for the IORI and TCI shares. The tender offers were completed on March 19, 2003. ARI paid $19.00 cash per IORI share and $17.50 cash per TCI share for the stock held by unaffiliated stockholders. Pursuant to the tender offers, ARI subsidiaries acquired 265,036 IORI shares and 1,213,226 TCI shares. The completion of the tender offer fulfilled the obligations under the Olive Settlement, and the Olive Litigation originally filed in February 1990 was dismissed with prejudice.

After the tender offer, ARI subsidiaries owned 64.8% of the outstanding shares of TCI and 62.5% of the outstanding shares of IORI (46.9% owned directly by ARI subsidiaries and 15.6% through TCI s ownership of IORI shares). ARI began consolidation of TCI s and IORI s accounts and operations effective March 31, 2003. The effect of consolidating TCI s and IORI s operations from the completion of the tender offer through March 31, 2003 was determined to be immaterial. Through June 30, 2003, ARI had the same advisor as TCI and IORI, and TCI and IORI had the same board of directors. At December 31, 2004, ARI and TCI have the same Board of Directors, and one director of ARI (Ted Stokely) serves as a director of IORI. Effective July 1, 2003, ARI and TCI have the same advisor.

On June 2, 2003, ARI subsidiaries exchanged all of their 674,971 IORI shares with Basic Capital Management, Inc. (BCM), receiving 650,000 TCI shares from BCM. After the exchange, ARI subsidiaries owned 72.9% of the outstanding shares of TCI. On June 30, 2003, ARI sold a participating interest in $5.8 million of its $15.5 million line of credit receivable from One Realco Corporation (One Realco) to BCM, receiving 314,141 TCI shares from BCM (See NOTE 3. NOTES AND INTEREST RECEIVABLE). After the transaction, ARI subsidiaries owned 76.8%

of the outstanding shares of TCI. In December 2003, ARI subsidiaries purchased 88,600 TCI shares in open market transactions and 204,633 TCI shares in transactions with related parties for a total of $1.4 million. At December 31, 2004, ARI subsidiaries owned 82.2% of the outstanding shares of TCI. ARI no longer directly owns any IORI shares. At December 31, 2004, TCI owned 24.0% of IORI shares. ARI ceased consolidation of IORI s accounts and operations effective June 2, 2003.

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Effective July 1, 2003, Prime Asset Management, Inc. (PAMI) became the advisor to ARI and TCI. PAMI is owned by Realty Advisors, Inc. (80%) and Syntek West, Inc. (Syntek West) (20%), related parties. Syntek West is owned by Gene Phillips. Effective August 18, 2003, PAMI changed its name to Prime Income Asset Management, Inc. (PIAMI). On October 1, 2003, Prime Income Asset Management, LLC (Prime), which is 100% owned by PIAMI, replaced PIAMI as the advisor to ARI and TCI.

Business Plan and Investment Policy

ARI s primary business is investing in equity interests in real estate (including equity securities of real estate-related entities), leases, joint venture development projects, and partnerships and, to a lesser extent, financing real estate and real estate activities through investments in mortgage loans, including first, wraparound and junior mortgage loans. Information regarding the real estate and mortgage notes receivable portfolios of ARI is set forth in ITEM 2. PROPERTIES, NOTE 3. NOTES AND INTEREST RECEIVABLE and in Schedules III and IV to the Consolidated Financial Statements included in ITEM 8. CONSOLIDATED FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA. ARI has six operating segments: apartments, commercial properties, hotels, land ownership, quick-service restaurants, and notes receivables. See NOTE 18 OPERATING SEGMENTS to the Consolidated Financial Statements.

ARI s business objective is to maximize long-term profitability for its stockholders by investing in commercial real estate through the ownership, management, development, and acquisition of apartments, commercial properties, hotels, and land. ARI intends to achieve this objective through offering properties in multiple markets and operating as a leading landlord within the industry. ARI believes that this objective will provide the benefits of enhanced investment opportunities, economies of scale, risk diversification, both in terms of geographic market and real estate product type, and access to capital. In pursuing its business objective, ARI seeks to achieve a combination of internal and external growth, maintain a strong balance sheet, and pursue a strategy of financial flexibility. When ARI s marketing efforts identify opportunities, ARI will in appropriate instances, pursue those opportunities. ARI seeks to maximize the profitability of its apartments and commercial properties by endeavoring to maintain high occupancy levels while obtaining competitive rental rates, controlling costs and focusing on customer service efforts.

Current general economic conditions have resulted in downward pressure on rental rates, and market rental rates have declined on a year-to-year basis. ARI seeks to generate increased cash flow from apartments and commercial properties in operation through annual contractual increases in rental rates under leases. ARI also seeks to identify the best practices across operating platforms in order to enhance cost savings and other efficiencies. ARI and its subsidiaries employ an annual capital improvement and preventive maintenance program designed to reduce the operating costs of the apartments and commercial properties and maintain the long-term value of those real estate assets.

ARI also pursues attractive development opportunities, focusing primarily upon new construction or development, either directly or in concert with unaffiliated parties or affiliates. A summary of the properties under construction is set forth under ITEM 2. PROPERTIES below.

ARI also seeks to acquire properties consistent with its business objectives and strategies. ARI executes its acquisition strategy by purchasing properties which management believes will create stockholder value over the long-term. During the year ended December 31, 2004, ARI, through its subsidiaries, acquired 19 properties and disposed of 31 properties. ARI s subsidiaries dispose of properties and land held for development, which no longer fit within ARI s business plan or with respect to which management believes it can optimize cash proceeds.

Although ARI seeks to maximize long-term profitability for its stockholders through the development, acquisition and disposition of properties, ARI intends to continue to pursue its development, acquisition and disposition strategies. ARI at all times, and currently, is in various stages of discussions and negotiations with

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respect to development, acquisition and disposition projects. The consummation of any current or future development, acquisition or disposition, if any, and the pace at which any may be completed cannot be assured or predicted.

Substantially all properties are owned by separate subsidiaries of ARI, many of which are single-asset entities. This structure permits greater access to financing for individual properties and permits flexibility in the type of transaction available for future disposition of each property by permitting a sale of either the asset or the equity ownership in the entity owning the asset. From time-to-time, subsidiaries have invested in joint ventures with others, which creates the possibility of risks that do not exist with properties solely owned by an ARI subsidiary. In those instances where other participants are involved, those other participants may, at any time, have business, economic or other objectives that are inconsistent with ARI s objectives, which may require a different action for the operation or ultimate disposition of the asset in question.

Real estate generally cannot be sold quickly. ARI and its subsidiaries may not be able to dispose of properties promptly in response to economic or other conditions. To offset this challenge, selective dispositions have been a part of ARI s strategy to create an efficient portfolio and provide additional sources of capital for future use. See the discussion under LIQUIDITY AND CAPITAL RESOURCES in MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS for information concerning sales of properties during the past three years. Similarly, ARI and its subsidiaries finance acquisitions at times through non-recourse mortgages, internally generated funds, and to a lesser extent, property sales. Those sources provide the bulk of funds for future acquisitions. ARI, from time-to-time, acquires properties subject to existing indebtedness by a subsidiary assuming such indebtedness. When properties are acquired in such manner, ARI and its subsidiaries customarily seek to refinance the asset in order to properly leverage the asset for future operation.

ARI, through its subsidiary, Milano Restaurants International Corporation (MRI), operates and franchises several quick-service restaurant concepts including pizzerias featuring pizza delivery, carryout and dine-in under the trademarks Me-N-Ed s Pizzerias, Me-N-Ed s Slices, and Angelo & Vito s Pizzerias. The first Me-N-Ed s Pizzeria opened in 1958. At December 31, 2004, there were 60 restaurants in operation, consisting of 41 owned and 19 franchised. Two of the restaurants were located in Texas and the remainder were in California. In addition to the Pizzerias, MRI has developed two new concepts: Pizzeria del Pane, a bakery/café concept and Zia Mia s Cucina Italiana, a full service Italian restaurant. The initial locations for each of the concepts opened in 2004.

ARI s businesses are not seasonal. With regard to real estate investments, ARI is seeking both current income and capital appreciation. ARI s plan of operation is to continue, to the extent its liquidity permits, to make equity investments in income producing real estate such as hotels, apartments, or commercial properties, or equity securities of real estate-related entities. ARI also intends to continue to pursue higher risk, higher reward investments, such as improved and unimproved land where it can obtain financing of substantially all of a property s purchase price. ARI intends to seek selected dispositions of certain of its assets, in particular, selected income producing properties in stabilized markets and certain of its land holdings where the prices obtainable for such assets justify their disposition. ARI has determined that it will no longer actively seek to fund or purchase mortgage loans. However, it may, in selected instances, originate mortgage loans or it may provide purchase money financing in conjunction with a property sale. See ITEM 2. PROPERTIES, NOTE 3. NOTES AND INTEREST RECEIVABLE and Schedules III and IV to the Consolidated Financial Statements included in ITEM 8. CONSOLIDATED FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

ARI s Board of Directors has broad authority under ARI s governing documents to make all types of investments, and may devote available assets to particular investments or types of investments, without restriction on the amount or percentage of assets that may be allocated to a single investment or to any particular type of investment, and without limit on the percentage of securities of any one issuer that may be acquired. Investment objectives and policies may be changed at any time by the Board without stockholder approval.

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The specific composition from time-to-time of ARI s real estate portfolio owned through subsidiaries depends largely on the judgment of management as to changing investment opportunities and the level of risk associated with specific investments or types of investments. Management intends to attempt to maintain a real estate portfolio diversified by location and type of property.

In addition to its equity investments in real estate, ARI and/or its subsidiaries have also invested in private and open market purchases of the equity securities of IORI and TCI, both affiliates of ARI. See ITEM 2. PROPERTIES Investments in Real Estate Companies.

Risk Factors Related to ARI s Business

Adverse events concerning existing tenants, or negative market conditions that may affect existing tenants could have an adverse impact on ARI s ability to attract new tenants, relet space, collect rent or renew leases, and thus could adversely affect cash flow from operations and inhibit growth. Cash flow from operations depends on the ability to lease space to tenants on economically favorable terms. ARI could be adversely affected by various facts and events over which there is limited control, such as:

- lack of demand for space in areas where the properties are located;
- inability to retain existing tenants and attract new tenants;
- oversupply of or reduced demand for space and changes in market rental rates;
- defaults by tenants or failure to pay rent on a timely basis;
- the need to periodically renovate and repair marketable space;
- physical damage to properties;
- economic or physical decline of the areas where properties are located;
- potential risk of functional obsolescence of properties over time.

At any time, any tenant may experience a downturn in its business that may weaken its financial condition. As a result, a tenant may delay a lease commencement, fail to make rental payments when due, decline to extend a lease upon its expiration, become insolvent or declare bankruptcy. Any tenant bankruptcy or insolvency, leasing delay or failure to make rental payments when due could result in the termination of the tenant s lease and material losses to the Company.

If tenants do not renew their leases as they expire, ARI may not be able to rent the space. Furthermore, leases that are renewed, and some new leases for space that is relet, may have terms that are less economically favorable than current lease terms, or may require ARI to incur significant costs, such as renovations, tenant improvements, or lease transaction costs.

Any of these events could adversely affect cash flow from operations and ARI s ability to make expected distributions to shareholders and service indebtedness.

A significant portion of the costs, such as real estate taxes, insurance costs, and debt service payments, generally are not reduced when circumstances cause a decrease in cash flow from the properties.

ARI may not be able to compete successfully with other entities that operate in our industry. ARI experiences a great deal of competition in attracting tenants for the properties and in locating land to develop and properties to acquire.

In ARI s effort to lease these properties, ARI competes for tenants with a broad spectrum of other landlords in each of the markets. These competitors include, among others, publicly-held REITs, privately-held entities, individual property owners and tenants who wish to sublease their space. Some of these competitors may be able to offer prospective tenants more attractive financial terms than ARI is able to offer.

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If the availability of land or high quality properties in ARI s markets diminishes, operating results could be adversely affected.

ARI may experience increased operating costs, which could adversely affect our operations. ARI s properties are subject to increases in operating expenses such as insurance, cleaning, electricity, heating, ventilation and air conditioning, administrative costs and other costs associated with security, landscaping, repairs, and maintenance of the properties. While current tenants generally are obligated to pay a significant portion of these costs, there is no assurance that these tenants will make such payments or agree to pay these costs upon renewal or new tenants will agree to pay these costs. If operating expenses increase in ARI s markets, ARI may not be able to increase rents or reimbursements in all of these markets to meet increased expenses, without at the same time decreasing occupancy rates. If this occurs, ARI s ability to make distributions to shareholders and service indebtedness could be adversely affected.

ARI s ability to achieve growth in operating income depends in part on the ability to develop properties, which may suffer under certain circumstances. ARI intends to continue to develop properties where warranted by market conditions. The decline in demand for real estate has reduced the amount of development ARI is undertaking. ARI has a number of ongoing development and land projects being readied for development.

Additionally, general construction and development activities include the following risks:

- construction and leasing of a property may not be completed on schedule, which could result in increased expenses and construction costs, and would result in reduced profitability for that property;

- construction costs may exceed original estimates due to increases in interest rates and increased materials, labor or other costs, possibly making the property unprofitable because of inability to increase rents to compensate for the increase in construction costs;

- some developments may fail to achieve expectations, possibly making them unprofitable;

- ARI may be unable to obtain, or face delays in obtaining, required zoning, land-use, building, occupancy, and other governmental permits and authorizations, which could result in increased costs and could require ARI to abandon their activities entirely with respect to a project;

- ARI may abandon development opportunities after the initial exploration, which may result in failure to recover costs already incurred. If ARI determines to alter or discontinue its development efforts, future costs of the investment may be expensed as incurred rather than capitalized and ARI may determine the investment is impaired resulting in a loss;

- ARI may expend funds on and devote management s time to projects which we do not complete;

- occupancy rates and rents at newly-completed properties may fluctuate depending on a number of factors, including market and economic conditions, which may result in lower than projected rental rates with the result that the investment is not profitable.

