

TEJON RANCH CO
Form 10-Q
November 08, 2016

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

FORM 10-Q
(Mark One)

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

For the quarterly period ended September 30, 2016
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: 1-7183

TEJON RANCH CO.
(Exact name of
Registrant as specified in
its charter)

Delaware 77-0196136
(State or other jurisdiction of (IRS Employer
incorporation or organization) Identification No.)
P.O. Box 1000, Tejon Ranch, California 93243
(Address of principal executive offices)
Registrant's telephone number, including area code: (661) 248-3000

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 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 the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer
Non-accelerated filer Non-accelerated filer

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

The number of the Company's outstanding shares of Common Stock on October 31, 2016 was 20,789,496.

TEJON RANCH CO. AND SUBSIDIARIES
TABLE OF CONTENTS

	Page
PART I. FINANCIAL INFORMATION	
Item 1. Financial Statements	
Unaudited Consolidated Statements of Operations for the Three and Nine Months Ended September 30, 2016 and 2015	<u>3</u>
Unaudited Consolidated Statements of Comprehensive Income (Loss) for the Three and Nine Months Ended September 30, 2016 and 2015	<u>4</u>
Consolidated Balance Sheets as of September 30, 2016 (unaudited) and December 31, 2015	<u>5</u>
Unaudited Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2016 and 2015	<u>6</u>
Unaudited Consolidated Statement of Changes in Equity and Noncontrolling Interests for the Nine Months Ended September 30, 2016	<u>7</u>
Notes to Unaudited Consolidated Financial Statements	<u>8</u>
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	<u>24</u>
Item 3. Quantitative and Qualitative Disclosures About Market Risk	<u>33</u>
Item 4. Controls and Procedures	<u>36</u>
PART II. OTHER INFORMATION	
Item 1. Legal Proceedings	<u>36</u>
Item 1A. Risk Factors	<u>36</u>
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds	<u>36</u>
Item 3. Defaults Upon Senior Securities	<u>36</u>
Item 4. Mine Safety Disclosures	<u>36</u>
Item 5. Other Information	<u>36</u>
Item 6. Exhibits	<u>37</u>
SIGNATURES	<u>41</u>

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

TEJON RANCH CO. AND SUBSIDIARIES
UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share amounts)

	Three Months Ended September 30, 2016		Nine Months Ended September 30, 2015	
	2016	2015	2016	2015
Revenues:				
Real estate - commercial/industrial	\$2,221	\$2,101	\$6,534	\$6,190
Mineral resources	1,125	1,322	13,052	14,174
Farming	9,319	8,076	11,042	12,470
Ranch operations	414	447	2,253	2,745
Total revenues	13,079	11,946	32,881	35,579
Costs and Expenses:				
Real estate - commercial/industrial	1,747	1,599	5,140	4,884
Real estate - resort/residential	323	558	1,252	1,885
Mineral resources	667	606	7,160	7,023
Farming	7,781	8,123	10,637	11,710
Ranch operations	1,374	1,674	4,263	4,686
Corporate expenses	3,096	2,927	9,262	9,214
Total expenses	14,988	15,487	37,714	39,402
Operating loss	(1,909)	(3,541)	(4,833)	(3,823)
Other Income:				
Investment income	112	116	350	413
Other income	32	125	120	180
Total other income	144	241	470	593
(Loss) from operations before equity in earnings of unconsolidated joint ventures	(1,765)	(3,300)	(4,363)	(3,230)
Equity in earnings of unconsolidated joint ventures, net	2,353	2,055	5,650	4,861
Income (loss) before income tax expense	588	(1,245)	1,287	1,631
Income tax expense (benefit)	271	(434)	503	464
Net income (loss)	317	(811)	784	1,167
Net loss attributable to non-controlling interest	(7)	(23)	(61)	(68)
Net income (loss) attributable to common stockholders	\$324	\$(788)	\$845	\$1,235
Net income (loss) per share attributable to common stockholders, basic	\$0.02	\$(0.04)	\$0.04	\$0.06
Net income (loss) per share attributable to common stockholders, diluted	\$0.02	\$(0.04)	\$0.04	\$0.06

See accompanying notes.

TEJON RANCH CO. AND SUBSIDIARIES
 UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(In thousands)

	Three Months Ended September 30, 2016		Nine Months Ended September 30, 2016	
Net income (loss)	\$317	\$(811)	\$784	\$1,167
Other comprehensive income (loss):				
Unrealized (loss) gain on available for sale securities	(57)	(21)	184	(78)
Unrealized gain (loss) on interest rate swap	578	(1,991)	(2,729)	(1,591)
Other comprehensive income (loss) before taxes	521	(2,012)	(2,545)	(1,669)
Benefit (provision) from income taxes related to other comprehensive income (loss) items	(182)	770	890	633
Other comprehensive income (loss)	339	(1,242)	(1,655)	(1,036)
Comprehensive income (loss)	656	(2,053)	(871)	131
Comprehensive (loss) attributable to non-controlling interests	(7)	(23)	(61)	(68)
Comprehensive income (loss) attributable to common stockholders	\$663	\$(2,030)	\$(810)	\$199
See accompanying notes.				

TEJON RANCH CO. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

(In thousands, except per share data)

	September 30, 2016 (unaudited)	December 31, 2015
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 3,425	\$ 1,930
Marketable securities - available-for-sale	27,617	32,815
Accounts receivable	8,612	6,511
Inventories	6,217	3,517
Prepaid expenses and other current assets	5,261	4,120
Total current assets	51,132	48,893
Real estate and improvements - held for lease, net	23,420	21,942
Real estate development (includes \$87,986 at September 30, 2016 and \$84,194 at December 31, 2015, attributable to Centennial Founders, LLC, Note 15)	245,728	235,466
Property and equipment, net	45,896	44,469
Investments in unconsolidated joint ventures	32,255	30,680
Long-term water assets	42,751	43,806
Deferred tax assets	4,794	4,659
Other assets	2,863	2,004
TOTAL ASSETS	\$ 448,839	\$ 431,919
LIABILITIES AND EQUITY		
Current Liabilities:		
Trade accounts payable	\$ 3,522	\$ 3,252
Accrued liabilities and other	4,166	3,492
Income taxes payable	—	1,237
Deferred income	2,418	1,525
Revolving line of credit	11,000	—
Current maturities of long-term debt	3,346	815
Total current liabilities	24,452	10,321
Long-term debt, less current portion	70,514	73,223
Long-term deferred gains	3,811	3,816
Other liabilities	16,431	13,251
Total liabilities	115,208	100,611
Commitments and contingencies		
Equity:		
Tejon Ranch Co. Stockholders' Equity		
Common stock, \$.50 par value per share:		
Authorized shares - 30,000,000		
Issued and outstanding shares - 20,741,867 at September 30, 2016 and 20,688,154 at December 31, 2015	10,371	10,344
Additional paid-in capital	219,970	216,803
Accumulated other comprehensive loss	(8,557) (6,902
Retained earnings	72,234	71,389
Total Tejon Ranch Co. Stockholders' Equity	294,018	291,634
Non-controlling interest	39,613	39,674
Total equity	333,631	331,308

TOTAL LIABILITIES AND EQUITY	\$ 448,839	\$ 431,919
See accompanying notes.		

TEJON RANCH CO. AND SUBSIDIARIES
 UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (In thousands)

	Nine Months Ended September 30,	
	2016	2015
Operating Activities		
Net income	\$784	\$1,167
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Depreciation and amortization	4,170	3,672
Amortization of premium/discount of marketable securities	386	424
Equity in earnings of unconsolidated joint ventures	(5,650)	(4,861)
Non-cash retirement plan expense	725	761
Deferred income taxes	755	989
Stock compensation expense	3,297	2,914
Distribution of earnings from unconsolidated joint ventures	4,500	—
Changes in operating assets and liabilities:		
Receivables, inventories and other assets, net	(6,622)	(3,572)
Current liabilities	(932)	47
Net cash provided by operating activities	1,413	1,541
Investing Activities		
Maturities and sales of marketable securities	9,010	23,276
Funds invested in marketable securities	(4,014)	(15,344)
Property and equipment expenditures	(19,760)	(18,968)
Communities Facilities District and other reimbursements	4,650	4,971
Investment in unconsolidated joint ventures	(1,900)	(53)
Distribution of equity from unconsolidated joint ventures	1,600	1,100
Other	—	(20)
Net cash used in investing activities	(10,414)	(5,038)
Financing Activities		
Borrowings of short-term debt	19,500	17,540
Repayments of short-term debt	(8,500)	(15,450)
Repayments of long-term debt	(190)	(190)
Taxes on vested stock grants	(314)	(529)
Net cash provided by financing activities	10,496	1,371
Increase (decrease) in cash and cash equivalents	1,495	(2,126)
Cash and cash equivalents at beginning of period	1,930	5,638
Cash and cash equivalents at end of period	\$3,425	\$3,512
Supplemental cash flow information		
Accrued capital expenditures included in current liabilities	\$1,253	\$(153)
Income taxes paid	\$1,350	\$2,153
See accompanying notes.		

TEJON RANCH CO. AND SUBSIDIARIES
 UNAUDITED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY AND NONCONTROLLING
 INTERESTS

(In thousands, except shares outstanding)

	Common Stock Shares Outstanding	Common Stock	Additional Paid-In Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total Stockholders' Equity	Noncontrolling Interest	Total Equity
Balance, December 31, 2015	20,688,154	\$ 10,344	\$ 216,803	\$ (6,902)	\$ 71,389	\$ 291,634	\$ 39,674	\$ 331,308
Net income (loss)	—	—	—	—	845	845	(61)	784
Other comprehensive loss	—	—	—	(1,655)	—	(1,655)	—	(1,655)
Restricted stock issuance	76,710	38	(38)	—	—	—	—	—
Stock compensation	—	—	3,508	—	—	3,508	—	3,508
Shares withheld for taxes and tax benefit of vested shares	(22,997)	(11)	(303)	—	—	(314)	—	(314)
Balance, September 30, 2016	20,741,867	\$ 10,371	\$ 219,970	\$ (8,557)	\$ 72,234	\$ 294,018	\$ 39,613	\$ 333,631

See accompanying notes.

TEJON RANCH CO. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION

The summarized information of Tejon Ranch Co. and its subsidiaries, (the Company, Tejon, we, us and our), furnished pursuant to the instructions to Part I of Form 10-Q is unaudited and reflects all adjustments which are, in the opinion of the Company's management, necessary for a fair statement of the results for the interim period. All such adjustments are of a normal recurring nature. We have evaluated subsequent events through the date of issuance of our consolidated financial statements.

The periods ending September 30, 2016 and 2015 include the consolidation of Centennial Founders, LLC's statement of operations within the resort /residential real estate development segment and statements of cash flows. The Company's September 30, 2016 and December 31, 2015 balance sheets and statements of changes in equity and noncontrolling interests are presented on a consolidated basis including the consolidation of Centennial Founders, LLC.

The Company has identified five reportable segments: commercial/industrial real estate development, resort/residential real estate development, mineral resources, farming, and ranch operations. Information for the Company's reported segments is presented in its consolidated statements of operations. The Company's reporting segments follow the same accounting policies used for the Company's consolidated financial statements. We use segment profit or loss, along with equity in earnings of unconsolidated joint ventures, as the primary measure of profitability to evaluate operating performance and to allocate capital resources.

The results of the period reported herein are not indicative of the results to be expected for the full year due to the seasonal nature of the Company's agricultural activities and timing of real estate sales and leasing activities. Historically, the Company's largest percentages of farming revenues are recognized during the third and fourth quarters of the fiscal year.

Reclassifications

Certain prior year amounts have been reclassified for consistency with the current period presentation. These reclassifications had no effect on results of operations.

Ranch Operations

During the fourth quarter of 2015, the Company reclassified revenues and expenses comprised of grazing leases, game management and other ancillary services supporting the ranch, from commercial/industrial into a new segment called ranch operations. As a result, the Company reclassified prior period ranch operation revenues and expenses on the consolidated statements of income. For the nine months ended September 30, 2015, revenues and expenses reclassified were \$2,745,000 and \$4,686,000, respectively. For the quarter ended September 30, 2015, revenues and expenses reclassified were \$447,000 and \$1,674,000, respectively.

For further information and a summary of significant accounting policies, 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, 2015.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board, or FASB, issued Accounting Standards Update, or ASU, 2014-09, "Revenue from Contracts with Customers", which provides guidance for revenue recognition that supersedes existing revenue recognition guidance (but does not apply to nor supersede accounting guidance for lease contracts). The ASU's core principle is that an entity will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU also requires more detailed disclosures to enable users of financial statements to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. The ASU is effective for reporting periods beginning after December 15, 2016, and should be applied retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying the ASU recognized at the date of initial application. In July 2015, the FASB affirmed its proposal to defer

the effective date by one year. The new standard will become effective for the Company beginning with the first quarter of fiscal 2018. The Company is currently in the process of evaluating the impact of the adoption of this ASU on the Company's consolidated financial statements.

In February 2015, the FASB issued ASU 2015-02, "Consolidation (Topic 810): Amendments to the Consolidation Analysis," which makes certain changes to both the variable interest model and the voting model, including changes to (1) the identification of variable interests (fees paid to a decision maker or service provider), (2) the variable interest entity characteristics for a limited partnership or similar entity, and (3) the primary beneficiary determination. ASU 2015-02 is effective for periods beginning after December 15, 2015. As a result of adopting this ASU, on January 1, 2016 we were not required to consolidate any legal entities that were previously unconsolidated or deconsolidate any legal entities that were previously consolidated. Therefore, upon adoption, we were not required to retrospectively adjust any prior period information or recognize a cumulative effect of the change in retained earnings as a result of the initial application of this update.

In January 2016, the FASB issued ASU 2016-01, "Financial Statements - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities," which requires equity investments in unconsolidated entities (other than those accounted for using the equity method of accounting) to be measured at fair value with changes in fair value recognized in net income. There will no longer be an available-for-sale classification for equity securities with readily determinable fair values. The new guidance is effective for periods beginning after December 15, 2017, with early adoption permitted. The Company is currently in the process of evaluating the impact of the adoption of this ASU on the Company's consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, "Leases." From the lessee's perspective, the new standard establishes a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement for a lessee. From the lessor's perspective, the new standard requires a lessor to classify leases as either sales-type, finance or operating. A lease will be treated as a sale if it transfers all of the risks and rewards, as well as control of the underlying asset, to the lessee. If risks and rewards are conveyed without the transfer of control, the lease is treated as a financing lease. If the lessor doesn't convey risks and rewards or control, an operating lease results. ASU 2016-02 is effective for periods beginning after December 15, 2018. The Company is currently in the process of evaluating the impact of the adoption of this ASU on the Company's consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15 "Statement of Cash Flows (Topic 230)," or ASU 2016-15. ASU 2016-15 is intended to reduce diversity in practice in how certain transactions are classified in the statement of cash flows. The new guidance addresses the classification of various transactions including debt prepayment or debt extinguishment costs, settlement of zero-coupon debt instruments, contingent consideration payments made after a business combination, distributions received from equity method investments, beneficial interests in securitization transactions, and others. The Company is currently in the process of evaluating the impact of the adoption of this ASU on the Company's consolidated financial statements.

