AMERICAN REALTY INVESTORS INC
Form 10-Q
November 13, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2015

or

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

For the transition period from ______ to ______

Commission File Number 001-15663

AMERICAN REALTY INVESTORS, INC.

(Exact Name of Registrant as Specified in Its Charter)

Nevada	75-2847135
(State or Other Jurisdiction of	(I.R.S. Employer
Incorporation or Organization)	Identification No.)

1603 Lyndon B. Johnson Freeway, Suite 800, Dallas, Texas 75234

(Address of principal executive offices)

(Zip Code)

(469) 522-4200

(Registrant's telephone number, including area code)

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

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

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

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

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

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

Common Stock, $.01 par value	15,514,360
(Class)	(Outstanding at November 6, 2015)

AMERICAN REALTY INVESTORS, INC.

FORM 10-Q

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

AMERICAN REALTY INVESTORS, INC.

CONSOLIDATED BALANCE SHEETS

(unaudited)

	September 30, 2015	December 31, 2014
	(dollars in thousands, except share and par value amounts)	
Assets		
Real estate, at cost	$961,099	$810,214
Real estate subject to sales contracts at cost, net of depreciation ($194 for 2015 and $2,300 for 2014)	9,213	19,026
Less accumulated depreciation	(145,101)	(129,477)
Total real estate	825,211	699,763
Notes and interest receivable		
Performing (including $121,099 in 2015 and $139,466 in 2014 from related parties)	132,452	149,484
Non-performing	—	3,161
Less allowance for doubtful accounts (including $15,537 in 2015 and 2014 from related parties)	(17,037)	(18,279)
Total notes and interest receivable	115,415	134,366
Cash and cash equivalents	11,989	12,299
Restricted cash	42,214	49,266
Investments in unconsolidated subsidiaries and investees	5,152	4,279
Receivable from related party	43,301	21,414
Other assets	43,829	44,111
Total assets	$1,087,111	$965,498
Liabilities and Shareholders' Equity		
Liabilities:		
Notes and interest payable	$782,570	$638,891
Notes related to subject to sales contracts	7,793	20,168
Deferred revenue (including $71,603 in 2015 and $72,564 in 2014 from sales to related parties)	71,672	74,409
Accounts payable and other liabilities (including $7,001 in 2015 and $11,024 in 2014 to related parties)	46,412	52,442
	908,447	785,910

Shareholders' equity:		
Preferred stock, Series A: $2.00 par value, authorized 15,000,000 shares, issued and outstanding 2,000,614 and 2,461,252 shares in 2015 and 2014 (liquidation preference $10 per share), including 900,000 shares in 2015 and 2014 held by ARL or subsidiaries.	2,205	3,126
Common stock, $0.01 par value, authorized 100,000,000 shares; issued 15,930,145 and 14,443,404 shares; outstanding 15,514,360 and 14,027,619 shares in 2015 and 2014, respectively; including 140,000 shares held by TCI (consolidated) in 2015 and 2014.	156	141
Treasury stock at cost; 415,785 shares	(6,395)	(6,395)
Paid-in capital	110,136	108,378
Retained earnings	18,435	19,090
Total American Realty Investors, Inc. shareholders' equity	124,537	124,340
Non-controlling interest	54,127	55,248
Total shareholders' equity	178,664	179,588
Total liabilities and shareholders' equity	$1,087,111	$965,498

