

INTERGROUP CORP  
Form 10-Q  
February 02, 2018

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

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

**For the quarterly period ended December 31, 2017**

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 1-10324**

**THE INTERGROUP CORPORATION**

(Exact name of registrant as specified in its charter)

DELAWARE                      13-3293645  
(State or other jurisdiction of (I.R.S. Employer  
Incorporation or organization) Identification No.)

Edgar Filing: INTERGROUP CORP - Form 10-Q

1100 Glendon Avenue, PH-1, Los Angeles, California 90024

(Address of principal executive offices) (Zip Code)

(310) 889-2500

(Registrant's telephone number, including area code)

---

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company.

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company

Emerging growth company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act):

Yes  No

The number of shares outstanding of registrant's Common Stock, as of January 30, 2018 was 2,355,098.



**TABLE OF CONTENTS**

	<b><u>Page</u></b>
<b><u>PART I – FINANCIAL INFORMATION</u></b>	
<b><u>Item 1.</u></b> <u>Financial Statements.</u>	
<u>Condensed Consolidated Balance Sheets as of December 31, 2017 and June 30, 2017</u>	<u>3</u>
<u>Condensed Consolidated Statements of Operations for the Three Months ended December 31, 2017 and 2016</u>	<u>4</u>
<u>Condensed Consolidated Statements of Operations for the Six Months ended December 31, 2017 and 2016</u>	<u>5</u>
<u>Condensed Consolidated Statements of Cash Flows for the Six months ended December 31, 2017 and 2016</u>	<u>6</u>
<b><u>Item 2.</u></b> <u>Legal Proceedings</u>	<u>16</u>
<b><u>Item 3.</u></b> <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations.</u>	<u>16</u>
<b><u>Item 4.</u></b> <u>Controls and Procedures.</u>	<u>24</u>
<b><u>PART II – OTHER INFORMATION</u></b>	
<b><u>Item 5.</u></b> <u>Exhibits.</u>	<u>24</u>
<b><u>Signatures</u></b>	<u>25</u>

**PART I****FINANCIAL INFORMATION****Item 1 - Condensed Consolidated Financial Statements****THE INTERGROUP CORPORATION****CONDENSED CONSOLIDATED BALANCE SHEETS****(UNAUDITED)**

As of	December 31, 2017	June 30, 2017
<b>ASSETS</b>		
Investment in hotel, net	\$ 40,820,000	\$42,092,000
Investment in real estate, net	54,402,000	54,984,000
Investment in marketable securities	13,209,000	17,177,000
Other investments, net	963,000	1,211,000
Cash and cash equivalents	2,309,000	2,871,000
Restricted cash	7,686,000	7,402,000
Other assets, net	3,075,000	3,365,000
Deferred income taxes	3,688,000	4,107,000
<b>Total assets</b>	<b>\$ 126,152,000</b>	<b>\$ 133,209,000</b>
<b>LIABILITIES AND SHAREHOLDERS' DEFICIT</b>		
<b>Liabilities:</b>		
Accounts payable and other liabilities	\$ 2,971,000	\$2,947,000
Accounts payable and other liabilities - hotel	11,870,000	12,833,000
Due to securities broker	2,792,000	3,012,000
Obligations for securities sold	2,071,000	3,710,000
Related party and other notes payable	5,920,000	6,112,000
Mortgage notes payable - hotel	115,038,000	115,615,000
Mortgage notes payable - real estate	63,597,000	64,298,000
<b>Total liabilities</b>	<b>204,259,000</b>	<b>208,527,000</b>
<b>Shareholders' deficit:</b>		
Preferred stock, \$.01 par value, 100,000 shares authorized; none issued	-	-
Common stock, \$.01 par value, 4,000,000 shares authorized; 3,395,616 and 3,395,616 issued; 2,355,098 and 2,359,724 outstanding, respectively	33,000	33,000
Additional paid-in capital	10,468,000	10,346,000

Edgar Filing: INTERGROUP CORP - Form 10-Q

Accumulated deficit	(46,915,000	)	(45,298,000 )
Treasury stock, at cost, 1,040,518 and 1,035,892 shares, respectively	(12,735,000	)	(12,626,000 )
Total InterGroup shareholders' deficit	(49,149,000	)	(47,545,000 )
Noncontrolling interest	(28,958,000	)	(27,773,000 )
Total shareholders' deficit	(78,107,000	)	(75,318,000 )
Total liabilities and shareholders' equity	\$ 126,152,000		\$ 133,209,000

The accompanying notes are an integral part of these (unaudited) condensed consolidated financial statements.

- 3 -

**THE INTERGROUP CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(UNAUDITED)**

For the three months ended December 31,	2017	2016
Revenues:		
Hotel	\$ 13,187,000	\$ 12,837,000
Real estate	3,625,000	3,605,000
Total revenues	16,812,000	16,442,000
Costs and operating expenses:		
Hotel operating expenses	(10,743,000)	(9,611,000 )
Real estate operating expenses	(2,102,000 )	(1,754,000 )
Depreciation and amortization expenses	(1,267,000 )	(1,370,000 )
General and administrative expenses	(730,000 )	(602,000 )
Total costs and operating expenses	(14,842,000)	(13,337,000)
Income from operations	1,970,000	3,105,000
Other income (expense):		
Interest expense - mortgages	(2,490,000 )	(2,402,000 )
Net loss on marketable securities	(1,178,000 )	(3,290,000 )
Impairment loss on other investments	(200,000 )	(24,000 )
Dividend and interest income	48,000	68,000
Trading and margin interest expense	(313,000 )	(291,000 )
Total other expense, net	(4,133,000 )	(5,939,000 )
Loss before income taxes	(2,163,000 )	(2,834,000 )
Income tax (expense) benefit	(344,000 )	825,000
Net loss	(2,507,000 )	(2,009,000 )
Less: Net loss attributable to the noncontrolling interest	1,302,000	293,000
Net loss attributable to InterGroup	\$(1,205,000 )	\$(1,716,000 )
Net loss per share		
Basic and diluted	\$(1.06 )	\$(0.85 )
Net loss per share attributable to InterGroup		
Basic and diluted	\$(0.51 )	\$(0.72 )
Weighted average number of basic and diluted common shares outstanding	2,371,125	2,375,654

The accompanying notes are an integral part of these (unaudited) condensed consolidated financial statements.