2. EQUITY

Earnings Per Share (EPS)

Basic net income per share attributable to common stockholders is based upon the weighted-average number of shares of common stock outstanding during the year. Diluted net income per share attributable to common stockholders is based upon the weighted-average number of shares of common stock outstanding and the weighted-average number of shares outstanding assuming the issuance of common stock upon exercise of warrants to purchase common stock, and the vesting of restricted stock grants per ASC 260, "Earnings Per Share."

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2016	2015	2016	2015
Weighted average number of shares outstanding:				
Common stock	20,732,767	20,669,348	20,719,900	20,658,750
Common stock equivalents-stock options, grants	128,334	79,544	125,940	70,969
Diluted shares outstanding	20,861,101	20,748,892	20,845,840	20,729,719
Warrants				

On August 7, 2013, the Company announced that its Board of Directors declared a dividend of 3,000,000 warrants, or the Warrants, to purchase shares of Company common stock, par value \$0.50 per share, or Common Stock, to holders of record of Common Stock as of August 21, 2013, the Record Date. The Warrants were issued pursuant to a Warrant Agreement between the Company, Computershare, Inc. and Computershare Trust Company, N.A., as warrant agent. The Warrants were distributed

to shareholders on August 28, 2013. Each Warrant entitles the holder to purchase one share of Common Stock at an initial exercise price of \$40.00 per share. The Warrants expired out of the money on August 31, 2016.

3. MARKETABLE SECURITIES

ASC 320, "Investments – Debt and Equity Securities" requires that an enterprise classify all debt securities as either held-to-maturity, trading or available-for-sale. The Company has elected to classify its securities as available-for-sale and therefore is required to adjust securities to fair value at each reporting date. All costs and both realized and unrealized gains and losses on securities are determined on a specific identification basis. The following is a summary of available-for-sale securities at:

(\$ in thousands)	Fair Value Hierarchy	September 30, 2016		December 31, 2015	
		Cost	Estimated Fair Value	Cost	Estimated Fair Value
Marketable Securities:					
Certificates of deposit					
with unrecognized losses for less than 12 months		\$40	\$ 39	\$4,810	\$ 4,797
with unrecognized losses for more than 12 months		—	—	239	238
with unrecognized gains		5,969	5,995	2,800	2,805
Total Certificates of deposit	Level 1	6,009	6,034	7,849	7,840
US Treasury and agency notes					
with unrecognized losses for less than 12 months		—	—	860	857
with unrecognized losses for more than 12 months		—	—	—	—
with unrecognized gains		1,935	1,941	736	738
Total US Treasury and agency notes	Level 2	1,935	1,941	1,596	1,595
Corporate notes					
with unrecognized losses for less than 12 months		5,595	5,575	14,638	14,516
with unrecognized losses for more than 12 months		1,461	1,439	2,080	2,061
with unrecognized gains		9,591	9,629	3,334	3,339
Total Corporate notes	Level 2	16,647	16,643	20,052	19,916
Municipal notes					
with unrecognized losses for less than 12 months		811	802	1,742	1,725
with unrecognized losses for more than 12 months		360	356	301	298
with unrecognized gains		1,831	1,841	1,435	1,441
Total Municipal notes	Level 2	3,002	2,999	3,478	3,464
		\$27,593	\$ 27,617	\$32,975	\$ 32,815

We evaluate our securities for other-than-temporary impairment based on the specific facts and circumstances surrounding each security valued below its cost. Factors considered include the length of time the securities have been valued below cost, the financial condition of the issuer, industry reports related to the issuer, the severity of any decline, our intention not to sell the security, and our assessment as to whether it is not more likely than not that we will be required to sell the security before a recovery of its amortized cost basis. We then segregate the loss between the amounts representing a decrease in cash flows expected to be collected, or the credit loss, which is recognized through earnings, and the balance of the loss which is recognized through other comprehensive income. At September 30, 2016, the fair market value of investment securities was \$24,000 higher than their cost basis.

As of September 30, 2016, the adjustment to accumulated other comprehensive loss in consolidated equity for the temporary change in the value of securities reflected an increase in the market value of available-for-sale securities of \$184,000, which includes estimated taxes of \$64,000. As of September 30, 2016, the Company's gross unrealized holding income equaled \$80,000 and gross unrealized holding losses equaled \$56,000.

The following tables summarize the maturities, at par, of marketable securities as of:

	September 30, 2016				
(\$ in thousands)	2016	2017	2018	2019	Total
Certificates of deposit	\$879	\$531	\$4,400	\$169	\$5,979
U.S. Treasury and agency notes	—	1,234	579	138	1,951
Corporate notes	—	5,207	7,723	3,240	16,170
Municipal notes	—	840	1,705	415	2,960
	\$879	\$7,812	\$14,407	\$3,962	\$27,060

	December 31, 2015				
(\$ in thousands)	2016	2017	2018	2019	Total
Certificates of deposit	\$2,492	\$631	\$4,510	169	\$7,802
U.S. Treasury and agency notes	100	759	579	188	1,626
Corporate notes	4,572	6,525	6,462	1,881	19,440
Municipal notes	995	940	1,455	—	3,390
	\$8,159	\$8,855	\$13,006	\$2,238	\$32,258

The Company's investments in corporate notes are with companies that have an investment grade rating from Standard & Poor's.

4. REAL ESTATE

(\$ in thousands)	September 30, December	
	2016	31, 2015
Real estate development		
Mountain Village	\$ 125,176	\$120,954
Centennial	87,986	84,194
Grapevine	22,404	18,285
Tejon Ranch Commerce Center	10,162	12,033
Real estate development	245,728	235,466
Real estate and improvements - held for lease, net		
Tejon Ranch Commerce Center	21,546	19,783
Rancho Santa Fe and Other	4,242	4,242
Real estate and improvements - held for lease	25,788	24,025
Less accumulated depreciation	(2,368) (2,083)
Real estate and improvements - held for lease, net	\$ 23,420	\$21,942

5. LONG-TERM WATER ASSETS

Long-term water assets consist of water and water contracts held for future use or sale. The water is held at cost, which includes the price paid for the water and the cost incurred to pump and deliver the water. A portion of our water is currently held in a water bank on Company land in southern Kern County. Banked water costs also include costs related to the right to receive additional acre-feet of water in the future from the Antelope Valley East Kern Water Agency, or AVEK. The Company has also banked water within an AVEK owned water bank.

We also purchase water for future use or sale. In 2008 we purchased 8,393 acre feet of transferable water and in 2009 we purchased an additional 6,393 acre-feet of transferable water, the remaining portion of which is held on our behalf by AVEK under an agreement where AVEK will return this water to us at a 1.5 to 1 factor. To date, 8,587 acre-feet of water has been returned and was placed in our Company water bank.

We also have secured State Water Project, or SWP, entitlement under long-term SWP water contracts within the Tulare Lake Basin Water Storage District, or TLBWS, and the Dudley-Ridge Water District, or DRWD, totaling 3,444 acre-feet of SWP entitlement annually, subject to annual SWP allocations. These contracts extend through 2035 and now have been transferred to AVEK for our use in the Antelope Valley. In 2013, the Company acquired from DMB Pacific, or DMB, a contract to purchase water that obligates the Company to purchase 6,693 acre feet of water each year from the Nickel Family, LLC, or Nickel, a California limited liability company that is located in Kern County. The initial term of the water purchase agreement with Nickel runs to 2044 and includes a Company option to extend the contract for an additional 35 years. Purchase costs in 2016 were \$695 per acre-foot. For future years, the purchase cost is subject to annual increases based on the greater of the consumer price index and 3%.

The water purchased under the contract with Nickel is expected to be used in the development of the Company's land for commercial/industrial development, residential development, and farming. Interim uses may include the sale of portions of this water to third party users on an annual basis until this water is fully allocated to Company uses.

On August 6, 2015, Tejon Ranchcorp, or Ranchcorp, a wholly-owned subsidiary of Tejon Ranch Co., entered into a Water Supply Agreement with Pastoria Energy Facility, L.L.C., or PEF. PEF is the current lessee under the power plant lease. Pursuant to the Water Supply Agreement, beginning on January 1, 2016, PEF may purchase from Ranchcorp up to 2,000 acre feet of water and, from January 1, 2017 through July 31, 2030, with an option to extend the term, PEF may purchase from Ranchcorp up to 3,500 acre feet of water per year. PEF is under no obligation to purchase water from Ranchcorp in any year, but is required to pay Ranchcorp an annual option payment equal to 30% of the maximum annual payment. The price of the water under the Water Supply Agreement is \$1,025 per acre foot of annual water, subject to 3% annual increases commencing January 1, 2017. The Water Supply Agreement contains other customary terms and conditions, including representations and warranties, which are typical for agreements of this type. The Company's commitments to sell water can be met through current water assets.

During the nine months ended September 30, 2016, we sold 7,285 acre feet of water totaling \$9,601,000 with a cost of \$5,925,000, which was recorded in the mineral resources segment on the unaudited consolidated statements of operations.

Water contracts with the Wheeler Ridge Maricopa Water Storage District, or WRMWS, and the Tejon-Castac Water District, or TCWD, are also in place, but were entered into with each district at inception of the contract and not purchased later from third parties, and do not have a related financial carrying cost on the books of the Company.

Therefore, there is no amortization expense related to these contracts. These contracts are also subject to annual SWP allocations. Water assets consist of the following:

(in acre-feet, unaudited)	September 30, 2016	December 31, 2015
Banked water and water for future delivery		
AVEK water bank	13,033	13,033
Company water bank	17,287	8,700
AVEK water for future delivery	2,362	2,362
Total Company and AVEK banked water	32,682	24,095
Transferable water*	9,061	14,786
Water Contracts - TLBWS, DRWD	3,444	3,444
Water Contracts - Nickel Water	6,693	6,693
Total purchased water - third parties	51,880	49,018
WRMWS - Contracts with Company	15,547	15,547
TCWD - Contracts with Company	5,749	5,749
TCWD - Banked water contracted to Company	33,390	34,496
Total purchased and contracted water sources in acre feet	106,566	104,810

*Any transferable water with AVEK that is used by the Company or returned by AVEK to the Company will be returned at a 1.5 to 1 factor giving the Company use of a total of 13,592 (9,061 x 1.5) acre feet as of September 30, 2016.

(\$ in thousands)	September 30, December	
	2016	31, 2015
Banked water and water for future delivery	\$ 4,778	\$4,779
Transferable water	9,076	9,117
Water contracts	30,248	31,261
Total long-term water assets	44,102	45,157
less: Current portion	(1,351) (1,351)
	\$ 42,751	\$43,806

6. ACCRUED LIABILITIES AND OTHER

Accrued liabilities and other consists of the following:

(\$ in thousands)	September 30, December	
	2016	31, 2015
Accrued vacation	\$ 832	\$ 801
Accrued paid personal leave	565	585
Accrued bonus	1,717	1,549
Property tax payable	825	—
Other	227	557
	\$ 4,166	\$ 3,492

7. LINE OF CREDIT AND LONG-TERM DEBT

Debt consists of the following:

(\$ in thousands)	September 30, December	
	2016	31, 2015
Revolving line of credit	\$ 11,000	\$—
Term Note	70,000	70,000
Promissory note	4,025	4,215
Total short-term and long-term debt	85,025	74,215
Less: line-of-credit and current maturities of long-term debt	(14,346) (815)
Less: deferred loan costs	(165) (177)
Long-term debt, less current portion	\$ 70,514	\$73,223

On October 13, 2014, the Company, through its wholly-owned subsidiary Ranchcorp, as borrower, entered into an Amended and Restated Credit Agreement, a Term Note and a Revolving Line of Credit Note, with Wells Fargo, or collectively the Credit Facility. The Credit Facility amended and restated the Company's existing credit facility dated as of November 5, 2010 and extended on December 4, 2013. The Credit Facility added a \$70,000,000 Term Note, to the existing \$30,000,000 revolving line of credit, or RLC. Funds from the Term Note were used to finance the Company's purchase of DMB TMV LLC's interest in Tejon Mountain Village LLC. Any future borrowings under the RLC will be used for ongoing working capital requirements and other general corporate purposes. To maintain availability of funds under the RLC, undrawn amounts under the RLC will accrue a commitment fee of 10 basis points per annum. The Company's ability to borrow additional funds in the future under the RLC is subject to compliance with certain financial covenants and making certain representations and warranties. As of September 30, 2016 and December 31, 2015, the RLC had an outstanding balance of \$11,000,000 and \$0, respectively. At the Company's option, the interest rate on this line of credit can float at 1.50% over a selected LIBOR or can be fixed at 1.50% above LIBOR for a fixed rate term. During the term of the Credit Facility (which matures in September 2019), we can borrow at any time and partially or wholly repay any outstanding borrowings and then re-borrow, as necessary. The interest rate per annum applicable to the Term Note is LIBOR (as defined in the Term Note) plus a margin of 170 basis points. The interest rate for the term of the note has been fixed through the use of an interest rate swap at a rate of 4.11%. The Term Note requires interest only payments for the first two years of the term and thereafter requires monthly amortization payments pursuant to a schedule set forth in the Term Note, with the final outstanding principal amount due October 5, 2024. The Company may make voluntary prepayments on the Term Note at any time without penalty (excluding any applicable LIBOR or interest rate swap breakage costs). Each optional prepayment will be

applied to reduce the most remote principal payment then unpaid. The Credit Facility is secured by the Company's farmland and farm assets, which include equipment, crops and crop receivables and the power plant lease and lease site, and related accounts and other rights to payment and inventory.

The Credit Facility requires compliance with three financial covenants: (a) total liabilities divided by tangible net worth not greater than 0.75 to 1.0 at each quarter end; (b) a debt service coverage ratio not less than 1.25 to 1.00 as of each quarter end on a rolling four quarter basis; and (c) maintain liquid assets equal to or greater than \$20,000,000. At September 30, 2016 and December 31, 2015, we were in compliance with all financial covenants.