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

AMERICAN REALTY INVESTORS, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(unaudited)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2015	2014	2015	2014
	(dollars in thousands, except per share amounts)			
Revenues:				
Rental and other property revenues (including $211 and $175 for the three months and $591 and $526 for the nine months ended 2015 and 2014, respectively, from related parties)	$27,826	$19,326	$75,223	$57,986
Expenses:				
Property operating expenses (including $202 and $172 for the three months and $551 and $511 for the nine months ended 2015 and 2014, respectively, from related parties)	14,499	10,766	37,467	30,677
Depreciation and amortization	6,569	4,463	16,410	13,099
General and administrative (including $634 and $926 for the three months and $2,554 and $2,686 for the nine months ended 2015 and 2014, respectively, from related parties)	1,417	1,590	5,215	6,770
Net income fee to related party	232	(186)	567	514
Advisory fee to related party	3,024	2,225	7,625	6,670
Total operating expenses	25,741	18,858	67,284	57,730
Net operating income (loss)	2,085	468	7,939	256
Other income (expenses):				
Interest income (including $3,886 and $4,699 for the three months and $13,190 and $14,692 for the nine months ended 2015 and 2014, respectively, from related parties)	3,950	5,106	13,722	15,264
Other income	(72)	1,332	4,040	1,738
Mortgage and loan interest (including $982 and $978 for the three months and $2,797 and $2,709 for the nine months ended 2015 and 2014, respectively, from related parties)	(13,481)	(9,901)	(34,203)	(28,651)
Loan charges and prepayment penalties	(1,545)	(1,044)	(2,260)	(2,626)
Earnings from unconsolidated subsidiaries and investees	81	320	276	266
Litigation settlement (expense)	(85)	(86)	(203)	3,666
Total other expenses	(11,152)	(4,273)	(18,628)	(10,343)
Loss before gain on land sales, non-controlling interest, and taxes	(9,067)	(3,805)	(10,689)	(10,087)

Gain on sale of income producing properties	735	—	735	—
Gain on land sales	1,958	40	7,861	634
Net income (loss) from continuing operations before taxes	(6,374)	(3,765)	(2,093)	(9,453)
Income tax benefit (expense)	16	786	107	5,030
Net income (loss) from continuing operations	(6,358)	(2,979)	(1,986)	(4,423)
Discontinued operations:				
Net income (loss) from discontinued operations	47	477	306	(454)
Gain on sale of real estate from discontinued operations	—	1,770	—	14,826
Income tax benefit (expense) from discontinued operations	(16)	(786)	(107)	(5,030)
Net income (loss) from discontinued operations	31	1,461	199	9,342
Net income (loss)	(6,327)	(1,518)	(1,787)	4,919
Net income (loss) attributable to non-controlling interest	1,164	200	1,132	(1,170)
Net income attributable to American Realty Investors, Inc.	(5,163)	(1,318)	(655)	3,749
Preferred dividend requirement	(275)	(428)	(941)	(1,653)
Net income applicable to common shares	$(5,438)	$(1,746)	$(1,596)	$2,096
Earnings per share - basic				
Net income (loss) from continuing operations	$(0.35)	$(0.24)	$(0.12)	$(0.59)
Net income from discontinued operations	—	0.11	0.01	0.76
Net income applicable to common shares	$(0.35)	$(0.13)	$(0.11)	$0.17
Earnings per share - diluted				
Net income (loss) from continuing operations	$(0.35)	$(0.24)	$(0.12)	$(0.59)
Net income (loss) from discontinued operations	—	0.11	0.01	0.76
Net income applicable to common shares	$(0.35)	$(0.13)	$(0.11)	$0.17
Weighted average common shares used in computing earnings per share	15,514,360	13,619,647	14,975,212	12,231,146
Weighted average common shares used in computing diluted earnings per share	15,514,360	13,619,646	14,975,212	12,231,146
Amounts attributable to American Realty Investors, Inc.				
Net income (loss) from continuing operations	$(5,194)	$(2,779)	$(854)	$(5,593)
Net income (loss) from discontinued operations	31	1,461	199	9,342
Net income applicable to American Realty Investors, Inc.	$(5,163)	$(1,318)	$(655)	$3,749

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

AMERICAN REALTY INVESTORS, INC.

CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

For the Nine Months Ended September 30, 2015

(unaudited, dollars in thousands, except share amounts)

	Total Equity	Comprehensive Income (Loss)	Preferred Stock	Common Stock Shares	Common Stock Amount	Treasury Stock	Paid-in Capital	Retained Earnings	Non-controlling Interest
Balance, December 31, 2014	$179,588	$(53,040)	$3,126	14,443,404	$141	$(6,395)	$108,378	$19,090	$55,248
Net income (loss)	(1,787)	(1,787)	—	—	—	—	—	(655)	(1,132)
Acquisition of non-controlling interest	—	—	—	—	—	—	—	—	—
Contributions from non-controlling interests	11	—	—	—	—	—	—	—	11
Distribution to non-controlling interests	—	—	—	—	—	—	—	—	—
Sale of controlling interest	—	—	—	—	—	—	—	—	—
Assumption of non-controlling interests	(470)	—	—	—	—	—	(470)	—	—
Sale of non-controlling interests	—	—	—	—	—	—	—	—	—
Conversion of preferred stock into common stock	2,263	—	(921)	1,070,956	15	—	3,169	—	—
Series A preferred stock dividend ($1.00 per share)	(941)	—	—	—	—	—	(941)	—	—
Repurchase/sale of treasury	—	—	—	—	—	—	—	—	—

shares, net									
Balance, September 30, 2015	$178,664	$(54,827)	$2,205	15,514,360	$156	$(6,395)	$110,136	$18,435	$54,127

