TRANSCONTINENTAL REALTY INVESTORS INC
Form 10-Q
August 14, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2014

or

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

For the transition period from to

Commission File Number 001-09240

TRANSCONTINENTAL REALTY INVESTORS, INC.
(Exact Name of Registrant as Specified in Its Charter)

Nevada (State or Other Jurisdiction of Incorporation or Organization)	94-6565852 (I.R.S. Employer 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. xYes ¨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).
xYes ¨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 the definitions 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 x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). ¨Yes xNo.

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 (Class)	8,717,767 (Outstanding at August 5, 2014)

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

TRANSCONTINENTAL REALTY INVESTORS, INC.
CONSOLIDATED BALANCE SHEETS
(unaudited)

	June 30, 2014	December 31, 2013
	(dollars in thousands, except share and par value amounts)	
Assets		
Real estate, at cost	$742,615	$777,974
Real estate held for sale at cost, net of depreciation ($1,489 for 2014 and $2,390 for 2013)	627	16,427
Real estate subject to sales contracts at cost, net of depreciation ($2,124 for 2014 and $1,949 for 2013)	24,842	29,353
Less accumulated depreciation	(106,832)	(127,952)
Total real estate	661,252	695,802
Notes and interest receivable:		
Performing (including $67,458 in 2014 and $66,431 in 2013 from related parties)	70,773	69,626
Non-performing	564	543
Less allowance for doubtful accounts (including $2,098 in 2014 and $2,098 in 2013 from related parties)	(2,263)	(2,262)
Total notes and interest receivable	69,074	67,907
Cash and cash equivalents	13,382	16,086
Restricted cash	25,052	31,799
Investments in unconsolidated joint ventures and investees	1,509	1,697
Receivable from related party	74,406	52,380
Other assets	36,548	32,000
Total assets	$881,223	$897,671
Liabilities and Shareholders' Equity		
Liabilities:		
Notes and interest payable	$569,199	$562,734
Notes related to real estate held for sale	3,006	17,100
Notes related to real estate subject to sales contracts	20,758	23,011
Deferred gain (from sales to related parties)	53,096	53,096
Accounts payable and other liabilities (including $5,103 in 2014 and $4,697 in 2013 to related parties)	37,008	50,160
Total liabilities	683,067	706,101
Shareholders' equity:		

Preferred stock, Series C: $0.01 par value, authorized 10,000,000 shares, issued and outstanding 30,000 shares in 2014 and 2013 (liquidation preference $100 per share). Series D: $0.01 par value, authorized, issued and outstanding 100,000 shares in 2013 and 2012 (liquidation preference $100 per share)	1	1
Common stock, $0.01 par value, authorized 10,000,000 shares, issued 8,413,669 shares in 2014 and 2013 and outstanding 8,413,469 shares in 2014 and 2013	84	84
Treasury stock at cost, 200 shares in 2014 and 2013	(2)	(2)
Paid-in capital	271,169	271,720
Retained earnings	(91,088)	(98,029)
Total Transcontinental Realty Investors, Inc. shareholders' equity	180,164	173,774
Non-controlling interest	17,992	17,796
Total shareholders' equity	198,156	191,570
Total liabilities and shareholders' equity	$881,223	$897,671

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

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TRANSCONTINENTAL REALTY INVESTORS, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2014	2013	2014	2013
	(dollars in thousands, except per share amounts)			
Revenues:				
Rental and other property revenues (including $175 and $166 for the three months and $350 and $331 for the six months ended 2014 and 2013, respectively, from related parties)	$19,859	$19,560	$39,476	$38,950
Expenses:				
Property operating expenses (including $148 and $160 for the three months and $293 and $353 for the six months ended 2014 and 2013, respectively, from related parties)	9,695	8,787	19,229	18,116
Depreciation and amortization	4,430	4,298	8,868	8,026
General and administrative (including $656 and $792 for the three months and $1,400 and $1,439 for the six months ended 2014 and 2013, respectively, from related parties)	2,737	1,615	4,295	3,237
Net income fee to related party	210	48	700	104
Advisory fee to related party	1,811	2,071	3,664	4,209
Total operating expenses	18,883	16,819	36,756	33,692
Net operating income	976	2,741	2,720	5,258
Other income (expenses):				
Interest income (including $4,004 and $2,149 for the three months and $6,117 and $4,288 for the six months ended 2014 and 2013, respectively, from related parties)	4,005	2,119	6,118	4,296
Other income	244	144	401	180
Mortgage and loan interest (including $0 and $439 for the three months and $31 and $926 for the six months ended 2014 and 2013, respectively, from related parties)	(7,932)	(7,874)	(14,765)	(15,797)
Deferred borrowing costs amortization	(334)	46	(1,266)	(2,371)
Loan charges and prepayment penalties	-	(26)	(1,582)	(3,963)
Loss on the sale of investments	-	-	-	(8)
Losses from unconsolidated joint ventures and investees	(11)	15	(16)	2
Litigation settlement	(86)	57	3,753	12
Total other expenses	(4,114)	(5,519)	(7,357)	(17,649)
Loss before gain on land sales, non-controlling interest, and taxes	(3,138)	(2,778)	(4,637)	(12,391)
Gain (loss) on land sales	(159)	-	594	(48)
Net loss from continuing operations before taxes	(3,297)	(2,778)	(4,043)	(12,439)