ARI faces risks associated with property acquisitions. ARI acquires individual properties and portfolios of properties, and intends to continue to do so. The acquisition activities and their success are subject to the following risks:

when ARI is able to locate a desired property, competition from other real estate investors may significantly increase the purchase price;

acquired properties may fail to perform as expected;

the actual costs of repositioning or redeveloping acquired properties may be higher than the estimates;

acquired properties may be located in new markets where ARI faces risks associated with an incomplete knowledge or understanding of the local market, a limited number of established business relationships in the area and a relative unfamiliarity with local governmental and permitting procedures;

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ARI may be unable to quickly and efficiently integrate new acquisitions, particularly acquisitions of portfolios of properties, into existing operations, and results of operations and financial condition could be adversely affected.

ARI may acquire properties subject to liabilities and without any recourse, or with only limited recourse, with respect to unknown liabilities. As a result, if a liability were asserted against ARI based upon ownership of those properties, ARI might have to pay substantial sums to settle it, which could adversely affect cash flow.

Many of ARI s properties are concentrated in our primary markets, and may suffer economic harm as a result of adverse conditions in those markets. ARI s properties are located principally in specific geographic areas in the Southwestern, Southeastern, and Midwestern United States. Due to the concentration of properties in these areas, performance is dependent on economic conditions. These areas have experienced periods of economic decline.

ARI is highly leveraged and may not be able to meet our debt service obligations. ARI had total indebtedness at December 31, 2004 of approximately $958.6 million. Substantially all assets have been pledged to secure debt. These borrowings increase the risk of loss because they represent a prior claim on assets and require fixed payments regardless of profitability. ARI s highly leveraged position makes it vulnerable to changes in economic conditions and may limit the ability to capitalize on significant business opportunities in the future.

The Company may not be able to access financial markets to obtain capital on a timely basis, or on acceptable terms. ARI relies on proceeds from property dispositions and third party capital sources for a portion of its capital needs, including capital for acquisitions and development. The public debt and equity markets are among the sources relied on. There is no guarantee ARI will be able to access these markets, or any other source of capital. The ability to access the public debt and equity markets depends on a variety of factors, including:

- general economic conditions affecting these markets;
- ARI s own financial structure and performance;
- the market s opinion of REITs and real estate companies in general;
- the market s opinion of REITs and real estate companies that own properties like ARI.

ARI may suffer adverse effects as a result of terms of and covenants relating to the Company s indebtedness. Required payments on ARI s indebtedness generally are not reduced if the economic performance of the portfolio declines. If the economic performance declines, net income, cash flow from operations and cash available for distribution to stockholders will be reduced. If payments on debt cannot be made, ARI could sustain a loss, or in the case of mortgages, suffer foreclosures by mortgagees or suffer judgments. Further, some obligations contain cross-default and/or cross-acceleration provisions, which means that a default on one obligation may constitute a default on other obligations.

ARI anticipates only a small portion of the principal of our debt will be repaid prior to maturity. Therefore, ARI is likely to need to refinance at least a portion of its outstanding debt as it matures. There is a risk that ARI may not be able to refinance existing debt or the terms of any refinancing will not be as favorable as the terms of the existing debt. If principal payments due at maturity cannot be refinanced, extended or repaid with proceeds from other sources, such as the proceeds of sales of assets or new equity securities, cash flow will not be sufficient to repay all maturing debt in years when significant balloon payments come due.

ARI s credit facilities and unsecured debt securities contain customary restrictions, requirements and other limitations on the ability to incur indebtedness, including total debt to asset ratios, secured debt to total asset ratios, debt service coverage ratios, and minimum ratios of unencumbered assets to unsecured debt, which ARI must maintain. ARI s continued ability to borrow is subject to compliance with financial and other covenants. In addition, failure to comply with such covenants could cause a default under credit facilities, and ARI may then be required to repay such debt with capital from other sources. Under those circumstances, other sources of capital may not be available, or be available only on unattractive terms.

The degree of leverage could affect ARI s ability to obtain additional financing for working capital, capital expenditures, acquisitions, development, or other general corporate purposes. The degree of leverage could also make ARI more vulnerable to a downturn in business or the economy or could affect the market price the common stock.

An increase in interest rates would increase interest costs on variable rate debt and could adversely impact the ability to refinance existing debt. ARI currently has, and may incur more, indebtedness that bears interest at variable rates. Accordingly, if interest rates increase, so will the interest costs, which would adversely affect cash flow and the ability to pay principal and interest on ARI s debt and the ability to make distributions to shareholders. Further, rising interest rates could limit ARI s ability to refinance existing debt when it matures.

Unbudgeted capital expenditures or cost overruns could adversely affect business operations and cash flow. If capital expenditures on ongoing or planned development projects, renovations, or condominium conversions exceed our expectations, the additional cost of these expenditures could have an adverse effect on business operations and cash flow. In addition, ARI might not have access to funds on a timely basis to meet the unexpected expenditures.

Construction costs are funded in large part through construction financing, which the Company often guarantees, and the Company s obligation to pay interest on this financing continues until the rental project is completed, leased up, and permanent financing is obtained, or the for sale project is sold out. Unexpected delays in completion of one or more ongoing projects could also have a significant adverse impact on business operations and cash flow.

ARI may need to sell properties from time-to-time for cash flow purposes. Because of the lack of liquidity of real estate investments generally, ARI s ability to respond to changing circumstances may be impaired. Real estate investments generally cannot be sold quickly. In the event that ARI must sell assets to generate cash flow, ARI cannot predict whether there will be a market for those assets in the time period desired or need to sell them, or whether ARI will be able to sell them at a price that will allow the Company to fully recoup the investment. ARI may not be able to realize the full potential value of the assets, and may incur costs related to the early pay-off of the debt secured by such assets.

The Company intends to devote increasing resources to the development of new projects. ARI plans to continue developing new projects as opportunities arise in the future. Development and construction activities entail a number of risks, including but not limited to the following:

- ARI may abandon a project after spending non-recoverable time and money determining its feasibility;

- Construction costs may materially exceed original estimates;

- The revenue from a new project may not be enough to make it profitable or generate a positive cash flow;

ARI may not be able to obtain financing on favorable terms for development of a property, if at all;

The Company may not complete construction and lease-ups on schedule, resulting in increased development or carrying costs;

ARI may not be able to obtain, or may be delayed in obtaining, necessary governmental permits.

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The overall business is subject to all of the risks associated with the real estate industry. ARI is subject to all risks incident to investment in real estate, many of which relate to the general lack of liquidity of real estate investments, including, but not limited to:

- changes in general or local economic conditions: because ARI s real estate assets are concentrated in the Southwest, Southeast, and Midwest any deterioration in the general economic conditions in any of those states could have an adverse effect on business and assets in that state;
- changes in interest rates may make the ability to satisfy debt service requirements materially more burdensome;
- lack of availability of financing may render the purchase, sale or refinancing of a property more difficult or unattractive;
- changes in real estate and zoning laws;
- increases in real estate taxes and insurance costs;
- federal or local economic or rent control, and
- floods, earthquakes and other similar natural disasters.

Risks Related to the Real Estate Industry

Real estate investments are illiquid, and the Company may not be able to sell our properties if and when we determine it is appropriate to do so. Real estate generally cannot be sold quickly. ARI may not be able to dispose of properties promptly in response to economic or other conditions. In addition, provisions of the Internal Revenue Code limit ARI s ability to sell properties in some situations when it may be economically advantageous to do so, thereby adversely affecting returns to stockholders and adversely impacting the ability to meet ARI s obligations to the holders of other securities.

Management of the Company

Although the Board of Directors is directly responsible for managing the affairs of ARI and for setting the policies, which guide it, its day-to-day operations are performed by Prime, a contractual advisor under the supervision of the Board. The duties of Prime include, among other things, locating, investigating, evaluating, and recommending real estate and mortgage note investments and sales opportunities, as well as financing and refinancing sources. Prime also serves as a consultant in connection with ARI s business plan and investment policy decisions made by the Board. Prime is indirectly owned by Gene E. Phillips (20%) and by a trust for the children of Gene E. Phillips (80%). Mr. Phillips is not an officer or director of Prime, but serves as a representative of the trust, is involved in daily consultation with the officers of Prime, and has significant influence over the conduct of Prime s business, including the rendering of advisory services and the making of investment decisions for itself and ARI. As of March 24, 2005, PIAMI, Prime s parent, owned 1,437,208 shares of ARI s Common Stock, approximately 13.2% of the shares then outstanding. Prime is more fully described in ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND ADVISOR OF THE

REGISTRANT The Advisor.

Prime has been providing advisory services to ARI since October 1, 2003. Prime also serves as advisor to TCI. The officers of ARI are also officers of IORI, TCI, and Prime. The directors of ARI also serve as directors of TCI. The Chairman of the Board of Directors of ARI also serves as the Chairman of the Board of Directors of TCI and IORI. Affiliates of Prime have provided property management services to ARI. Currently, Triad Realty Services, Ltd. (Triad), an affiliate, and Carmel Realty, Inc. (Carmel) provide such property management services. Triad and Carmel subcontract with other entities for property-level management services. The general partner of Triad is BCM. The limited partner of Triad is Highland Realty Services, Inc. (Highland). Triad subcontracts the property-level management and leasing of 30 of ARI s commercial properties (shopping centers, office buildings and industrial warehouses) to Regis Realty I, LLC (Regis I) which is owned by Highland.

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Regis I receives property and construction management fees and leasing commissions in accordance with the terms of its property-level management agreement with Triad. Since January 1, 2003, Regis Hotel I, LLC, has managed ARI s 11 hotels. The sole member of Regis I and Regis Hotel I, LLC is Highland. Carmel is a company previously owned by First Equity Properties, Inc., which is a company affiliated with Prime. On May 1, 2004, Regis I acquired the ownership of Carmel.

Regis I is also entitled to receive real estate brokerage commissions in accordance with the terms of the Advisory Agreement as discussed in ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND ADVISOR OF THE REGISTRANT The Advisor.

ARI has no employees itself, but MRI has 843 employees. Employees of Prime render services to ARI.

Competition

Real Estate. The real estate business is highly competitive, and ARI competes with numerous entities engaged in real estate activities (including certain entities described in ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS Related Party Transactions), some of which have greater financial resources than ARI. Management believes that success against such competition is dependent upon the geographic location of the property, the performance of property-level managers in areas such as marketing, collections and control of operating expenses, the amount of new construction in the area, and the maintenance and appearance of the property. Additional competitive factors with respect to commercial properties are the ease of access to the property, the adequacy of related facilities, such as parking, and sensitivity to market conditions in setting rent levels. With respect to apartments, competition is also based upon the design and mix of the units and the ability to provide a community atmosphere for the tenants. With respect to hotels, competition is also based upon the market served, i.e., transient, commercial or group users. Management believes that beyond general economic circumstances and trends, the rate at which properties are renovated or the rate new properties are developed in the vicinity of each of ARI s properties, in particular its improved and unimproved land, are also competitive factors. See also Risk Factors Related to ARI s Business.

To the extent that ARI seeks to sell any of its properties, the sales prices for the properties may be affected by competition from other real estate entities and financial institutions, also attempting to sell properties in areas where ARI s properties are located, as well as aggressive buyers attempting to dominate or penetrate a particular market.

As described above and in ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS Related Party Transactions, the officers of ARI also serve as officers of IORI (with the exception of the CFO) and TCI, both of which have business objectives similar to ARI s. ARI s officers and advisor owe fiduciary duties to both IORI and TCI as well as to ARI under applicable law. In determining whether a particular investment opportunity will be allocated to ARI, IORI, or TCI, management and the advisor consider the respective investment objectives of each and the appropriateness of a particular investment in light of the existing real estate and mortgage notes receivable portfolios of each. To the extent that any particular investment opportunity is appropriate to more than one of the entities, the investment opportunity will be allocated to the entity, which has had funds available for investment for the longest period of time, or, if appropriate, the investment may be shared among all or some of the entities.

In addition, also as described in ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, ARI competes with entities, which are affiliates of Prime having similar investment objectives in the purchasing, selling, leasing, and financing of real estate and real estate-related investments. In resolving any potential conflicts of interest which may arise, Prime has informed ARI that it intends to continue to exercise its best judgment as to what is fair and reasonable under the circumstances in accordance with applicable law.

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ARI is subject to all the risks incident to ownership and financing of real estate and interests therein, many of which relate to the general illiquidity of real estate investments. These risks include, but are not limited to, changes in general or local economic conditions, changes in interest rates and availability of permanent mortgage financing which may render the purchase, sale, or refinancing of a property difficult or unattractive, and which may make debt service burdensome, changes in real estate and zoning laws, increases in real estate taxes, federal or local economic or rent controls, floods, earthquakes, hurricanes and other acts of God and other factors beyond the control of management or the advisor. The illiquidity of real estate investments may also impair the ability of management to respond promptly to changing circumstances. Management believes that such risks are partially mitigated by the diversification by geographic region and property type of ARI s real estate and mortgage notes receivable portfolios. However, to the extent that property sales, new property investments, in particular improved and unimproved land, or mortgage lending are concentrated in any particular region, the advantages of geographic diversification are mitigated.

Virtually all of ARI s real estate, equity security holdings in IORI and TCI and its portfolio of equity securities are held subject to secured indebtedness. Such borrowings increase the risk of loss because they represent a prior claim on ARI s assets and require fixed payments regardless of profitability. In the event of default, the lender may foreclose on the assets securing such indebtedness, and ARI could lose its investment in the pledged assets.

Pizza Parlors. The pizza parlor business is highly competitive and is affected by changes in consumer tastes and eating habits, as well as national, regional, and local economic conditions, and demographic trends. The performance of an individual pizza parlor can be affected by changes in traffic patterns, demographics, and the type, number and location of competing restaurants.