**THE INTERGROUP CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(UNAUDITED)**

For the six months ended December 31,	2017	2016
Revenues:		
Hotel	\$27,624,000	\$27,442,000
Real estate	7,302,000	7,254,000
Total revenues	34,926,000	34,696,000
Costs and operating expenses:		
Hotel operating expenses	(21,332,000)	(19,867,000)
Real estate operating expenses	(3,997,000 )	(3,561,000 )
Depreciation and amortization expenses	(2,541,000 )	(2,638,000 )
General and administrative expenses	(1,561,000 )	(1,330,000 )
Total costs and operating expenses	(29,431,000)	(27,396,000)
Income from operations	5,495,000	7,300,000
Other income (expense):		
Interest expense - mortgages	(4,983,000 )	(4,864,000 )
Net loss on marketable securities	(2,200,000 )	(2,136,000 )
Impairment loss on other investments	(200,000 )	(44,000 )
Dividend and interest income	131,000	110,000
Trading and margin interest expense	(626,000 )	(553,000 )
Total other expense, net	(7,878,000 )	(7,487,000 )
Loss before income taxes	(2,383,000 )	(187,000 )
Income tax expense	(419,000 )	(227,000 )
Net loss	(2,802,000 )	(414,000 )
Less: Net loss (income) attributable to the noncontrolling interest	1,185,000	(111,000 )
Net loss attributable to InterGroup	\$(1,617,000 )	\$(525,000 )
Net loss per share		
Basic and diluted	\$(1.18 )	\$(0.17 )
Net loss per share attributable to InterGroup		
Basic and diluted	\$(0.68 )	\$(0.22 )
Weighted average number of basic and diluted common shares outstanding	2,371,445	2,378,690

The accompanying notes are an integral part of these (unaudited) condensed consolidated financial statements.

- 5 -

**THE INTERGROUP CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(UNAUDITED)**

For the six months ended December 31,	2017	2016
Cash flows from operating activities:		
Net loss	\$(2,802,000)	\$(414,000 )
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	2,597,000	2,638,000
Net unrealized loss on marketable securities	2,081,000	2,448,000
Impairment loss on other investments	200,000	44,000
Stock compensation expense	122,000	140,000
Deferred taxes	419,000	227,000
Changes in assets and liabilities:		
Investment in marketable securities	1,887,000	(5,210,000)
Other assets	290,000	2,648,000
Accounts payable and other liabilities	(939,000 )	(3,406,000)
Due to securities broker	(220,000 )	2,530,000
Obligations for securities sold	(1,639,000)	867,000
Net cash provided by operating activities	1,996,000	2,512,000
Cash flows from investing activities:		
Investment in hotel, net	(109,000 )	(317,000 )
Investment in real estate, net	(578,000 )	(615,000 )
Investment in Santa Fe	-	(30,000 )
Proceeds from other investments	48,000	-
Net cash used in investing activities	(639,000 )	(962,000 )
Cash flows from financing activities:		
Restricted cash - payment of mortgage impounds	(284,000 )	(962,000 )
Net payments of mortgage and other notes payable	(1,526,000)	(1,869,000)
Purchase of treasury stock	(109,000 )	(352,000 )
Net cash used in financing activities	(1,919,000)	(3,183,000)
Net decrease in cash and cash equivalents	(562,000 )	(1,633,000)
Cash and cash equivalents at the beginning of the period	2,871,000	5,404,000
Cash and cash equivalents at the end of the period	\$2,309,000	\$3,771,000
Supplemental information:		
Interest paid	\$5,336,000	\$5,167,000

The accompanying notes are an integral part of these (unaudited) condensed consolidated financial statements.



**THE INTERGROUP CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(UNAUDITED)**

**NOTE 1. BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES**

The condensed consolidated financial statements included herein have been prepared by The InterGroup Corporation (“InterGroup” or the “Company”), without audit, according to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in the condensed consolidated financial statements prepared in accordance with generally accepted accounting principles (U.S. GAAP) have been condensed or omitted pursuant to such rules and regulations, although the Company believes the disclosures that are made are adequate to make the information presented not misleading. Further, the condensed consolidated financial statements reflect, in the opinion of management, all adjustments (which included only normal recurring adjustments) necessary for a fair statement of the financial position, cash flows and results of operations as of and for the periods indicated. It is suggested that these financial statements be read in conjunction with the audited financial statements of InterGroup and the notes therein included in the Company's Annual Report on Form 10-K for the year ended June 30, 2017. The June 30, 2017 Condensed Consolidated Balance Sheet was derived from the Company’s Form 10-K for the year ended June 30, 2017.

The results of operations for the three and six months ended December 31, 2017 are not necessarily indicative of results to be expected for the full fiscal year ending June 30, 2018.

Basic and diluted loss per share is computed by dividing net loss available to common stockholders by the weighted average number of common shares outstanding. The computation of diluted income per share is similar to the computation of basic earnings per share except that the weighted-average number of common shares is increased to include the number of additional common shares that would have been outstanding if potential dilutive common shares had been issued. The Company's only potentially dilutive common shares are stock options.

As of December 31, 2017, the Company had the power to vote 85.8% of the voting shares of Santa Fe Financial Corporation (“Santa Fe”), a public company (OTCBB: SFEF). This percentage includes the power to vote an approximately 4% interest in the common stock in Santa Fe owned by the Company’s Chairman and President pursuant to a voting trust agreement entered into on June 30, 1998.

Santa Fe's primary business is conducted through the management of its 68.8% owned subsidiary, Portsmouth Square, Inc. ("Portsmouth"), a public company (OTCBB: PRSI). Portsmouth's primary business is conducted through its general and limited partnership interest in Justice Investors Limited Partnership; a California limited partnership ("Justice" or the "Partnership"). InterGroup also directly owns approximately 13.4% of the common stock of Portsmouth.