During the third quarter of 2013, we entered into a promissory note agreement with CMFG Life Insurance Company, to pay a principal amount of \$4,750,000 with principal and interest due monthly starting on October 1, 2013. The interest rate on this promissory note is 4.25% per annum, with monthly principal and interest payments of \$102,700 ending on September 1, 2028. The proceeds from this promissory note were used to eliminate debt that had been previously used to provide long-term financing for a building being leased to Starbucks and provide additional working capital for future investment. The current balance on the note is \$4,025,000. The balance of this long-term debt instrument listed above approximates the fair value of the instrument.

8. OTHER LIABILITIES

Other liabilities consist of the following:

(\$ in thousands)	September 30, December 31,	
	2016	2015
Pension liability (See Note 13)	\$ 2,488	\$ 2,263
Interest rate swap liability (See Note 10)	5,634	2,905
Supplemental executive retirement plan liability (See Note 13)	8,106	7,999
Other	203	84
Total	\$ 16,431	\$ 13,251

For the captions presented in the table above, please refer to the respective Notes to Unaudited Consolidated Financial Statements for further detail.

9. STOCK COMPENSATION - RESTRICTED STOCK AND PERFORMANCE SHARE GRANTS

The Company's stock incentive plans provide for the making of awards to employees based upon a service condition or through the achievement of performance-related objectives. The Company has issued three types of stock grant awards under these plans: restricted stock with service condition vesting; performance share grants that only vest upon the achievement of specified performance conditions, such as corporate cash flow goals, or Performance Condition Grants; and performance share grants that include threshold, target, and maximum achievement levels based on the achievement of specific performance milestones, or Performance Milestone Grants. The Company has also granted performance share grants that contain both performance-based and market-based conditions. Compensation cost for these awards is recognized based on either the achievement of the performance-based conditions, if they are considered probable, or if they are not considered probable, on the achievement of the market-based condition. Failure to satisfy the threshold performance conditions will result in the forfeiture of shares. Forfeiture of share awards with service conditions or performance-based restrictions results in a reversal of previously recognized share-based compensation expense. Forfeiture of share awards with market-based restrictions does not result in a reversal of previously recognized share-based compensation expense.

The following is a summary of the Company's performance share grants with performance conditions for the nine months ended September 30, 2016:

Performance Share Grants with Performance Conditions	
Below threshold performance	—
Threshold performance	211,698
Target performance	389,357
Maximum performance	587,930

The following is a summary of the Company's stock grant activity, both time and performance share grants, assuming target achievement for outstanding performance share grants for the following periods:

	September 30, December 31,	
	2016	2015
Stock grants outstanding beginning of the year at target achievement	272,353	237,045
New stock grants/additional shares due to maximum achievement	257,753	114,221
Vested grants	(51,028)	(52,436)
Expired/forfeited grants	(524)	(26,477)
Stock grants outstanding September 30, 2016 at target achievement	478,554	272,353

The unamortized costs associated with nonvested stock grants and the weighted-average period over which it is expected to be recognized as of September 30, 2016 were \$3,739,716 and 20 months, respectively. The fair value of restricted stock with time-based vesting features is based upon the Company's share price on the date of grant and is expensed over the service period. Fair value of performance share grants that cliff vest based on the achievement of performance conditions is based on the share price of the Company's stock on the day of grant once the Company determines that it is probable that the award will vest. This fair value is expensed over the service period applicable to these grants. For performance share grants that contain a range of shares from zero to maximum we determine, based on historic and projected results, the probability of (1) achieving the performance objective, and (2) the level of achievement. Based on this information, we determine the fair value of the award and measure the expense over the service period related to these grants. Because the ultimate vesting of all performance share grants is tied to the achievement of a performance condition, we estimate whether the performance condition will be met and over what period of time. Ultimately, we adjust compensation cost according to the actual outcome of the performance condition.

Under the Non-Employee Director Stock Incentive Plan, or NDSI Plan, each non-employee director receives his or her annual compensation in stock. The stock is granted at the end of each quarter based on the quarter ending stock price.

The following table summarizes stock compensation costs for the Company's Employee 1998 Stock Incentive Plan, or the Employee Plan, and NDSI Plan for the following periods:

(\$ in thousands)	Nine Months	
	Ended	
	September 30,	September 30,
Employee Plan:	2016	2015
Expensed	\$2,747	\$2,321
Capitalized	211	121
	2,958	2,442
NDSI Plan - Expensed	550	593
Total Stock Compensation Costs	\$3,508	\$3,035

10. INTEREST RATE SWAP LIABILITY

During October 2014, the Company entered into an interest rate swap agreement to hedge cash flows tied to changes in the underlying floating interest rate tied to LIBOR for the Term Note as discussed in Note 7 (Line of Credit and Long-Term Debt) The ineffective portion of the change in fair value of our interest rate swap agreement is required to be recognized directly in earnings. During the quarter ended September 30, 2016, our interest rate swap agreement was 100% effective; because of this, no hedge ineffectiveness was recognized in earnings. Changes in fair value, including accrued interest and adjustments for non-performance risk, on the effective portion of our interest rate swap agreements that are designated and that qualify as cash flow hedges are classified in accumulated other comprehensive income. Amounts classified in accumulated other comprehensive income are subsequently reclassified into earnings in the period during which the hedged transactions affect earnings. As of September 30, 2016, the fair value of our interest rate swap agreement aggregating a liability balance was classified in other liabilities.

We had the following outstanding interest rate swap agreement designated as a cash flow hedge of interest rate risk as of September 30, 2016 (\$ in thousands):

Effective Date	Maturity Date	Fair Value
----------------	---------------	------------

Edgar Filing: TEJON RANCH CO - Form 10-Q

	Fair Value Hierarchy	Weighted Average Interest Rate		Notional Amount	
October 15, 2014	October 5, 2024	Level 2	4.11%	\$(5,634)	\$70,000

15

11. INCOME TAXES

For the nine months ended September 30, 2016, the Company's income tax expense was \$503,000 compared to an income tax expense of \$464,000 for the nine months ended September 30, 2015. These represent effective income tax rates of approximately 39% and 28% for the nine months ended September 30, 2016 and, 2015, respectively. As of September 30, 2016, we did not have income taxes payable.

The Company classifies interest and penalties incurred on tax payments as income tax expense. During the nine months ended September 30, 2016, the Company made \$1,350,000 of income tax payments for the 2015 tax year.

12. COMMITMENTS AND CONTINGENCIES

In 2016, the Company paid \$8,529,000 for water contracts. Water contract payments consist of SWP, contracts with WRMWDS, TCWD, TLBWS, DRWD and the Nickel water contract. The SWP contracts run through 2035 and the Nickel water contract runs to 2044, with an option to extend an additional 35 years. As discussed in Note 5 (Long-Term Water Assets), we purchased the assignment of a contract to purchase water in late 2013. The assigned water contract is with Nickel Family, LLC, and obligates us to purchase 6,693 acre-feet of water annually through the term of the contract.

The Company is obligated to make payments of approximately \$800,000 per year to the Tejon Ranch Conservancy as prescribed in the Conservation Agreement we entered into with five major environmental organizations in 2008. Our advances to the Tejon Ranch Conservancy are dependent on the occurrence of certain events and their timing, and are therefore subject to change in amount and period. These amounts are recorded in real estate development for the Centennial and Mountain Village at Tejon Ranch, or MV, projects. Our obligation under this commitment terminates at the end of 2021.

The Company exited a consulting contract during the second quarter of 2014 related to the Grapevine Development and is obligated to pay an earned incentive fee at the time of successful receipt of project entitlements and at a value measurement date five-years after entitlements have been achieved for Grapevine. The final amount of the incentive fees will not be finalized until the future payment dates. The Company believes that net savings from exiting the contract over this future time period will more than offset the incentive payment costs.

The Tejon Ranch Public Facilities Financing Authority, or TRPFFA, is a joint powers authority formed by Kern County and TCWD to finance public infrastructure within the Company's Kern County developments. TRPFFA has created two Community Facilities Districts, or CFDs, the West CFD and the East CFD. The West CFD has placed liens on 420 acres of the Company's land to secure payment of special taxes related to \$28,620,000 of bond debt sold by TRPFFA for TRCC-West. The East CFD has placed liens on 1,931 acres of the Company's land to secure payments of special taxes related to \$55,000,000 of bond debt sold by TRPFFA for TRCC-East. At TRCC-West, the West CFD has no additional bond debt approved for issuance. At TRCC-East, the East CFD has approximately \$65,000,000 of additional bond debt authorized by TRPFFA that can be sold in the future.

In connection with the sale of bonds there is a standby letter of credit for \$5,426,000 related to the issuance of East CFD bonds. The standby letter of credit is in place to provide additional credit enhancement and cover approximately two years' worth of interest on the outstanding bonds. This letter of credit will not be drawn upon unless the Company, as the largest landowner in the CFD, fails to make its property tax payments. The Company believes that the letter of credit will never be drawn upon. The letter of credit is for two years and will be renewed in two-year intervals as necessary. The annual cost related to the letter of credit is approximately \$83,000.

The Company is obligated, as a landowner in each CFD, to pay its share of the special taxes assessed each year. The secured lands include both the TRCC-West and TRCC-East developments. Proceeds from the sale of West CFD bonds went to reimburse the Company for public infrastructure related to the TRCC-West development. As of September 30, 2016, there were no additional improvement funds remaining from the West CFD bonds. During the first quarter of 2016, the East CFD reimbursed the Company approximately \$4,162,000 for public infrastructure. After this payment, there is \$13,923,000 in funds remaining in the East CFD improvement fund. There were no reimbursement payments made to the Company during the second or third quarters of 2016. During 2016, the Company paid approximately \$1,292,425 in special taxes. As development continues to occur at TRCC, new owners of land and new lease tenants, through triple-net leases, will bear an increasing portion of the assessed special tax. This amount could change in the future based on the amount of bonds outstanding and the amount of taxes paid by

new owners of land and new lease tenants. The assessment of each individual property sold or leased is not determinable at this time because it is based on the current tax rate and the assessed value of the property at the time of sale or on its assessed value at the time it is leased to a third-party. Accordingly, the Company is not currently required to recognize an obligation.

In July 2014, the Company received a copy of a Notice of Intent to Sue, or Notice, dated July 17, 2014 indicating that the Center for Biological Diversity, the Wishtoyo Foundation and Dee Dominguez intend to initiate a lawsuit against the U.S. Fish and Wildlife Service, or USFWS, under the federal Endangered Species Act challenging USFWS's approval of Ranchcorp's Tehachapi Uplands Multiple Species Habitat Conservation Plan, or TUMSHCP, and USFWS's issuance of an Incidental Take Permit, or ITP, to Ranchcorp for the take of federally listed species. The foregoing approvals authorize, among other things, removal of California condor habitat associated with Ranchcorp's potential future development of MV. No lawsuit has been filed at this time. It is not possible to predict whether any lawsuit will actually be filed or whether the Company or Ranchcorp will incur any damages from such a lawsuit.

National Cement

The Company leases land to National Cement Company of California Inc., or National, for the purpose of manufacturing Portland cement from limestone deposits on the leased acreage. The California Regional Water Quality Control Board, or RWQCB, for the Lahontan Region issued orders in the late 1990s with respect to environmental conditions on the property currently leased to National.

One order directs the Company's former tenant Lafarge Corporation (or Lafarge), the current tenant National, and the Company to clean up groundwater contamination on the leased property. Lafarge and National installed a groundwater cleanup system in 2003 and that system continues to operate. National and Lafarge have consolidated, closed, and capped cement kiln dust piles located on land leased from the Company. A second order directs National, Lafarge, and the Company to maintain and monitor the effectiveness of the cap.

The Company is not aware of any failure by Lafarge or National to comply with directives of the RWQCB. Under current and prior leases, National and Lafarge are obligated to indemnify the Company for costs and liabilities arising out of their use of the leased premises. The Company believes that the matters described above are included within the scope of the National or Lafarge indemnity obligations. If the Company is required to perform the work at its own cost, it is unlikely that the amount of any such expenditure by the Company would be material and there is no reasonable likelihood of continuing risk from this matter.

Antelope Valley Groundwater Cases

On November 29, 2004, a conglomerate of public water suppliers filed a cross-complaint in the Los Angeles Superior Court seeking a judicial determination of the rights to groundwater within the Antelope Valley basin, including the groundwater underlying the Company's land near the Centennial project. Four phases of a multi-phase trial have been completed. Upon completion of the third phase, the court ruled that the groundwater basin is currently in overdraft and established a current total sustainable yield. The fourth phase of trial occurred in the first half of 2013 and resulted in confirmation of each party's groundwater pumping for 2011 and 2012. The fifth phase of the trial commenced in February 2014, and concerned 1) whether the United States has a federal reserved water right to basin groundwater, and 2) the rights to return flows from imported water. The court heard evidence on the federal reserve right but continued the trial on the return flow issues while most of the parties to the adjudication discussed a settlement, including rights to return flows. In February 2015, more than 140 parties representing more than 99% of the current water use within the adjudication boundary agreed to a settlement. On March 4, 2015, the settling parties, including Tejon, submitted a Stipulation for Entry of Judgment and Physical Solution to the court for approval. On December 23, 2015, the court entered Judgment approving the Stipulation for Entry of Judgment and Physical Solution. The Company's water supply plan for the Centennial project anticipated reliance on, among other sources, a certain quantity of groundwater underlying the Company's lands in the Antelope Valley. The Company's allocation in the Judgment is consistent with that amount. Prior to the Judgment becoming final, on February 19 and 22, 2016, several parties, including the Willis Class and Phelan Pinon Hills CSD, filed notices of appeal from the Judgment. Notwithstanding the appeals, the parties with assistance from the Court have begun establishment of the Watermaster and administration of the Physical Solution, consistent with the Judgment.

Summary and Status of Kern Water Bank Lawsuits

On June 3, 2010, the Central Delta and South Delta Water Agencies and several environmental groups, including the Center for Biological Diversity (collectively, "Central Delta"), filed a complaint in the Sacramento County Superior Court against the California Department of Water Resources, or DWR, Kern County Water Agency and a number of

“real parties in interest,” including the Company and TCWD. The lawsuit challenges certain amendments to the SWP contracts that were originally approved in 1995, known as the “Monterey Amendments.”