Income tax benefit	2,035	5,222	3,918	7,554
Net income (loss) from continuing operations	(1,262)	2,444	(125)	(4,885)
Discontinued operations:				
Net loss from discontinued operations	(1,189)	(3,154)	(1,862)	(2,682)
Gain on sale of real estate from discontinued operations	7,003	18,074	13,057	24,265
Income tax expense from discontinued operations	(2,035)	(5,222)	(3,918)	(7,554)
Net income from discontinued operations	3,779	9,698	7,277	14,029
Net income	2,517	12,142	7,152	9,144
Net loss attributable to non-controlling interest	(127)	(115)	(211)	(226)
Net income attributable to Transcontinental Realty Investors, Inc.	2,390	12,027	6,941	8,918
Preferred dividend requirement	(277)	(277)	(551)	(551)
Net income applicable to common shares	$2,113	$11,750	$6,390	$8,367
Earnings per share - basic				
Net income (loss) from continuing operations	$(0.20)	$0.24	$(0.11)	$(0.67)
Net income from discontinued operations	0.45	1.15	0.86	1.67
Net income applicable to common shares	$0.25	$1.39	$0.75	$1.00
Earnings per share - diluted				
Net income (loss) from continuing operations	$(0.20)	$0.23	$(0.11)	$(0.67)
Net income from discontinued operations	0.45	1.10	0.86	1.67
Net income applicable to common shares	$0.25	$1.33	$0.75	$1.00
Weighted average common shares used in computing earnings per share	8,413,469	8,413,469	8,413,469	8,413,469
Weighted average common shares used in computing diluted earnings per share	8,413,469	8,796,699	8,413,469	8,413,469
Amounts attributable to Transcontinental Realty Investors, Inc.				
Net income (loss) from continuing operations	$(1,389)	$2,329	$(336)	$(5,111)
Net income from discontinued operations	3,779	9,698	7,277	14,029
Net income	$2,390	$12,027	$6,941	$8,918

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

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TRANSCONTINENTAL REALTY INVESTORS, INC.
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
For the Six Months Ended June 30, 2014
(unaudited, dollars in thousands)

	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, 2013	$191,570	$ (99,647)	$1	8,413,669	$84	$(2)	$271,720	$(98,029)	$ 17,796
Series C preferred stock dividends (7.0% per year)	(106)	-	-	-	-	-	(106)	-	-
Series D preferred stock dividends (9.0% per year)	(445)	-	-	-	-	-	(445)	-	-
Net income	7,152	7,152	-	-	-	-	-	6,941	211
Sale of controlling interest	-	-	-	-	-	-	-	-	-
Distributions to non-controlling interests	(15)	-	-	-	-	-	-	-	(15)
Balance, June 30, 2014	$198,156	$ (92,495)	$1	8,413,669	$84	$(2)	$271,169	$(91,088)	$ 17,992

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

TRANSCONTINENTAL REALTY INVESTORS, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(unaudited)

	For the Six Months Ended June 30,	
	2014	2013
	(dollars in thousands)	
Net income	$7,152	$9,144
Other comprehensive income (loss)	-	-
Total comprehensive income	7,152	9,144
Comprehensive income attributable to non-controlling interest	(211)	(226)
Comprehensive income attributable to Transcontinental Realty Investors, Inc.	$6,941	$8,918

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

TRANSCONTINENTAL REALTY INVESTORS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