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

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AMERICAN REALTY INVESTORS, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(unaudited)

	For the Nine Months Ended September 30,	
	2015	2014
	(dollars in thousands)	
Net income	$(1,787)	$4,919
Other comprehensive income (loss)	—	—
Total comprehensive income	(1,787)	4,919
Comprehensive (income) loss attributable to non-controlling interest	1,132	(1,170)
Comprehensive income attributable to American Realty Investors, Inc.	$(655)	$3,749

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

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AMERICAN REALTY INVESTORS, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

	For the Nine Months Ended September 30,	
	2015	**2014**
	(dollars in thousands)	
Cash Flow From Operating Activities:		
Net income	$(1,787)	$4,919
Adjustments to reconcile net income applicable to common shares to net cash flow from operating activities:		
Gain on sale of land	(7,861)	(634)
Gain on sale of income-producing properties	(735)	(14,826)
Depreciation and amortization	16,410	13,763
Amortization of deferred borrowing costs	1,748	2,415
Earnings from unconsolidated subsidiaries and investees	(276)	54
Decrease (increase) in assets:		
Accrued interest receivable	764	10,727
Other assets	1,397	2,002
Prepaid expense	(12,953)	(2,318)
Escrow	5,845	3,556
Earnest money	(1,193)	(5)
Rent receivables	(1,384)	(15)
Related party receivables	(21,887)	—
Increase (decrease) in liabilities:		
Accrued interest payable	(242)	43
Payable to related parties	—	(8,844)
Other liabilities	(6,030)	(17,294)
Net cash used in operating activities	(28,184)	(6,457)
Cash Flow From Investing Activities:		
Proceeds from notes receivable	27,084	—
Origination or advances of notes receivable	(7,655)	(20,798)
Acquisition of land held for development	—	(3,425)
Acquisition of income producing properties	(131,220)	(19,534)
Proceeds from sale of income-producing properties	—	41,666
Proceeds from sale of land	12,364	6,252
Investment in unconsolidated real estate entities	(597)	(402)
Improvement of land held for development	(2,930)	(1,654)
Improvement of income-producing properties	(7,945)	(3,625)
Sale of non-controlling interest	(336)	(289)

Construction and development of new properties	(5,110)	(1,026)
Net cash provided by (used in) investing activities	(116,345)	(2,835)
Cash Flow From Financing Activities:		
Proceeds from notes payable	225,950	110,308
Recurring amortization of principal on notes payable	(22,202)	(14,540)
Debt assumption by buyer, part of seller proceeds	(18,495)	—
Payments on maturing notes payable	(33,860)	(97,564)
Stock-secured borrowings	—	(568)
Deferred financing costs	(8,552)	(5,707)
Distributions to non-controlling interests	11	(257)
Preferred stock dividends - Series A	(941)	(1,653)
Conversion of preferred stock into common stock	2,308	7,219
Net cash provided by (used in) financing activities	144,219	(2,762)
Net increase (decrease) in cash and cash equivalents	(310)	(12,054)
Cash and cash equivalents, beginning of period	12,299	16,437
Cash and cash equivalents, end of period	$11,989	$4,383
Supplemental disclosures of cash flow information:		
Cash paid for interest	$9,193	$28,004

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

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. ORGANIZATION AND BASIS OF PRESENTATION

Organization

As used herein, the terms “ARL”, “the Company”, “we”, “our” or “us” refer to American Realty Investors, Inc., a Nevada corporation, which was formed in 1999.