Justice, through its subsidiaries Justice Holdings Company, LLC ("Holdings"), a Delaware Limited Liability Company, Justice Operating Company, LLC ("Operating") and Justice Mezzanine Company, LLC ("Mezzanine"), owns a 544-room hotel property located at 750 Kearny Street, San Francisco California, known as the Hilton San Francisco Financial District (the "Hotel") and related facilities including a five-level underground parking garage. Holdings and Mezzanine are both wholly-owned subsidiaries of the Partnership; Operating is a wholly-owned subsidiary of Mezzanine. Mezzanine is the borrower under certain mezzanine indebtedness of Justice, and in December 2013, the Partnership conveyed ownership of the Hotel to Operating. The Hotel is operated by the partnership as a full-service Hilton brand hotel pursuant to a Franchise License Agreement with HLT Franchise Holding LLC (Hilton).

Justice had a management agreement with Prism Hospitality L.P. ("Prism") to perform certain management functions for the Hotel. The management agreement with Prism had an original term of ten years, subject to the Partnership's right to terminate at any time with or without cause. Effective January 2014, the management agreement with Prism was amended by the Partnership to change the nature of the services provided by Prism and the compensation payable to Prism, among other things. Prism's management agreement was terminated upon its expiration date of February 3, 2017. Effective December 1, 2013, GMP Management, Inc. ("GMP"), a company owned by a Justice limited partner and a related party, also provided management services for the Partnership pursuant to a management services agreement, with a three-year term, subject to the Partnership's right to terminate earlier for cause. In June 2016, GMP resigned. After a lengthy review process of several national third-party hotel management companies, on February 1, 2017, Justice entered into a Hotel management agreement ("HMA") with Interstate Management Company, LLC ("Interstate") to manage the Hotel with an effective takeover date of February 3, 2017. The term of management agreement is for an initial period of 10 years commencing on the takeover date and automatically renews for an additional year not to exceed five years in the aggregate subject to certain conditions. The HMA also provides for Interstate to advance a key money incentive fee to the Hotel for capital improvements in the amount of \$2,000,000 under certain terms and conditions described in a separate key money agreement. The \$2,000,000 is included in the restricted cash and related party and other notes payable balances in the condensed consolidated balance sheets as of December 31, 2017 and June 30, 2017.

The parking garage that is part of the Hotel property was managed by Ace Parking pursuant to a contract with the Partnership. The contract was terminated with an effective termination date of October 4, 2016. The Company began managing the parking garage in-house after the termination of Ace Parking. Effective February 3, 2017, Interstate took over the management of the parking garage along with the Hotel.

In addition to the operations of the Hotel, the Company also generates income from the ownership, management and, when appropriate, sale of real estate. Properties include fifteen apartment complexes, one commercial real estate property and three single-family houses. The properties are located throughout the United States, but are concentrated in Dallas, Texas and Southern California. The Company also has an investment in unimproved real property. As of December 31, 2017, all of the Company's residential and commercial rental properties are managed in-house.

#### **Due to Securities Broker**

Various securities brokers have advanced funds to the Company for the purchase of marketable securities under standard margin agreements. These advanced funds are recorded as a liability.

#### **Obligations for Securities Sold**

Obligation for securities sold represents the fair market value of shares sold with the promise to deliver that security at some future date and the fair market value of shares underlying the written call options with the obligation to deliver that security when and if the option is exercised. The obligation may be satisfied with current holdings of the same security or by subsequent purchases of that security. Unrealized gains and losses from changes in the obligation are included in the condensed consolidated statements of operations.

#### **Income Tax**

The Company consolidates Justice ("Hotel") for financial reporting purposes and is not taxed on its non-controlling interest in the Hotel. The income tax expense during the three and six months ended December 31, 2017 and 2016 represents the income tax effect on the Company's pretax income which includes its share in the net income of the Hotel.

## Financial Condition and Liquidity

The Company's cash flows are primarily generated from its Hotel operations. The Company also receives cash generated from the investment of its cash and marketable securities and other investments.

To fund the redemption of limited partnership interests and to repay the prior mortgage of \$42,940,000, Justice obtained a \$97,000,000 mortgage loan and a \$20,000,000 mezzanine loan. The mortgage loan is secured by the Partnership's principal asset, the Hotel. The mortgage loan bears an interest rate of 5.275% per annum with interest only payments due thru January 2017. Beginning in February 2017, the loan began to amortize over a thirty-year period thru its maturity date of January 2024. As additional security for the mortgage loan, there is a limited guaranty executed by the Company in favor of mortgage lender. The mezzanine loan is secured by the Operating membership interest held by Mezzanine and is subordinated to the Mortgage Loan. The mezzanine interest only loan bears interest at 9.75% per annum and matures in January 2024. As additional security for the mezzanine loan, there is a limited guaranty executed by the Company in favor of mezzanine lender.

Effective as of May 11, 2017, InterGroup agreed to become an additional guarantor under the limited guaranty and an additional indemnitor under the environmental indemnity for Justice Investors limited partnership's \$97,000,000 mortgage loan and the \$20,000,000 mezzanine loan. Pursuant to the agreement, InterGroup is required to maintain a certain net worth and liquidity. As of December 31, 2017, InterGroup is in compliance with both requirements.



Despite an uncertain economy, the Hotel has continued to generate positive operating income. While the debt service requirements related the loans may create some additional risk for the Company and its ability to generate cash flows in the future, management believes that cash flows from the operations of the Hotel and the garage will continue to be sufficient to meet all of the Partnership's current and future obligations and financial requirements.

The Company has invested in short-term, income-producing instruments and in equity and debt securities when deemed appropriate. The Company's marketable securities are classified as trading with unrealized gains and losses recorded through the consolidated statements of operations.

Management believes that its cash, marketable securities, and the cash flows generated from those assets and from the partnership management fees, will be adequate to meet the Company's current and future obligations. Additionally, management believes there is significant appreciated value in the Hotel property to support additional borrowings, if necessary.

