

AMERICAN REALTY INVESTORS INC
Form 10-K
March 31, 2008
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2007

OR

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

Commission File Number 001-15663

American Realty Investors, Inc.

(Exact name of registrant as specified in its charter)

Nevada
(State or other jurisdiction of

75-2847135
(IRS Employer

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Incorporation or organization)
1800 Valley View Lane, Suite 300

Identification Number)

Dallas, Texas
(Address of principal executive offices)

(469) 522-4200

75234
(Zip Code)

Registrant's Telephone Number, including area code

Securities registered pursuant to Section 12(b) of the Act:

<i>Title of Each Class</i>	<i>Name of each exchange on which registered</i>
Common Stock, \$0.01 par value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

NONE

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definitions of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act (check one).

Large accelerated filer 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 aggregate market value of the shares of voting and non-voting common equity held by non-affiliates of the Registrant, computed by reference to the closing price at which the common equity was last sold which was the sales price of the Common Stock on the New York Stock Exchange as of June 30, 2007 (the last business day of the Registrant's most recently completed second fiscal quarter) was \$14,220,379 based upon a total of 1,736,310 shares held as of June 30, 2007 by persons believed to be non-affiliates of the Registrant. The basis of the calculation does not constitute a determination by the Registrant as defined in Rule 405 of the Securities Act of 1933, as amended, such calculation, if made as of a date within sixty days of this filing, would yield a different value.

As of March 20, 2008, there were 11,217,914 shares of common stock outstanding, which includes 746,972 shares issued to and owned by Transcontinental Realty Investors, Inc.

Documents Incorporated By Reference:

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

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FORWARD-LOOKING STATEMENTS

Certain Statements in this Form 10-K are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, and Section 21E of the Securities Exchange Act of 1934. The words estimate, plan, intend, expect, anticipate, believe, and similar expressions are intended to identify forward-looking statements. The forward-looking statements are found at various places throughout this Report and in the documents incorporated herein by reference. The Company disclaims any intention or obligations to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Although we believe that our expectations are based upon reasonable assumptions, we can give no assurance that our goals will be achieved. Important factors that could cause our actual results to differ from estimates or projections contained in any forward-looking statements are described in Item 1A. Risk Factors .

PART I

ITEM 1. BUSINESS

General

As used herein, the terms ARI, the Company, we, our or us refer to American Realty Investors, Inc., a Nevada corporation, individually or together with its subsidiaries. The Company's common stock trades on the New York Stock Exchange under the symbol ARL . ARI is a C corporation for U.S. federal income tax purposes. ARI was organized in 1999. In August 2000 the Company acquired American Realty Trust, Inc., a Georgia corporation (ART) and National Realty LP, a Delaware limited partnership (NRLP). ART was the successor to a District of Columbia business trust organized in 1961. The business trust was merged into ART in 1988. NRLP was organized in 1987 and subsequently acquired all of the assets and assumed all of the liabilities of several public and private limited partnerships. NRLP also owned a portfolio of real estate and mortgage loan investments.

ARI subsidiaries own approximately 80.2 percent of the outstanding shares of common stock of Transcontinental Realty Investors, Inc., a Nevada corporation (TCI) whose common stock is traded on the New York Stock Exchange under the symbol TCI . TCI owns approximately 24.88% of the outstanding common shares of Income Opportunity Realty Investors, Inc., (IORI) whose common stock is traded on the American Stock Exchange under the symbol IOT . ARI's ownership of the TCI shares was achieved through a series of transactions, including a cash tender offer completed in 2003, an exchange by certain ARI subsidiaries of securities with Basic Capital Management, Inc. (BCM) and a sale of a participating interest in certain loans made by One Realco Corporation (One Realco) to BCM, as well as certain open market purchases of TCI shares in 2003. BCM and One Realco are companies affiliated with ARI. ARI has consolidated TCI's accounts and operations since March 2003.