The Company is headquartered in Dallas, Texas and its common stock trades on the New York Stock Exchange (“NYSE”) under the symbol (“ARL”). Approximately 86.7% of ARL’s stock is owned by related parties. Subsidiaries of ARL own approximately 80.9% of the outstanding shares of common stock of Transcontinental Realty Investors, Inc. (“TCI”), a Nevada corporation, which has its common stock listed and traded on the NYSE under the symbol (“TCI”). Accordingly, TCI’s financial results are consolidated with those of ARL. In 2012, May Realty Holdings, Inc. (“MRHI”) subsidiaries acquired more than 80% of ARL stock and as a result, ARL is included in the MRHI consolidated group for federal income tax reporting. We have no employees.

TCI, a subsidiary of ARL, owns approximately 81.1% of the common stock of Income Opportunity Realty Investors, Inc. (“IOT”). IOT’s financial results are consolidated with those of TCI and its subsidiaries. Shares of IOT are traded on the New York Stock Exchange Euronext (“NYSE MKT”) under the symbol (“IOT”).

ARL invests in real estate through direct ownership, leases and partnerships and also invests in mortgage loans on real estate. Pillar Income Asset Management, Inc. (“Pillar”) is the Company’s external Advisor and Cash Manager. Although the Board of Directors is directly responsible for managing the affairs of ARL, and for setting the policies which guide it, the day-to-day operations of ARL are performed by Pillar, as the contractual Advisor, under the supervision of the Board. Pillar’s duties include, but are not limited to: locating, evaluating and recommending real estate and real estate-related investment opportunities and arranging debt and equity financing for the Company with third party lenders and investors. Additionally, Pillar serves as a consultant to the Board with regard to their decisions in connection with ARL’s business plan and investment policy. Pillar also serves as an Advisor and Cash Manager to TCI and IOT.

Regis Realty Prime, LLC (“Regis”) manages our commercial properties and provides brokerage services. ARL engages third-party companies to lease and manage its apartment properties.

Properties

We own or had interests in a total property portfolio of 55 income-producing properties as of September 30, 2015. The properties consisted of:

- 10 commercial properties consisting of five office buildings, one industrial warehouse, three retail centers and a golf course, comprising in aggregate approximately 2.2 million rentable square feet;
- 45 apartment communities totaling 7,511 units, excluding apartments being developed; and
- 4,000 acres of developed and undeveloped land.

We join with various third-party development companies to construct residential apartment communities. We are in the predevelopment process on several residential apartment communities that have not yet begun construction. At September 30, 2015, we had two apartment projects in development. The third-party developer typically holds a general partner as well as a majority limited partner interest in a limited partnership formed for the purpose of building a single property, while we generally take a minority limited partner interest in the limited partnership. We may contribute land to the partnership as part of our equity contribution or we may contribute the necessary funds to the partnership to acquire the land. We are required to fund all necessary equity contributions while the third-party developer is responsible for obtaining construction financing, hiring a general contractor and for the overall management, successful completion and delivery of the project. We generally bear all the economic risks and rewards of ownership in these partnerships and therefore include these partnerships in our Consolidated Financial Statements. The third-party developer is paid a developer fee typically equal to a percentage of the construction costs. When the project reaches stabilized occupancy, we acquire the third-party developer's partnership interests in exchange for any remaining unpaid developer fees.

Basis of Presentation

The accompanying unaudited Consolidated Financial Statements have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") have been condensed or omitted in accordance with such rules and regulations, although management believes the disclosures are adequate to prevent the information presented from being misleading. In the opinion of management, all adjustments (consisting of normal recurring matters) considered necessary for a fair presentation have been included. The results of operations for the nine months ended September 30, 2015, are not necessarily indicative of the results that may be expected for other interim periods or for the full fiscal year.

The year-end Consolidated Balance Sheet at December 31, 2014 was derived from the audited Consolidated Financial Statements at that date, but does not include all of the information and disclosures required by U.S. GAAP for complete financial statements. For further information, refer to the Consolidated Financial Statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2014. Certain 2014 Consolidated Financial Statement amounts have been reclassified to conform to the 2015 presentation, including adjustments for discontinued operations.