	For the Six Months Ended June 30, 2014	2013
	(dollars in thousands)	
Cash Flow From Operating Activities:		
Net income	$7,152	$9,144
Adjustments to reconcile net income applicable to common shares to net cash flows from operating activities:		
Loss (gain) on sale of land	(594)	48
Gain on sale of income-producing properties	(13,057)	(24,265)
Depreciation and amortization	9,061	10,761
Amortization of deferred borrowing costs	1,544	3,383
Losses (earnings) from unconsolidated joint ventures and investees	286	(23)
Decrease (increase) in assets:		
Accrued interest receivable	7,281	296
Other assets	574	-
Prepaid expense	(1,182)	(1,008)
Escrow	8,910	10,227
Earnest money	(265)	525
Rent receivables	(397)	2,924
Related party receivables	-	(7,125)
Increase (decrease) in liabilities:		
Accrued interest payable	104	(2,186)
Related party payables	(22,026)	(10,057)
Other liabilities	(13,082)	(8,081)
Net cash used in operating activities	(15,691)	(15,437)
Cash Flow From Investing Activities:		
Originations or advances on notes receivable	(8,449)	(343)
Acquisition of land held for development	(93)	(7)
Proceeds from sale of income-producing properties	41,428	75,874
Proceeds from sale of land	2,221	2,537
Investment in unconsolidated real estate entities	(98)	(278)
Improvement of land held for development	(181)	(290)
Improvement of income-producing properties	(3,134)	(3,333)
Sales of controlling interest	-	54
Construction and development of new properties	(620)	(179)
Net cash provided by investing activities	31,074	74,035
Cash Flow From Financing Activities:		
Proceeds from notes payable	59,487	136,172
Recurring amortization of principal on notes payable	(10,133)	(7,504)
Payments on maturing notes payable	(61,740)	(193,031)
Deferred financing costs	(5,135)	(1,296)
Distributions to non-controlling interests	(15)	(14)

Preferred stock dividends - Series C	(106)	(105)
Preferred stock dividends - Series D	(445)	(446)
Net cash used in financing activities	(18,087)	(66,224)
Net decrease in cash and cash equivalents	(2,704)	(7,626)
Cash and cash equivalents, beginning of period	16,086	16,620
Cash and cash equivalents, end of period	$13,382	$8,994
Supplemental disclosures of cash flow information:		
Cash paid for interest	$15,153	$20,125

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 “TCI”, “the Company”, “we”, “our” or “us” refer to Transcontinental Realty Investors, Inc., a Neva corporation. TCI is the successor to a California business trust which was organized on September 6, 1983, and commenced operations on January 31, 1984. Effective March 31, 2003, TCI’s financial results were consolidated in American Realty Investors, Inc. (“ARL”) Form 10-K and related consolidated financial statements.

The Company is headquartered in Dallas, Texas and its common stock trades on the New York Stock Exchange (“NYSE”) under the symbol (“TCI”). Subsidiaries of ARL own approximately 83.8% of the Company’s common stock. ARL’s common stock trades on the New York Stock Exchange under the symbol (“ARL”). We have no employees.

TCI is a “C” corporation for U.S. federal income tax purposes and files an annual consolidated tax return with ARL and its ultimate parent, Realty Advisors Management, Inc. (“RAMI”).

TCI owns approximately 81.1% of the common stock of Income Opportunity Realty Investors, Inc. (“IOT”). Effective July 17, 2009, IOT’s financial results were consolidated with those of ARL and TCI and their subsidiaries. Shares of IOT are traded on the NYSE MKT under the symbol (“IOT”).

TCI 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 TCI, and for setting the policies which guide it, the day-to-day operations of TCI 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 TCI’s business plan and investment policy. Pillar also serves as an Advisor and Cash Manager to ARL and IOT.

Regis Realty Prime, LLC (“Regis”) manages our commercial properties and provides brokerage services for our real estate portfolio. TCI engages third-party companies to lease and manage its apartment properties. TCI also has a development agreement with Unified Housing Foundation, Inc. (“UHF”), a non-profit corporation that provides management services for the development of residential apartment projects in the future. This development agreement was terminated December 31, 2013.

Properties

We own or had interests in a total property portfolio of 43 income-producing properties as of June 30, 2014. The properties consisted of:

- 8 commercial buildings consisting of five office buildings, one industrial warehouse and two retail centers comprising in aggregate approximately 1.8 million rentable square feet;
- 35 apartment communities totaling 5,846 units; excluding apartments being developed; and
- 4,040 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 but have not yet begun construction. At June 30, 2014, we had no 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 required 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, or 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 six months ended June 30, 2014, 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, 2013, was derived from the audited financial statements at that date, but does not include all of the information and disclosures required by GAAP for complete financial statements. For further information, refer to the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2013. Certain 2013 financial statement amounts have been reclassified to conform to the 2014 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 generally is 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 ARL 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, "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 Topic 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. 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. This classification of operating results as discontinued operations applies retroactively for all periods presented. Additionally, gains and losses on assets designated as held for sale are classified as part of discontinued operations.

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.

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 Pronouncements

We have considered all other newly issued accounting guidance that is applicable to our operations and the preparation of our Consolidated Financial Statements, including that which we have not yet adopted. We do not believe that any such guidance will have a material effect on our financial position or results of operations.