The quick-service restaurant industry is extremely competitive with respect to price, service, location, and food quality. MRI and its franchisees compete with a variety of other restaurants in the quick-service restaurant industry; including those that offer dine-in, carryout, and delivery services. These competitors include national and regional chains, franchisees of other restaurant chains, and local owner-operated restaurants. Some of these competitors have been in existence longer and have an established market presence in certain geographic regions, and some have substantially greater financial, marketing, and other resources than MRI and its franchisees. MRI competes for qualified franchisees with many other restaurant concepts, including national and regional restaurant chains.

MRI s success is largely dependent upon the efforts of its management and other key personnel. The loss of the service of one or more members of management could have an adverse effect on MRI s operations. Significant transitions in management involve important risks, including potential loss of key personnel, difficulties in implementing changes to operational strategies and maintaining relationships with franchisees.

At December 31, 2004, MRI owned and operated 41 and franchised 19 pizza parlors. The results achieved by MRI s relatively small pizza parlor base may not be indicative of the results of a larger number of pizza parlors in a more geographically dispersed area. Because of MRI s relatively small pizza parlor base, an unsuccessful pizza parlor has a more significant effect on MRI s results of operations than would be the case in a company owning more pizza parlors.

MRI s existing pizza parlors, both owned and franchised, are located in California or Texas. At December 31, 2004, there were 58 pizza parlors in California and two in Texas. Accordingly, MRI s results of operations may be affected by economic or other conditions in those regions. Also, given MRI s present geographic concentration, publicity relating to MRI s pizza parlors could have a more pronounced effect on MRI s overall sales than might be the case if MRI s pizza parlors were geographically dispersed.

All of MRI s owned pizza parlors are operated on premises leased from third parties. Most of the pizza parlor leases provide for a minimum annual rent. There can be no assurance that MRI will be able to renew leases

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upon expiration or that the lease terms on renewal will be as favorable as the current lease terms. In 2004, MRI closed one company-owned store, opened two new franchise stores, reopened a remodeled franchised store, with two franchise stores leaving the system. In 2005, three new franchise stores are scheduled to open.

In July 2003, ARI sold its interest in MRI to Gruppa Florentina, LLC (Gruppa), for $18.5 million, receiving $7.4 million in cash after debt assumption and providing purchase money financing of $2.3 million. ARI owns 20.0% of Gruppa, thereby retaining a 20.0% interest in MRI. ARI remains as the guarantor of $8.7 million of assumed debt and is one of the guarantors of $7.5 million in new debt obtained by Gruppa. Due to the debt guarantees and ARI s continuing ownership interest in MRI, management has determined that this should be accounted for as a financing transaction. In September 2003, ARI sold the note to Syntek West for $2.3 million, plus accrued and unpaid interest, to reduce affiliate debt.

Available Information

ARI maintains an internet site at http://www.amrealtytrust.com. Available through the website, free of charge, are Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, reports filed pursuant to Section 16, and amendments to those reports as soon as reasonably practicable after they are electronically filed or furnished to the Securities and Exchange Commission. In addition, ARI has posted the charters for the Audit Committee, Compensation Committee, and Governance and Nominating Committee, as well as the Code of Business Conduct and Ethics, Corporate Governance Guidelines on Director Independence, and other information on the website. These charters and principles are not incorporated in this Report by reference. ARI will also provide a copy of these documents free of charge to stockholders upon written request. ARI issues Annual Reports containing audited financial statements to its common stockholders.

ITEM 2. *PROPERTIES*

ARI s principal offices are located at 1800 Valley View Lane, Suite 300, Dallas, Texas 75234 and are, in the opinion of management, suitable and adequate for ARI s present operations.

Details of ARI s and its subsidiaries real estate and mortgage notes receivable portfolios at December 31, 2004, are set forth in SCHEDULES III and IV, respectively, to the Consolidated Financial Statements included in ITEM 8. CONSOLIDATED FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA. The discussions set forth below under the headings Real Estate and Mortgage Loans provide certain summary information concerning ARI s real estate and mortgage notes receivable portfolios.

At December 31, 2004, no single asset accounted for 10.0% or more of total assets. At December 31, 2004, 82.6% of ARI s assets consisted of real estate, and 6.1% consisted of notes and interest receivable. The remaining 11.3% of ARI s assets were cash, cash equivalents, marketable equity securities, pizza parlor equipment, investments in equity investees, goodwill and other intangibles, and other assets. The percentage of assets invested in any one category is subject to change and no assurance can be given that the composition of ARI s assets in the future will approximate the percentages listed above.

ARI s real estate is geographically diverse, with concentrations in the Southwest, Southeast, and Midwest regions. At December 31, 2004, ARI s real estate was located in all geographic regions of the continental United States, other than the Northeast region, as shown more specifically in the table under Real Estate below. ARI also holds mortgage notes receivable secured by real estate located in the Southwest, Southeast, Pacific and Midwest regions of the continental United States. See SCHEDULE IV to the Consolidated Financial Statements included in ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA for a detailed description of ARI s notes receivable portfolio.

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Geographic Regions

Excluded from above are 78 parcels of improved and unimproved land, and a single-family residence, as described below.

Real Estate

At December 31, 2004, 83.1% of ARI s assets were invested in real estate and the equity securities of IORI. ARI invests in real estate located throughout the continental United States, either on a leveraged or non-leveraged basis. ARI s real estate portfolio consists of properties held for investment, properties held for sale, investments in partnerships, and investments in equity securities of IORI.

Types of Real Estate Investments. ARI s real estate consists of apartments, commercial properties (office buildings, industrial warehouses, shopping centers, and a merchandise mart), hotels, and improved and unimproved land. In selecting real estate for investment, the location, age and type of property, gross rents, lease terms, financial and business standing of tenants, operating expenses, fixed charges, land values, and physical condition are among the factors considered. Properties may be purchased subject to debt, or existing debt may be assumed and properties may be mortgaged, pledged or otherwise collateralized to obtain financing. The Board of Directors may alter the types of and criteria for selecting new real estate investments and for obtaining financing without a vote of stockholders.

Although ARI has typically invested in developed real estate, it may also invest in new construction or development either directly or in partnership with unaffiliated parties or affiliates (subject to approval by the Board of Directors). To the extent that it invests in construction and development projects, such as the apartments described below, ARI is subject to business risks, which include cost overruns and construction delays, associated with higher risk projects.

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At December 31, 2004, ARI had the following properties under construction:

Property	Location	Units	Amount Expended	Additional Amount to Expend	Construction Loan Funding
Apartments					
Blue Lake Villas II	Waxahachie, TX	76 Units	$ 4,454	$ 217	$ 4,234
Bluffs at Vista Ridge	Lewisville, TX	272 Units	17,239	3,347	15,500
Bridges on Kinsey	Tyler, TX	232 Units	11,572	4,509	14,477
Dakota Arms	Lubbock, TX	208 Units	12,611	1,326	12,549
Kingsland Ranch	Houston, TX	398 Units	24,573	1,081	23,000
Laguna Vista	Farmers Branch, TX	206 Units	3,432	17,673	17,741
Lake Forest	Houston, TX	240 Units	13,919	519	12,815
Parc at Maumelle	Maumelle, AR	240 Units	4,502	14,196	16,829
Stonebridge at City Park (formerly 288 City Park)	Houston, TX	240 Units	15,486	1,201	15,005
Vistas of Vance Jackson	San Antonio, TX	240 Units	13,393	4,708	16,056
Wildflower Villas	Temple, TX	220 Units	9,377	6,220	14,073

In 2004, ARI completed the 248 unit DeSoto Ranch Apartments in DeSoto, Texas, the 314 unit Verandas at Cityview Apartments in Fort Worth, Texas, the 216 unit Mariposa Villas (Echo Valley) in Dallas, Texas, the 176 unit Breakwater Bay Apartments in Beaumont, Texas, the 156 unit Capitol Hill Apartments in Little Rock, Arkansas and the 332 unit Vistas of Pinnacle Park Apartments in Dallas, Texas.

In the opinion of management, the properties owned by ARI are adequately covered by insurance.

The following table sets forth the percentages, by property type and geographic region, of owned real estate (excluding 78 parcels of improved and unimproved land, a hotel in Wroclaw, Poland and a single-family residence, described below) at December 31, 2004.

Region	Apartments	Commercial Properties	Hotels
Midwest	5%	15%	11%
Mountain		19	11
Pacific		1	49
Southeast	10	10	29
Southwest	85	55	
	100%	100%	100%

The foregoing table is based solely on the number of apartment units, amount of commercial square footage, and number of hotel rooms owned, and does not reflect the value of ARI s investment in each region. See SCHEDULE III to the Consolidated Financial Statements included in ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA for a detailed description of owned real estate.

Excluded from the table above are a 165 room hotel in Wroclaw, Poland, a single family residence in Dallas, Texas, and 78 parcels of improved and unimproved land consisting of: four parcels in Austin, Texas, totaling 484.2 acres; a 7.6 acre parcel in Carrollton, Texas; two parcels in Collin County, Texas, totaling 53.1 acres; seven parcels in Dallas County, Texas, totaling 392.4 acres; six parcels in Dallas, Texas, totaling 61.1 acres; a 13.9 acre parcel in Denton, Texas; a 105.4 acre parcel in Denton County, Texas; a 202.0 acre parcel in Desoto, Texas; 18 parcels in Farmers Branch, Texas, totaling 494.8 acres; a 18.9 acre parcel in Fort Wayne, Indiana; a 4.7 acre parcel in Fruitland Park, Florida; four parcels in Ft. Worth, Texas, totaling 86.3 acres; a 13.9 acre parcel in Grand Prairie, Texas; a 130.6 acre parcel in Harris County, Texas; two parcels in Houston, Texas,

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totaling 38.2 acres; a 16.9 acre parcel in Humble, Texas; four parcels in Irving, Texas, totaling 39.9 acres; a 52.9 acre parcel in Kent, Ohio; six parcels in Las Colinas, Texas, totaling 351.2 acres; a 79.0 acre parcel in Lewisville, Texas; a 2.9 acre parcel in Lubbock, Texas; a 10.8 acre parcel in Maumelle, Arkansas; a 127.4 acre parcel in Nashville, Tennessee; a 0.4 acre parcel in New Orleans, Louisiana; a 110.05 acre parcel in Palm Desert, California; a 11.8 acre parcel in Plano, Texas; a 21.9 acre parcel in Pulaski County, Arkansas; a 20.1 acre parcel in Rogers, Arkansas; a 0.7 acre parcel in San Angelo, Texas; a 20.7 acre parcel in Siskiyou County, California; a 4.0 acre parcel in Springfield, Virginia; two parcels in Tarrant County, Texas, totaling 31.3 acres; and a 63.3 acre parcel in Travis County, Texas. See SCHEDULE III to the Consolidated Financial Statements included in ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA for a detailed description of ARI s real estate portfolio.

A summary of the activity in the owned real estate portfolio during 2004 is as follows:

Owned properties at January 1, 2004	216
Properties purchased (excluding additions to existing land parcels)	19
Properties sold (excluding partial sales)	(31)
Owned properties at December 31, 2004	204

Operating Properties. Set forth below are ARI s operating properties and the monthly rental rate for apartments, the average annual rental rate for commercial properties, the average daily room rate and room revenue divided by total available rooms for hotels, and occupancy at December 31, 2004, 2003 and 2002 for apartments and commercial properties and average occupancy during 2004, 2003 and 2002 for hotels. The 2002 information for the properties added through the consolidation of TCI, as identified with (T) , is provided for comparative purposes only.

			Rent Per Square Foot			Occupancy %		
Property	**Location**	**Units/Square Footage**	**2004**	**2003**	**2002**	**2004**	**2003**	**2002**
Apartments								
4400 (T)	Midland, TX	92 Units/94,472 Sq. Ft.	$ .51	$ .49	$ .49	97	86	86
Apple Lane (T)	Lawrence, KS	75 Units/30,000 Sq. Ft.	1.08	1.05	1.04	100	100	93
Arbor Point (T)	Odessa, TX	195 Units/178,920 Sq. Ft.	.47	.45	.43	90	95	87
Arlington Place	Pasadena, TX	230 Units/205,476 Sq. Ft.	.76	.76	.75	97	97	94
Ashton Way (T)	Midland, TX	178 Units/138,964 Sq. Ft.	.45	.43	.43	95	87	82
Autumn Chase (T)	Midland, TX	64 Units/58,652 Sq. Ft.	.57	.55	.54	98	98	98
Bay Walk (T)	Galveston, TX	192 Units/153,120 Sq. Ft.	.75	.75	.74	90	95	95
Blue Lake Villas (T)	Waxahachie, TX	186 Units/169,746 Sq. Ft.	.91	.91	*	90	92	*
Bluffs at Vista Ridge (T)	Lewisville, TX	272 Units/257,432 Sq. Ft.	**	**	**	**	**	**
Breakwater Bay (T)	Beaumont, TX	176 Units/145.688 Sq. Ft.	.93	*	*	87	*	*
Bridgestone	Friendswood, TX	76 Units/65,519 Sq. Ft.	.74	.74	.74	96	96	92
By the Sea (T)	Corpus Christi, TX	153 Units/123,945 Sq. Ft.	.88	.88	.86	96	91	88
Capitol Hill (T)	Little Rock, AR	156 Units/151,116 Sq. Ft.	.88	*	*	70	*	*
Château	Bellevue, NE	115 Units/99,220 Sq. Ft.	.73	.73	.71	86	86	96
Château Bayou	Ocean Springs, MS	122 Units/105,536 Sq. Ft.	.67	.67	.67	94	94	94
Courtyard (T)	Midland, TX	133 Units/111,576 Sq. Ft.	.47	.46	.45	94	99	93
Coventry (T)	Midland, TX	120 Units/105,608 Sq. Ft.	.45	.44	.43	96	84	91
DeSoto Ranch (T)	DeSoto, TX	248 Units/240,718 Sq. Ft.	.95	.94	*	98	98	*