The original Environmental Impact Report, or EIR, for the Monterey Amendments was determined to be insufficient in an earlier lawsuit. The current lawsuit principally (i) challenges the adequacy of the remedial EIR that DWR prepared as a result of the original lawsuit and (ii) challenges the validity of the Monterey Amendments on various grounds, including the transfer of the Kern Water Bank, or KWB, from DWR to the Kern County Water Agency and in turn to the Kern Water Bank Authority, or KWBA, whose members are various Kern and Kings County interests, including TCWD, which TCWD has a 2% interest in the KWBA. A parallel lawsuit was also filed by Central Delta in Kern County Superior Court on July 2, 2010, against Kern County Water Agency, also naming the Company and TCWD as real parties in interest, which has been stayed pending the outcome of the other action against DWR. The Company is named on the ground that it “controls” TCWD. This lawsuit has since been moved to the Sacramento County Superior Court. Another lawsuit was filed in Kern County Superior Court on June 3, 2010, by two districts adjacent to the KWB, namely Rosedale Rio Bravo and Buena Vista Water Storage Districts, or Rosedale, asserting that the remedial EIR did not adequately evaluate potential impacts arising from operations of the KWB, but this lawsuit did not name the Company, only TCWD. TCWD has a contract right for water stored in the KWB and rights to recharge and withdraw water. This lawsuit has since been moved to the Sacramento County Superior Court. In an initial favorable ruling on January 25, 2013, the court determined that the challenges to the validity of the Monterey Amendments, including the transfer of the KWB, were not timely and were barred by the statutes of limitation, the doctrine of laches, and by the annual validating statute. The substantive hearing on the challenges to the EIR was held on January 31, 2014. On March 5, 2014 the court issued a decision, rejecting all of Central Delta’s California Environmental Quality Act, or CEQA, claims, except the Rosedale claim, joined by Central Delta, that the EIR did not adequately evaluate future impacts from operation of the KWB, in particular potential impacts on groundwater and water quality.

On November 24, 2014, the court issued a writ of mandate that requires DWR to prepare a revised EIR regarding the Monterey Amendments evaluating the potential operational impacts of the KWB. The writ authorizes the continued operation of the KWB pending completion of the revised EIR subject to certain conditions including those described in an interim operating plan negotiated between the KWBA and Rosedale. The writ of mandate, as revised by the court, requires DWR to certify the revised EIR and file the return to the writ of mandate by September 28, 2016. On September 20, 2016 the Director of DWR (a) certified the Revised EIR as in compliance with CEQA, (b) adopted findings, a statement of overriding considerations, and a mitigation, monitoring and reporting program as required by CEQA, (c) made a new finding pertaining to carrying out the Monterey Amendments through continued use and operation of the KWB by the KWBA, and (d) caused a notice of determination to be filed with the Office of Planning and Resources of the State of California on September 22, 2016. On September 28, 2016, DWR filed with the Superior Court its return to the writ of mandate. The Superior Court has not scheduled a hearing on DWR’s return to the writ of mandate. To the extent that there may be an adverse outcome of the claims, the monetary value cannot be estimated at this time.

On November 24, 2014, the court entered a judgment in the Central Delta case (1) dismissing the challenges to the validity of the Monterey Amendments and the transfer of the KWB in their entirety and (2) granting in part, and denying, in part, the CEQA petition for writ of mandate. Central Delta has appealed the judgment and the KWBA and certain other parties have filed a cross-appeal with regard to certain defenses to the CEQA cause of action. The appeals are pending in the California Court of Appeal.

On December 3, 2014, the court entered judgment in the Rosedale case (i) in favor of Rosedale in the CEQA cause of action, and (ii) dismissing the declaratory relief cause of action. No appeal of the Rosedale judgment has been filed.

Proceedings Incidental to Business

From time to time, we are involved in other proceedings incidental to our business, including actions relating to employee claims, environmental law issues, real estate disputes, contractor disputes and grievance hearings before labor regulatory agencies.

The outcome of these other proceedings is not predictable. However, based on current circumstances, we do not believe that the ultimate resolution of these other proceedings, after considering available defenses and any insurance coverage or indemnification rights, will have a material adverse effect on our financial position, results of operations or cash flows either individually or in the aggregate.

13. RETIREMENT PLANS

The Company has a defined benefit plan that covers many of its employees, or the Benefit Plan. The benefits are based on years of service and the employee's five-year final average salary. Contributions are intended to provide for benefits attributable to service both to-date and expected-to-be provided in the future. The Company funds the plan in accordance with the Employee Retirement Income Security Act of 1974 (ERISA) and the Pension Protection Act. The Company anticipates contributing approximately \$450,000 to the plan during 2016.

Plan assets consist of equity, debt and short-term money market investment funds. The plan's current investment policy targets 65% equities, 25% debt and 10% money market funds. Equity and debt investment percentages are allowed to fluctuate plus or minus 20% to take advantage of market conditions. As an example, equities could fluctuate from 78% to 52% of plan assets. At September 30, 2016, the investment mix was approximately 60% equity, 34% debt, and 6% money market funds. At December 31, 2015, the investment mix was approximately 61% equity, 33% debt and 6% money market funds. Equity investments consist of a combination of individual equity securities plus value funds, growth funds, large cap funds and international stock funds. Debt investments consist of U.S. Treasury securities and investment grade corporate debt. The weighted-average discount rate used in determining the periodic pension cost is 4.6% in 2016 and 2015. The expected long-term rate of return on plan assets is 7.5% in 2016 and 2015. The long-term rate of return on plan assets is based on the historical returns within the plan and expectations for future returns.

The expected total pension and retirement expense for the Benefit Plan was as follows:

	Nine Months Ended September 30,	
(\$ in thousands)	2016	2015
Cost components:		
Service cost-benefits earned during the period	\$(167)	\$(199)
Interest cost on projected benefit obligation	(305)	(350)
Expected return on plan assets	387	462
Net amortization and deferral	(138)	(213)
Total net periodic pension cost	\$(223)	\$(300)

The Company has a Supplemental Executive Retirement Plan, or SERP, to restore to executives designated by the Compensation Committee of the Board of Directors the full benefits under the pension plan that would otherwise be restricted by certain limitations now imposed under the Internal Revenue Code. The SERP is currently unfunded. The pension and retirement expense for the SERP was as follows:

	Nine Months Ended September 30,	
(\$ in thousands)	2016	2015
Cost components:		
Interest cost on projected benefit obligation	(242)	(208)
Net amortization and deferral	(257)	(253)
Total net periodic pension cost	\$(499)	\$(461)

14. BUSINESS SEGMENTS

We currently operate in five business segments: commercial/industrial real estate development, resort/residential real estate development, mineral resources, farming, and ranch operations.

Commercial lease revenue consists of land and building leases to tenants at our commercial retail and industrial developments, base and percentage rents from our Pastoria Energy Facility power plant lease, communication tower rents, and payments from easement leases.

The revenue components of the commercial/industrial real estate development segment were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(\$ in thousands)	2016	2015	2016	2015
Pastoria Energy Facility Lease	\$967	\$963	\$2,698	\$2,755
Commercial leases	881	766	2,687	2,167
Communication leases	205	196	599	588
Landscaping and other	168	176	550	680

Edgar Filing: TEJON RANCH CO - Form 10-Q

Commercial/industrial revenues	2,221	2,101	6,534	6,190
Equity in earnings from unconsolidated joint ventures	2,353	2,055	5,650	4,861
Total commercial/industrial revenues and equity in earnings from unconsolidated joint ventures	4,574	4,156	12,184	11,051
Operating income from commercial/industrial and unconsolidated joint ventures	\$2,827	\$2,557	\$7,044	\$6,167

19

The resort/residential real estate development segment is actively involved in the land entitlement and development process internally and through a joint venture. The segment incurs costs and expenses related to its development activities, but currently generates no revenue. The segment produced losses of \$1,252,000 and \$1,885,000 for the nine months ended September 30, 2016 and 2015, respectively. The segment produced losses of \$323,000 and \$558,000 for the quarters ended September 30, 2016 and 2015, respectively.

The mineral resources segment receives oil and mineral royalties in addition to periodic reimbursable costs from lessors. The segment also generates revenues through water sales. The revenue components of the mineral resources segment were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(\$ in thousands)	2016	2015	2016	2015
Oil and gas	\$394	\$640	\$1,163	\$2,333
Water sales	—	—	9,601	10,165
Rock aggregate	306	282	813	629
Cement	367	373	996	916
Land lease for oil exploration	25	27	151	131
Reimbursable costs	33	—	328	—
Total mineral resources revenues	1,125	1,322	13,052	14,174
Income from mineral resources	\$458	\$716	\$5,892	\$7,151

The farming segment produces revenues from the sale of almonds, pistachios, wine grapes, and hay. The revenue components of the farming segment were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(\$ in thousands)	2016	2015	2016	2015
Almonds	\$1,310	\$3,687	\$2,654	\$7,066
Pistachios	5,745	2,136	6,003	2,899
Wine grapes	1,961	1,986	1,961	1,986
Hay and other	303	267	424	519
Total farming revenues	9,319	8,076	11,042	12,470
(Loss) income from farming	\$1,538	\$(47)	\$405	\$760

Ranch operations consists of game management, ranch and property maintenance, and ancillary land uses such as grazing leases and filming. Within game management, we offer a wide variety of guided big game hunts including trophy Rocky Mountain elk, deer, turkey and wild pig. The revenue components of the ranch operations segment were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(\$ in thousands)	2016	2015	2016	2015
Game management	\$258	\$327	\$1,110	\$1,444
Grazing	(8)	27	765	938
Filming and other	164	93	378	363
Total ranch operations revenues	414	447	2,253	2,745

(Loss) income from ranch operations \$(960) \$(1,227) \$(2,010) \$(1,941)

20

15. INVESTMENT IN UNCONSOLIDATED AND CONSOLIDATED JOINT VENTURES

The Company accounts for its investments in unconsolidated joint ventures using the equity method of accounting unless the venture is a variable interest entity, or VIE, and meets the requirements for consolidation or is a voting interest entity and is controlled by the Company. The Company's investment in its unconsolidated joint ventures at September 30, 2016 was \$32,255,000. The equity in earnings of unconsolidated joint ventures was \$2,353,000 and \$5,650,000 for the three and nine months ended September 30, 2016, respectively. The Company's current joint ventures are as follows:

Petro Travel Plaza Holdings LLC – TA/Petro is an unconsolidated joint venture with TravelCenters of America, LLC for the development and management of travel plazas and convenience stores. The Company has 50% voting rights and shares 60% of profit and losses in this joint venture. It houses multiple commercial eating establishments as well as diesel and gasoline operations in TRCC. The Company does not control the investment due to its having only 50% voting rights, and because our partner in the joint venture is the managing partner and performs all of the day-to-day operations and has significant decision making authority regarding key business components such as fuel inventory and pricing at the facility. At September 30, 2016, the Company had an equity investment balance of \$16,566,000 in this joint venture.

Majestic Realty Co. – Majestic Realty Co., or Majestic, is a privately-held developer and owner of master planned business parks in the United States. The Company partnered with Majestic to form two 50/50 joint ventures to acquire, develop, manage, and operate industrial real estate at TRCC. The partners have equal voting rights and equally share in the profit and loss of the joint venture. At September 30, 2016, the Company's investment in these joint ventures was \$1,888,000, which includes our outside basis.

In August 2016, we partnered with Majestic to form TRC-MRC 2, LLC to acquire, lease, and maintain a fully occupied warehouse at TRCC-West. The partnership acquired the 651,909 square foot building for \$24,773,000 and was largely financed through a \$21,080,000 promissory note guaranteed by both partners. The note matures in September 2020 and currently has an outstanding principal balance, less loan fees, of \$20,926,000.

In September 2016, TRC-MRC 1, LLC was formed to develop and operate an approximately 480,480 square foot industrial building at TRCC-East. The joint venture is currently in the initial planning and design phase of the industrial building.

Rockefeller Joint Ventures – The Company has three joint ventures with Rockefeller Group Development Corporation or Rockefeller. At September 30, 2016, the Company's combined equity investment balance in these three joint ventures was \$13,801,000.

Two joint ventures are for the development of buildings on approximately 91 acres and are part of an agreement for the potential development of up to 500 acres of land in TRCC including pursuing Foreign Trade Zone, or FTZ, designation and development of the property within the FTZ for warehouse distribution and light manufacturing. The Company owns a 50% interest in each of the joint ventures. Currently the Five West Parcel LLC joint venture owns and leases a 606,000 square foot building to Dollar General which has now been extended to April 2022, and includes an option to extend for an additional three years. For operating revenue, please see the following table. The Five West Parcel joint venture currently has an outstanding term loan with a balance of \$10,385,000 that matures on May 5, 2022. The Company and Rockefeller guarantee the performance of the debt. The second of these joint ventures, 18-19 West LLC, was formed in August 2009 through the contribution of 61.5 acres of land by the Company, which is being held for future development. Both of these joint ventures are being accounted for under the equity method due to both members having significant participating rights in the management of the ventures.

The third joint venture is the TRCC/Rock Outlet Center LLC joint venture that was formed during the second quarter of 2013 to develop, own, and manage a net leasable 326,000 square foot outlet center on land at TRCC-East. The cost of the outlet center was approximately \$87,000,000 and was funded through a construction loan for up to 60% of the costs and the remaining 40% was through equity contributions from the two members. The Company controls 50% of the voting interests of TRCC/Rock Outlet Center LLC, thus it does not control by voting interest alone. The Company is the named managing member, as such we considered the presumption that a managing member controls the limited liability company. The managing member's responsibilities relate to the routine day-to-day activities of TRCC/Rock Outlet Center LLC. However, all operating decisions during development and operations, including the setting and monitoring of the budget, leasing, marketing, financing and selection of the contractor for any of the project's construction, are jointly made by both members of the joint venture. Therefore, the Company concluded that both members have significant participating rights that are sufficient to overcome the presumption of the Company controlling the joint venture through it being named the managing member. Therefore, the investment in TRCC/Rock Outlet Center LLC is being accounted for under the equity method. The TRCC/Rock Outlet Center LLC joint venture is separate from the aforementioned agreement to potentially develop up to 500 acres of land in TRCC. During the fourth quarter of 2013, the TRCC/Rock Outlet Center LLC joint venture entered into a construction line of credit agreement with a financial institution for \$52,000,000 that, as of September 30, 2016, had an outstanding balance of \$51,378,000. The Company and Rockefeller guarantee the performance of the debt.

Centennial Founders, LLC – Centennial Founders, LLC is a joint venture with TRI Pointe Homes (formerly Pardee Homes), Lewis Investment Company, and CalAtlantic Group Inc. (formerly Standard Pacific Corp.) that was organized to pursue the entitlement and development of land that the Company owns in Los Angeles County. Based on the Second Amended and Restated Limited Liability Company Agreement of Centennial Founders, LLC and the change in control and funding that resulted from the amended agreement, Centennial Founders, LLC qualified as a VIE, beginning in the third quarter of 2009 and the Company was determined to be the primary beneficiary. As a result, Centennial Founders, LLC has been consolidated into our financial statements beginning in that quarter. Our partners retained a noncontrolling interest in the joint venture. At September 30, 2016 the Company had a 76.32% ownership position in Centennial Founders, LLC.