NOTE 2. REAL ESTATE ACTIVITY

Below is a summary of the real estate owned as of June 30, 2014 (dollars in thousands):

Apartments	$433,243
Commercial properties	164,764
Land held for development	144,608
Real estate held for sale	2,116
Real estate subject to sales contract	26,966
Total real estate	$771,697
Less accumulated depreciation	(110,445)
Total real estate, net of depreciation	$661,252

The highlights of our significant real estate transactions for the six months ended June 30, 2014, are listed below:

On February 6, 2014, the Company sold a 232-unit apartment complex known as Pecan Pointe located in Temple, Texas for a sales price of $23.1 million to an independent third party. The buyer assumed the existing debt of $16.5 million secured by the property. A gain of $6.1 million was recorded on the sale.

On March 26, 2014, the Company sold 6.314 acres of land known as McKinney Ranch land located in McKinney, Texas to an independent third party, for a sales price of $1.7 million. We paid $1.5 million on the existing mortgage to satisfy a portion of the multi-tract collateral debt of $6.6 million, secured by various land parcels located in McKinney, Texas. A gain of $0.8 million was recorded on the land parcel sale.

On April 3, 2014, the Company sold 1010 Common, a 512,593 square foot commercial building, located in New Orleans, Louisiana, for a sales price of $16.6 million to an independent third party. A gain of $7.0 million was recorded on the sale.

As of June 30, 2014, there is one apartment complex, one commercial building and 134 acres of land that we have sold to a related party and have deferred the recognition of the sale. These are treated as “subject to sales contract” on the Consolidated Balance Sheets. These properties were sold to a related party in order to help facilitate an appropriate debt or organizational restructure and may or may not be transferred back to the seller upon resolution. These properties have mortgages that are secured by the property and many have corporate guarantees. According to the loan documents, the maker is currently in default on these mortgages primarily due to lack of payment and is actively involved in discussions with every lender in order to settle or cure the default situation. We have reviewed each asset and taken impairment to the extent we feel the value of the property was less than our current basis. The Company did not recognize or record the sale in accordance with ASC 360-20 due to our continuing involvement, which included the potential payment of cash shortfalls, future obligations under the existing mortgage and guaranty, the buyer’s inadequate initial investment and the Company’s questionable recovery of investment cost. The Company determined that no sale had occurred for financial reporting purposes and therefore the asset remained on the books and continued to record operating expenses and depreciation as a period cost until a sale occurred that met the requirements of ASC 360-20. The buyers received no compensation for the facilitation of the bankruptcy or debt restructuring process.

We continue to invest in the development of apartment projects. During the six months ended June 30, 2014, we have expended $0.6 million related to the construction or predevelopment of various apartment complexes.

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 personal guarantees of the borrower and, 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.

Our mortgage notes receivable consist of first, wraparound and junior mortgage loans (dollars in thousands):

Borrower	Maturity Date	Interest Rate	Amount	Security
Performing loans:				
Miscellaneous related party notes (1)	Various	Various	$ 2,091	Various secured interests
S Breeze I-V, LLC	06/14	5.00%	3,314	6% Class A and 25% Class B Limited Partner Interests
Unified Housing Foundation, Inc. (Echo Station) (1)	12/32	12.00%	1,481	100% Interest in Unified Housing of Temple, LLC
Unified Housing Foundation, Inc. (Lakeshore Villas) (1)	12/32	12.00%	2,000	Unsecured
Unified Housing Foundation, Inc. (Lakeshore Villas) (1)	12/32	12.00%	6,363	Membership interest in Housing for Seniors of Humble, LLC
Unified Housing Foundation, Inc. (Limestone Canyon) (1)	12/32	12.00%	4,663	100% Interest in Unified Housing of Austin, LLC
Unified Housing Foundation, Inc. (Limestone Canyon) (1)	12/32	12.00%	3,057	100% Interest in Unified Housing of Austin, LLC
Unified Housing Foundation, Inc. (Limestone Ranch) (1)	12/32	12.00%	6,000	100% Interest in Unified Housing of Vista Ridge, LLC
Unified Housing Foundation, Inc. (Limestone Ranch) (1)	12/32	12.00%	2,250	100% Interest in Unified Housing of Vista Ridge, LLC
Unified Housing Foundation, Inc. (Parkside Crossing) (1)	12/32	12.00%	1,936	100% Interest in Unified Housing of Parkside Crossing, LLC
Unified Housing Foundation, Inc. (Sendero Ridge) (1)	12/32	12.00%	4,812	100% Interest in Unified Housing of Sendero Ridge, LLC
Unified Housing Foundation, Inc. (Sendero Ridge) (1)	12/32	12.00%	5,174	100% Interest in Unified Housing of Sendero Ridge, LLC
Unified Housing Foundation, Inc. (Timbers of Terrell) (1)	12/32	12.00%	1,323	100% Interest in Unified Housing of Terrell, LLC
Unified Housing Foundation, Inc. (Tivoli) (1)	12/32	12.00%	7,966	100% Interest in Unified Housing of Tivoli, LLC
Unified Housing Foundation, Inc. (1)	12/13	5.00%	6,000	Unsecured
Foundation for Better Housing, Inc. (Preserve at Prairie Pointe) (1)	03/19	12.00%	1,810	Unsecured