El Chapparal (T)	San Antonio, TX	190 Units/174,220 Sq. Ft.	.95	.73	.72	94	96	79
Fairway View Estates (T)	El Paso, TX	264 Units/204,000 Sq. Ft.	.65	.64	.63	90	96	92
Fairways (T)	Longview, TX	152 Units/134,176 Sq. Ft.	.59	.58	.56	96	93	92
Falcon Lakes (T)	Arlington, TX	284 Units/207,960 Sq. Ft.	.96	.96	.97	94	94	11
Fountain Lake (T)	Texas City, TX	166 Units/161,220 Sq. Ft.	.62	.62	.62	86	96	89
Fountains of Waterford (T)	Midland, TX	172 Units/129,200 Sq. Ft.	.55	.53	.53	96	99	85
Foxwood	Memphis, TN	220 Units/212,000 Sq. Ft.	.61	.61	.61	83	83	85
Governor s Square	Tallahassee, FL	169 Units/146,550 Sq. Ft.	.73	.73	.66	95	95	95
Harper s Ferry (T)	Lafayette, LA	122 Units/112,500 Sq. Ft.	.61	.60	.59	95	90	83

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Property	Location	Units/Square Footage	Rent Per Square Foot 2004	Rent Per Square Foot 2003	Rent Per Square Foot 2002	Occupancy % 2004	Occupancy % 2003	Occupancy % 2002
Heather Creek (T)	Mesquite, TX	200 Units/170,212 Sq. Ft.	$ .94	$ *	$ *	93	*	*
Hunters Glen (T)	Midland, TX	260 Units/174,180 Sq. Ft.	.42	.39	.38	93	94	81
Island Bay (T)	Galveston, TX	458 Units/374,784 Sq. Ft.	.83	.83	.81	93	91	90
Kingsland Ranch (T)	Houston, TX	398 Units/350,574 Sq. Ft.	**	**	**	**	**	**
Limestone Canyon (T)	Austin, TX	260 Units/216,000 Sq. Ft.	1.06	1.06	1.06	96	91	88
Limestone Ranch (T)	Lewisville, TX	252 Units/219,600 Sq. Ft.	.95	.94	.94	95	91	91
Longwood	Long Beach, MS	200 Units/187,048 Sq. Ft.	.58	.58	*	90	90	*
Marina Landing (T)	Galveston, TX	256 Units/205,504 Sq. Ft.	.83	.83	.82	92	95	96
Mariposa Villas (T)	Dallas, TX	216 Units/199,656 Sq. Ft.	.89	.89	*	95	97	*
Mediterranean Villas	San Antonio, TX	140 Units/158,960 Sq. Ft.	.56	.56	.55	92	92	84
Mountain Plaza (T)	El Paso, TX	188 Units/220,710 Sq. Ft.	.52	.52	.51	90	94	97
Oak Park IV (T)	Clute, TX	108 Units/78,708 Sq. Ft.	.56	.56	.56	93	91	95
Oak Tree	Grandview, MO	189 Units/160,591 Sq. Ft.	.66	.66	.65	93	93	89
Paramount Terrace (T)	Amarillo, TX	181 Units/123,840 Sq. Ft.	.61	.60	.59	91	93	91
Plantation (T)	Tulsa, OK	138 Units/103,500 Sq. Ft.	.61	.61	.61	90	92	0
Quail Oaks (T)	Balch Springs, TX	131 Units/72,848 Sq. Ft.	.83	.83	.83	95	95	85
Quail Pointe	Huntsville, AL	184 Units/202,602 Sq. Ft.	.46	.46	.47	91	91	90
River Oaks (T)	Wylie, TX	180 Units/164,604 Sq. Ft.	.86	.86	*	95	98	*
Sendero Ridge (T)	San Antonio, TX	384 Units/340,880 Sq. Ft.	1.02	1.01	*	94	80	*
Somerset (T)	Texas City, TX	200 Units/163,368 Sq. Ft.	.68	.68	.68	85	88	87
Southgate (T)	Odessa, TX	180 Units/151,656 Sq. Ft.	.46	.43	.43	98	93	90
Spy Glass (T)	Mansfield, TX	256 Units/239,264 Sq. Ft.	.96	.95	*	92	97	*
Sunchase (T)	Odessa, TX	300 Units/223,048 Sq. Ft.	.51	.49	.49	97	96	91
Sun Hollow	El Paso, TX	216 Units/156,000 Sq. Ft.	.74	.74	.72	92	92	91
Sunset	Odessa, TX	240 Units/160,400 Sq. Ft.	.50	.50	.47	100	100	89
Terrace Hills (T)	El Paso, TX	310 Units/233,192 Sq. Ft.	.70	.70	.69	94	96	93
Timbers (T)	Tyler, TX	180 Units/101,666 Sq. Ft.	.60	.60	.59	96	92	93
Tivoli (T)	Dallas, TX	190 Units/168,862 Sq. Ft.	.95	.95	.96	92	92	27
Treehouse (T)	Irving, TX	160 Unite/153,072 Sq. Ft.	.80	***	.80	96	***	94
Verandas at City View (T)	Fort Worth, TX	314 Units/295,170 Sq. Ft.	.92	.60	*	93	92	*
Villa Del Mar	Wichita, KS	162 Units/128,004 Sq. Ft.	.62	.62	.62	89	89	86
Villager	Ft. Walton, FL	33 Units/22,840 Sq. Ft.	.79	.79	.77	100	100	88
Vistas of Pinnacle Park (T)	Dallas, TX	332 Units/276,928 Sq. Ft.	.91	*	*	96	*	*
Waters Edge III	Gulfport, MS	238 Units/212,216 Sq. Ft.	.64	.64	.63	91	91	90
Waters Edge IV	Gulfport, MS	80 Units/76,400 Sq. Ft.	.76	.76	.76	94	94	74
Westwood	Mary Ester, FL	120 Units/93,000 Sq. Ft.	.74	.74	.72	100	100	98
Westwood (T)	Odessa, TX	79 Units/49,001 Sq. Ft.	.46	.44	.49	91	100	80
Whispering Pines	Topeka, KS	320 Units/299,264 Sq. Ft.	.55	.55	.54	91	91	91
Willow Creek (T)	El Paso, TX	112 Units/103,140 Sq. Ft.	.58	.57	.55	97	96	94
Willo-Wick Gardens (T)	Pensacola, FL	152 Units/153,360 Sq. Ft.	.55	.55	.54	95	91	84
Windsong (T)	Ft. Worth, TX	188 Units/169,464 Sq. Ft.	.89	*	*	91	*	*
Windsor Tower	Ocala, FL	64 Units/66,000 Sq. Ft.	.56	.56	.55	98	98	97
Woodhollow	San Antonio, TX	546 Units/348,692 Sq. Ft.	.71	.71	.68	79	79	84
Woodlake	Carrollton, TX	256 Units/210,208 Sq. Ft.	.87	.87	.85	92	92	89
Woodview (T)	Odessa, TX	232 Units/165,840 Sq. Ft.	.53	.52	.51	93	94	85
Office Buildings								
1010 Common (T)	New Orleans, LA	494,579 Sq. Ft.	14.08	13.63	12.77	84	82	74
225 Baronne (T)	New Orleans, LA	416,834 Sq. Ft.	10.70	10.63	9.89	69	65	76
9033 Wilshire (T)	Los Angeles, CA	44,253 Sq. Ft.	33.75	30.16	29.24	70	70	63
Amoco (T)	New Orleans, LA	378,244 Sq. Ft.	13.66	13.37	12.73	69	78	79
Bay Plaza (T)	Tampa, FL	75,780 Sq. Ft.	13.96	14.98	15.85	54	80	86
Bay Plaza II (T)	Tampa, FL	78,882 Sq.Ft.	12.79	13.23	13.01	77	78	72
Cooley Building	Farmers Branch, TX	27,000 Sq. Ft.	12.63	12.63	11.49	100	100	100
Durham Center	Durham, NC	207,171 Sq. Ft.	17.73	17.73	17.79	83	83	98
Eton Square (T)	Tulsa, OK	222,654 Sq. Ft.	11.09	11.60	11.35	75	38	42
Executive Court	Memphis, TN	41,840 Sq. Ft.	8.00	8.00	11.24			

Forum (T)	Richmond, VA	79,791 Sq. Ft.	13.68	14.23	15.32	76	61	60
Four Hickory Centre	Farmers Branch, TX	226,911 Sq. Ft.	18.70	18.70	*	4	4	*
Institute Place (T)	Chicago, IL	144,915 Sq. Ft.	16.67	17.21	17.13	69	83	88

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Property	Location	Units/Square Footage	Rent Per Square Foot 2004	2003	2002	Occupancy % 2004	2003	2002
Lexington Center (T)	Colorado Springs, CO	74,603 Sq. Ft.	$ 10.56	$ 12.33	$ 13.41	58	70	84
One Hickory Centre	Farmers Branch, TX	102,615 Sq. Ft.	20.34	20.34	20.42	74	74	74
Parkway North (T)	Dallas, TX	71,041 Sq. Ft.	16.58	18.08	17.41	60	64	72
Signature Athletic Club (T)	Dallas, TX	56,532 Sq. Ft.	10.00	****	****	100	****	****
Two Hickory Centre	Farmers Branch, TX	96,127 Sq. Ft.	21.47	21.47	21.23	100	100	93
University Square	Anchorage, AK	22,260 Sq. Ft.	14.64	14.64	15.54	100	100	100
Westgrove Air Plaza (T)	Addison, TX	78,326 Sq. Ft.	12.68	13.26	13.96	74	94	66
Industrial Warehouses								
5360 Tulane (T)	Atlanta, GA	30,000 Sq. Ft.	2.85	2.80	2.75	100	65	100
5700 Tulane (T)	Atlanta, GA	67,850 Sq. Ft.	1.88	2.14	2.45	65	65	12
Addison Hanger (T)	Addison, TX	23,650 Sq. Ft.	7.54	7.94	8.12	67	100	98
Addison Hanger II (T)	Addison, TX	29,000 Sq. Ft.	9.24	9.64	9.33	92	92	97
Encon (T)	Fort Worth, TX	256,410 Sq. Ft.	3.12	3.17	3.17	100	100	100
Space Center (T)	San Antonio, TX	101,500 Sq. Ft.	3.41	3.43	3.46	61	84	84
Shopping Centers								
Bridgeview Plaza (T)	LaCrosse, WI	116,008 Sq. Ft.	6.97	7.25	*	89	90	*
Cross County Mall	Mattoon, IL	304,575 Sq. Ft.	5.44	5.44	5.34	88	88	87
Cullman (T)	Cullman, AL	92,466 Sq. Ft.	3.55	3.53	3.39	27	95	91
Dunes Plaza (T)	Michigan City, IN	223,869 Sq. Ft.	5.91	5.51	5.83	64	61	69
Promenade (T)	Highland Ranch, CO	133,558 Sq. Ft.	10.45	10.94	12.41	85	79	81
Merchandise Mart								
Denver Mart	Denver, CO	509,508 Sq. Ft.	11.75	11.75	11.48	92	92	92
Single Family Residence								
Tavel Circle	Dallas, TX	2,271 Sq. Ft.						

Property	Location	Rooms	Average Room Rate 2004	2003	2002	Occupancy % 2004	2003	2002	Total Room Revenues Divided By Total Available Rooms 2004	2003	2002
Hotels											
Akademia (T)	Wroclaw, Poland	165 Rooms	$ 55.33	$ 47.78	$ 48.92	65	51	33	$ 35.98	$ 46.86	$ 15.97
Best Western	Virginia Beach, VA	110 Rooms	108.92	108.92	105.78	65	65	69	70.56	70.56	72.79
Château Inn	Fresno, CA	78 Rooms	63.42	63.42	61.89	58	58	53	36.52	36.52	32.56
City Suites (T)	Chicago, IL	45 Rooms	126.29	120.16	131.46	58	58	56	71.60	76.78	73.38
Majestic Inn (T)	San Francisco, CA	57 Rooms	129.43	107.67	141.62	50	52	37	64.10	66.68	52.25
Picadilly Airport	Fresno, CA	185 Rooms	79.25	79.25	75.18	63	63	61	50.04	50.04	45.83
Picadilly Shaw	Fresno, CA	194 Rooms	81.19	81.19	78.24	69	69	69	55.70	55.70	53.87
Picadilly University	Fresno, CA	190 Rooms	68.21	68.21	69.58	63	63	59	43.03	43.03	40.93
Quality Inn	Denver, CO	161 Rooms	56.10	56.10	53.62	55	55	60	30.80	30.80	32.13
The Majestic (T)	Chicago, IL	55 Rooms	129.64	124.47	133.79	52	48	52	65.91	57.86	64.31
Williamsburg Hospitality House	Williamsburg, VA	296 Rooms	93.97	93.97	99.79	53	53	49	49.98	49.98	48.86
Willows (T)	Chicago, IL	52 Rooms	119.84	121.24	129.76	57	53	49	67.62	69.54	63.35

* Property was purchased or constructed in 2003 or 2004.
** Property was under construction at December 31, 2004.
*** Property was sold in 2003 and repurchased in 2004.
**** No applicable data for Signature Athletic Club. ARI sold the Athletic Club in November 2004, but retained the Signature office building.

Occupancy presented above and throughout this ITEM 2. is without reference to whether leases in effect are at, below or above market rates.