The Company's investment balance in its unconsolidated joint ventures differs from its respective capital accounts in the respective joint ventures. The differential represents the difference between the cost basis of assets contributed by the Company and the agreed upon contribution value of the assets contributed.

Unaudited condensed balance sheet information of the Company's unconsolidated and consolidated joint ventures as of September 30, 2016 and December 31, 2015 and unaudited condensed statements of operations for the nine months ended September 30, 2016 and 2015 are as follows:

Statement of Operations for the nine months ended September 30, 2016

	Unconsolidated				Consolidated	
	Petro Travel					
(\$ in thousands)	Plaza	Majestic	Rockefeller	Total	Centennial-VIE	
	Holdings					
Revenues	\$76,277	\$ 228	\$ 9,222	\$85,727	\$ 311	
Net income (loss)	9,067	(163)	583	9,487	(298)	
Partner's share of net income (loss)	3,627	(82)	292	3,837	(17)	
Equity in earnings (loss)	\$5,440	\$ (81)	\$ 291	\$5,650	\$ —	

Statement of Operations for the nine months ended September 30, 2015

	Unconsolidated				Consolidated	
	Petro Travel					
(\$ in thousands)	Plaza	Majestic	Rockefeller	Total	Centennial-VIE	
	Holdings					
Revenues	\$78,483	\$ —	—\$ 9,281	\$87,764	\$ 205	
Net income (loss)	8,119	—	(20)	8,099	(175)	

Edgar Filing: TEJON RANCH CO - Form 10-Q

Partner's share of net income (loss)	3,248	—	(10)	3,238	(45)
Equity in earnings (loss)	\$4,871	\$	—	\$(10)	\$4,861	\$ —

Balance Sheet Information as of September 30, 2016

(\$ in thousands)	Unconsolidated				Consolidated
	Petro Travel				Centennial-VIE
	Plaza	Majestic	Rockefeller	Total	
	Holdings				
Current assets	\$10,960	\$219	\$8,759	\$19,938	\$32
Real Estate	54,977	25,893	81,507	162,377	84,784
Other assets	166	(1,340)	18,154	16,980	3
Long-term debt	(15,274)	(20,926)	(61,763)	(97,963)	—
Other liabilities	(2,552)	(319)	(1,418)	(4,289)	(590)
Net assets	\$48,277	\$3,527	\$45,239	\$97,043	\$84,229

Balance Sheet Information as of December 31, 2015

(\$ in thousands)	Unconsolidated				Consolidated
	Petro Travel				Centennial-VIE
	Plaza	Majestic	Rockefeller	Total	
	Holdings				
Current assets	\$12,013	\$—	\$8,033	\$20,046	\$230
Real Estate	52,296	—	83,163	135,459	81,742
Other assets	264	—	20,011	20,275	9
Long-term debt	(14,973)	—	(62,282)	(77,255)	—
Other liabilities	(2,890)	—	(1,181)	(4,071)	(754)
Net assets	\$46,710	\$—	\$47,744	\$94,454	\$81,227

16. RELATED PARTY TRANSACTIONS

TCWD is a not-for-profit governmental entity, organized on December 28, 1965, pursuant to Division 13 of the Water Code, State of California. TCWD is a landowner voting district, which requires an elector, or voter, to be an owner of land located within the district. TCWD was organized to provide the water needs for future municipal and industrial development. The Company is the largest landowner and taxpayer within TCWD. The Company has a water service contract with TCWD that entitles us to receive all of TCWD's State Water Project entitlement and all of TCWD's banked water. TCWD is also entitled to make assessments of all taxpayers within the district, to the extent funds are required to cover expenses and to charge water users within the district for the use of water. From time to time, we transact with TCWD in the ordinary course of business.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains forward-looking statements, including without limitation statements regarding strategic alliances, the almond, pistachio and grape industries, the future plantings of permanent crops, future yields, prices and water availability for our crops and real estate operations, future prices, production and demand for oil and other minerals, future development of our property, future revenue and income of our jointly-owned travel plaza and other joint venture operations, potential losses to the Company as a result of pending environmental proceedings, the adequacy of future cash flows to fund our operations, market value risks associated with investment and risk management activities and with respect to inventory, accounts receivable and our own outstanding indebtedness and other future events and conditions. In some cases these statements are identifiable through the use of words such as “anticipate”, “believe”, “estimate”, “expect”, “intend”, “plan”, “project”, “target”, “can”, “could”, “will”, “should”, “would”, and similar expressions. In addition, any statements that refer to projections of our future financial performance, our anticipated growth, and trends in our business and other characterizations of future events or circumstances are forward-looking statements. We caution you not to place undue reliance on these forward-looking statements. These forward-looking statements are not a guarantee of future performances and are subject to assumptions and involve known and unknown risks, uncertainties and other important factors that could cause the actual results, performance or achievements of the Company, or industry results, to differ materially from any future results, performance, or achievement implied by such forward-looking statements. These risks, uncertainties and important factors include, but are not limited to, weather, market and economic forces, availability of financing for land development activities, competition and success in obtaining various governmental approvals and entitlements for land development activities. No assurance can be given that the actual future results will not differ materially from the forward-looking statements that we make for a number of reasons including those described above in the section entitled, “Risk Factors” in this report and our Annual Report on Form 10-K.

Overview

We are a diversified real estate development and agribusiness company committed to responsibly using our land and resources to meet the housing, employment, and lifestyle needs of Californians and to create value for our shareholders. In support of these objectives, we have been investing in land planning and entitlement activities for new industrial and master planned communities and in infrastructure improvements within our active industrial development. Our prime asset is approximately 270,000 acres of contiguous, largely undeveloped land that, at its most southerly border, is 60 miles north of Los Angeles and, at its most northerly border, is 15 miles east of Bakersfield. Our primary business objective is to maximize long-term shareholder value through the monetization of our land-based assets. A key element of our strategy is to entitle and then develop large-scale residential master planned communities to serve the growing populations of Southern and Central California. We are currently engaged in commercial sales and leasing at our fully operational commercial/industrial center. All of these efforts are supported by diverse revenue streams generated from other operations, including farming, mineral resources, ranch operations and our various joint ventures.

We currently operate in five business segments: commercial/industrial real estate, resort/residential real estate, mineral resources, farming, and ranch operations.

Activities within the commercial/industrial real estate segment include: entitling, planning, and permitting of land for development; construction of infrastructure; construction of pre-leased buildings; construction of buildings to be leased or sold; and the sale of land to third parties for their own development. The commercial/industrial segment also includes activities related to power plant leases, communications leases, and landscape maintenance services. The primary commercial/industrial development is the Tejon Ranch Commerce Center, or TRCC. TRCC includes developments east and west of Interstate 5 at TRCC-East and TRCC-West, respectively.

We are also involved in multiple joint ventures with several partners. Our joint venture with TravelCenters of America, or TA/Petro, owns and operates two travel and truck stop facilities, and also operates five separate gas stations with convenience stores within TRCC-West and TRCC-East. We are involved in three joint ventures with Rockefeller Development Group: Five West Parcel LLC, which owns a 606,000 square foot building in TRCC-West that is fully leased; 18-19 West LLC, which owns 61.5 acres of land for future development within TRCC-West; and

TRCC/Rock Outlet Center LLC, which operates the Outlets at Tejon, a net leasable 326,000 square foot shopping experience with 70 premiere retailers. Lastly, we have partnered with Majestic Realty Co. to develop, manage, and operate industrial buildings within TRCC. The joint ventures help us to expand our commercial/industrial business activities within TRCC.

The resort/residential real estate segment is actively involved in the land entitlement and development process through wholly-owned subsidiaries and a joint venture. Our active developments within resort/residential are Mountain Village at Tejon, or MV, Centennial at Tejon, or Centennial, and Grapevine at Tejon, or Grapevine. Please refer to our Annual Report on Form 10-K for the year ended December 31, 2015 for a more detailed description of our active developments within resort/residential

Our mineral resources segment generates revenues from oil and gas royalty leases, rock and aggregate mining leases, a lease with National Cement, and water sales.

The farming segment produces revenues from the sale of wine grapes, almonds, pistachios, and hay.

Our ranch operations segment consist of game management revenues and ancillary land uses such as grazing leases and filming. Ranch operations is charged with the upkeep, maintenance, and security of all 270,000 acres of land.

Within game management we operate High Desert Hunt Club, a premier upland bird hunting club, along with various game hunting memberships.

For the first nine months of 2016 we had net income attributable to common stockholders of \$845,000 compared to net income attributable to common stockholders of \$1,235,000 for the first nine months of 2015. This decrease was primarily attributable to declines in crop revenues, a result of reduced inventory carryover from the 2015 harvest and falling commodity prices. Oil royalties have also declined as a result of depressed oil prices leading to lower production volumes. These declines were partially offset by an increase in income from our unconsolidated joint ventures.

This Management's Discussion and Analysis of Financial Condition and Results of Operations provides a narrative discussion of our results of operations. It contains the results of operations for each operating segment of the business and is followed by a discussion of our financial position. It is useful to read the business segment information in conjunction with Note 14 (Business Segments) of the Notes to Unaudited Consolidated Financial Statements.

Critical Accounting Policies

The preparation of our interim financial statements in accordance with GAAP requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. We consider an accounting estimate to be critical if (1) the accounting estimate requires us to make assumptions about matters that were highly uncertain at the time the accounting estimate was made, and (2) changes in the estimates that are likely to occur from period to period, or use of different estimates that we reasonably could have used in the current period, would have a material impact on our financial condition or results of operations. On an on-going basis, we evaluate our estimates, including those related to revenue recognition, impairment of long-lived assets, capitalization of costs, profit recognition related to land sales, stock compensation, and our defined benefit retirement plan. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Our critical accounting policies have not changed since the filing of our Annual Report on Form 10-K for the year ended December 31, 2015. Please refer to that filing for a description of our critical accounting policies.

Results of Operations

Comparison of nine months ended September 30, 2016 to nine months ended September 30, 2015

Total revenues for the first nine months of 2016 were \$32,881,000 compared to \$35,579,000 for the first nine months of 2015. This decrease of \$2,698,000, or 8%, is primarily attributable to a decline in farming revenues of \$1,428,000 and mineral resources revenues of \$1,122,000 resulting from reduced water sales and oil royalties.

Commercial/industrial real estate segment revenues were \$6,534,000 for the first nine months of 2016, an increase of \$344,000, or 6%, compared to the first nine months of 2015. Leasing activity is driving our commercial revenue growth. Most notably, we generated \$195,000 in additional leasing revenues after delivering a multi-tenant building to Habit Burger and Baja Fresh during the first quarter of 2016. Additionally, we recognized \$53,000 in additional leasing revenue from Pieology which was placed into service during the second quarter of 2015. Following the growth of TRCC East, landscaping revenues increased \$83,000.

Commercial/industrial real estate segment expenses were \$5,140,000 during the first nine months of 2016, an increase of \$256,000, or 5%, compared to the same period in 2015. This variance is a result of increases in professional

services of \$106,000, maintenance association fees of \$58,000, and repairs and maintenance of \$44,000. Resort/residential real estate segment expenses were \$1,252,000 during the first nine months of 2016, a decrease of \$633,000, or 34%. The decrease is attributed to additional capitalization of payroll and overhead costs of \$431,000 that were identified to be incremental to our master plan development projects. In addition, there were decreases in professional services of \$91,000, property taxes of \$74,000, and fees of \$56,000.

Mineral resources segment revenues were \$13,052,000 for the first nine months of 2016, a decrease of \$1,122,000, or 8%, compared to the same period in 2015. The \$1,122,000 decrease resulted from a decrease in oil royalty revenues of \$1,171,000 driven by declines in both the price per barrel and production volume. Production for the nine months ended September 30, 2016 and 2015 was 230,131 and 357,507 barrels, respectively. The average price per barrel of oil for the nine months ended September 30, 2016 and 2015 was \$35 and \$49, respectively. We expect no new oil drilling activity and continued slowing in production through 2016 based on current oil prices. Water sales volumes decreased from 7,922 acre feet in 2015 to 7,285 in 2016 resulting in a revenue decrease of \$564,000. Offsetting the decreases were increases in recoverable costs, rock aggregate royalties and cement royalties of \$328,000, \$184,000 and \$80,000, respectively.

Mineral resources segment expenses were \$7,160,000 for the first nine months of 2016, an increase of \$137,000, or 2%, compared to the same period in 2015. This variance is largely due to increases in fuel costs of \$76,000 related to transferring and banking water. Also contributing to the increase was a higher cost of sales per acre-foot of water.

Farming segment revenues were \$11,042,000 for the first nine months of 2016, a decrease of \$1,428,000, or 11%, compared to the same period in 2015. The \$1,428,000 decrease is primarily attributed to the following:

2015 almond carryover crop revenues decreased \$3,194,000. The reduction in sales resulted from our decision to sell more almonds in 2015 in order to take advantage of higher commodity prices resulting in a smaller carryover crop.

Comparatively, we sold 418,645 pounds and 886,366 pounds during the nine months ended September 30, 2016 and 2015, respectively.

2016 almond current crop revenues decreased \$1,219,000. Commodity prices, timing of sales and reduction of yields as a result of our decision to replant older crops drove the decline in revenues. Comparatively, we sold 403,819 pounds and 555,408 pounds during the during the nine months ended September 30, 2016 and 2015, respectively.

2015 pistachio carryover crop revenues decreased \$2,440,000. Decreases in commodity prices and units sold drove the decrease. Comparatively, we sold 50,648 pounds and 167,393 pounds during the nine months ended September 30, 2016 and 2015, respectively.

2016 pistachio current crop revenues increased \$5,544,000. Revenues increased because of improved crop yields in 2016 when compared to 2015. Crop yields were 3,200,000 pounds and 73,000 pounds during 2016 and 2015, respectively. The mild winter of 2015, had an adverse effect on our 2015 crop whereby 90% of our pistachio crop yielded blanks. We sold 2,848,000 pounds and 63,507 pounds during the nine months ended September 30, 2016 and 2015, respectively.

Farming segment expenses were \$10,637,000 for the first nine months of 2016, a decrease of \$1,073,000, or 9%, compared to the same period in 2015. The decline in carryover almond sales accounted for \$1,004,000 of the decrease in farming expenses.

Ranch operations revenues were \$2,253,000 for the first nine months of 2016, a decrease of \$492,000, or 18%, compared to the same period in 2015. The decrease is attributed to a \$334,000 decrease in game management revenues. Also contributing to the decrease is a drought clause taking effect within our grazing leases, amidst the California drought, of \$173,000.