Foundation for Better Housing, Inc. (Preserve at Prairie Pointe) (1)	03/17	12.00%	1,156	Unsecured
Foundation for Better Housing, Inc. (Vista Ridge) (1)	04/19	12.00%	3,923	Unsecured
Accrued interest			5,454	
Total Performing			$ 70,773	
Non-Performing loans:				
Miscellaneous non-related party notes	Various	Various	507	Various secured and unsecured interests
Accrued interest			57	
Total Non-Performing			$ 564	
Allowance for doubtful accounts			(2,263)	
Total			$ 69,074	

(1) Related party notes

At June 30, 2014, we had junior mortgage loans and accrued interest receivable from related parties, net of allowances, totaling $65.4 million. We recognized interest income of $4.8 million related to these notes receivables.

The Company has various notes receivable from Unified Housing Foundation, Inc. ("UHF"). UHF is determined to be a related party due to our significant investment in the performance of the collateral secured under the notes receivable. Payments are due from surplus cash flow of operations. Sale or refinance of any of the properties underlying these notes will be used to repay outstanding interest and principal for the remaining notes. These notes are cross-collateralized but to the extent cash is received from a specific UHF property, it is applied against any outstanding interest for the related-property note. The allowance on the UHF notes was a purchase allowance that was netted against the notes when acquired.

On March 31, 2014, the Company invested $3.2 million of notes and accrued interest receivable from Foundation for Better Housing, Inc. for the acquisition and refinance of Preserve at Prairie Pointe. The notes accrue interest at 12% and mature at various times.

On April 1, 2014, the Company invested $4.0 million of a note and accrued interest receivable from Foundation for Better Housing, Inc. for the acquisition of Vista Ridge. The note accrues interest at 12% and matures in April 2019.

NOTE 4. INVESTMENT IN UNCONSOLIDATED JOINT VENTURES AND INVESTEES

Investments in unconsolidated joint ventures and other investees in which we have a 20% to 50% interest or otherwise exercise significant influence, are carried at cost and adjusted for the Company's proportionate share of their undistributed earnings or losses under the equity method of accounting. ARL is our parent company (owning together with subsidiaries 82% of TCI's Common Stock) and is considered as an unconsolidated joint venture.

Investments in unconsolidated joint ventures and investees consist of the following:

	Percentage ownership as of	
	June 30, 2014	June 30, 2013
American Realty Investors, Inc.(1)	1.99 %	1.99 %

(1) Unconsolidated investment in parent company owning 229,214 shares of ARL Common Stock

Our interest in the common stock of ARL in the amount of 1.99% is accounted for under the equity method because we exercise significant influence over the operations and financial activities. Accordingly, the investments are carried at cost, adjusted for the Company's proportionate share of earnings or losses.

The Company acquired 135,000 shares of ARL Series K preferred stock on May 7, 2013. It was pledged as collateral on a $5.0 million promissory note relating to the Amoco Building settlement agreement. This note has been paid in full and the stock was released. The par value per share was $2 and the liquidation preference was $22 per share. It was convertible to common stock at a rate of 5 to 1. The Series K preferred stock was cancelled May 7, 2014.

The following is a summary of the financial position and results of operations from our unconsolidated parent (dollars in thousands):

As of June 30,	2014	2013
Real estate, net of accumulated depreciation	$ 15,149	$ 44,886
Notes receivable	68,940	44,544
Other assets	128,581	132,221
Notes payable	(52,369)	(61,410)
Other liabilities	(100,149)	(87,205)
Shareholders' equity	(60,152)	(73,036)

For the Six Months Ended June 30,	2014	2013
Rents and interest and other income	$ 5,894	$ 6,948
Depreciation	(138)	(152)
Operating expenses	(3,093)	(3,694)
Gain on land sales	-	12
Interest expense	(3,447)	(2,922)
Income (loss) from continuing operations	(784)	192
Income from discontinued operations	-	(15)