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In 2004, ARI purchased the following properties:

Property	Location	Units/Acres	Purchase Price	Net Cash Paid/ (Received)	Debt Incurred	Interest Rate	Maturity Date
Apartments							
288 City Park(1)	Houston, TX	240 Units	$ 3,056	$ 612	$ 2,444	5.95%	04/45
Blue Lake Villas II(1)	Waxahachie, TX	70 Units	729	(164)	729	5.80	04/45
Bridges on Kinsey(1)	Tyler, TX	232 Units	2,291	596	1,687	5.74	08/45
Dakota Arms(1)	Lubbock, TX	208 Units	2,472	681	1,791	5.85	06/45
Laguna Vista(1)	Farmers Branch, TX	206 Units	2,424	902	1,522	5.50	09/46
Lake Forest(1)	Houston, TX	240 Units	2,316	(470)	2,316	5.60	03/45
Parc at Maumelle(1)	Maumelle, AR	240 Units	3,120	916	2,204	5.37	07/46
Treehouse(3)	Irving, TX	160 Units	7,519	(498)	5,027(4)	5.00	08/13
Vistas of Vance Jackson(1)	San Antonio, TX	240 Units	3,550	771	2,779	5.78	06/45
Wildflower Villas(1)	Temple, TX	220 Units	2,045	79	1,996	5.99	10/45
Land							
Cooks Lane	Ft. Worth, TX	21.9 Acres	1,000	1,034			
Denton-Coonrod	Denton, TX	13.9 Acres	1,644	1,046	840	6.25	11/06
DeSoto	DeSoto, TX	202.0 Acres	2,516	1,364	1,265	6.25	11/06
Granbury Station	Ft. Worth, TX	15.7 Acres	923	236	738	7.00	09/07
Ladue	Farmers Branch, TX	8.0 Acres	1,743	659	1,206	6.65(2)	06/06
Las Colinas	Irving, TX	45.5 Acres	4,802	1,674	3,121	7.00	12/06
Las Colinas(5)	Irving, TX	268.0 Acres	4,687	159			
Lubbock	Lubbock, TX	2.9 Acres	224	224			
Meloy Road	Kent, OH	54.2 Acres	4,900	343	4,900	5.00(2)	01/06
Railroad	Dallas, TX	0.3 Acres	708	704			
Rogers	Rogers, AR	20.1 Acres	1,390	619	1,130	10.50	04/05
West End	Dallas, TX	0.2 Acres	71	71			

(1) Initial construction loan funding to purchase land and begin apartment construction. Does not represent actual units purchased.
(2) Variable interest rate.
(3) Purchased from IORI, a related party, for assumption of debt and a note receivable, less $498 in cash received.
(4) Assumed debt of seller.
(5) Obtained in exchange for 13.0 acres of Las Colinas land.

In 2004, ARI sold the following properties:

Property	Location	Units/Sq.Ft./ Acres	Sales Price	Net Cash Received/ (Paid)	Debt Discharged	Gain/ (Loss) on Sale
Apartments						
Cliffs of El Dorado(5)	McKinney, TX	208 Units	$ 13,442	$ 10	$ 10,323(1)	$
Falcon House	Ft. Walton, FL	82 Units	3,330	1,178	1,950(1)	1,209
In the Pines	Gainesville, FL	242 Units	11,300	3,247	5,201	5,517
La Mirada	Jacksonville, FL	320 Units	10,500	2,576	7,098	7,576
Park Avenue	Tallahassee, FL	121 Units	6,225	926	4,320(1)	3,922
Sandstone	Mesa, AZ	238 Units	8,650	2,920	5,531	1,688
Tiberon Trails	Merrillville, IN	376 Units	10,325	2,869	6,189(1)	49
Industrial Warehouses						

Kelly (Cash Road)	Dallas, TX	97,150 Sq. Ft.	1,500	1,077	422	454
Kelly (Pinewood)	Dallas, TX	100,000 Sq. Ft.	1,650	65	65	153
Ogden Industrial	Ogden, UT	107,112 Sq. Ft.	2,600	668	668	1,474
Texstar Warehouse	Arlington, TX	97,846 Sq. Ft.	2,400			(3)
Land						
Allen	Collin County, TX	492.5 Acres	19,962	7,956	4,088	$ 7,915(2)
Marine Creek	Ft. Worth, TX	10.7 Acres	1,488	1,198	991	(7)
Mason Goodrich	Houston, TX	5.7 Acres	686	45	588	379

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Property	Location	Units/Sq.Ft./ Acres	Sales Price	Net Cash Received/ (Paid)	Debt Discharged	Gain/ (Loss) on Sale
Mason Goodrich	Houston, TX	8.0 Acres	$ 1,045	$ 251	$ 200	$ 617
Mason Goodrich	Houston, TX	4.0 Acres	523	33	436	306
Mason Goodrich	Houston, TX	2.4 Acres	250	15	200	115
Mason Goodrich	Houston, TX	5.0 Acres	515	466		254
Mason Goodrich	Houston, TX	12.0 Acres	1,492	1,338		854
Meloy Road	Kent, OH	1.3 Acres	135		135	11
Rasor	Plano, TX	24.5 Acres	2,600	2,600	1,260	220
Red Cross	Dallas, TX	2.9 Acres	8,500	2,842	4,450	
Vineyards	Tarrant County, TX	1.6 Acres	1,307	(275)	548	677
Vineyards II	Tarrant County, TX	1.5 Acres	1,239	(261)	200	551
Vista Ridge	Lewisville, TX	1.3 Acres	310	259		131
Office Buildings						
4135 Beltline	Addison, TX	90,000 Sq. Ft.	4,900	2,472	2,009	337
Ambulatory Surgery Center	Sterling, VA	33,832 Sq. Ft.	8,675	5,448	2,899	784
Atrium	Palm Beach, FL	74,603 Sq. Ft.	5,775	1,842	3,772	708
Brandeis[6]	Omaha, NE	319,234 Sq. Ft.				(92)
Centura Tower[4]	Farmers Branch, TX	410,901 Sq. Ft.	84,075	36,350	49,878	38,154
Corporate Pointe	Chantilly, VA	65,918 Sq. Ft.	9,000	5,025	3,585	5,533
Countryside Harmon	Sterling, VA	72,062 Sq. Ft.	9,150	4,608	3,865	1,931
Countryside Mimado	Sterling, VA	35,127 Sq. Ft.	4,000	102	941	72
Countryside Retail	Sterling, VA	133,422 Sq. Ft.	27,100	3,408	3,408	6,807
One Steeplechase	Sterling, VA	103,376 Sq. Ft.	11,900	3,743	7,654	6,786
Venture Center	Atlanta, GA	38,272 Sq. Ft.	4,000	997	2,550	1,381
Shopping Centers						
Collection	Denver, CO	267,812 Sq. Ft.	21,200	6,703	13,153	3,314
K-Mart	Cary, NC	92,033 Sq. Ft.	3,200		1,677[1]	[3]
Plaza on Bachman Creek	Dallas, TX	80,278 Sq. Ft.	7,850	1,808	5,358	4,073
Sadler Square	Amelia Island, FL	70,295 Sq. Ft.	4,500	1,876	2,680	1,897
Other						
Signature Athletic Club[2]	Dallas, TX	N/A	120	(154)	88	(47)

(1) Debt assumed by purchaser.

(2) Signature Athletic Club was sold for the assumption of capital leases by purchaser. Net cash paid is from prepaid dues and unearned revenues due purchaser.

(3) Sold to BCM, a related party, for assumption of debt and a secured note receivable. See NOTE 3. NOTES AND INTEREST RECEIVABLE. Gain of $1,157 (Texstar) and $521 (K-Mart) deferred until sale to unrelated party.

(4) ARI sold a 95% limited partnership interest, retaining a 1% general partner and 4% limited partner interest.

(5) Sold to Unified Housing Foundation, Inc. (UHF), a related party, in 2003. See NOTE 9. RELATED PARTY TRANSACTIONS. Gain of $2,542 deferred until sale to unrelated party.

(6) Returned to lender. See NOTE 7. NOTES AND INTEREST PAYABLE.

(7) Sold to UHF. Gain of $581 deferred until sale to unrelated party.

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In 2004, ARI financed/refinanced or obtained second mortgage financing on the following:

Property	Location	Units/Sq. Ft. Rooms/Acres	Debt Incurred	Debt Discharged	Net Cash Received/ (Paid)	Interest Rate	Maturity Date
Apartments							
Mountain Plaza	El Paso, TX	188 Units	$ 5,184	$ 4,257	$ 370	5.16%	12/34
Treehouse	Irving, TX	160 Units	5,780	5,027	138	5.06	07/34
Villager	Fort Walton, FL	33 Units	804	507	129	5.15	06/34
Waters Edge III	Gulfport, MS	238 Units	3,250		(5)	12.50	12/04(9)
Hotels							
City Suites	Chicago, IL	45 Rooms	3,640		3,548	6.75(1)	09/09
Majestic Inn	San Francisco, CA	57 Rooms	2,000(8)	5,138	(1,238)	5.75(1)	10/05
Williamsburg Hospitality House	Williamsburg, VA	296 Rooms	11,500	12,332	(13,689)(3)	7.00(1)	03/05(10)
Willows	Chicago, IL	52 Rooms	3,500		3,411	6.75(1)	09/09
Land							
Bonneau	Dallas County, TX	8.4 Acres	9,661(6)	10,283(7)	76	6.75(1)	09/05
Centura	Farmers Branch, TX	8.8 Acres	4,485	4,000	(183)	7.00(1)	02/05(11)
Chase Oaks	Plano, TX	5.8 Acres	(6)				
Cooks Lane	Ft. Worth, TX	23.2 Acres	550			6.75	11/06
Dalho	Farmers Branch, TX	2.9 Acres	(6)				
Dominion/Hollywood	Farmers Branch, TX	66.1 Acres	6,985	6,222	(67)	7.00(1)	02/05(12)
HSM	Farmers Branch, TX	6.2 Acres	(6)				
JHL Connell	Carrollton, TX	7.6 Acres	(6)				
Katy	Harris County, TX	130.6 Acres	7,500		(75)(4)	6.00(1)	02/07
Lacy Longhorn	Farmers Branch, TX	17.1 Acres	1,965	1,800	78	4.03(1)	07/07
Las Colinas	Las Colinas, TX	1.5 Acres	(6)				
Marine Creek	Ft. Worth, TX	28.4 Acres	1,785		1,746	4.03(1)	07/07
Mason/Goodrich	Houston, TX	39.4 Acres	2,133	714	1,345	6.00(1)	08/05
Stagliano	Farmers Branch, TX	3.2 Acres	(6)				
Vista Ridge	Lewisville, TX	64.9 Acres	(6)				
Walker	Dallas County, TX	132.6 Acres	8,750	7,950	264	5.90(1)	06/06
Office Buildings							
225 Baronne	New Orleans, LA	416,834 Sq. Ft.	500(8)			5.75(1)	10/05
1010 Common	New Orleans, LA	494,579 Sq. Ft.	16,250	8,000	7,829	4.03(1)	07/07
Amoco	New Orleans, LA	378,244 Sq. Ft.	1,500(8)			5.75(1)	10/05
Centura Tower	Farmers Branch, TX	410,901 Sq. Ft.	34,000(2)	36,889	(4,588)	5.50(1)	04/06
Centura Tower	Farmers Branch, TX	410,901 Sq. Ft.	3,800(2)		3,737	5.75(1)	04/06
Centura Tower	Farmers Branch, TX	410,901 Sq. Ft.	50,000	37,594	2,989	4.94	10/09
Cooley	Farmers Branch, TX	27,000 Sq. Ft.	2,600	1,726	811	5.50(1)	09/06
Two Hickory Centre	Farmers Branch, TX	96,127 Sq. Ft.	7,500	7,500	(164)	3.60(1)	05/06
Warehouses							
Addison Hangers I & II	Addison, TX	52,650 Sq. Ft.	4,500	2,592	1,635	10.00	09/14

(1) Variable interest rate.
(2) Repaid with proceeds of subsequent $50,000 loan.
(3) Cash of $10,961 was received by an affiliate, increasing ARI s affiliate receivable.
(4) Cash of $7,400 was received by an affiliate, increasing ARI s affiliate receivable.
(5) Cash of $3,250 was received by an affiliate, increasing ARI s affiliate receivable.
(6) Single note, with all properties as collateral.
(7) Debt forgiveness of $2,268 recognized.
(8) The Majestic Inn, 225 Baronne Office Building and Amoco Office Building are cross collateralized. The debt incurred on 225 Baronne and Amoco are 2nd lien loans.
(9) Repaid in December 2004.
(10) Maturity date extended to September 2005.

(11) Repaid in February 2005.
(12) Maturity date extended to February 2006.
(13) The Addison Hangers were sold in September 2004 to a third party but were then leased back for 10 years on a triple net lease basis. This transaction has been recorded as a financing transaction for accounting purposes.