ARI's contractual Advisor is Prime Income Asset Management, LLC (Prime), the sole member of which is Prime Income Asset Management, Inc., a Nevada corporation (PIAMI). PIAMI is owned by Realty Advisors, Inc. (RAI)(80%) and Syntek West, Inc. (SWI)(20%), SWI is owned by Gene E. Phillips, Realty Advisors, Inc. is owned by a Trust for the benefit of the children of Gene E. Phillips (the Trust). Gene E. Phillips is an officer and director of SWI and serves as a representative of the Trust. While Mr. Phillips is not an officer or director of ARI, he does periodically consult with the executive officers and directors of ARI rendering advice and input with respect to investment decisions affecting ARI. PIAMI also owns approximately 14.9% of the common stock of ARI and approximately 7.4% of the Series A 10% cumulative convertible preferred Stock of ARI.

ARI's Board of Directors represents the Company's shareholders and is responsible for directing the overall affairs of ARI and for setting the strategic policies that guide the Company. The Board of Directors has delegated the day-to-day management of the Company to Prime Income Asset Management, LLC (Prime) under a written advisory agreement that is reviewed annually by ARI's Board of Directors.

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Prime is a limited liability company whose sole member is a Nevada corporation indirectly owned 80 percent by the Trust and 20 percent by another Nevada corporation wholly-owned by Mr. Phillips. Prime owns approximately 13 percent of the outstanding common stock of ARI. Prime's duties include but are not limited to locating, evaluating and recommending real estate and real estate-related investment opportunities. Prime also arranges, for ARI's benefit, debt and equity financing with third party lenders and investors. Prime is compensated by ARI under an advisory agreement that is more fully described in Part III, Item 10, Directors, Executive Officers and Corporate Governance.

Prime also serves as advisor to TCI. The officers of ARI are also officers of IORI, TCI, and Prime. The directors of ARI also serve as directors of TCI. The Chairman of the Board of Directors of ARI also serves as the Chairman of the Board of Directors of TCI. One director of ARI also serves as a director of TCI and IORI. Affiliates of Prime have provided property management services to ARI. Currently, Triad Realty Services, LP. (Triad), an affiliate, and Carmel Realty, Inc. (Carmel) provide such property management services. Triad and Carmel subcontract with other entities for property-level management services. The general partner of Triad is Prime Income Asset Management, Inc. (PIAMI). The limited partner of Triad is Highland Realty Services, Inc. (HRS Holdings LLC (HRSHLLC)). Triad subcontracts the property-level management and leasing our commercial properties (shopping centers, office buildings, and industrial warehouses) to Regis Realty I, LLC (Regis I) which is owned by HRSHLLC. Regis I receives property and construction management fees and leasing commissions in accordance with the terms of its property-level management agreement with Triad. Regis Hotel I, LLC, manages our hotels. The sole member of Regis I and Regis Hotel I, LLC is HRSHLLC. Carmel is owned by Regis I.

Regis I is also entitled to receive real estate brokerage commissions in accordance with the terms of the Advisory Agreement as discussed in ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE.

ARI's primary business is the acquisition, development and ownership of income-producing residential, hotel and commercial real estate properties. In addition, ARI opportunistically acquires land for future development in in-fill or high-growth suburban markets. From time to time and when we believe it appropriate to do so, we will also sell land and income-producing properties. We generate revenues by leasing apartment units to residents; leasing office, industrial and retail space to various for-profit businesses as well as certain local, state and federal agencies; leasing trade show and exhibit space to temporary as well as long-term tenants; and renting hotel rooms to guests. We also generate revenues from gains on sales of income-producing properties and land. At December 31, 2007, our income-producing properties consisted of:

5.9 million rentable square feet of commercial properties, including 18 office buildings, 7 industrial properties, 5 retail properties and a four-story, 344,975 square-foot trade show and exhibit hall located in Denver, Colorado

69 residential apartment communities comprising almost 12,788 units

Nine hotels comprising 1,125 rooms

Subsequent to the year ended, we purchased and sold various properties. See NOTE 22 Subsequent Events.