Net Income (loss)	$ (784)	$ 177
Company's proportionate share of earnings (loss) (1)	$ (16)	$ 4

(1) Earnings (loss) represents continued and discontinued operations

NOTE 5. NOTES PAYABLE

Below is a summary of our notes and interest payable as of June 30, 2014 (dollars in thousands):

	Notes Payable	Accrued Interest	Total Debt
Apartments	$ 397,243	$ 1,165	$ 398,408
Commercial	93,630	439	94,069
Land	70,062	117	70,179
Real estate held for sale	2,202	-	2,202
Real estate subject to sales contract	19,174	1,584	20,758
Other	7,347	-	7,347
Total	$ 589,658	$ 3,305	$ 592,963

The segment labeled as "Other" consists of unsecured or stock-secured notes payable.

With respect to the additional notes payable due to the acquisition of properties or refinancing of existing mortgages, a summary of some of the more significant transactions is discussed below:

On February 12, 2014, the Company exercised the first prepayment option on the settlement with the lender relating to the Amoco Building and paid $1.2 million to settle all obligations. The remaining balance of the note in the amount of $3.5 million, along with accrued interest, was forgiven. The 135,000 shares of Series K Convertible Preferred Stock of ARL that was pledged to the lender has been released to TCI. The Series K preferred stock was cancelled May 7, 2014.

On February 28, 2014, the Company refinanced the existing mortgage on Parc at Denham Springs apartments, a 224-unit complex located in Denham Springs, LA, for a new mortgage of $19.2 million. TCI paid off the existing mortgage of $19.2 million and $1.6 million in closing costs. The note accrues interest at 3.75% and payments of interest and principal are due monthly, maturing April 1, 2051.

On March 25, 2014, the Company exercised its lender granted option under the settlement agreement relating to the Galleria East Center Retail / Showcase Chevrolet land which was transferred to the existing lender on February 4, 2011. TCI paid the balance of the notes along with all accrued and unpaid interest and received a reduction in price of $0.4 million.

On March 28, 2014, the Company secured financing of $40.0 million from an independent third party. The note has a term of five years at an interest rate of 12.0%. The note is interest only for the first year with quarterly principal payments due of $500,000 starting April 1, 2015. The loan is secured by various equity interests in residential apartments and can be prepaid at a penalty rate of 4% for year 1 with the penalty declining by 1% each year thereafter.

On March 31, 2014, the Company entered into a settlement agreement relating to the Fenton Centre building which was transferred to the existing lender on June 7, 2011. The total amount of the settlement was $7.0 million, $5.0 million was paid at the time of the settlement and the remaining $2.0 million will be paid out in equal monthly installments through November 5, 2015.

On May 28, 2014, a $1.5 million principal payment was made to the existing Realty Advisors, Inc. mortgage and two additional land parcels, including 8.0 acres of Ladue land owned by TCI and 16.75 acres of Valwood land owned by ARL, were substituted as collateral under the note in exchange for a release of a $4 million deposit account. The principal balance is allocated based on the land valuation.

There are various land mortgages, secured by the property, that are in the process of a modification or extension to the original note due to expiration of the loan. We are in constant contact with these lenders, working together in order to modify the terms of these loans and we anticipate a timely resolution that is similar to the existing agreement or subsequent modification.

The properties that we have sold to a related party and have deferred the recognition of the sale are treated as "subject to sales contract" on the Consolidated Balance Sheets. These properties were sold to a related party in order to help facilitate an appropriate debt or organizational restructure and may or may not be transferred back to the seller upon resolution. These properties have mortgages that are secured by the property and many have corporate guarantees. According to the loan documents, the maker is currently in default on these mortgages primarily due to lack of payment and is actively involved in discussions with every lender in order to settle or cure the default situation. We have reviewed each asset and taken impairment to the extent we feel the value of the property was less than our current basis.

NOTE 6. RELATED PARTY TRANSACTIONS

The following table reconciles the beginning and ending balances of accounts receivable from and (accounts payable) to related parties as of June 30, 2014 (dollars in thousands):

	Pillar	ARL	Total
Related party receivable, December 31, 2013	$-	$52,380	$52,380
Cash transfers	31,718	-	31,718
Advisory fees	(3,664)	-	(3,664)
Net income fee	(700)	-	(700)
Fees and commissions	(1,066)	-	(1,066)
Cost reimbursements	(1,310)	-	(1,310)
Interest (to) from advisor	-	1,272	1,272
Notes receivable purchased	(8,437)	-	(8,437)
Expenses paid by advisor	(3,257)	-	(3,257)
Financing (mortgage payments)	(2,287)	-	(2,287)
Sales/purchases transactions	7,329	-	7,329
Series K preferred stock cancellation	270	-	270
Purchase of obligations	(18,596)	20,754	2,158
Related party receivable, June 30, 2014	$-	$74,406	$74,406

During the ordinary course of business, we have related party transactions that include, but are not limited to, rental income, interest income, interest expense, general and administrative costs, commissions, management fees, and property expenses. In addition, we have assets and liabilities that include related party amounts. The related party amounts included in assets and liabilities, and the related party revenues and expenses received/paid are shown on the face of the financial statements.