#### **Recently Issued Accounting Pronouncements and U.S. Tax Reform**

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* (ASU 2014-09), which amends the existing accounting standards for revenue recognition. In August 2015, the FASB issued ASU No. 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, which delays the effective date of ASU 2014-09 by one year. The FASB also agreed to allow entities to choose to adopt the standard as of the original effective date. In March 2016, the FASB issued Accounting Standards Update No. 2016-08, *Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)* (ASU 2016-08) which clarifies the implementation guidance on principal versus agent considerations. The guidance includes indicators to assist an entity in determining whether it controls a specified good or service before it is transferred to the customers. The new revenue recognition standard will be effective for the Company in the first quarter of 2019, with the option to adopt it in the first quarter of 2018. We currently anticipate adopting the new standard effective July 1, 2019. The new standard also permits two methods of adoption: retrospectively to each prior reporting period presented (full retrospective method), or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application (the modified retrospective method). The Company currently anticipates adopting the standard using the modified retrospective method. While the Company is still in the process of completing the analysis on the impact this guidance will have on the consolidated financial statements and related disclosures, the Company does not expect the impact to be material.

In August 2014, the FASB issued ASU No. 2014-15, *Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern* that requires management to evaluate whether there are conditions and events that raise substantial doubt about the Company's ability to continue as a going concern within one year after the financial statements are issued on both an interim and annual basis. Management is required to provide certain footnote

disclosures if it concludes that substantial doubt exists or when its plans alleviate substantial doubt about the Company's ability to continue as a going concern. ASU No. 2014-15 becomes effective for annual periods beginning after December 15, 2016 and for interim reporting periods thereafter. The Company's adoption of this ASU did not have a material impact on its consolidated financial statements.

On June 16, 2016, the FASB issued ASU 2016-13, "*Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments.*" This ASU modifies the impairment model to utilize an expected loss methodology in place of the currently used incurred loss methodology, which will result in the more timely recognition of losses. ASU No. 2016-13 will be effective for us as of January 1, 2020. The Company is currently reviewing the effect of ASU No. 2016-13.

On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the "Tax Act"). The Tax Act significantly revises the future ongoing corporate income tax by, among other things, lowering corporate income tax rates. As the Company has a June 30 fiscal year-end, the lower corporate income tax rate will be phased in, resulting in a statutory federal rate of approximately 28% for our fiscal year ending June 30, 2018, and 21% for subsequent fiscal years.

The reduction of the corporate tax rate will cause us to reduce our deferred tax asset to the lower federal base rate of 21%. As a result, a provisional net charge of \$879,000 was included in the income tax expense for the quarter ended December 31, 2017.

The changes included in the Tax Act are broad and complex. The final transition impacts of the Tax Act may differ from the above estimate, possibly materially, due to, among other things, changes in interpretations of the Tax Act, any legislative action to address questions that arise because of the Tax Act, any changes in accounting standards for income taxes or related interpretations in response to the Tax Act, or any updates or changes to estimates the company has utilized to calculate the transition impact. The Securities Exchange Commission has issued rules that would allow for a measurement period of up to one year after the enactment date of the Tax Act to finalize the recording of the related tax impacts. We currently anticipate finalizing and recording any resulting adjustments by the end of our current fiscal year ending June 30, 2018.

## NOTE 2 – INVESTMENT IN HOTEL, NET

Investment in hotel consisted of the following as of:

December 31, 2017	Cost	Accumulated Depreciation	Net Book Value
Land	\$2,738,000	\$-	\$2,738,000
Furniture and equipment	27,896,000	(25,297,000)	2,599,000
Building and improvements	64,324,000	(28,841,000)	35,483,000
	\$94,958,000	\$(54,138,000)	\$40,820,000

June 30, 2017	Cost	Accumulated Depreciation	Net Book Value
Land	\$2,738,000	\$-	\$2,738,000
Furniture and equipment	27,681,000	(24,569,000)	3,112,000
Building and improvements	64,308,000	(28,066,000)	36,242,000
	\$94,727,000	\$(52,635,000)	\$42,092,000

## NOTE 3 – INVESTMENT IN REAL ESTATE

Investment in real estate consisted of the following:

As of	December 31, 2017	June 30, 2017
Land	\$ 25,033,000	\$ 25,033,000
Buildings, improvements and equipment	67,382,000	66,804,000
Accumulated depreciation	(38,013,000	) (36,853,000 )
Investment in real estate, net	\$ 54,402,000	\$ 54,984,000

In July 2015, the Company purchased residential house in Los Angeles, California as a strategic asset for \$1,975,000 in cash. In August 2016, the Company obtained a mortgage note payable on the house in the amount of \$1,000,000. The note has an adjustable interest rate of 5.25% as of December 31, 2017 and requires interest only payments for the first twenty-three months with a balloon payment at maturity in August 2018.

#### **NOTE 4 – INVESTMENT IN MARKETABLE SECURITIES**

The Company's investment in marketable securities consists primarily of corporate equities. The Company has also periodically invested in corporate bonds and income producing securities, which may include interests in real estate based companies and REITs, where financial benefit could transfer to its shareholders through income and/or capital gain.

At December 31, 2017 and June 30, 2017, all of the Company's marketable securities are classified as trading securities. The change in the unrealized gains and losses on these investments are included in earnings. Trading securities are summarized as follows:

Investment	Cost	Gross Unrealized Gain	Gross Unrealized Loss	Net Unrealized Loss	Fair Value
<b>As of December 31, 2017</b>					
Corporate Equities	\$27,296,000	\$ 2,251,000	\$ (16,338,000 )	\$ (14,087,000 )	\$13,209,000
<b>As of June 30, 2017</b>					
Corporate Equities	\$29,170,000	\$ 1,768,000	\$ (13,761,000 )	\$ (11,993,000 )	\$17,177,000

As of December 31, 2017 and June 30, 2017, approximately 16% and 28%, respectively, of the investment marketable securities balance above is comprised of the common stock of Comstock Mining, Inc.

As of December 31, 2017 and June 30, 2017, the Company had unrealized losses of \$16,105,000 and \$13,294,000, respectively, related to securities held for over one year.