Principles of Consolidation

The accompanying Consolidated Financial Statements include the accounts of the Company, its subsidiaries, generally all of which are wholly-owned, and all entities in which we have a controlling interest. Arrangements that are not controlled through voting or similar rights are accounted for as a Variable Interest Entity ("VIE"), in accordance with the provisions and guidance of ASC Topic 810, "Consolidation", whereby we have determined that we are a primary beneficiary of the VIE and meet certain criteria of a sole general partner or managing member as identified in accordance with Emerging Issues Task Force ("EITF") Issue 04-5, Investor's Accounting for an Investment in a Limited Partnership when the Investor is the Sole General Partner and the Limited Partners have Certain Rights ("EITF 04-5"). VIEs are generally entities that lack sufficient equity to finance their activities without additional financial support from other parties or whose equity holders as a group lack adequate decision making ability, the obligation to absorb expected losses or residual returns of the entity, or have voting rights that are not proportional to their economic interests. The primary beneficiary is generally the entity that provides financial support and bears a majority of the financial risks, authorizes certain capital transactions, or makes operating decisions that materially affect the entity's financial results. All significant intercompany balances and transactions have been eliminated in consolidation.

In determining whether we are the primary beneficiary of a VIE, we consider qualitative and quantitative factors, including, but not limited to: the amount and characteristics of our investment; the obligation or likelihood for us or other investors to provide financial support; our and the other investors' ability to control or significantly influence key decisions for the VIE; and the similarity with and significance to the business activities of us and the other investors. Significant judgments related to these determinations include estimates about the current future fair values and performance of real estate held by these VIEs and general market conditions.

For entities in which we have less than a controlling financial interest or entities where we are not deemed to be the primary beneficiary, the entities are accounted for using the equity method of accounting. Accordingly, our share of the net earnings or losses of these entities is included in consolidated net income. Our investment in Gruppa Florentina, LLC is accounted for under the equity method.

Real Estate, Depreciation and Impairment

Real estate assets are stated at the lower of depreciated cost or fair value, if deemed impaired. Major replacements and betterments are capitalized and depreciated over their estimated useful lives. Depreciation is computed on a straight-line basis over the useful lives of the properties (buildings and improvements: 10-40 years; furniture, fixtures and equipment: 5-10 years). The Company continually evaluates the recoverability of the carrying value of its real estate assets using the methodology prescribed in ASC Topic 360 ("ASC 360"), "Property, Plant and Equipment". Factors considered by management in evaluating impairment of its existing real estate assets held for investment include significant declines in property operating profits, annually recurring property operating losses and other significant adverse changes in general market conditions that are considered permanent in nature. Under ASC 360, a real estate asset held for investment is not considered impaired if the undiscounted, estimated future cash flows of an asset (both the annual estimated cash flow from future operations and the estimated cash flow from the theoretical sale of the asset) over its estimated holding period are in excess of the asset's net book value at the balance sheet date. If any real estate asset held for investment is considered impaired, a loss is provided to reduce the carrying value of the asset to its estimated fair value.

Real Estate Held For Sale

We periodically classify real estate assets as "held for sale". An asset is classified as held for sale after the approval of our Board of Directors, after an active program to sell the asset has commenced and if the sale is probable. One of the deciding factors in determining whether a sale is probable is whether the firm purchase commitment is obtained and whether the sale is probable within the year. Upon the classification of a real estate asset as held for sale, the carrying value of the asset is reduced to the lower of its net book value or its estimated fair value, less costs to sell the asset. Subsequent to the classification of assets as held for sale, no further depreciation expense is recorded. Real estate assets held for sale are stated separately on the accompanying Consolidated Balance Sheets. Upon a decision that the sale is no longer probable, the asset is classified as an operating asset and depreciation expense is reinstated.

Prior to January 1, 2015, the operating results of real estate assets held for sale and sold are reported as discontinued operations in the accompanying Consolidated Statements of Operations. Income from discontinued operations includes the revenues and expenses, including depreciation and interest expense, associated with the assets. Subsequent to January 1, 2015, Accounting Standards Update 2014-08, "Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity" ("ASU 2014-08") substantially changed the criteria for determining whether a disposition qualifies for discontinued operations presentation. Adoption of this standard will result in substantially fewer of the Company's dispositions meeting the discontinued operations criteria.

Cost Capitalization

Costs related to planning, developing, leasing and constructing a property are capitalized and classified as Real Estate in the Consolidated Balance Sheets. We capitalize interest to qualifying assets under development based on average accumulated expenditures outstanding during the period. In capitalizing interest to qualifying assets, we first use the interest incurred on specific project debt, if any, and next use the weighted average interest rate of non-project specific debt. We capitalize interest, real estate taxes and certain operating expenses until building construction is substantially complete and the building is ready for its intended use, but no later than one year from the cessation of major construction activity.