NOTE 7. OPERATING SEGMENTS

Our segments are based on our method of internal reporting which classifies our operations by property type. Our property types are grouped into commercial, apartments, land and other operating segments. Significant differences between and among the accounting policies of the operating segments as compared to the Consolidated Financial Statements principally involve the calculation and allocation of administrative and other expenses. Management evaluates the performance of each of the operating segments and allocates resources to them based on their net operating income and cash flow.

Items of income that are not reflected in the segments are interest, other income, gain on debt extinguishment, gain on condemnation award, equity in partnerships, and gains on sale of real estate. Expenses that are not reflected in the segments are provision for losses, advisory fees, net income and incentive fees, general and administrative, non-controlling interests and net loss from discontinued operations before gains on sale of real estate.

The segment labeled as “Other” consists of revenue and operating expenses related to the notes receivable and corporate debt.

Presented below is our reportable segments' operating income for the six months ended June 30, 2014 and 2013, including segment assets and expenditures (dollars in thousands):

For the Three Months Ended June 30, 2014	Commercial Properties	Apartments	Land	Other	Total
Rental and other property revenues	$4,426	$15,419	$-	$14	$19,859
Property operating expenses	2,968	6,522	205	-	9,695
Depreciation	1,733	2,697	-	-	4,430
Mortgage and loan interest	1,541	4,049	1,305	1,037	7,932
Deferred borrowing costs amortization	5	101	42	186	334
Interest income	-	-	-	4,005	4,005
Gain on land sales	-	-	(159)	-	(159)
Segment operating income (loss)	$(1,821)	$2,050	$(1,711)	$2,796	$1,314
Capital expenditures	1,859	99	68	-	2,026
Real estate assets	129,607	374,022	157,623	-	661,252
Property Sales					
Sales price	$16,600	$-	$717	$-	$17,317
Cost of sale	9,597	-	876	-	10,473
Gain (loss) on sale	$7,003	$-	$(159)	$-	$6,844

For the Three Months Ended June 30, 2013	Commercial Properties	Apartments	Land	Other	Total
Rental and other property revenues	$4,816	$14,740	$-	$4	$19,560
Property operating expenses	2,233	6,302	219	33	8,787
Depreciation	1,643	2,655	-	-	4,298
Mortgage and loan interest	1,582	4,222	1,378	692	7,874
Deferred borrowing costs amortization	19	(97)	31	1	(46)
Loan charges and prepayment penalties	-	26	-	-	26
Interest income	-	-	-	2,119	2,119
Segment operating gain (loss)	$(661)	$1,632	$(1,628)	$1,397	$740
Capital expenditures	2,236	79	228	-	2,543
Real estate assets	137,331	384,308	170,941	-	692,580
Property Sales					
Sales price	$26,974	$24,822	$-	$-	$51,796
Cost of sale	14,914	18,808	-	-	33,722
Gain on sale	$12,060	$6,014	$-	$-	$18,074

The table below reconciles the segment information to the corresponding amounts in the Consolidated Statements of Operations:

	For the Three Months Ended June 30, 2014	2013
Segment operating income	$ 1,314	$ 740
Other non-segment items of income (expense)		
General and administrative	(2,737)	(1,615)

Net income fee to related party	(210)	(48)
Advisory fee to related party	(1,811)	(2,071)
Other income	244	144
Earnings (loss) from unconsolidated joint ventures and investees	(11)	15
Litigation settlement	(86)	57
Income tax benefit	2,035	5,222
Net income (loss) from continuing operations	$ (1,262)	$ 2,444

The table below reconciles the segment information to the corresponding amounts in the Consolidated Balance Sheets:

	June 30, 2014	June 30, 2013
Segment assets	$ 661,252	$ 692,580
Investments in real estate partnerships	1,509	5,740
Notes and interest receivable	69,074	59,145
Other assets	149,388	212,349
Total assets	$ 881,223	$ 969,814