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The following table sets forth the location of our real estate held for investment (income-producing properties only) by asset type as of December 31, 2007:

Location	Apartments		Commercial		Hotels	
	No.	Units	No.	SF	No.	Rooms
Greater Dallas-Ft. Worth, TX	18	3,825	13	2,769,587		
Greater Houston, TX	9	2,202				
Midland-Odessa, TX	15	2,457				
San Antonio, TX	4	1,112	1	101,500		
Other Texas	6	1,193				
Mississippi	7	450				
Arkansas	3	428				
Florida	3	322				
New Orleans, LA			6	1,369,388		
Denver, CO			2	419,791	1	161
Fresno, CA					4	647
Chicago, IL					3	152
Other	4	799	9	1,241,305	1	165
Totals	69	12,788	31	5,901,571	9	1,125

We finance our acquisitions primarily through operating cash flow, proceeds from the sale of land and income-producing properties and debt financing primarily in the form of property-specific first-lien mortgage loans from commercial banks and institutional lenders. We finance our development projects principally with short-term, variable-rate construction loans that are refinanced with the proceeds of long-term, fixed-rate amortizing mortgages when the development has been completed and occupancy has been stabilized. When we sell properties, we may carry a portion of the sales price generally in the form of a short-term, interest bearing seller-financed note receivable, secured by the property being sold. We may also from time to time enter into partnerships or joint ventures with various investors to acquire land or income-producing properties or to sell interests in certain of our properties.

We partner with various third-party development companies to construct residential apartment communities. The third-party developer typically holds a general partner as well as a limited partner interest in a limited partnership formed for the purpose of building a single property while we generally take a limited partner interest in the limited partnership. We may contribute land to the partnership as part of our equity contribution or we may contribute the necessary funds to the partnership to acquire the land. We are required to fund all required equity contributions while the third-party developer is responsible for obtaining construction financing, hiring and a general contractor and for the overall management, successful completion and delivery of the project. We generally bear all the economic risks and rewards of ownership in these partnerships and therefore include these partnerships in our consolidated financial statements. The third-party developer is paid a developer fee typically equal to a percentage of the construction costs. When the project reaches stabilized occupancy, we acquire the third-party developer's partnership interests in exchange for any remaining unpaid developer fees.

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At December 31, 2007, our projects in development included:

Property	Location	No. of Units	Costs to Date	Total Projected Costs
Bolivar Homes	Cleveland, MS	65	\$ 5,273	\$ 8,613
Broadway Estates	Greenville, MS	104	4,385	8,362
Dorado Ranch	Odessa, TX	224	2,690	19,137
Huntington Ridge Desoto	Desoto, TX	198	13,691	17,873
Lakeview @ Pecan Creek/Preserve	Denton, TX	192	5,296	18,008
Lincoln Estate I	Leake County, MS	55	1,536	7,708
Longfellow Arms	Longview, TX	216	12,684	16,672
Mansions of Mansfield	Mansfield, TX	208	5,618	18,687
Mason Park	Houston, TX	312	14,436	23,018
Northside of Travis	Sherman, TX	200	2,078	16,999
Parc at Rogers	Rogers, AR	250	22,205	24,192
Parc at Clarksville	Clarksville, TN	168	14,291	14,291
Parkway Place	Greenwood, MS	65	1,369	16,999
Pecan Pointe	Temple, TX	232	17,643	19,526
Portafino Lago Vista	Farmer s Branch, TX	212	20,078	26,450
Sunflower Estates	Indianola, MS	65	4,266	8,435
Yazoo Estates	Yazoo City, MS	96	4,101	8,351
Castleglen	Garland, TX	150	760	11,380
Pioneer Crossing	Austin, TX	240	814	22,000
		3,252	\$ 153,214	\$ 306,701

Our Subsidiary, TCI, has formed a number of joint ventures with Icon Partners, LLC (Icon) to develop various residential, commercial and mixed-use projects. The subsidiary typically owns 75 percent of these joint ventures, arranges for and guarantees all debt financing and provides all required equity capital. The terms of the joint ventures also allow our subsidiary to receive its cumulative investment plus a preferred return before Icon receives any equity distribution. Icon provides various development and project management services to the joint ventures and is paid monthly developer fees for those services. We include these joint ventures in the Company s consolidated financial statements and record a minority interest for Icon s equity in the venture.