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Land Properties. Set forth below are ARI s land properties, consisting of both improved and unimproved land:

Property	Location	Acres
1013 Common	New Orleans, LA	0.4
2301 Valley Branch	Farmers Branch, TX	23.8
2524 Valley View	Farmers Branch, TX	0.5
Alamo Springs	Dallas, TX	0.7
Backlick	Springfield, VA	4.0
Bee Street	Farmers Branch, TX	0.5
Bonneau	Dallas County, TX	8.4
Centura	Farmers Branch, TX	8.8
Chase Oaks	Plano, TX	11.8
Cooks Lane	Ft. Worth, TX	23.2
Croslin	Dallas County, TX	0.8
Dalho	Farmers Branch, TX	3.4
Denton-Coonrod	Denton, TX	82.2
DeSoto	DeSoto, TX	21.9
Dominion	Dallas, TX	14.4
Elm Fork	Denton County, TX	105.4
Fiesta	San Angelo, TX	0.7
Folsom	Dallas, TX	36.8
Fort Wayne	Fort Wayne, IN	23.2
Fruitland	Fruitland Park, FL	4.7
FRWM Cummings	Farmers Branch, TX	6.5
Granbury Station	Ft. Worth, TX	15.7
Hollywood Casino	Farmers Branch, TX	42.8
HSM	Farmers Branch, TX	6.2
JHL Connell	Carrollton, TX	7.6
Katrina	Palm Desert, CA	110.5
Katy Road	Harris County, TX	130.6
Kelly	Dallas County, TX	0.8
Lacy Longhorn	Farmers Branch, TX	17.1
LaDue	Farmers Branch, TX	8.0
Lakeshore Villas	Humble, TX	16.9
Lamar/Parmer	Austin, TX	17.1
Las Colinas	Las Colinas, TX	1.6
Las Colinas	Las Colinas, TX	4.7
LCLLP	Las Colinas, TX	45.5
Lemmon Carlisle	Dallas, TX	2.1
Leone	Irving, TX	8.2
Limestone Canyon II	Austin, TX	10.0
Lubbock	Lubbock, TX	2.9
Manhattan	Farmers Branch, TX	108.9
Marine Creek	Ft. Worth, TX	43.3
Mason Park	Houston, TX	18.0
Mason/Goodrich	Houston, TX	20.2
Maumelle	Maumelle, AR	10.8
McKinney 36	Collin County, TX	34.6
McKinney Corners II	Collin County, TX	18.5
Meloy	Kent, OH	52.9
Mendoza	Dallas County, TX	0.4

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Property	Location	Acres
Mira Lago	Farmers Branch, TX	8.9
Nashville	Nashville, TN	127.4
Pac Trust	Farmers Branch, TX	7.1
Payne	Las Colinas, TX	268.0
Pioneer Crossing	Austin, TX	439.1
Pulaski	Pulaski County, AR	21.9
Railroad	Dallas, TX	3
Rochelle I	Las Colinas, TX	10.1
Rochelle II	Las Colinas, TX	21.3
Rogers	Rogers, AR	20.1
Round Mountain	Austin, TX	18.0
Seminary West	Ft. Worth, TX	5.4
Sheffield Village	Grand Prairie, TX	13.9
Siskiyou	Siskiyou County, CA	20.7
Sladek	Travis County, TX	63.3
Stagliano	Farmers Branch, TX	3.2
Thompson	Farmers Branch, TX	4.0
Thompson II	Dallas County, TX	3.3
Tomlin	Farmers Branch, TX	9.2
Travelers	Farmers Branch, TX	202.0
Valley Ranch	Irving, TX	6.8
Valley Ranch III	Irving, TX	12.5
Valley Ranch IV	Irving, TX	12.4
Valley View 34	Farmers Branch, TX	33.9
Valwood	Dallas County, TX	246.1
Vineyards	Tarrant County, TX	14.2
Vineyards II	Tarrant County, TX	17.1
Vista Ridge	Lewisville, TX	79.0
Walker	Dallas County, TX	132.6
West End	Dallas, TX	6.8

Partnership Properties. ARI accounts for partnership properties using the equity method. ARI had no property information for properties owned by partnerships.

ARI is a 30% general partner in Sacramento Nine (SAC 9), which owned the Prospect Park #29 Office Building. In December 2004, SAC 9 sold the Prospect Park #29 office building for $3.7 million, of which ARI received $1.1 million after closing costs and fees. ARI recognized a gain on the sale of investment in SAC 9 of $882,000 relating to this transaction.

In December 2004, ARI sold a 95% interest in Garden Centura, L.P. that owns the 410,901 sq. ft. Centura Tower office building located in Farmers Branch, Texas. ARI retained a non-controlling 1% general partner and 4% limited partner interest in Garden Centura, L.P. ARI will account for its investment in this partnership on the cost basis.

Mortgage Loans

In addition to real estate, a portion of ARI s assets are invested in mortgage notes receivable, secured by income-producing real estate, unimproved land and partnership interests. Management expects that the percentage of ARI s assets invested in mortgage loans will decline, as ARI will no longer seek to fund or acquire new mortgage loans. However, ARI may, in selected instances, originate mortgage loans or it may provide purchase money financing in conjunction with a property sale. Management intends to service and hold for investment the mortgage notes currently in the portfolio. Mortgage notes receivable consist primarily of first mortgage loans.

Types of Properties Subject to Mortgages. The types of properties securing mortgage notes receivable at December 31, 2004, consisted of one apartment, four commercial buildings, unimproved land and partnership

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interests. The type of properties subject to mortgages in which ARI invests may be altered without a vote of stockholders.

As of December 31, 2004, the obligors on $43.3 million or 59.0% of the mortgage notes receivable portfolio were affiliates of ARI. Also at that date, $6.6 million or 8.9% of the mortgage notes receivable portfolio was non-performing.

The following table sets forth the percentages (based on the outstanding mortgage loan balance at December 31, 2004), by property type and geographic region, of the income producing properties that serve as collateral for ARI s mortgage notes receivable. Excluded are $55.5 million of mortgage notes that are secured by unimproved land and other security, or are unsecured. See SCHEDULE IV to the Consolidated Financial Statements included in ITEM 8. CONSOLIDATED FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA for additional details of ARI s mortgage notes receivable portfolio.

Region	Commercial Properties
Midwest	5%
Southwest	95
	100%

A summary of the activity in the mortgage notes receivable portfolio during 2004 is as follows:

Mortgage notes receivable at January 1, 2004	25
Loans funded	38
Loans collected in full	(5)
Loans sold	(1)
Mortgage notes receivable at December 31, 2004	57

During 2004, $5.9 million in interest and $11.6 million in principal were collected on mortgage notes receivable.

First Mortgage Loans. These loans generally provide for level periodic payments of principal and interest sufficient to substantially repay the loan at or prior to maturity, but may involve interest-only payments, moderate or negative amortization of principal, or all interest and a balloon principal payment at maturity. With respect to first mortgage loans, it is ARI s general policy to require that the borrower provide a title policy or an acceptable legal opinion of title as to the validity and the priority of ARI s mortgage lien over all other obligations, except liens arising from unpaid property taxes and other exceptions normally allowed by first mortgage lenders. ARI may grant participations in first mortgage loans that it originates to other lenders.

The following discussion briefly describes first mortgage loans funded in 2004, as well as events during 2004 that affected previously funded first mortgage loans.

In March 2004, ARI sold an 8.0 acre tract of its Mason Goodrich land parcel for $1.0 million, receiving $251,000 after payment of closing costs and providing purchase money financing of $523,000. The secured loan bears interest at 10.0% per annum, requires monthly payments of accrued interest and matures in March 2006. All principal and accrued but unpaid interest is due at maturity.

In March 2004, ARI sold 492.5 acres in Collin County, Texas for $20.0 million, receiving $8.0 million after payment of debt and closing costs, and providing purchase money financing of $7.2 million for a portion of the land on a contingent basis. The secured note bore interest at 7.0% per annum and matured in September 2004.

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The purchaser extended the note to December 2004 with a $1.1 million extension payment in September 2004. In December 2004, the note was collected in full, including accrued but unpaid interest.

In October 2004, ARI sold the In The Pines apartments to a third party and provided $1.0 million of the purchase price as seller financing in the form of two notes. The first note bears interest at 7.0% per annum, requires monthly interest payments and matured in January 2005. The Purchaser extended this note to March 2005 by paying 1.0% of the outstanding principal balance as an extension fee and then extended the note an additional 30 days to April 2005 by paying an extension fee of 0.5% of the outstanding principal balance. In the event of a default, the note is also secured by membership rights in the purchaser s entity. The second note is unsecured; bears interest at 8.5% per annum, requires monthly interest payments and matured in January 2005. The Purchaser extended this note to March 2005 by paying 1.0% of the outstanding principal balance as an extension fee and then extended the note an additional 30 days to April 2005 by paying an extension fee of 0.5% of the outstanding principal balance.

In November 2004, ARI sold a 1.6 acre tract of its Vineyards II land parcel for $2.5 million, paying $536,000 after mortgage paydowns, closing costs, and providing purchase money financing of $2.0 million. In November 2004, the note was sold to an unrelated party for $2.0 million plus accrued and unpaid interest.

In March 2002, ARI sold the 174,513 sq. ft. Hartford Office Building in Dallas, Texas, for $4.0 million and provided the $4.0 million purchase price as seller financing and an additional $1.4 million line of credit for leasehold improvements in the form of a first lien mortgage note. The note bears interest at a variable interest rate, currently 7.0% per annum, requires monthly payments of accrued interest and matures in March 2007. As of March 2005, ARI has funded $788,000 of the additional line of credit.

In October 2002, ARI sold its Varner Road land parcel for $3.7 million, receiving $0.7 million after payment of closing costs and providing purchase money financing of $2.8 million. The loan bore interest at 9.0% per annum, matured in October 2004 and required quarterly interest payments. All principal and accrued but unpaid interest were due at maturity. In October 2004, the note was collected in full, including accrued but unpaid interest.

In February 2003, ARI sold an 89.3 acre tract of its Katrina land parcel for $8.5 million, paying $410,000 after payment of closing costs and debt pay down and providing purchase money financing of $5.6 million. The note bears interest at 8.0% per annum and matures three years after the recording of the Deed of Trust. Interest will begin accruing after improvements to the site have been completed by ARI. At April 2004, the improvements were begun. The future costs to ARI to complete the improvements, estimated to be $2.5 million, were accrued in 2002. A principal payment of $450,000 is due within ten days after a Tentative Parcel Map (the Map) is recorded. At March 2005, negotiations with the buyer to settle any further obligations are under way. Interest payments will be due on the first day of each calendar quarter, beginning with the first quarter following the completion of the site improvements.

Junior participations. In August 2001, ARI agreed to fund up to $5.6 million secured by a second lien on an office building in Dallas, Texas. The note receivable bore interest at a variable rate, required monthly payments of accrued interest and matured in January 2003. As of March 2005, ARI has funded a total of $4.3 million and the note is classified as non-performing. The collateral used to secure ARI s second lien was seized by the first lien holder. In March 2004, ARI agreed to accept an assignment of claims in litigation as security for the note. In December 2004, ARI agreed to a Modification Agreement with the borrower, which was effective November 1, 2003. As of the modified effective date, accrued interest of $582,000 was applied to the principal balance of the note, the interest rate was set to a fixed rate of 9.0% per annum and all principal and interest is due November 2005. ARI also received Pledge and Security Agreements in various partnership interests belonging to the borrower and received various Assignments of Proceeds from sales in certain entities owned by the borrower. ARI also agreed to reduce accrued interest and principal by $1.5 million from the receipt of notes receivable assigned to ARI by borrower and by $605,000 from cash received. ARI also received $1.4 million in January

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2005 that was applied to accrued interest and principal effective December 30, 2004. As a result of this modification, ARI has released $1.4 million of allowance for loan losses to expense. The following notes were assigned to ARI as payment on the note:

$678,000 from a partnership that owns an apartment building. This note is unsecured, bears no interest and has no maturity date. Distributions made from the partnership operations will be used to pay the principal on the note.

$264,000 secured by a second lien on 13 acres of unimproved land. This note bears interest at 9.0% and matured in February 2003.

$341,000 secured by a second lien on 23.3 acres of unimproved land. This note bears interest at 4.0% and is payable upon demand.

$125,000 secured by a 100% interest in an affiliated company that owns an apartment building. This note bears interest at 12.0%, only requires payments if surplus cash is available and matures in April 2009.

In June 2003, ARI sold the 104 unit Willow Wick Apartments in North Augusta, South Carolina, for $2.7 million and provided $42,000 of the purchaser s closing costs as seller financing. The note bore interest at 5.0% per annum and required all interest and principal payments be paid at maturity in December 2003. This loan was extended until February 2004 and $10,000 was received in March 2004. The note, including accrued and unpaid interest, was paid in June 2004. ARI discounted the note $2,000 and recognized a loss of $2,000.

In September 2003, ARI sold a 367.4 acre tract of its Pioneer Crossing land parcel for $22.5 million, receiving $4.9 million after payment of closing costs and providing purchase money financing of $16.9 million. The note bears interest at 8.0% per annum, matures in September 2006 and requires quarterly payments of accrued interest beginning in January 2004. All principal and accrued but unpaid interest are due at maturity. In November 2003, ARI sold an interest in $8.0 million of the note for $7.5 million, receiving $7.2 million in cash after payment of closing costs and debt paydown. In February 2004, ARI sold an additional interest in $6.6 million of the note for $6.3 million, receiving $6.3 million in cash after payment of closing costs.

In December 2003, ARI sold a tract of Marine Creek land to a subsidiary of United Housing Foundation, Inc. (UHF) for $1.5 million, receiving cash and a note receivable. This sale was not recognized as a sale at that time because UHF is a related party and ARI has continuing involvement and control. In February 2004, Marine Creek was refinanced by UHF, which paid in full ARI s note payable on the land. ARI recorded the sale of the land and received a note receivable of $270,000, which was the difference between the sales price and the amount of ARI s note payable. The note bears interest at 6.0%, requires quarterly payments from available surplus cash and matures in December 2007. See Note 9. RELATED PARTY TRANSACTIONS.

Other. In July 2002, ARI entered into an agreement to fund up to $300,000 under a revolving line of credit secured by 100% interest in a partnership of the borrower. The line of credit bears interest at 12.0% per annum, requires monthly payments of accrued interest, and matures in June 2005. ARI has funded the entire $300,000.

In September 1999, in conjunction with the sale of two apartments in Austin, Texas, $2.1 million in purchase money financing was provided, secured by limited partnership interests in two limited partnerships owned by the buyer. The financing bore interest at 16.0% per annum, required monthly payments of interest only at 6.0%, beginning in February 2000 and required a $200,000 principal paydown in December 1999, which was not received, and matured in August 2000. ARI had the option of obtaining the buyer s general and limited partnership interests in the collateral partnerships in full satisfaction of the financing. In March 2000, ARI agreed to forbear foreclosing on the collateral securing the note and released one of the partnership interests, in exchange for a payment of $250,000 and executed deeds of trusts on certain properties owned by the buyer. In March 2000, the borrower made a $1.1 million payment, upon receipt of which ARI returned the deeds of trust. The borrower executed a replacement promissory note for the remaining note balance of $1.0 million, which was unsecured, non-interest bearing and matured in April 2003. In April 2004, a demand letter was sent to the debtor. ARI initiated legal action in June 2004.

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Related Parties. In March 2004, ARI sold a K-Mart in Cary, North Carolina to BCM for $3.2 million, including the assumption of debt. ARI also provided $1.5 million of the purchase price as seller financing. The secured note bears interest at 2.0% over the prime rate, currently 7.75%, and matures in April 2005.