Net loss on marketable securities on the statement of operations is comprised of realized and unrealized gains (losses). Below is the composition of the two components for the respective periods:

For the three months ended December 31,	2017	2016
Realized gain (loss) on marketable securities	\$181,000	\$(107,000 )
Unrealized gain (loss) on marketable securities	726,000	(260,000 )
Unrealized loss on marketable securities related to Comstock	(2,085,000)	(2,923,000)
Net loss on marketable securities	\$(1,178,000)	\$(3,290,000)

For the six months ended December 31,	2017	2016
Realized (loss) gain on marketable securities	\$(119,000 )	\$312,000
Unrealized gain (loss) on marketable securities	673,000	(57,000 )
Unrealized loss on marketable securities related to Comstock	(2,754,000)	(2,391,000)
Net loss on marketable securities	\$(2,200,000)	\$(2,136,000)

**NOTE 5 – OTHER INVESTMENTS, NET**

The Company may also invest, with the approval of the securities investment committee and other Company guidelines, in private investment equity funds and other unlisted securities, such as convertible notes through private placements. Those investments in non-marketable securities are carried at cost on the Company's balance sheet as part of other investments, net of other than temporary impairment losses. Other investments also include non-marketable warrants carried at fair value.

- 11 -

Other investments, net consist of the following:

Type	December 31, 2017	June 30, 2017
Private equity hedge fund, at cost	\$ 582,000	\$ 782,000
Other preferred stock, at cost	381,000	429,000
	\$ 963,000	\$ 1,211,000

#### NOTE 6 – FAIR VALUE MEASUREMENTS

The carrying values of the Company’s financial instruments not required to be carried at fair value on a recurring basis approximate fair value due to their short maturities (i.e., accounts receivable, other assets, accounts payable and other liabilities and obligations for securities sold) or the nature and terms of the obligation (i.e., other notes payable and mortgage notes payable).

The assets measured at fair value on a recurring basis are as follows:

As of	12/31/2017	6/30/2017
	Total - Level 1	Total - Level 1
Assets:		
Investment in marketable securities:		
Basic materials	\$ 2,640,000	\$ 6,222,000
Technology	3,039,000	4,134,000
REITs and real estate companies	1,494,000	1,820,000
Energy	472,000	1,345,000
Corporate Bonds	1,774,000	1,683,000
Other	3,790,000	1,973,000
	\$ 13,209,000	\$ 17,177,000

The fair values of investments in marketable securities are determined by the most recently traded price of each security at the balance sheet date.

Financial assets that are measured at fair value on a non-recurring basis and are not included in the tables above include “Other investments in non-marketable securities,” that were initially measured at cost and have been written down to fair value as a result of impairment or adjusted to record the fair value of new instruments received (i.e., preferred shares) in exchange for old instruments (i.e., debt instruments). The following table shows the fair value

hierarchy for these assets measured at fair value on a non-recurring basis as follows:

<b>Assets</b>	<b>Level 3</b>	<b>December 31, 2017</b>	<b>Net loss for the six months ended December 31, 2017</b>
Other non-marketable investments	\$963,000	\$ 963,000	\$(200,000 )

  

<b>Assets</b>	<b>Level 3</b>	<b>June 30, 2017</b>	<b>Net loss for the six months ended December 31, 2016</b>
Other non-marketable investments	\$1,211,000	\$ 1,211,000	\$(44,000 )

Other investments in non-marketable securities are carried at cost net of any impairment loss. The Company has no significant influence or control over the entities that issue these investments and holds less than 20% ownership in each of the investments. These investments are reviewed on a periodic basis for other-than-temporary impairment. The Company reviews several factors to determine whether a loss is other-than-temporary. These factors include but are not limited to: (i) the length of time an investment is in an unrealized loss position, (ii) the extent to which fair value is less than cost, (iii) the financial condition and near term prospects of the issuer and (iv) our ability to hold the investment for a period of time sufficient to allow for any anticipated recovery in fair value.



**NOTE 7 – STOCK BASED COMPENSATION PLANS**

The Company follows Accounting Standard Codification (ASC) Topic 718 “Compensation – Stock Compensation”, which addresses accounting for equity-based compensation arrangements, including employee stock options and restricted stock units.

Please refer to Note 16 – Stock Based Compensation Plans in the Company's Form 10-K for the year ended June 30, 2017 for more detail information on the Company's stock-based compensation plans.

During the three months ended December 31, 2017 and 2016, the Company recorded stock option compensation cost of \$60,000 and \$66,000, respectively, related to stock options that were previously issued. For the six months ended December 31, 2017 and 2016, the Company recorded stock option compensation cost of \$122,000 and \$140,000, respectively, related to stock options that were previously issued. As of December 31, 2017, there was a total of \$181,000 of unamortized compensation related to stock options which is expected to be recognized over the weighted-average period of 2.90 years.

Option-pricing models require the input of various subjective assumptions, including the option's expected life and the price volatility of the underlying stock. The expected stock price volatility is based on analysis of the Company's stock price history. The Company has selected to use the simplified method for estimating the expected term. The risk-free interest rate is based on the U.S. Treasury interest rates whose term is consistent with the expected life of the stock options. No dividend yield is included as the Company has not issued any dividends and does not anticipate issuing any dividends in the future.