Ranch operations expenses were \$4,263,000 for the first nine months of 2016, a decrease of \$423,000, or 9%, compared to the same period in 2015. This variance is in-line with our expectations given the activity volume within Ranch Operations. The decrease resulted from declines in staffing costs, outside services, supply costs, and repairs and maintenance of \$125,000, \$128,000, \$82,000, \$47,000 respectively.

Corporate general and administrative costs increased \$48,000, or 1%, to \$9,262,000 during the first nine months of 2016 compared to the same period in 2015. During the first nine months of 2016, payroll and overhead decreased \$477,000 resulting from a reduction in full-time employees. The decrease in payroll was offset by increases in stock compensation of \$269,000 resulting from meeting performance milestones, political contributions of \$166,000 and insurance of \$88,000.

Our share of earnings from our joint ventures was \$5,650,000, an increase of \$789,000, or 16%, during the first nine months of 2016 when compared to the same period in 2015, primarily due to a \$569,000 increase in our share of earnings from our TA/Petro joint venture. The improvement in operations within the TA/Petro joint venture is driven by increased diesel and gas sales volume of 1,415,000 gallons and 667,000 gallons, respectively. The improvement in the volume of fuel sales is continuing to be driven by increased traffic within TRCC as a result of expanded offerings

at TRCC East such as Pieology and Starbucks, and the new Shell gas station. Fuel margins for the TA/Petro joint venture were 21% and 15% as of September 30, 2016 and 2015, respectively, improving net income. The remainder of the increase is attributed to improved operating results from the Outlets at Tejon.

Comparison of three months ended September 30, 2016 to three months ended September 30, 2015

Total revenues for the quarter ended September 30, 2016 were \$13,079,000 compared to \$11,946,000 for the quarter ended September 30, 2015. This increase of \$1,133,000, or 9%, is primarily attributable to improvements in farming revenues driven by pistachio sales.

Commercial/industrial real estate segment revenues were \$2,221,000 for the quarter ended September 30, 2016, an increase of \$120,000, or 6%, compared to the same period in 2015. Leasing activity is driving our commercial revenue growth. Most notably, we generated \$66,000 in additional leasing revenues during the third quarter after delivering a multi-tenant building to Habit Burger and Baja Fresh during the first quarter of 2016. Also during the third quarter, we earned \$60,000 a one-time early termination fee from a tenant. We have identified a new tenant who will be taking possession of the vacated unit during the fourth quarter of 2016.

Commercial/industrial real estate segment expenses were \$1,747,000 during the quarter ended September 30, 2016, an increase of \$148,000, or 9%, compared to the same period in 2015. The increase resulted from writing off unamortized tenant allowances of \$53,000. Additionally, repairs and maintenance costs increased \$85,000.

Resort/residential real estate segment expenses were \$323,000 during the quarter ended September 30, 2016, a decrease of \$235,000, or 42%. The decrease comprised of reductions in professional services, fees, and compensation costs of 79,000, \$71,000, and \$19,000, respectively.

Mineral resources segment revenues were \$1,125,000 for the quarter ended September 30, 2016, a decrease of \$197,000, or 15%, compared to the same period in 2015. For the quarter, oil royalties decreased \$246,000, a result of reduced commodity prices and production volume discussed above. Improvements in rock aggregate production and recoverable costs of \$24,000 and \$33,000, respectively, helped to offset declines in oil royalties.

Mineral resources segment expenses were \$667,000 for the quarter ended September 30, 2016, an increase of \$61,000, or 10%, compared to the same period in 2015. The increase is attributed to increase fuel charges related to transferring and banking water.

Farming segment revenues were \$9,319,000 for the quarter ended September 30, 2016, an increase of \$1,243,000, or 15%, compared to the same period in 2015. The \$1,243,000 increase is attributable to the following:

2015 almond carryover crop revenues decreased \$1,158,000. A majority of the decrease is attributed to a \$1,053,000 decrease in market price adjustments occurring during the third quarter of 2016 as compared to the third quarter of 2015. This is consistent with the decline in commodity prices and units sold during 2016.

2016 almond current crop revenues decreased \$1,219,000. Commodity prices, timing of sales and reduction of yields as a result of our decision to replant older crops drove the decline in revenues. Comparatively, we sold 403,819 pounds and 555,408 pounds during the quarters ended September 30, 2016 and 2015, respectively.

2015 pistachio carryover crop revenues decreased \$1,935,000. Decreases in commodity prices and units sold drove the decrease. Comparatively, we sold 3,052 pounds and 56,328 pounds during the quarters September 30, 2016 and 2015, respectively.

2016 pistachio current crop revenues increased \$5,544,000. Revenues increased because of improved crop yields in 2016 when compared to 2015. The mild winter of 2015, had an adverse effect on our crop whereby 90% of our pistachio crop yielded blanks. Crop yields were 3,200,000 pounds and 73,000 pounds during 2016 and 2015, respectively. Comparatively, we sold 2,848,000 pounds and 63,507 pounds during the quarters ended September 30, 2016 and 2015, respectively.

Farming segment expenses were \$7,781,000 for the quarter ended September 30, 2016, a decrease of \$342,000, or 4%, compared to the same period in 2015. The decrease is attributed to the declines in commodity sales.

Ranch operations revenues were \$414,000 for the quarter ended September 30, 2016, a decrease of \$33,000, or 7%, compared to the same period in 2015. The decrease is attributed to declines in game management revenues.

Ranch operations expenses were \$1,374,000 for the quarter ended September 30, 2016, a decrease of \$300,000, or 18%, compared to the same period in 2015. This variance resulted from decreases in professional and other services of \$101,000, compensation of \$77,000, repairs and maintenance of \$55,000, rentals of \$33,000, and supplies of \$16,000.

Corporate general and administrative costs were \$3,096,000 for the quarter ended September 30, 2016, an increase of \$169,000, or 6%, compared to the same period in 2015. For the quarter, professional service costs increased \$269,000 resulting from increased legal and information security costs. Additionally, there was an increase in political contributions of \$72,000. The increases noted were offset by an overall reduction in corporate compensation of

\$162,000.

27

Our share of earnings from our joint ventures was \$2,353,000, an increase of \$298,000, or 15%, during the quarter ended September 30, 2016 when compared to the same period in 2015, primarily due to an \$241,000 increase in our share of earnings from our TA/Petro joint venture. The improvement in operations within the TA/Petro joint venture is driven by increased diesel and gas volumes of 375,000 gallons and 329,000, respectively. Fuel margins for the TA/Petro joint venture were 19% and 17% for the quarter ended September 30, 2016 and 2015, respectively. The remainder of the increase is attributed to improved operating results from the Outlets at Tejon.

General Outlook

Thus far in 2016 our commercial retail activity has continued to grow as new leases have come on-line with Habit Burger and Baja Fresh. For the nine-months ended September 30, 2016 we had no leases that expired, nor did we have any material lease renewals. Our TA/Petro joint venture began construction of an Arby's that is scheduled to open in early 2017.

On August 6, 2016, we entered into a limited liability company agreement with Majestic Realty Co., a Los Angeles based commercial/industrial developer, for the purchase of, ownership of, and management of a fully-leased, 651,909 square foot industrial building located at Tejon Ranch Commerce Center. We have a 50% interest in this joint venture. On September 19, 2016, we entered into a second joint venture with Majestic Realty Co. to develop, construct, lease, and manage an industrial building with approximately 480,000 square feet on the Company's property at Tejon Ranch Commerce Center-East. We have a 50% interest in this joint venture.

The logistics operators currently located within our commerce center have demonstrated success in serving all of California and the western region of the United States and we are building from their success in our marketing efforts. We will continue to focus our efforts for TRCC-East and TRCC-West, on the significant labor and logistical benefits of our site, the pro-business approach of Kern County, and the success that the current tenants and owners within our development have experienced to capture more of the warehouse distribution market. Our strategy fits within the logistics model that many companies are using, which favors large centralized distribution facilities which have been strategically located to maximize the balance of inbound and outbound efficiencies rather than a number of decentralized smaller distribution centers. The world class logistics operators located within TRCC have demonstrated success through utilization of this model. They are also demonstrating success with e-commerce fulfillment. We believe that our ability to provide fully entitled shovel-ready land parcels to support buildings of any size, especially buildings 1.0 million feet or larger can provide us with a potential marketing advantage in the future. We are also expanding our marketing efforts to include industrial users in the Santa Clarita Valley of northern Los Angeles County and the northern part of the San Fernando Valley due to the limited availability of new product and high real estate costs in these locations. Tenants in these geographic areas are typically users of relatively smaller facilities.

A potential disadvantage to our development strategy is our distance from the ports of Los Angeles and Long Beach in comparison to the warehouse/distribution centers located in the Inland Empire, a large industrial area located east of Los Angeles, which continues its expansion eastward beyond Riverside, and San Bernardino to include Perris, Moreno Valley, and Beaumont. As development in the Inland Empire continues to move east and farther away from the ports, our potential disadvantage of our distance from the ports is being mitigated. Strong demand for large distribution facilities is driving development farther east in a search for large entitled parcels. Through the third quarter of 2016, vacancy rates in the Inland Empire were comparable to 2015, primarily due to demand keeping pace with the development of new buildings for lease. Without the increase in new development the vacancy rate would have declined. As lease rates increase in the Inland Empire and northern Los Angeles County, we may begin to have a greater pricing advantage due to our low land basis.

We expect that the commercial/industrial segment will continue to incur costs at current levels, net of amounts capitalized, primarily related to marketing costs, commissions, planning costs, and staffing costs as we continue forward with our development plans.

Most of the expenditures and capital investment incurred within our resort/residential segment will be focused on the achievement of entitlement for Grapevine, Centennial, and tentative tract maps for MV. The tentative tract maps process is expected to be completed in late 2017.

Due to our exposure to the commodity markets, we are unable to accurately predict revenue and we cannot pass on to our customers any cost increases caused by general inflation, except to the extent such inflation is reflected in market conditions and commodity prices. All of our crops are sensitive to the size of each year's world crop. Large crops in

California and abroad can rapidly depress prices. Thus far in 2016, prices for almonds and pistachios have declined in comparison to recent years as a result of increasing almond and pistachio supply. Based on current global inventory estimates, lower prices could carry into 2017.

Thus far, wine grape and almond yields are comparable with 2015 yields. Pistachio yields improved drastically from the historical lows experienced in 2015.

Because of the oversupply in the oil markets, we expect to continue to see lower oil prices as compared to 2015, which will continue to negatively impact us through the remainder of 2016.

The operations of the Company are seasonal and future results of operations cannot be predicted based on quarterly results. Future real estate sales and leasing activity are dependent on market circumstances and specific opportunities and therefore are difficult to predict from period to period. Historically, the Company's largest percentages of farming revenues are recognized during the third and fourth quarters of the fiscal year.

For further discussion of the risks and uncertainties that could potentially adversely affect us, please refer to Part I, Item 7 – “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in the Company’s Annual Report on Form 10-K for the year ended December 31, 2015, or Annual Report, and to Part I, Item 1A - "Risk Factors" of our Annual Report. We continue to be involved in various legal proceedings related to leased acreage. For a further discussion, please refer to Note 12 (Commitments and Contingencies) of the Notes to Unaudited Consolidated Financial Statements in this report.

Income Taxes

For the nine months ended September 30, 2016, the Company incurred a net income tax expense of \$503,000 compared to a net income tax expense of \$464,000 for the nine months ended 2015. These represent effective income tax rates of approximately 39% and 28% for the nine months ended 2016 and, 2015, respectively. As of September 30, 2016, we did not have income taxes payable. The Company classifies interest and penalties incurred on tax payments as income tax expenses.

Cash Flow and Liquidity

We manage our cash and marketable securities along with cash flow to allow us to pursue our strategies of land entitlement, development, farming, and conservation. Accordingly, we have established well-defined priorities for our available cash, including investing in core business segments to achieve profitable future growth. We have historically funded our operations with cash flows from operating activities, investment proceeds, short-term borrowings from our bank credit facilities, and long-term debt tied to revenue producing assets. In the past, we have also issued common stock and used the proceeds for capital investments. To enhance shareholder value, we will continue to make investments in our real estate segments to secure land entitlement approvals, build infrastructure for our developments, and acquire water rights to ensure adequate future water supply. Within our farming segment, we will make investments as needed to improve efficiency and add capacity to its operations when it is profitable to do so. Our cash, cash equivalents and marketable securities totaled \$31,042,000 at September 30, 2016, a decrease of \$3,703,000, or 11%, from December 31, 2015. Cash, cash equivalents and marketable securities decreased during the first nine months of September 30, 2016 due to property and equipment expenditures and real estate investments, which included infrastructure development costs, and increases in farming inventory. These decreases were partially offset by water sale proceeds, reimbursement proceeds for public infrastructure costs from the East CFD, and use of our revolving line of credit.

The following table shows our cash flow activities for the nine months ended September 30,

(in thousands)	2016	2015
Operating activities	\$1,413	\$1,541
Investing activities	\$(10,414)	\$(5,038)
Financing activities	\$10,496	\$1,371

Operating Activities

During the first nine months of 2016, our operations provided \$1,413,000 of cash primarily related to distributions from our joint ventures of \$4,500,000 offset by payments on current liabilities and farm crop inventory costs.

During the first nine months of 2015, our operations provided \$1,541,000 of cash primarily attributable to net income including adjustments for non-cash items, partially offset by increases in farming inventories.

Investing Activities

During the first nine months of 2016, investing activities used \$10,414,000 as a result of \$19,760,000 in capital expenditures. Capital expenditures include predevelopment activities for our master plan communities which amounted to \$3,914,000 for MV, \$3,663,000 for Grapevine, and \$3,832,000 for Centennial. At TRCC East, we spent \$3,345,000 for infrastructure projects along with completing the multi-tenant building housing Baja Fresh and Habit Burger. Within our farming segment, we spent \$1,837,000 replacing old machinery and equipment along with

developing a new almond orchard. We spent \$1,845,000 within our mineral resources group for new wells and water turnouts. Within ranch operations we acquired \$476,000 in new machinery and equipment. Our capital outlays were offset by reimbursements for public infrastructure costs through the East CFD and other reimbursements of \$4,650,000. Additionally, we received \$4,966,000 in net proceeds from marketable securities transactions.

We continuously evaluate our short-term and long-term capital investment needs. Based on the timing of capital investments, we may supplement our current cash, marketable securities, and operational funding sources through the sale of common stock and the use of additional debt.