For the Six Months Ended June 30, 2014	Commercial Properties	Apartments	Land	Other	Total
Rental and other property revenues	$8,875	$30,579	$-	$22	$39,476
Property operating expenses	5,846	12,985	393	5	19,229
Depreciation	3,524	5,344	-	-	8,868
Mortgage and loan interest	2,948	8,134	2,415	1,268	14,765
Deferred borrowing costs amortization	18	987	73	188	1,266
Loan charges and prepayment penalties	9	1,573	-	-	1,582
Interest income	-	-	-	6,118	6,118
Gain on land sales	-	-	594	-	594
Segment operating income (loss)	$(3,470)	$1,556	$(2,287)	$4,679	$478
Capital expenditures	2,989	99	151	-	3,239
Real estate assets	129,607	374,022	157,623	-	661,252
Property Sales					
Sales price	$16,600	$23,131	$717	$-	$40,448
Cost of sale	9,597	17,077	123	-	26,797
Gain on sale	$7,003	$6,054	$594	$-	$13,651

For the Six Months Ended June 30, 2013	Commercial Properties	Apartments	Land	Other	Total
Rental and other property revenues	$9,764	$29,148	$34	$4	$38,950
Property operating expenses	5,235	12,351	521	9	18,116
Depreciation	2,726	5,300	-	-	8,026
Mortgage and loan interest	2,840	8,773	2,781	1,403	15,797
Deferred borrowing costs amortization	40	2,241	87	3	2,371
Loan charges and prepayment penalties	-	3,937	-	26	3,963
Interest income	-	-	-	4,296	4,296
Loss on land sales	-	-	(48)	-	(48)
Segment operating gain(loss)	$(1,077)	$(3,454)	$(3,403)	$2,859	$(5,075)
Capital expenditures	2,913	110	281	-	3,304
Real estate assets	137,331	384,308	170,941	-	692,580
Property Sales					
Sales price	$26,974	$50,122	$2,250	$-	$79,346
Cost of sale	14,914	37,917	2,298	-	55,129
Gain (loss) on sale	$12,060	$12,205	$(48)	$-	$24,217

The tables below reconcile the segment information to the corresponding amounts in the Consolidated Statements of Operations:

	For the Six Months Ended June 30,	
	2014	2013
Segment operating income (loss)	$ 478	$ (5,075)
Other non-segment items of income (expense)		
General and administrative	(4,295)	(3,237)
Net income fee to related party	(700)	(104)
Advisory fee to related party	(3,664)	(4,209)
Other income	401	180
Loss on sale of investment	-	(8)
Earnings (loss) from unconsolidated joint ventures and investees	(16)	2
Litigation settlement	3,753	12
Income tax benefit	3,918	7,554
Net loss from continuing operations	$ (125)	$ (4,885)

The table below reconciles the segment information to the corresponding amounts in the Consolidated Balance Sheets:

	June 30,	
	2014	2013
Segment assets	$ 661,252	$ 692,580
Investments in real estate partnerships	1,509	5,740
Notes and interest receivable	69,074	59,145
Other assets	149,388	212,349
Total assets	$ 881,223	$ 969,814

NOTE 8. DISCONTINUED OPERATIONS

We apply the provisions of ASC Topic 360 “Property, Plant and Equipment”. ASC Topic 360 requires that long-lived assets that are to be disposed of by sale be measured at the lesser of (1) book value or (2) fair value less cost to sell. In addition, it requires that one accounting model be used for long-lived assets to be disposed of by sale and broadens the presentation of discontinued operations to include more disposal transactions.

Discontinued operations relates to properties that were either sold or held for sale as of the period ended June 30, 2014. Included in discontinued operations are a total of three and 18 properties for 2014 and 2013, respectively. Properties sold in 2014 have been reclassified to discontinued operations for current and prior year reporting periods. In 2014, we sold one apartment complex (Pecan Pointe) and one commercial property (1010 Common) and have one commercial property held for sale (Sesame Square). In 2013, we sold 11 apartment complexes (Dorado Ranch, Huntington Ridge, Laguna Vista, Legends of El Paso, Mariposa Villas, Paramount Terrace, River Oaks, Savoy of Garland, Stonebridge at City Park, Verandas at City View and Vistas of Pinnacle Park) and four commercial properties (225 Baronne, Amoco, Ergon and Eton Square). The gain on sale of the properties is also included in discontinued operations for those years. The following table summarizes revenue and expense information for the properties sold and held for sale (dollars in thousands):

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2014	2013	2014	2013
Revenues:				
Rental and other property revenues	$ (7)	$ 8,039	$ 1,251	$ 17,103
	(7)	8,039	1,251	17,103
Expenses:				
Property operating expenses	221	3,375	1,208	7,891
Depreciation	21	1,297	193	2,735
General and administrative	140	256	305	525
Total operating expenses	382	4,928	1,706	11,151

Other income (expense):