The following table summarizes the stock options activity from July 1, 2016 through December 31, 2017:

		Shares	Exercise Price	Remaining Life	Intrinsic Value
Outstanding at	July 1, 2016	350,000	\$ 16.70	5.95 years	\$ 3,082,000
Granted		18,000	27.30		
Exercised		-	-		
Forfeited		-	-		
Exchanged		-	-		
Outstanding at	June 30, 2017	368,000	\$ 17.21	5.17 years	\$ 3,046,000
Exercisable at	June 30, 2017	286,000	\$ 16.19	5.20 years	\$ 2,635,000
Vested and Expected to vest at	June 30, 2017	368,000	\$ 17.21	5.17 years	\$ 3,046,000

Oustanding at	July 1, 2017	368,000	\$ 17.21	5.17 years	\$ 3,046,000
Granted		-	-		
Exercised		-	-		
Forfeited		-	-		
Exchanged		-	-		
Oustanding at	December 31, 2017	368,000	\$ 17.21	4.67 years	\$ 2,500,575
Exercisable at	December 31, 2017	318,000	\$ 16.47	4.80 years	\$ 2,345,000
Vested and Expected to vest at	December 31, 2017	368,000	\$ 17.21	4.67 years	\$ 2,500,575

## NOTE 8 – SEGMENT INFORMATION

The Company operates in three reportable segments, the operation of the hotel (“Hotel Operations”), the operation of its multi-family residential properties (“Real Estate Operations”) and the investment of its cash in marketable securities and other investments (“Investment Transactions”). These three operating segments, as presented in the financial statements, reflect how management internally reviews each segment’s performance. Management also makes operational and strategic decisions based on this information.

Information below represents reported segments for the three and six months ended December 31, 2017 and 2016. Operating income from hotel operations consist of the operation of the hotel and operation of the garage. Operating income for rental properties consist of rental income. Operating income (loss) for investment transactions consist of net investment gain (loss), impairment loss on other investments, net unrealized gain (loss) on other investments, dividend and interest income and trading and margin interest expense. The other segment consists of corporate general and administrative expenses and the income tax expense for the entire Company.

Edgar Filing: INTERGROUP CORP - Form 10-Q

As of and for the three months ended December 31, 2017	Hotel Operations	Real Estate Operations	Investment Transactions	Corporate	Total
Revenues	\$ 13,187,000	\$ 3,625,000	\$-	\$-	\$ 16,812,000
Segment operating expenses	(10,743,000)	(2,102,000)	-	(730,000)	(13,575,000)
Segment income (loss) from operations	2,444,000	1,523,000	-	(730,000)	3,237,000
Interest expense - mortgage	(1,850,000)	(640,000)	-	-	(2,490,000)
Depreciation and amortization expense	(682,000)	(585,000)	-	-	(1,267,000)
Loss from investments	-	-	(1,643,000)	-	(1,643,000)
Income tax expense	-	-	-	(344,000)	(344,000)
Net income (loss)	\$(88,000)	\$298,000	\$(1,643,000)	\$(1,074,000)	\$(2,507,000)
Total assets	\$49,626,000	\$54,402,000	\$14,172,000	\$7,952,000	\$126,152,000

As of and for the three months ended December 31, 2016	Hotel Operations	Real Estate Operations	Investment Transactions	Corporate	Total
Revenues	\$ 12,837,000	\$ 3,605,000	\$-	\$-	\$ 16,442,000
Segment operating expenses	(9,611,000)	(1,754,000)	-	(602,000)	(11,967,000)
Segment income (loss) from operations	3,226,000	1,851,000	-	(602,000)	4,475,000
Interest expense - mortgage	(1,750,000)	(652,000)	-	-	(2,402,000)
Depreciation and amortization expense	(810,000)	(560,000)	-	-	(1,370,000)
Loss from investments	-	-	(3,537,000)	-	(3,537,000)
Income tax benefit	-	-	-	825,000	825,000
Net income (loss)	\$666,000	\$639,000	\$(3,537,000)	\$223,000	\$(2,009,000)
Total assets	\$50,206,000	\$55,856,000	\$18,029,000	\$8,701,000	\$132,792,000

As of and for the six months ended December 31, 2017	Hotel Operations	Real Estate Operations	Investment Transactions	Corporate	Total
Revenues	\$27,624,000	\$7,302,000	\$-	\$-	\$34,926,000
Segment operating expenses	(21,332,000)	(3,997,000)	-	(1,561,000)	(26,890,000)
Segment income (loss) from operations	6,292,000	3,305,000	-	(1,561,000)	8,036,000
Interest expense - mortgage	(3,703,000)	(1,280,000)	-	-	(4,983,000)
Depreciation and amortization expense	(1,381,000)	(1,160,000)	-	-	(2,541,000)
Loss from investments	-	-	(2,895,000)	-	(2,895,000)
Income tax expense	-	-	-	(419,000)	(419,000)
Net income (loss)	\$1,208,000	\$865,000	\$(2,895,000)	\$(1,980,000)	\$(2,802,000)
Total assets	\$49,626,000	\$54,402,000	\$14,172,000	\$7,952,000	\$126,152,000

As of and for the six months ended December 31, 2016	Hotel Operations	Real Estate Operations	Investment Transactions	Corporate	Total
Revenues	\$27,442,000	\$7,254,000	\$-	\$-	\$34,696,000
Segment operating expenses	(19,867,000)	(3,561,000)	-	(1,330,000)	(24,758,000)
Segment income (loss) from operations	7,575,000	3,693,000	-	(1,330,000)	9,938,000
Interest expense - mortgage	(3,579,000)	(1,285,000)	-	-	(4,864,000)
Depreciation and amortization expense	(1,523,000)	(1,115,000)	-	-	(2,638,000)
Loss from investments	-	-	(2,623,000)	-	(2,623,000)

Edgar Filing: INTERGROUP CORP - Form 10-Q

Income tax expense	-	-	-	(227,000 )	(227,000 )
Net income (loss)	\$2,473,000	\$1,293,000	\$(2,623,000 )	\$(1,557,000)	\$(414,000 )
Total assets	\$50,206,000	\$55,856,000	\$18,029,000	\$8,701,000	\$132,792,000

- 14 -

## NOTE 9 – RELATED PARTY TRANSACTIONS

On July 2, 2014, the Partnership obtained from the Company an unsecured loan in the principal amount of \$4,250,000 at 12% per year fixed interest, with a term of 2 years, payable interest only each month. InterGroup received a 3% loan fee. The loan may be prepaid at any time without penalty. The loan was extended to December 31, 2018.

Also included in the balance of related party note payable at December 31, 2017 is the obligation to Hilton (Franchisor) in the form of a self-exhausting, interest free development incentive note which is reduced by approximately \$316,000 annually through 2030 by Hilton if the Partnership is still a Franchisee with Hilton. The outstanding balance of the note as of December 31, 2017 and June 30, 2017, was \$3,800,000 and \$3,958,000, respectively.