In March 2004, ARI sold the Texstar Warehouse in Arlington, Texas to BCM for $2.4 million, including the assumption of debt. ARI also provided $1.3 million of the purchase price as seller financing. The secured note bears interest at 2.0% over the prime rate, currently 7.75%, and matures in April 2005.

In October 2004, ARI contemplated the sale of the common stock of TCI Lexington Corporation, which owns the Lexington Center office building in Colorado Springs, Colorado, to One Realco Office Investors, Inc., a related party, for the assumption of debt of $5.1 million, which was subject to lender approval, and a seller note of $237,000. The assumption of debt by One Realco Office Investors, Inc. was not approved by the lender; therefore, the Board of Directors rescinded their approval of the transaction. ARI extended the loan on the Lexington Center with the lender in December 2004.

In October 2004, ARI advanced $3.3 million to the Class A Limited Partners of Edina Park Plaza Associates, Limited Partnership, of which ARI is the general partner. The loans bear interest at 10.0% per annum and mature in September 2017. Interest due to ARI will be deducted from the quarterly return owed by ARI to the Class A Limited Partners, eliminating the quarterly payments. The outstanding principal is due at maturity.

In October 1999, ARI funded a $4.7 million loan to Realty Advisors. The loan, to provide funds for acquisitions or working capital needs, was secured by all of the outstanding shares of common stock of American Reserve Life Insurance Company. The loan bore interest at 10.25% per annum and matured in November 2001. In January 2000, $100,000 was collected. In November 2001, the maturity date was extended to November 2004. The collateral was changed to a pledge of 850,000 shares of ARI Common Stock owned by BCM. The interest rate was changed to 2.0% over the prime rate, currently 7.75% per annum, and the accrued but unpaid interest of $1.0 million was added to the principal. The new principal balance is $5.6 million. In September 2003, $673,000 in accrued interest was collected. In August 2004, $342,000 in accrued interest was collected. In November 2004, the maturity date was extended to November 2006. All principal and accrued interest are due at maturity.

In March 2001, ARI funded $13.6 million of a $15.0 million unsecured line of credit to One Realco. A wholly-owned subsidiary of One Realco owns approximately 2.2% of the outstanding shares of ARI s Common Stock. One Realco periodically borrows money to meet its cash obligations. The line of credit bore interest at 12.0% per annum. All principal and interest were due at maturity in February 2002. The line of credit is guaranteed by BCM. In June 2001, $810,000 in principal and interest was collected. In December 2001, $825,000 in principal and interest was collected. In February 2002, the line of credit was increased to $18.0 million, accrued but unpaid interest of $217,000 was added to the principal, and the maturity date was extended to February 2004. In March 2002, ARI funded an additional $1.8 million, increasing the outstanding principal balance to $15.5 million. In October 2002, $856,900 in interest was collected, by the return of 85,690 shares of ARI Series A Preferred Stock. In June 2003, ARI sold a participating interest in $5.8 million of the $15.5 million balance to BCM, receiving 314,141 TCI shares from BCM (see NOTE 1. BASIS OF PRESENTATION.) In February 2004, $2.3 million in interest was collected, accrued but unpaid interest of $161,000 was added to the principal, the maturity date was extended to February 2007, and the interest rate was changed to 3.0% over the prime rate, currently at 8.75%. All principal and interest are due at maturity. Ronald E. Kimbrough, Acting Principal Executive Officer, Executive Vice President and Chief Financial Officer of ARI until May 31, 2004, was a 10.0% shareholder of One Realco until July 31, 2004. Mr. Kimbrough did not participate in the day-to-day operations or management of One Realco.

Investments in Real Estate Companies

Real estate entities. ARI s investment in real estate entities includes the equity securities of a publicly traded real estate company, IORI, and interests in real estate joint venture partnerships.

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The Board of Directors authorized the expenditure of up to an aggregate of $50.0 million to acquire, in open market purchases, shares of IORI, excluding private purchase transactions which were separately authorized. Through December 31, 2004, ARI had expended an aggregate of $10.0 million to acquire shares of IORI, in open market purchases, in accordance with these authorizations. As of December 31, 2004, ARI and its subsidiaries, other than TCI, owned no shares of common stock of IORI but TCI continued to own 345,728 IORI shares (approximately 24.0% of the outstanding IORI shares). ARI may make additional investments in the equity securities of IORI to the extent its liquidity permits.

The following summary description of IORI is based on information publicly reported by IORI in its Form 10-K Annual Report to the Commission for the fiscal year ended December 31, 2004.

Pertinent information regarding ARI s investment in the equity securities of the IORI at December 31, 2004, is summarized below (dollars in thousands):

Investee	Percentage of ARI s Ownership at December 31, 2004	Carrying Value of Investment at December 31, 2004	Equivalent Investee Book Value at December 31, 2004	Market Value of Investment at December 31, 2004
IORI	19.73%	$ 5,765	$ 10,545	$ 5,532

IORI owns real estate, some of which has been held for many years. Because of depreciation, IORI may earn substantial amounts in periods in which it sells real estate and will probably incur losses in periods in which it does not. ARI s reported income or loss attributable to IORI will differ materially from its cash flow attributable to it.

IORI is a Nevada corporation, which was originally organized on December 14, 1984, as a California business trust and commenced operations on April 10, 1985. IORI s business is investing in real estate through direct equity investments and partnerships. At December 31, 2004, IORI had total assets of $91.2 million and owned six apartments, one office building, one shopping center, one industrial warehouse, and one parcel of unimproved land, all within the State of Texas. In 2004, IORI sold two apartments, two office buildings and a parcel of unimproved land for a total of $24.5 million, receiving net cash of $4.8 million after paying off $15.8 million in mortgage debt and the payment of various closing costs. IORI recognized gains of $5.6 million on the sales, of which ARI s equity share was $1.1 million. In 2003, IORI sold three office buildings and a parcel of unimproved land for a total of $55.7 million, receiving net cash of $10.1 million after paying off $9.5 million in mortgage debt and the payment of various closing costs. IORI recognized gains of $3.0 million on the sales, of which ARI s equity share was $715,000.

ARI received no dividends from IORI in 2004.

ITEM 3. ***LEGAL PROCEEDINGS***

Innovo Realty, Inc. On August 10, 2004, American Realty Investors, Inc. (ARI), Investors, Inc. (TCI) and Income Opportunity Realty Investors, Inc. (IOT) instituted an action in Texas State District Court as Cause No. 2004-60231-393 styled *American Realty Investors, Inc., Transcontinental Realty Investors, Inc. and Income Opportunity Realty Investors, Inc., Plaintiffs v. Innovo Realty, Inc. and Innovo Group, Inc., Involuntary Plaintiffs v. Innovo Realty, Inc., Metra Capital LLC, Innovo Group, Inc., Joseph Mizrachi, Simon Mizrachi, Hubert Guez, Third*

Millennium Partners LLC, Third Millennium Partners, Inc., Third Millennium Group LLC and Sunridge Management Group, Inc., Defendants. Plaintiffs Complaint alleges that Joseph Mizrachi, a former director of ARI and others, offered a plan to the Plaintiffs to create one or more joint venture arrangements with one or more of the Plaintiffs to pursue alternative forms of financing or refinancing portions of Plaintiffs real estate portfolios, which entailed the creation of 22 separate limited partnerships to acquire 28 separate apartment complexes in three states (Texas, Florida and Louisiana), the general partners of which are affiliates of, or controlled by, Joseph Mizrachi. Plaintiffs Complaint alleges that the overall transaction required the establishment of a sinking fund by

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the Defendants and the 22 limited partnerships as a trust for the benefit of certain preferred shareholders of Innovo Group, Inc. and the payment of certain proceeds to the Plaintiffs. Plaintiffs assert that payments have not been made pursuant to the agreement of the parties. Plaintiffs allege that Defendants conduct constituted a common business enterprise, alleges breach of contract and derivative claims on behalf of Innovo Group, Inc. against Joseph Mizrachi and others, and requests declaratory relief involving the Plaintiffs rights in the partnerships, an accounting of proceeds, and the creation of a constructive trust. Plaintiffs Complaint also alleges that Joseph Mizrachi engaged in fraud, negligent misrepresentation and/or breach of fiduciary duty and seeks unspecified damages, attorneys fees, the establishment of a constructive trust and other relief.

Sunset Management, LLC. On October 5, 2004, Sunset Management LLC (Sunset) filed a Complaint as a purported stockholder s derivative action on behalf of Transcontinental Realty Investors, Inc. (TCI) in the United States District Court for the Northern District of Texas, Dallas Division, against American Realty Investors, Inc. (ARI), Basic Capital Management, Inc. (BCM), Prime Income Asset Management, Inc. (PIAMI), Prime Income Asset Management LLC (Prime), Income Opportunity Realty Investors, Inc. (IOT), United Housing Foundation, Inc. (United), Regis Realty, Inc. (Regis), TCI, TCI s current directors and officers and others. Sunset s Complaint was instituted as Case No. 3:04-CV-02162-B styled *Sunset Management LLC, Derivatively on Behalf of Transcontinental Realty Investors, Inc. v. American Realty Investors, Inc., et al.* Sunset s Complaint alleges (i) Sunset is the owner of 10 shares of Common Stock of TCI and Sunset is the pledgee and beneficial owner of 3,673,115 shares of Common Stock of TCI, (ii) Sunset is a single-member limited liability company, (iii) all of the Defendants have in their various capacities breached fiduciary duties to TCI, and (iv) unjust enrichment of the various Defendants. Sunset s Complaint seeks an injunction prohibiting TCI from entering into any related-party transactions that are not fair to TCI and approved by disinterested directors and/or the stockholders of TCI with full knowledge of the common interest of the directors and/or officers, unspecified damages, attorneys fees and costs. Individual directors and officers of TCI do not believe their interests are adverse to TCI in this matter. All Defendants believe the action is not properly brought as a derivative action on behalf of TCI, as Sunset s interests are adverse to the interests of TCI. The current action brought by Sunset contains many of the same allegations raised by Sunset in four other cases which, as rulings have occurred, have resulted in a denial of Sunset s requested relief. The Defendants intend to vigorously defend the action, and on November 8, 2004, filed a Motion to Dismiss the case pursuant to Rules 12 and 23.1 of the Federal Rules of Civil Procedure on the basis that Sunset s allegations are insufficient to evade the stringent demand requirement under the futility exception for stockholder derivative actions, and that Sunset cannot fairly and adequately represent the interests of other stockholders. On January 4, 2005, the Defendants also filed a Motion to Stay Discovery and For Protective Order based on the concept that the Motion to Dismiss should dispose of the matter. No hearing has been held or order issued by the Court on either Motion through March 30, 2005. Separately, one of the individual Defendants filed on January 4, 2005 a Motion to Disqualify Sunset s Counsel.

On December 23, 2004, Sunset filed another Complaint in the United States District Court for the Northern District of Texas, Dallas Division, against ARI, BCM, EQK Holdings, Inc. (EQK) and American Realty Trust, Inc. (ART). EQK and ART are subsidiaries of ARI. Sunset s Complaint was instituted as Case No. 3:04-CV-2710-K styled *Sunset Management LLC, Plaintiff v. American Realty Investors, Inc., Basic Capital Management, Inc., EQK Holdings, Inc. and American Realty Trust, Inc.*, alleging (i) that on September 17, 2001, Sunset lent BCM, EQK, ART and ART Williamsburg, Inc. $30,000,000, and in connection with such loan, BCM, EQK and ART pledged 3,673,115 shares of TCI stock to Sunset; 2,129,701 TCI shares pledged to Sunset by EQK; 920,507 TCI shares pledged to Sunset by BCM, and 622,907 shares pledged to Sunset by ART, (ii) that each of the stock pledge agreements specifically provides that the borrower will not without the written consent of Sunset, sell, dispose of, transfer directly or indirectly, or further encumber the Pledged Securities, (iii) some or all of the shares pledged by BCM and ART had been transferred to one or more subsidiaries of ARI in violation of the stock pledge agreements, (iv) BCM and ART have allegedly breached the stock pledge agreements by transferring certain shares of TCI, (v) that ARI and EQK have allegedly tortuously interfered with existing contractual relationships among BCM, ART and Sunset. Sunset s Complaint seeks specific performance under the stock pledge agreements, and that the Court enter an Order (a) requiring ART to reacquire at least 534,307 pledged shares it allegedly transferred to EQK, (b) requiring BCM to reacquire at least 920,507 pledged shares it allegedly transferred to EQK, (c) requiring EQK to transfer 534,307 pledged shares back to ART, and (d) requiring EQK 920,507 pledged shares back to BCM. On February 2, 2005, the Defendants in this case filed a Motion to Dismiss or in the Alternative to Stay Action Pending the Resolution of Prior Proceedings in a sister federal court based upon dependency of an adversary proceeding in the United States Bankruptcy Court for the Eastern District of Texas, Sherman Division (Plano, Texas), styled *American Realty Trust, Inc. v. Sunset Management LLC*, Adversary Proceeding No. 03-4256 (E.D. Texas), which is described in the following paragraphs as the Texas Litigation. No hearing has been held or Order issued by the Court on such Motion through March 30, 2005.

The current Sunset Complaint is the fifth in a continuing series of actions involving Sunset, certain subsidiaries of ARI and ARI resulting from a loan in September 2001 to BCM and three subsidiaries of ARI in the original amount of $30 million ($19.5 million of which bore interest at 24% per annum, while the remaining $10.5 million of which bore interest at 20%). In September 2002, $15 million in principal was repaid leaving a $15 million aggregate balance, which Sunset orally agreed to extend the maturity date and accept substitute collateral, an arrangement which Sunset did not honor, resulting in the original litigation filed in Texas State Court during October 2002 as Cause No. 02-09433-I in the 162nd Judicial District Court of Dallas County, Texas styled *American Realty Trust, Inc., ART Williamsburg, Inc., Basic Capital Management, Inc. and EQK Holdings, Inc. v. Sunset Management LLC* (the Texas Litigation). The Texas Litigation alleged breach of contract, misrepresentation, breach of duty of good faith and fair dealing and slander of title by Sunset and sought certain declaratory relief against Sunset, as well as temporary and permanent anti-suit injunction against Sunset.