During the first nine months of 2015, investing activities used \$5,038,000 of cash primarily as a result of \$18,968,000 in capital expenditures consisting of \$6,425,000 of investments in TRCC infrastructure, primarily associated with expansion of road infrastructure, utilities, and buildings on land at TRCC-East, \$3,306,000 related to the Grapevine Development Area for entitlement activities, \$5,263,000 related to TMV pre-development activities, and \$2,392,000 related to Centennial Founders LLC for entitlement activities. The remaining capital expenditures related to ordinary capital expenditures such as farming equipment, IT equipment replacements and computer software. These expenditures were partially offset by net proceeds of \$7,932,000 from the sale and maturity of marketable securities, reimbursements of \$4,971,000 for public infrastructure costs through the East CFD, and distributions of \$1,100,000 from our Rockefeller unconsolidated joint venture partner.

Our estimated capital investment for the remainder of 2016 will be primarily related to real estate projects. Estimated capital investment includes approximately \$2,200,000 of infrastructure development at TRCC-East. This new infrastructure is to support continued commercial retail and industrial development within TRCC-East and to expand water facilities to support future demand. We expect to possibly invest \$860,000 for land planning and entitlement activities for the Grapevine, \$534,000 for developing tentative tract maps for MV, and \$900,000 for entitlement work for Centennial. We will continue to add to our current water assets and water infrastructure as opportunities arise to help secure our ability to supply water to our real estate and farming activities and as an investment, since we believe that the cost of water in California will continue to increase and expect to invest up to \$1,000,000 in water assets and infrastructure. We are also planning to invest approximately \$200,000 for farming equipment, almond orchards, and grape vines.

Financing Activities

During the first nine months of 2016, financing activities provided \$10,496,000 in cash mainly due to the timing of drawdowns and repayments on the Company's line of credit. As of September 30, 2016, there was an outstanding balance of \$11,000,000 on our revolving line of credit. The use of our line of credit primarily reflects the cyclical nature of cash flow in our farming segment as inventory costs build as we move into the second half of the year and the harvest season begins.

During the first nine months of 2015, financing activities generated \$1,371,000 in cash mainly due to the timing of draw downs on the Company's line of credit. At September 30, 2015, there was an outstanding balance of \$8,940,000 on our revolving line of credit. Cash used in financing activities was also tied to the buyback of stock at time of the vesting of stock grants for the payment of payroll taxes.

It is difficult to accurately predict cash flows due to the nature of our businesses and fluctuating economic conditions. Our earnings and cash flows will be affected from period to period by the commodity nature of our farming operations, the timing of sales and leases of property within our development projects, and the beginning of development within our residential projects. The timing of sales and leases within our development projects is difficult to predict due to the time necessary to complete the development process and negotiate sales or lease contracts. Often, the timing aspect of land development can lead to particular years or periods having more or less earnings than comparable periods. Based on our experience, we believe we will have adequate operating cash flows and availability on our line of credit over the next twelve months to fund ongoing operations.

Capital Structure and Financial Condition

At September 30, 2016, total capitalization at book value was \$407,491,000 consisting of \$73,860,000 of long-term debt and \$333,631,000 of equity, resulting in a long-term debt-to-total-capitalization ratio of approximately 18.1%, which is similar to the long-term debt-to-total-capitalization ratio at December 31, 2015.

The Company has a Term Note and a Revolving Line of Credit Note, with Wells Fargo, or collectively the Credit Facility. The Credit Facility consists of a \$70,000,000 term note, or Term Note, and a \$30,000,000 revolving line of credit, or RLC. Funds from the Term Note were used to finance the Company's purchase of DMB TMV LLC's interest in Tejon Mountain Village LLC as disclosed in the Current Report on Form 8-K filed on July 16, 2014. Any future borrowings under the RLC will be used for ongoing working capital requirements and other general corporate

purposes. To maintain availability of funds under the RLC, undrawn amounts under the RLC will accrue a commitment fee of 10 basis points per annum. The Company's ability to borrow additional funds in the future under the RLC is subject to compliance with certain financial covenants and making certain representations and warranties. At the Company's option, the interest rate on the RLC can float at 1.50% over a selected LIBOR or can be fixed at 1.50% above LIBOR for a fixed rate term. During the term of the Credit Facility (which matures in September 2019), we can borrow at any time and partially or wholly repay any outstanding borrowings and then re-borrow, as necessary. At September 30, 2016 the RLC had an outstanding balance of \$11,000,000. At December 31, 2015, the RLC had no outstanding balance.

The interest rate per annum applicable to the Term Note is LIBOR (as defined in the Term Note) plus a margin of 170 basis points. The interest rate for the term of the note has been fixed through the use of an interest rate swap at a rate of 4.11%. The Term Note requires interest only payments for the first two years of the term and thereafter requires monthly amortization payments pursuant to a schedule set forth in the Term Note, with the final outstanding principal amount due October 5, 2024. The Company may make voluntary prepayments on the Term Note at any time without penalty (excluding any applicable LIBOR or interest rate swap breakage costs). Each optional prepayment will be applied to reduce the most remote principal payment then unpaid. The Credit Facility is secured by the Company's farmland and farm assets, which include equipment, crops and crop receivables and the power plant lease and lease site, and related accounts and other rights to payment and inventory.

The Credit Facility requires compliance with three financial covenants: (a) total liabilities divided by tangible net worth not greater than 0.75 to 1.0 at each quarter end; (b) a debt service coverage ratio not less than 1.25 to 1.00 as of each quarter end on a rolling four quarter basis; and (c) maintain liquid assets equal to or greater than \$20,000,000. At September 30, 2016 and December 31, 2015, we were in compliance with all financial covenants.

We also have a promissory note agreement to pay a principal amount of \$4,750,000 with CMFG Life Insurance Company, to pay principal and interest due monthly. The interest rate on this promissory note is 4.25% per annum, with principal and interest payments of \$102,700 ending on September 1, 2028. The current outstanding balance is \$4,025,000. The proceeds from this promissory note were used to eliminate debt that had been previously used to provide long-term financing for a building being leased to Starbucks and provide additional working capital for future investment. The balance of this long-term debt instrument listed above approximates the fair value of the instrument. Our current and future capital resource requirements will be provided by current cash and marketable securities, cash flow from on-going operations, proceeds from the sale of developed and undeveloped parcels, potential sales of assets, additional use of debt, proceeds from the reimbursement of public infrastructure costs through Community Facilities District bond debt (described below under "Off-Balance Sheet Arrangements"), and the issuance of common stock. During April 2016, we filed a shelf registration statement on Form S-3 that went effective in May 2016. Under the shelf registration statement, we may offer and sell in the future one or more offerings, consisting of common stock, preferred stock, debt securities, warrants or any combination of the foregoing.

As noted above, at September 30, 2016, we had \$31,042,000 in cash and securities and had \$19,000,000 available on our RLC to meet any short-term liquidity needs.

We continue to expect that substantial future investments will be required in order to develop our land assets. In order to meet these long-term capital requirements, we may need to issue common stock and secure additional debt financing and continue to renew our existing credit facilities. In addition, we will use other capital alternatives such as entering into joint ventures. We will use a combination of the above funding sources to properly match funding requirements with the assets or development project being funded. There is no assurance in the future that we can obtain financing or that we can obtain financing at favorable terms. We believe we have adequate capital resources to fund our cash needs and our capital investment requirements as described earlier in the cash flow and liquidity discussions.

Contractual Cash Obligations

The following table summarizes our contractual cash obligations and commercial commitments as of September 30, 2016, to be paid over the next five years and thereafter:

(In thousands)	Payments Due by Period				
	Total	One Year or Less	Years 2-3	Years 4-5	Thereafter
CONTRACTUAL OBLIGATIONS:					
Estimated water payments	\$267,580	\$ 8,384	\$ 17,218	\$ 17,846	\$ 224,132
Long-term debt	74,025	3,346	7,759	8,458	54,462
Interest on long-term debt	19,287	2,750	5,518	4,851	6,168
Revolving line of credit borrowings	11,000	11,000	—	—	—
Cash contract commitments	4,520	2,311	1,138	—	1,071
Defined Benefit Plan	2,825	94	417	508	1,806
SERP	8,106	437	1,000	980	5,689
Tejon Ranch Conservancy	4,200	800	1,600	1,600	200
Financing fees and interest	163	163	—	—	—
Total contractual obligations	\$391,706	\$ 29,285	\$ 34,650	\$ 34,243	\$ 293,528

The categories above include purchase obligations and other long-term liabilities reflected on our balance sheet under GAAP. A “purchase obligation” is defined in Item 303(a)(5)(ii)(D) of Regulation S-K as “an agreement to purchase goods or services that is enforceable and legally binding on the registrant that specifies all significant terms, including: fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction.” Based on this definition, the table above includes only those contracts that include fixed or minimum obligations. It does not include normal purchases, which are made in the ordinary course of business. Our financial obligations to the Tejon Ranch Conservancy are prescribed in the Conservation Agreement. Our advances to the Tejon Ranch Conservancy are dependent on the occurrence of certain events and their timing, and are therefore subject to change in amount and period. The amounts included above are the minimum amounts we anticipate contributing through the year 2021, at which time our current contractual obligation terminates.

As discussed in Note 13 (Retirement Plans) of the Notes to Unaudited Consolidated Financial Statements, we have long-term liabilities for deferred employee compensation, including pension and supplemental retirement plans. Payments in the above table reflect estimates of future defined benefit plan contributions from the Company to the plan trust, estimates of payments to employees from the plan trust, and estimates of future payments to employees from the Company that are in the SERP program. We estimate that we will contribute approximately \$450,000 to the defined benefit plan during 2016.

Our cash contract commitments consist of contracts in various stages of completion related to infrastructure development within our industrial developments and entitlement costs related to our industrial and residential development projects.

Our operating lease obligations are for office equipment, several vehicles, and a temporary trailer providing office space and average approximately \$25,000 per month. At the present time, we do not have any capital lease obligations or purchase obligations outstanding.

Estimated water payments include SWP contracts with WRMWDS, TCWD, TLBWSD, and DRWD. These contracts for the supply of future water run through 2035. In addition, in late 2013 we purchased the assignment of a contract to purchase water. The assigned water contract is with Nickel Family, LLC and obligates us to purchase 6,693 acre-feet of water annually starting in 2014 and running to 2044. Please refer to Note 5 (Long-Term Water Assets) of the Notes to Unaudited Consolidated Financial Statements for additional information regarding water assets.

Off-Balance Sheet Arrangements

The following table shows contingent obligations we have with respect to certain bonds issued by the CFD:

(\$ in thousands)	Amount of Commitment Expiration Per Period				
	Total	< 1 year	1 -3 Years	4 -5 Years	After 5 Years

OTHER COMMERCIAL COMMITMENTS:

Standby letter of credit	\$5,426	\$	-\$ 5,426	\$	-\$	—
Total other commercial commitments	\$5,426	\$	-\$ 5,426	\$	-\$	—

32

The Tejon Ranch Public Facilities Financing Authority, or TRPFFA, is a joint powers authority formed by Kern County and TCWD to finance public infrastructure within the Company's Kern County developments. TRPFFA created two CFDs, the West CFD and the East CFD. The West CFD has placed liens on 420 acres of the Company's land to secure payment of special taxes related to \$28,620,000 of bond debt sold by TRPFFA for TRCC-West. The East CFD has placed liens on 1,931 acres of the Company's land to secure payments of special taxes related to \$55,000,000 of bond debt sold by TRPFFA for TRCC-East. At TRCC-West, the West CFD has no additional bond debt approved for issuance. At TRCC-East, the East CFD has approximately \$65,000,000 of additional bond debt authorized by TRPFFA.

In connection with the sale of bonds there is a standby letter of credit for \$5,426,000 related to the issuance of East CFD bonds. The standby letter of credit is in place to provide additional credit enhancement and cover approximately two years of interest on the outstanding bonds. This letter of credit will not be drawn upon unless the Company, as the largest landowner in the CFD, fails to make its property tax payments. As development occurs within TRCC-East there is a mechanism in the bond documents to reduce the amount of the letter of credit. The Company believes that the letter of credit will never be drawn upon. This letter of credit is for a two-year period of time and will be renewed in two-year intervals as necessary. The annual cost related to the letter of credit is approximately \$83,000. The assessment of each individual property sold or leased within each CFD is not determinable at this time because it is based on the current tax rate and the assessed value of the property at the time of sale or on its assessed value at the time it is leased to a third-party. Accordingly, the Company is not required to recognize an obligation at September 30, 2016.

At September 30, 2016, aggregate outstanding debt of unconsolidated joint ventures was \$97,963,000. We provided a guarantee on \$82,689,000 of this debt, relating to our joint ventures with Rockefeller and Majestic. We do not provide a guarantee on the \$15,274,000 of debt related to our joint venture with TA/Petro.

Non-GAAP Measures

EBITDA represents earnings before interest, taxes, depreciation, and amortization, a non-GAAP financial measure, and is used by us and others as a supplemental measure of performance and liquidity. We use Adjusted EBITDA to assess the performance of our core operations, for financial and operational decision making, and as a supplemental or additional means of evaluating period-to-period comparisons on a consistent basis. Adjusted EBITDA is calculated as EBITDA, excluding stock compensation expense. We believe Adjusted EBITDA provides investors relevant and useful information because it permits investors to view income from our operations on an unleveraged basis before the effects of taxes, depreciation and amortization, and stock compensation expense. By excluding interest expense and income, EBITDA and Adjusted EBITDA allow investors to measure our performance independent of our capital structure and indebtedness and, therefore, allow for a more meaningful comparison of our performance to that of other companies, both in the real estate industry and in other industries. We believe that excluding charges related to share-based compensation facilitates a comparison of our operations across periods and among other companies without the variances caused by different valuation methodologies, the volatility of the expense (which depends on market forces outside our control), and the assumptions and the variety of award types that a company can use. EBITDA and Adjusted EBITDA have limitations as measures of our performance. EBITDA and Adjusted EBITDA do not reflect our historical cash expenditures or future cash requirements for capital expenditures or contractual commitments. While EBITDA and Adjusted EBITDA are relevant and widely used measures of performance, they do not represent net income or cash flows from operations as defined by GAAP, and they should not be considered as alternatives to those indicators in evaluating performance or liquidity. Further, our computation of EBITDA and Adjusted EBITDA may not be comparable to similar measures reported by other companies.

	Three Months		Nine Months	
	Ended		Ended	
	September 30,		September 30,	
(\$ in thousands)	2016	2015	2016	2015
Net income (loss)	\$317	\$(811)	\$784	\$1,167
Interest, net	(130)	(153)	(396)	(465)
Income tax expense (benefit)	271	(434)	503	464

Depreciation and amortization	1,360	1,241	4,170	3,672
EBITDA	\$1,818	\$(157)	\$5,061	\$4,838
Stock compensation expense	1,166	1,014	3,297	2,914
Adjusted EBITDA	\$2,984	\$857	\$8,358	\$7,752

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk represents the risk of loss that may impact the financial position, results of operations, or cash flows of the Company due to adverse changes in financial or commodity market prices or rates. We are exposed to market risk in the areas of interest rates and commodity prices.