We capitalize leasing costs which include commissions paid to outside brokers, legal costs incurred to negotiate and document a lease agreement and any internal costs that may be applicable. We allocate these costs to individual tenant leases and amortize them over the related lease term.

Fair Value Measurement

We apply the guidance in ASC Topic 820, "Fair Value Measurements and Disclosures", to the valuation of real estate assets. These provisions define fair value as the price that would be received to sell an asset or paid to transfer a liability in a transaction between market participants at the measurement date, establish a hierarchy that prioritizes the information used in developing fair value estimates and require disclosure of fair value measurements by level within the fair value hierarchy. The hierarchy gives the highest priority to quoted prices in active markets (Level 1 measurements) and the lowest priority to unobservable data (Level 3 measurements), such as the reporting entity's own data.

The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date and includes three levels defined as follows:

Level 1 –	Unadjusted quoted prices for identical and unrestricted assets or liabilities in active markets.
Level 2 –	Quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
Level 3 –	Unobservable inputs that are significant to the fair value measurement.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

Deferred Costs

Costs relating to the financing of properties are deferred and amortized over the life of the related financing agreement. Amortization is reflected as interest expense in the Consolidated Statements of Operations, with remaining terms ranging from 6 months to 40 years. Unamortized financing costs are written off when the financing agreement is extinguished before the maturity date.

Related Parties

We apply ASC Topic 805, "Business Combinations", to evaluate business relationships. Related parties are persons or entities who have one or more of the following characteristics, which include entities for which investments in their equity securities would be required, trust for the benefit of persons including principal owners of the entities and members of their immediate families, management personnel of the entity and members of their immediate families and other parties with which the entity may deal if one party controls or can significantly influence the decision making of the other to an extent that one of the transacting parties might be prevented from fully pursuing its own separate interests, or affiliates of the entity.

Newly Issued Accounting Standards

In April 2014, the Financial Accounting Standards Board (“FASB”) issued ASU 2014-08, ”Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity”, which changes the criteria for determining which disposals qualify to be accounted for as discontinued operations and modifies related reporting and disclosure requirements.

Disposals representing a strategic shift in operations, such as a change in a major line of business, a major geographical area or major equity investment, that have a major effect on a company's operations and financial results will be presented as discontinued operations. If the disposal does qualify as a discontinued operation under ASU 2014-08, the Company will be required to expand their disclosures about discontinued operations to provide more information on the assets, liabilities, income and expenses of the disposed component. The classification of operating results as discontinued operations are applied retroactively for all periods presented. The new standard was effective January 1, 2015. We adopted ASU 2014-08 as of January 1, 2015 and believe future sales of our individual operating properties will no longer qualify as discontinued operations. Adoption of this standard has resulted in substantially fewer of the Company's dispositions meeting the discontinued operations criteria. See Note 8 below.

In May 2014, Accounting Standards Update ("ASU") No. 2014-09 ("ASU 2014-09"), "Revenue from Contracts with Customers," was issued. This new guidance established a new single comprehensive revenue recognition model and provides for enhanced disclosures. Under the new policy, the nature, timing and amount of revenue recognized for certain transactions could differ from those recognized under existing accounting guidance. This new standard does not affect revenue recognized under lease contracts. ASU 2014-09 is effective for reporting periods beginning after December 15, 2017. The Company is currently evaluating the impact the adoption of this guidance has on its financial position and results of operations, if any.

In April 2015, the FASB issued ASU 2015-03, "Simplifying the Presentation of Debt Issuance Costs" ("ASU 2015-03"). ASU 2015-03 requires debt issuance costs to be presented in the balance sheet as a direct deduction from the carrying value of the associated debt liability, consistent with the presentation of a debt discount. Prior to the issuance of the standard, debt issuance costs were required to be presented in the balance sheet as an asset. The Company has adopted this standard effective June 30, 2015. The accompanying financials have been reclassified to reflect the adoption.