During January 2003, without notice to the Plaintiffs in the Texas Litigation, Sunset institute an action in Federal District Court in Las Vegas, Nevada against Commonwealth Land Title (Commonwealth) seeking disposition of certain shares of Common Stock of TCI held by Commonwealth as Pledge Holder. On January 31, 2003, after a Temporary Restraining Order was issued in the Texas Litigation against Sunset, Sunset instituted a separate lawsuit in Nevada State Court styled *Sunset Management LLC v. American Realty Trust, Inc., et al.*, Cause No. A462587 pending in District Court of Clark County, Nevada (the Nevada Litigation). On February 12, 2003, the Nevada State Court held a hearing on Sunset s request for emergency relief and denied all of Sunset s requested relief and indicated that a stay of the Nevada Litigation may be appropriate, which stay of litigation (including claims against TCI) was granted on May 2, 2003. Notwithstanding the stay of the Nevada Litigation, Sunset has attempted to re-litigate the underlying issues already determined in the Texas Litigation and the Nevada Litigation through cross-claims and counterclaims in the Texas Litigation and renewed motions for injunctions and the appointment of a receiver in the Nevada Litigation. During September 2003, the Texas Litigation was removed to Bankruptcy Court for the Northern District of Texas and subsequently transferred to the Eastern District of Texas. Sunset and the Plaintiffs have filed cross-motions for partial summary judgment in the Bankruptcy Court which had been briefed but remain pending at this time. The parties have also filed an Agreed Motion to Withdraw the reference and have the case transferred to a United States District Judge for trial, which has been denied without prejudice pending resolution of pre-trial motions, including the motions for summary judgment.

On February 10, 2004, Sunset filed yet another lawsuit in Nevada styled *Sunset Management LLC v. Transcontinental Realty Investors, Inc.*, Case No. CV04-00345 in the Superior Court of Washoe County, seeking to compel a new election of directors, alleging that Sunset was improperly denied voting rights with respect to certain pledged shares at the 2003 stockholders meeting of TCI. TCI responded to that action by informing the Nevada Court that the issue of the validity and effectiveness of proxies purportedly held by Sunset in connection with the loan was already pending before the Bankruptcy Court. On May 12, 2004, the Nevada District Court denied Sunset s motion to compel and election of corporate directors because of the dispute pending in the Texas Bankruptcy Court concerning the status of the loan. Subsequently, the Nevada District Court denied two motions for reconsideration filed by Sunset. Sunset is currently appealing the rulings of the Washoe County District Court.

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The ownership of property and provision of services to the public as tenants entails an inherent risk of liability. Although the Company and its subsidiaries are involved in various items of litigation incidental to and in the ordinary course of its business, in the opinion of management, the outcome of such litigation will not have a material adverse impact upon the Company s financial condition, results of operations or liquidity.

ITEM 4. ***SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS***

Not applicable.

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PART II

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

ARI s Common Stock is traded on the New York Stock Exchange using the symbol ARL. The following table sets forth the high and low sales prices as reported in the consolidated reporting system of the New York Stock Exchange.

Quarter Ended	High	Low
March 31, 2005 (through March 24, 2005)	$ 9.99	$ 8.90
March 31, 2004	11.25	7.58
June 30, 2004	9.80	6.99
September 30, 2004	9.17	8.20
December 31, 2004	11.60	7.54
March 31, 2003	10.65	7.50
June 30, 2003	13.10	8.30
September 30, 2003	12.25	10.00
December 31, 2003	12.55	8.95

As of March 24, 2005, the closing market price of ARI s Common Stock on the New York Stock Exchange was $9.35 per share.

As of March 24, 2005, ARI s Common Stock was held by approximately 2,900 stockholders of record.

During the second quarter of 1999, the Board of Directors established the policy that dividend declarations on ARI s Common Stock would be determined on an annual basis following the end of each year. In accordance with that policy, the Board determined not to pay any dividends in 2004. Future distributions to Common stockholders will be dependent upon ARI s realized income, financial condition, capital requirements and other factors deemed relevant by the Board.

15,000,000 shares of Series A 10.0% Cumulative Convertible Preferred Stock are authorized under ARI s Amended Articles of Incorporation, with a par value of $2.00 per share and a liquidation preference of $10.00 per share plus accrued and unpaid dividends. Dividends are payable at the annual rate of $1.00 per share, or $.25 per share quarterly, to stockholders of record on the last day of each March, June, September, and December, when and as declared by the Board of Directors. The Series A Preferred Stock may be converted into Common Stock at 90.0% of the average daily closing price of ARI s Common Stock for the prior 20 trading days. At December 31, 2004, 3,469,350 shares of Series A Preferred Stock were outstanding and 869,808 shares were reserved for issuance as future consideration in various business transactions. Of the outstanding shares, 300,000 shares are owned by ART Edina, Inc., and 600,000 shares are owned by ART Hotel Equities, Inc., wholly-owned subsidiaries of ARI. Dividends are not paid on the shares owned by ARI subsidiaries.

231,750 shares of Series C Cumulative Convertible Preferred Stock are authorized under ARI s Amended Articles of Incorporation, with a par value of $2.00 per share and liquidation preference of $100.00 per share plus accrued and unpaid dividends. The Series C Preferred Stock bears a quarterly dividend of $2.50 per share to stockholders of record on the last day of March, June, September and December when and as declared by the Board of Directors. The Series C Preferred Stock is reserved for conversion of the Class A limited partner units of ART Palm, L.P. (Art Palm). At December 31, 2003, 10,188,750 Class A units were outstanding. The Class A units may be exchanged for Series C Preferred Stock at the rate of 100 Class A units for each share of Series C Preferred Stock. At June 30, 2003, shares of Series C Preferred Stock could be converted into 57,500 shares of ARI Common Stock. On or after December 31, 2005, additional shares of Series C Preferred Stock may be converted into 16,250 shares of ARI Common Stock. On or after December 31, 2006, all remaining outstanding

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shares of Series C Preferred Stock may be converted into ARI Common Stock. All conversions of Series C Preferred Stock into ARI Common Stock will be at 90.0% of the average daily closing price of ARI s Common Stock for the prior 20 trading days. In January 2001, 2.5 million Class A limited partner units of ART Palm were redeemed for $2.5 million in cash. In December 2001, 7.2 million Class A limited partner units of ART Palm were redeemed for $5.8 million, including $2.5 million in cash. ARI gave a note payable for the remaining $3.3 million. The note was paid in full in January 2003, including accrued but unpaid interest. In July 2002, 1.6 million Class A limited partner units of ART Palm were redeemed for $1.6 million in cash. In August 2003, 1.6 million Class A limited partner units of ART Palm were redeemed for $1.6 million in cash. In June 2004, 2.6 million Class A limited partner units were redeemed for $2.6 million in cash. In December 2004, 750,000 Class A limited partner units were redeemed for $750,000 in cash. At December 31, 2004, no Series C Preferred Stock was outstanding.

91,000 shares of Series D 9.50% Cumulative Preferred Stock are authorized under ARI s Amended Articles of Incorporation, with a par value of $2.00 per share, and a liquidation preference of $20.00 per share. Dividends are payable at the annual rate of $1.90 per year or $.475 per quarter to stockholders of record on the last day of each March, June, September and December when and as declared by the Board of Directors. The Series D Preferred Stock is reserved for the conversion of the Class A limited partner units of Ocean Beach Partners, L.P. The Class A units may be exchanged for Series D Preferred Stock at the rate of 20 Class A units for each share of Series D Preferred Stock. No more than one-third of the Class A units could be exchanged prior to May 31, 2001. Between June 1, 2001 and May 31, 2006, all unexchanged Class A units are exchangeable. At December 31, 2004, no Series D Preferred Stock was outstanding.

500,000 shares of Series E 6.0% Cumulative Preferred Stock are authorized under ARI s Amended Articles of Incorporation, with a par value $2.00 per share and a liquidation preference of $10.00 per share. Dividends are payable at the annual rate of $.60 per share or $.15 per quarter to stockholders of record on the last day of each March, June, September and December when and as declared by the Board of Directors. At December 31, 2004, 50,000 shares of Series E Preferred Stock were outstanding.

The following table sets forth information regarding purchases made by ARI of shares of ARI Common Stock on a monthly basis during the fourth quarter of 2004:

Period	(a) Total Number of Shares Purchased	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs(1)	(d) Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs(1)
October 2004		$		465,393
November 2004				465,393
December 2004	335,900	11.25	335,900	129,493
Total	335,900	$ 11.25	335,900	

(1) The repurchase program was announced in September 2000. 1,000,000 shares may be repurchased through the program. The program has no expiration date.

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ITEM 6. ***SELECTED FINANCIAL DATA***

	For the Years Ended December 31,				
	2004	2003	2002	2001	2000
		Restated[1]			
	(dollars in thousands, except per share)				
EARNINGS DATA					
Operating income	$ 42,746	$ 34,772	$ 11,922	$ 14,081	$ 29,620
Gain on land sales	11,781	43,831	16,727	7,883	29,001
Pizza parlor gross margin	7,812	7,006	6,750	6,278	5,784
Income from operations	62,339	85,609	35,399	28,242	64,405
Equity in loss of investees	(41)	(4,441)	(20,914)	(13,352)	(4,581)
Loss on sale of investments in equity investees			(286)	(387)	(8,744)
Equity in gain on sale of real estate by equity investees				22,542	18,571
Other income	22,526	24,640	8,590	2,448	2,039
Other expenses	143,115	123,354	78,897	91,806	126,255
Gain on sale of real estate				77,816	67,727
Net income (loss) from continuing operations	(58,291)	(17,546)	(56,108)	25,503	13,162
Net income (loss) from discontinued operations	91,485	29,409	47,644	(8,149)	(10,483)
Net income (loss)	33,194	11,863	(8,464)	17,354	2,679
Preferred dividend requirement	(2,601)	(2,351)	(2,401)	(2,485)	(2,327)
Income (loss) applicable to Common shares	$ 30,593	$ 9,512	$ (10,865)	$ 14,869	$ 352
PER SHARE DATA					
Net income (loss) from continuing operations	$ (5.76)	$ (1.85)	$ (5.15)	$ 1.96	$ 1.04
Net income (loss) from discontinued operations	8.66	2.73	4.19	(.69)	(1.01)
Net income (loss) applicable to Common shares	$ 2.90	$ .88	$ (.96)	$ 1.27	$ .03
Weighted average shares outstanding	10,559,571	10,789,352	11,375,127	11,714,374	10,399,890
BALANCE SHEET DATA					
Real estate, net	$ 983,422	$ 1,054,735	$ 466,042	$ 590,488	$ 653,744
Notes and interest receivable, net	72,661	70,595	82,133	30,382	13,831
Total assets	1,190,843	1,240,880	711,330	761,048	787,015
Notes and interest payable	939,921	986,769	475,433	564,298	616,331
Margin borrowings	18,663	21,194	8,558	28,040	13,485
Stockholders equity	103,009	76,871	79,527	88,169	73,402
Book value per share	$ 9.04	$ 6.75	$ 6.99	$ 7.75	$ 6.21

(1) The 2004 Restatement adjustments affecting 2003 are set forth in the following table:

	2003	
	As Previously Reported	**As Restated**
	(dollars in thousands)	
Net income (loss)	$ 8,321	$ 9,512
Net income (loss) per Common Share	$ .77	$ .88
Financial Position Data (at December 31):		
Total Assets	$ 1,240,181	$ 1,240,880
Stockholders Equity	$ 75,680	$ 76,871

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The 2004 Restatement adjustments affecting 2003 are adjustments with respect to net income (loss), as described in ITEM 8. CONSOLIDATED FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA. NOTE 24. RESTATEMENT OF 2003 FINANCIAL STATEMENTS.

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

Introduction

ARI was organized in 1999. In August 2000, ARI acquired American Realty Trust, Inc. (ART) and National Realty, L.P. (NRLP), ART was organized in 1961 to provide investors with a professionally managed, diversified portfolio of real estate and mortgage loan investments selected to provide opportunities for capital appreciation as well as current income. ART owns a portfolio of real estate and mortgage loan investments. NRLP was organized in 1987, and subsequently acquired all of the assets and assumed all of the liabilities of 35 public and private limited partnerships. NRLP also owns a portfolio of real estate and mortgage loan investments.

Critical Accounting Policies

Critical accounting policies are those that are both important to the presentation of ARI s financial condition and results of operations and require management s most difficult, complex or subjective judgments. ARI s critical accounting policies relate to the evaluation of impairment of long-lived assets and the evaluation of the collectibility of accounts and notes receivable.

If events or changes in circumstances indicate that the carrying value of a rental property to be held and used or land held for development may be impaired, management performs a recoverability analysis based on estimated undiscounted cash flows to be generated from the property in the future. If the analysis indicates that the carrying value is not recoverable from future cash flows, the property is written down to estimated fair value and an impairment loss is recognized. If management decides to sell rental properties or land held for development, management evaluates the recoverability of the carrying amounts of the assets. If the evaluation indicates that the carrying value is not recoverable from estimated net sales proceeds, the property is written down to estimated fair value, less costs to sell and an impairment loss is recognized within income from continuing operations. ARI s estimates of cash flow and fair values of the properties are based on current market conditions and consider matters such as rental rates and occupancies for comparable properties, recent sales data for comparable properties and, where applicable, contracts or the results of negotiations with purchasers or prospective purchasers. ARI s estimates are subject to revision as market conditions and ARI s assessments of them change. In the third quarter of 2004, ARI recognized asset impairments of $3.4 million. In the fourth quarter of 2004, ARI recognized asset impairments of $7.1 million.

ARI s allowance for doubtful accounts re