We have made substantial investments in a number of large tracts of undeveloped and partially developed land and intend to a) continue to improve these tracts of land for our own development purposes or b) make the improvements necessary to ready the land for sale to other developers.

At December 31, 2007, our investments in undeveloped and partially developed land consisted of the following:

Property	Location	Date(s)		Acres	Cost	Primary
		Acquired				Intended Use
Mercer Crossing	Dallas, TX	1996-2007	772	108,230		Mixed use
Windmill Farms	Dallas, TX	2006	3,035	55,881		Single-family residential
Pioneer Crossing	Austin, TX	1997-2005	760	33,935		Multi-family residential
Circle C Ranch	Austin, TX	2006	1,092	32,669		Single-family residential
McKinney Ranch	Dallas, TX	1997-2005	306	26,385		Mixed use
Las Colinas Multi-Tracts	Dallas, TX	1995-2006	277	23,238		Commercial
Dallas North Tollway	Dallas, TX	2006	17	15,905		Commercial
Mandhal Bay	St. Thomas, USVI	2005	91	14,710		Single-family residential
Kaufman County	Dallas, TX	2000-2005	2,633	13,001		Single-family residential

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Waco Multi-Tracts	Waco, TX	2005-2006	545	5,469	Single-family residential
Meloy Portage	Kent, OH	2004	53	5,119	Multi-family residential
Jackson Convention Center	Jackson, MS	2007	2	3,848	Mixed use
Beltine-Geller Road	Dallas, TX	2007	379	2,888	Commercial
Subtotal			9,962	341,278	
Other land holdings	Various	1990-2007	912	48,714	Various
Total land holdings			10,874	389,992	

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In addition, we own 1) a non-controlling 20 percent interest in Milano Restaurants International, which operates and franchises several quick service restaurant concepts in California and 2) various other interests in real estate and real-estate related entities. We generally use the equity method to account for these investments.

Transactions during 2007

Land and income producing properties acquired during 2007 consisted of:

Property	Acres/ SF/ Units	Location	Property Type/ Intended Use	Date Acquired	Purchase Price	Debt Incurred	Annual Interest Rate	Fixed/ Variable	Maturity Date
Income-Producing Properties:									
Parkwest I	383,000SF	Dallas, TX	Office	Jan-07	40,604	35,000	6.06%	Fixed	Jan-08
Parkwest II	708,000SF	Dallas, TX	Office	Jan-07	69,694	62,000	9.32%		Jan-08
Thornwood ⁽¹⁾	109Units	Midland, TX	Multi-family residential		1,895	1,638			
Subtotal					112,193	98,638			
Land:									
Keller Springs	6Acres	Dallas, TX	Multi-family residential	Jan-07	2,646	2,021	8.25%	Prime + 100 bps	8-Feb
Audubon Terrace ⁽²⁾	29Acres	Natchez, MS	Multi-family residential	Mar-07					
Waco 151	151Acres	Waco, TX	Single-family residential	Apr-07	2,106	1,300	8.25%	Prime + 100 bps	10-Apr
Senlac Road	4Acres	Dallas, TX	Commercial	Apr-07	1,005		NA	NA	NA
Hines Meridian	40Acres	Dallas, TX	Commercial	May-07	8,490	5,000	9.25%	Fixed	10-Jun
William Sprowles	1Acres	Dallas, TX	Commercial	Jun-07	288		NA	NA	NA
Jackson Convention Center	2Acres	Jackson, MS	Mixed use	Jul-07	3,848		NA	NA	NA
Dorado Ranch	11Acres	Odessa, TX	Multi-family residential	Jul-07	733	467			
Austin Landing	11Acres	Sherman, TX	Multi-family residential	Oct-07	1,301	950	5.35%		9-Feb
Denham Springs	16Acres	Denham Springs, LA	Multi-family residential	Oct-07	1,350	892			
Beltline-Geller Road	379Acres	Dallas, TX	Commercial	Nov-07	2,782	1,909			
Subtotal					24,549	12,539			
Total					\$ 136,742	\$ 111,1			