Financial Market Risks

Our exposure to financial market risks includes changes to interest rates and credit risks related to marketable securities, interest rates related to our outstanding indebtedness and, market and credit risks related to trade receivables.

The primary objective of our investment activities is to preserve principal while at the same time maximizing yields and prudently managing risk. To achieve this objective and limit interest rate exposure, we limit our investments to securities with a maturity of less than five years and an investment grade rating from Moody's or Standard & Poor's. See Note 3 (Marketable Securities) of the Notes to Unaudited Consolidated Financial Statements.

Our current RLC has an outstanding balance of \$11,000,000. The interest rate on the RLC can either float at 1.50% over a selected LIBOR, or can be fixed at 1.50% above LIBOR for a fixed term for a limited period of time and change only at maturity of the fixed rate portion. The floating rate and fixed rate options within our RLC help us manage our interest rate exposure on any outstanding balances.

We are exposed to interest rate risk on our long-term debt. Long-term debt consists of two term loans. The first term loan is for \$70,000,000 and has a rate that is tied to LIBOR plus a margin of 1.70%. The interest rate for the term of this loan has been fixed through the use of an interest rate swap that fixed the rate at 4.11%. The second term loan has an outstanding balance of \$4,025,000 and has a fixed rate of 4.25%. We believe it is prudent at times to limit the variability of floating-rate interest payments and have from time-to-time entered into interest rate swap arrangements to manage those fluctuations, as we did with the first loan mentioned above.

Market risk related to our farming inventories ultimately depends on the value of almonds, grapes, and pistachios at the time of payment or sale. Market risk related to our farming inventories is discussed below in the section pertaining to commodity price exposure. Credit risk related to our receivables depends upon the financial condition of our customers. Based on historical experience with our current customers and periodic credit evaluations of our customers' financial conditions, we believe our credit risk is minimal.

The following tables provide information about our financial instruments that are sensitive to changes in interest rates. The tables present our debt obligations and marketable securities and their related weighted-average interest rates by expected maturity dates.

Interest Rate Sensitivity Financial Market Risks

Principal Amount by Expected Maturity

At September 30, 2016

(In thousands except percentage data)

	2016	2017	2018	2019	2020	Thereafter	Total	Fair Value
Assets:								
Marketable securities	\$879	\$7,902	\$14,686	\$4,126	—	—	27,593	\$27,617
Weighted average interest rate	0.67%	1.31%	1.60%	1.76%	—	—	1.51%	
Liabilities:								
Revolving line of credit	\$11,000	—	—	—	—	—	\$11,000	\$11,000
Weighted average interest rate	1.95%	—	—	—	—	—	1.95%	
Long-term debt (\$4.75M note)	\$65	\$266	\$277	\$289	\$302	\$2,826	\$4,025	\$4,025
Weighted average interest rate	4.25%	4.25%	4.25%	4.25%	4.25%	4.25%	4.25%	
Long-term debt (\$70.0M note)	\$561	\$3,393	\$3,563	\$3,715	\$3,881	\$54,887	\$70,000	\$70,000
Weighted average interest rate	4.11%	4.11%	4.11%	4.11%	4.11%	4.11%	4.11%	

Interest Rate Sensitivity Financial Market Risks

Principal Amount by Expected Maturity

At December 31, 2015

(In thousands except percentage data)

	2016	2017	2018	2019	2020	Thereafter	Total	Fair Value
Assets:								
Marketable securities	\$8,257	\$9,068	\$13,315	\$2,335	—	—	\$32,975	\$32,815
Weighted average interest rate	1.14%	1.54%	1.89%	2.16%	—	—	1.40%	
Liabilities:								
Long-term debt (\$4.75M note)	\$255	\$266	\$277	\$289	\$302	\$2,826	\$4,215	\$4,215
Weighted average interest rate	4.25%	4.25%	4.25%	4.25%	4.25%	4.25%	4.25%	
Long-term debt (\$70.0M note)	\$561	\$3,393	\$3,563	\$3,715	\$3,881	\$54,887	\$70,000	\$70,000
Weighted average interest rate	4.11%	4.11%	4.11%	4.11%	4.11%	4.11%	4.11%	

Commodity Price Exposure

As of September 30, 2016, we have exposure to adverse price fluctuations associated with certain inventories and accounts receivable. Farming inventories consist of farming cultural and processing costs related to 2015 and 2016 crop production. The farming costs inventoried are recorded at actual costs incurred. Historically, these costs have been recovered each year when that year's crop harvest has been sold.

With respect to accounts receivable, the amount at risk relates primarily to farm crops. These receivables are recorded as estimates of the prices that ultimately will be received for the crops. The final price is generally not known for several months following the close of our fiscal year. Of the \$8,612,000 of accounts receivable outstanding at September 30, 2016, \$5,900,000 or 77%, is at risk to changing prices. Of the amount at risk to changing prices, \$5,736,000 is attributable to pistachios and \$164,000 is attributable to almonds. The comparable amount of accounts receivable at risk to price changes at December 31, 2015 was \$3,529,000, or 54% of the total accounts receivable of \$6,511,000.

The price estimated for recording accounts receivable for pistachios recorded at September 30, 2016 was \$2.01 per pound compared to \$2.88 per pound at December 31, 2015. For each \$0.01 change in the price of pistachios, our receivable for pistachios increases or decreases by \$28,000. Although the final price of pistachios (and therefore the extent of the risk) is not presently known, over the last three years prices have ranged from \$3.82 to \$4.92. With respect to almonds, the price estimated for recording the receivable was \$2.00 per pound compared to \$3.44 per pound at December 31, 2015. For each \$0.01 change in the price of almonds, our receivable for almonds increases or decreases by \$820. The range of final prices over the last three years for almonds has ranged from \$1.71 to \$4.24 per pound.

ITEM 4. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rules 13a-15 and 15d-15 of the Securities Exchange Act of 1934, as amended, or the Exchange Act. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective in ensuring that all information required in the reports we file or submit under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure and is recorded, processed, summarized and reported within the time period required by the rules and regulations of the SEC.

(b) Changes in Internal Control over Financial Reporting

There have been no changes in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Rule 13a-15 or Rule 15d-15 under the Exchange Act that occurred during our last fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

Please refer to Note 12. Commitments and Contingencies in the Notes to Unaudited Consolidated Financial Statements in this report.

Item 1A. Risk Factors

There have been no material changes to the risk factors disclosed in Item 1A or elsewhere in our most recent Annual Report on Form 10-K.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Not applicable.

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

On October 27, 2016, the Kern County Planning Commission unanimously recommended approval of the company's Grapevine community by the Kern County Board of Supervisors after its review of the Environmental Impact Report and the Grapevine Specific and Community Plan, which is the final step in the local plan approval process. The company's master planned Grapevine community includes 12,000 residential units and 5.1 million square feet of commercial and industrial space. The Kern County Board of Supervisors is expected to take action on the recommendation in December 2016.

Edgar Filing: TEJON RANCH CO - Form 10-Q

Item 6. Exhibits:

3.1	Restated Certificate of Incorporation	FN 1
3.2	By-Laws	FN 1
4.1	Form of First Additional Investment Right	FN 2
4.2	Form of Second Additional Investment Right	FN 3
4.3	Registration and Reimbursement Agreement	FN 10
10.1	Water Service Contract with Wheeler Ridge-Maricopa Water Storage District (without exhibits), amendments originally filed under Item 11 to Registrant's Annual Report on Form 10-K	FN 4
10.7	*Severance Agreement	FN 5
10.8	*Director Compensation Plan	FN 5
10.9	*Amended and Restated Non-Employee Director Stock Incentive Plan	FN 13
10.9(1)	*Stock Option Agreement Pursuant to the Non-Employee Director Stock Incentive Plan	FN 5
10.10	*Amended and Restated 1998 Stock Incentive Plan	FN 14
10.10(1)	*Stock Option Agreement Pursuant to the 1998 Stock Incentive Plan	FN 5
10.12	Lease Agreement with Pastoria Energy Facility L.L.C.	FN 6
10.15	Form of Securities Purchase Agreement	FN 7
10.16	Form of Registration Rights Agreement	FN 8
10.17	*2004 Stock Incentive Program	FN 9
10.18	*Form of Restricted Stock Agreement for Directors	FN 9
10.19	*Form of Restricted Stock Unit Agreement	FN 9
10.23	Tejon Mountain Village LLC Operating Agreement	FN 11
10.24	Tejon Ranch Conservation and Land Use Agreement	FN 12
10.25	Second Amended and Restated Limited Liability Agreement of Centennial Founders, LLC	FN 15
10.26	*Executive Employment Agreement - Allen E. Lyda	FN 16
10.27	Limited Liability Company Agreement of TRCC/Rock Outlet Center LLC	FN 17
10.28	Warrant Agreement	FN 18

10.29	Amendments to Limited Liability Company Agreement of Tejon Mountain Village LLC	FN 19
10.30	Membership Interest Purchase Agreement - TMV LLC	FN 20
10.31	Amended and Restated Credit Agreement	FN 21
10.32	Term Note	FN 21
10.33	Revolving Line of Credit	FN 21

Edgar Filing: TEJON RANCH CO - Form 10-Q

10.34	Amendments to Lease Agreement with Pastoria Energy Facility L.L.C.	FN 22
10.35	Water Supply Agreement with Pastoria Energy Facility L.L.C.	FN 23
10.36	*Separation Agreement - Gregory J. Tobias	FN 24
10.37	Limited Liability Agreement of TRC-MRC 2, LLC	FN 25
10.38	Limited Liability Agreement of TRC-MRC 1, LLC	Filed herewith
31.1	Certification as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	Filed herewith
31.2	Certification as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	Filed herewith
32	Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed herewith
101.INS	XBRL Instance Document.	Filed herewith
101.SCH	XBRL Taxonomy Extension Schema Document.	Filed herewith
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.	Filed herewith
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.	Filed herewith
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.	Filed herewith
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.	Filed herewith
*Management contract, compensatory plan or arrangement.		

- FN 1 This document, filed with the Securities and Exchange Commission in Washington D.C. (file number 1-7183) under Item 14 to our Annual Report on Form 10-K for year ended December 31, 1987, is incorporated herein by reference.
- FN 2 This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) as Exhibit 4.3 to our Current Report on Form 8-K filed on May 7, 2004, is incorporated herein by reference.
- FN 3 This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number I-7183) as Exhibit 4.4 to our Current Report on Form 8-K filed on May 7, 2004, is incorporated herein by reference.
- FN 4 This document, filed with the Securities and Exchange Commission in Washington D.C. (file number 1-7183) under Item 14 to our Annual Report on Form 10-K for year ended December 31, 1994, is incorporated herein by reference.
- FN 5 This document, filed with the Securities and Exchange Commission in Washington D.C. (file number 1-7183) under Item 14 to our Annual Report on Form 10-K, for the period ending December 31, 1997, is incorporated herein by reference.
- FN 6 This document filed with the Securities and Exchange Commission in Washington D.C. (file number 1-7183) under Item 14 to our Annual Report on Form 10-K for the year ended December 31, 2001, is incorporated herein by reference.
- FN 7 This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) as Exhibit 4.1 to our Current Report on Form 8-K filed on May 7, 2004, is incorporated herein by reference.
- FN 8 This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) as Exhibit 4.2 to our Current Report on Form 8-K filed on May 7, 2004, is incorporated herein by reference.
- FN 9 This document, filed with the Securities and Exchange Commission in Washington D.C. (file number 1-7183) under Item 15 to our Annual Report on Form 10-K for the year ended December 31, 2004, is incorporated herein by reference.
- FN 10 This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) as Exhibit 4.1 to our Current Report on Form 8-K filed on December 20, 2005, is incorporated herein by reference.
- FN 11 This document, filed with the Securities and Exchange Commission in Washington D.C. (file number 1-7183) as Exhibit 10.24 to our Current Report on Form 8-K filed on May 24, 2006, is incorporated herein by reference.
- FN 12 This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) as Exhibit 10.28 to our Current Report on Form 8-K filed on June 23, 2008, is incorporated herein by reference.
- FN 13 This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) as Exhibit 10.9 to our Annual Report on form 10-K for the year ended December 31, 2008, is incorporated herein by reference.
- FN 14 This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) as Exhibit 10.10 to our Annual Report on form 10-K for the year ended December 31, 2008, is incorporated herein by reference.
- FN 15 This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) under Item 6 to our Quarterly Report on Form 10-Q for the period ending June 30, 2009, is incorporated herein by reference.
- FN 16 This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) under Item 6 to our Quarterly Report on Form 10-Q for the period ending March 31, 2013, is incorporated herein by reference.
- FN 17 This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) as Exhibit 10.27 to our Current Report on Form 8-K filed on June 4, 2013, is incorporated herein by reference.
- FN 18 This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) as Exhibit 10.1 to our Current Report on Form 8-K filed on August 8, 2013, is incorporated herein by

reference.

FN
19

This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) as Exhibit 10.29 to our Amended Annual Report on Form 10-K/A for the year ended December 31, 2013, is incorporated herein by reference.

FN
20

This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) as Exhibit 10.30 to our Current Report on Form 8-K filed on July 16, 2014, is incorporated herein by reference.

FN
21

This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) as Exhibits 10.31-10.33 to our Current Report on Form 8-K filed on October 17, 2014, is incorporated herein by reference.

FN
22

This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) as Exhibit 10.34 to our Annual Report on Form 10-K for the year ended December 31, 2014, is incorporated herein by reference.

39

FN
23 This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) as Exhibit 10.35 to our Quarterly Report on Form 10-Q for the period ending June 30, 2015, is incorporated herein by reference.

FN
24 This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) as Exhibit 10.36 to our Quarterly Report on Form 10-Q for the period ending September 30, 2015, is incorporated herein by reference.

FN
25 This document, filed with the Securities and Exchange Commission in Washington, D.C. (file number 1-7183) as Exhibit 10.37 to our Quarterly Report on Form 10-Q for the period ending June 30, 2016, is incorporated herein by reference.

40

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Company has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized, on November 8, 2016.

TEJON RANCH CO.
(The Company)

/s/ Allen E. Lyda
Allen E. Lyda
Executive Vice President, Chief Financial Officer and Corporate Treasurer

/s/ Robert D. Velasquez
Robert D. Velasquez
Vice President of Finance, Chief Accounting Officer