On February 1, 2017, Justice entered into a Hotel management agreement (“HMA”) with Interstate Management Company, LLC (“Interstate”) to manage the Hotel with an effective takeover date of February 3, 2017. The term of management agreement is for an initial period of 10 years commencing on the takeover date and automatically renews for an additional year not to exceed five years in the aggregate subject to certain conditions. The HMA also provides for Interstate to advance a key money incentive fee to the Hotel for capital improvements in the amount of \$2,000,000 under certain terms and conditions described in a separate key money agreement. The key money contribution shall be amortized in equal monthly amounts over an eight (8) year period commencing on the second (2<sup>nd</sup>) anniversary of the takeover date. The \$2,000,000 is included in restricted cash and related party and other notes payable balances in the condensed consolidated balance sheets as of December 31, 2017 and June 30, 2017.

In April 2017, Portsmouth obtained from InterGroup an unsecured short-term loan in the amount of \$1,000,000 at 5% per year fixed interest, with a term of five months and maturing September 6, 2017. The loan was extended to September 15, 2017 and paid off on September 13, 2017.

Effective May 12, 2017, InterGroup agreed to become an additional guarantor under the limited guaranty and an additional indemnitor under environmental indemnity for Justice Investors limited partnership’s \$97,000,000 mortgage loan and the \$20,000,000 mezzanine loan, in order to maintain certain minimum net worth and liquidity guarantor covenant requirements that Portsmouth was unable to satisfy independently.

In connection with the redemption of the limited partnership interest of Justice, Justice Operating Company, LLC agreed to pay a total of \$1,550,000 in fees to certain officers and directors of the Company for services rendered in connection with the redemption of the partnership interests, refinancing of the Justices properties and reorganization of Justice. This agreement was superseded by a letter dated December 11, 2013 from Justice, in which Justice

assumed the payment obligations of Justice Operating Company, LLC. As of December 31, 2017, \$400,000 of these fees remain payable.

As of June 30, 2017, Justice had an outstanding accounts payable balance to InterGroup for \$316,000 for management of the Hotel from June to December of 2016. As of December 31, 2017, that balance was paid off.

Four of the Portsmouth directors serve as directors of InterGroup. Three of those directors also serve as directors of Santa Fe. The three Santa Fe directors also serve as directors of InterGroup.

As Chairman of the Securities Investment Committee, the Company's President and Chief Executive Officer (CEO), John V. Winfield, directs the investment activity of the Company in public and private markets pursuant to authority granted by the Board of Directors. Mr. Winfield also serves as Chief Executive Officer and Chairman of the Portsmouth and Santa Fe and oversees the investment activity of those companies. Depending on certain market conditions and various risk factors, the Chief Executive Officer, Portsmouth and Santa Fe may, at times, invest in the same companies in which the Company invests. Such investments align the interests of the Company with the interests of related parties because it places the personal resources of the Chief Executive Officer and the resources of the Portsmouth and Santa Fe, at risk in substantially the same manner as the Company in connection with investment decisions made on behalf of the Company.

## **Item 2 – LEGAL PROCEEDINGS**

We are involved from time to time in legal proceedings of types regarded as common in our business, including administrative or judicial proceedings, such as employment or labor disputes, breach of contract liability and premises liability litigation. Where appropriate, we may establish financial reserves for such proceedings. We also maintain insurance to mitigate certain of such risks.

On April 21, 2014, the Partnership commenced arbitration against Glaser Weil Fink Howard Avchen & Shapiro, LLP, Brett J. Cohen, Gary N. Jacobs, Janet S. McCloud, Paul B. Salvaty, and Joseph K. Fletcher III (“Respondents”) in connection with the redemption transaction. The arbitration alleges legal malpractice and also seeks declaratory relief regarding provisions of the redemption option agreement. The arbitration proceedings are active; discovery is proceeding. The hearing is set for April 2018 before JAMS in Los Angeles, California. The parties began a series of mediation sessions prior to the scheduled hearing. No prediction can be given as to the outcome of this matter.

On May 5, 2016, Justice and Portsmouth entered into a settlement agreement relating to previously reported litigation with Evon Corporation and certain other parties. Under the settlement agreement, Justice, a subsidiary of Portsmouth agreed to pay Evon Corporation \$5,575,000. The final installment due was made in January 2017 and all conditions of the settlement agreement have been satisfied by Justice and Portsmouth.

## **Item 3 – MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

### **FORWARD-LOOKING STATEMENTS AND PROJECTIONS**

The Company may from time to time make forward-looking statements and projections concerning future expectations. When used in this discussion, the words “anticipate,” “estimate,” “expect,” “project,” “intend,” “plan,” “believe,” “could,” “will”, “would” and similar expressions, are intended to identify forward-looking statements. These statements are subject to certain risks and uncertainties, such as national and worldwide economic conditions, including the impact of recessionary conditions on tourism, travel and the lodging industry, the impact of terrorism and war on the national and international economies, including tourism and securities markets, energy and fuel costs, natural disasters, general economic conditions and competition in the hotel industry in the San Francisco area, seasonality, labor relations and labor disruptions, actual and threatened pandemics such as swine flu, partnership distributions, the ability to obtain financing at favorable interest rates and terms, securities markets, regulatory factors, litigation and other factors discussed below in this Report and in the Company’s Annual Report on Form 10-K for the fiscal year ended June 30, 2017, that could cause actual results to differ materially from those projected. Readers are cautioned not to place

undue reliance on these forward-looking statements, which speak only as to the date hereof. The Company undertakes no obligation to publicly release the results of any revisions to those forward-looking statements, which may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

## **RESULTS OF OPERATIONS**

As of December 31, 2017, the Company owned approximately 81.9% of the common shares of its subsidiary, Santa Fe and Santa Fe owned approximately 68.8% of the common shares of Portsmouth Square, Inc. InterGroup also directly owns approximately 13.4% of the common shares of Portsmouth. The Company's principal sources of revenue continue to be derived from the general and limited partnership interests of its subsidiary, Portsmouth, in the Justice Investors limited partnership ("Justice" or the "Partnership"), rental income from its investments in multi-family real estate properties and income received from investment of its cash and securities assets. Justice owns a 544- room hotel property located at 750 Kearny Street, San Francisco, California 94108, known as the "Hilton San Francisco Financial District" (the "Hotel" or the "Property") and related facilities, including a five-level underground parking garage. The financial statements of Justice have been consolidated with those of the Company.