NOTE 2. REAL ESTATE ACTIVITY

Below is a summary of the real estate owned as of September 30, 2015 (dollars in thousands):

Apartments	$578,838
Apartments under construction	7,503
Commercial properties	218,447
Land held for development	156,310
Real estate subject to sales contract	9,408
Total real estate	$970,506
Less accumulated depreciation	(145,295)
Total real estate, net of depreciation	$825,211

The highlights of our significant real estate transactions for the nine months ended September 30, 2015 are listed below:

Purchases

For the nine months ended September 30, 2015, The Company acquired five income-producing apartment complexes from third parties in the states of Texas (2), Tennessee (1) and Florida (2), increasing the total number of units by 761, for a combined purchase price of $67.5 million. In addition, the Company acquired three income-producing apartment complexes from related parties in the states of Texas (2) and Kansas (1), increasing the total number of units by 698, for a combined purchase price of $11.6 million. The Company also purchased a commercial office building in Texas, comprised of 92,723 square feet for $16.8 million.

Sales

For the nine months ended September 30, 2015, The Company sold approximately 198 acres of land located in Texas to independent third parties for a total sales price of $12 million. We recorded a total gain of $5.1 million from the sales.

In addition, one income-producing apartment complex consisting of 200 units located in Ohio was foreclosed upon. The Company recorded a gain of $0.7 million related to the extinguishment of debt.

As of September 30, 2015, The company has 110 acres of land, at various locations, that were sold to related parties in multiple transactions. These transactions are treated as “subject to sales contract” on the Consolidated Balance Sheets. Due to the related party nature of the transactions TCI has deferred the recording of the sales in accordance with ASC 360-20.

We continue to invest in the development of apartment projects. During the nine months ended September 30, 2015, we have expended $5.1 million related to the construction or predevelopment of various apartment complexes and capitalized $0.4 million of interest costs.

NOTE 3. NOTES AND INTEREST RECEIVABLE

A portion of our assets are invested in mortgage notes receivable, principally secured by real estate. We may originate mortgage loans in conjunction with providing purchase money financing of property sales. Notes receivable are generally collateralized by real estate or interests in real estate and guarantees, unless noted otherwise, are so secured. Management intends to service and hold for investment the mortgage notes in our portfolio. A majority of the notes receivable provide for principal to be paid at maturity. Below is a summary of our notes receivable (dollars in thousands):

Borrower	**Maturity Date**	**Interest Rate**	**Amount**	**Collateral**
Performing loans:				
Foundation for Better Housing, Inc. (Overlook at Allensville) (1)	11/19	12.00%	2,472	Secured
Foundation for Better Housing, Inc. (Vista Ridge) (1)	04/19	12.00%	3,923	Secured
H198, LLC (Las Vegas Land)	01/20	12.00%	5,907	Secured
One Realco Corporation (1) (2)	01/17	3.00 %	7,000	Unsecured
Realty Advisors Management, Inc. (1)	12/16	2.28 %	20,387	Unsecured
Unified Housing Foundation, Inc. (Cliffs of El Dorado) (1)	12/32	12.00%	2,097	Secured
Unified Housing Foundation, Inc. (Echo Station) (1)	12/32	12.00%	1,481	Secured
Unified Housing Foundation, Inc. (Inwood on the Park) (1)	12/32	12.00%	5,059	Secured
Unified Housing Foundation, Inc. (Kensington Park) (1)	12/32	12.00%	3,936	Secured
Unified Housing Foundation, Inc. (Lakeshore Villas) (1)	12/32	12.00%	2,000	Secured
Unified Housing Foundation, Inc. (Lakeshore Villas) (1)	12/32	12.00%	9,096	Secured
Unified Housing Foundation, Inc. (Limestone Canyon) (1)	12/32	12.00%	3,057	Secured
Unified Housing Foundation, Inc. (Limestone Canyon) (1)	12/32	12.00%	4,663	Secured
Unified Housing Foundation, Inc. (Limestone Ranch) (1)	12/32	12.00%	2,250	Secured
Unified Housing Foundation, Inc. (Limestone Ranch) (1)	12/32	12.00%	6,000	Secured
Unified Housing Foundation, Inc. (Parkside Crossing) (1)	12/32	12.00%	1,936	Secured
Unified Housing Foundation, Inc. (Reserve at White Rock Phase I) (1)	12/32	12.00%	2,485	Secured
Unified Housing Foundation, Inc. (Reserve at White Rock Phase II) (1)	12/32	12.00%		