The Hotel is operated by the Partnership as a full service Hilton brand hotel pursuant to a Franchise License Agreement (the "License Agreement") with HLT Franchise Holding LLC ("Hilton"). The Partnership entered into the License Agreement on December 10, 2004. The term of the License Agreement was for an initial period of 15 years commencing on the opening date, with an option to extend the License Agreement for another five years, subject to certain conditions. On June 26, 2015, the Partnership and Hilton entered into an amended franchise agreement which extended the License Agreement through 2030, modified the monthly royalty rate, extended geographic protection to the Partnership and also provided the Partnership certain key money cash incentives to be earned through 2030. The key money cash incentives were received on July 1, 2015.

Justice had a management agreement with Prism Hospitality L.P. ("Prism") to perform certain management functions for the Hotel. The management agreement with Prism had an original term of ten years and can be terminated at any time with or without cause by the Partnership. Effective January 2014, the management agreement with Prism was amended by the Partnership to change the nature of the services provided by Prism and the compensation payable to Prism, among other things. Prism's management agreement was terminated upon its expiration date of February 3, 2017. Effective December 1, 2013, GMP Management, Inc. ("GMP"), a company owned by a Justice limited partner and a related party, began to provide management services for the Partnership pursuant to a management services agreement with a term of three years, subject to the Partnership's right to terminate earlier, for cause. In June 2016, GMP resigned. After a lengthy review process of several national third party hotel management companies, on February 1, 2017, Justice entered into a Hotel management agreement ("HMA") with Interstate Management Company, LLC ("Interstate") to manage the Hotel with an effective takeover date of February 3, 2017. The term of management agreement is for an initial period of 10 years commencing on the takeover date and automatically renews for an additional year not to exceed five years in the aggregate subject to certain conditions. The HMA also provides for Interstate to advance a key money incentive fee to the Hotel for capital improvements in the amount of \$2,000,000 under certain terms and conditions described in a separate key money agreement. The \$2,000,000 is included in restricted cash and related party and other notes payable in the condensed consolidated balance sheets as of December 31, 2017 and June 30, 2017.

The parking garage that is part of the Hotel property was managed by Ace Parking pursuant to a contract with the Partnership. The contract was terminated with an effective termination date of October 4, 2016. The Company began managing the parking garage in-house after the termination of Ace Parking. Effective February 3, 2017, Interstate took over the management of the parking garage along with the Hotel.

In addition to the operations of the Hotel, the Company also generates income from the ownership and management of real estate. Properties include sixteen apartment complexes, one commercial real estate property, and three single-family houses as strategic investments. The properties are located throughout the United States, but are concentrated in Texas and Southern California. The Company also has an investment in unimproved real property. All of the Company's residential and commercial rental operating properties are managed in-house.

The Company acquires its investments in real estate and other investments utilizing cash, securities or debt, subject to approval or guidelines of the Board of Directors. The Company also invests in income-producing instruments, equity and debt securities and will consider other investments if such investments offer growth or profit potential.

### **Three Months Ended December 31, 2017 Compared to the Three Months Ended December 31, 2016**

The Company had a net loss of \$2,507,000 for the three months ended December 31, 2017 compared to net loss of \$2,009,000 for the three months ended December 31, 2016. The increase in the net loss is primarily attributable to higher operating expenses from the Hotel operations and the increase in income tax expense.

#### **Hotel Operations**

The Company had net loss from Hotel operations of \$88,000 for the three months ended December 31, 2017 compared to net income of \$666,000 for the three months ended December 31, 2016. The change is primarily due to increased operating expenses. The increase in revenues were offset by increased franchise fees, legal fees and union wages during the quarter ended December 31, 2017 compared to December 31, 2016.

The following table sets forth a more detailed presentation of Hotel operations for the three months ended December 31, 2017 and 2016.

For the three months ended December 31,	2017	2016
Hotel revenues:		
Hotel rooms	\$ 10,710,000	\$ 10,497,000
Food and beverage	1,614,000	1,506,000
Garage	735,000	643,000
Other operating departments	128,000	191,000
Total hotel revenues	13,187,000	12,837,000
Operating expenses excluding depreciation and amortization	(10,743,000)	(9,611,000)
Operating income before interest, depreciation and amortization	2,444,000	3,226,000
Interest expense - mortgage	(1,850,000)	(1,750,000)
Depreciation and amortization expense	(682,000)	(810,000)
Net income (loss) from Hotel operations	\$(88,000)	\$ 666,000

For the three months ended December 31, 2017, the Hotel had operating income of \$2,444,000 before interest expense, depreciation and amortization on total operating revenues of \$13,187,000 compared to operating income of \$3,226,000 before interest expense, depreciation and amortization on total operating revenues of \$12,837,000 for the three months ended December 31, 2016. Room revenues increased by \$213,000 for the three months ended December 31, 2017 compared to the three months ended December 31, 2016 primarily due to Salesforce citywide conference moving from third quarter in 2016 to fourth quarter in 2017. Food and beverage revenue increased by \$108,000 as a result of increased catering and banquet services. Garage revenues increased by \$92,000.

Total operating expenses increased by \$1,132,000 this quarter as compared to the previous comparable quarter primarily due to increased operating expenses related to food and beverage, rooms, franchise fees, and legal fees.

The following table sets forth the average daily room rate, average occupancy percentage and room revenue per available room (“RevPAR”) of the Hotel for the three months ended December 31, 2017 and 2016.

Three Months Ended December 31,	Average Daily Rate	Average Occupancy %	RevPAR
2017	\$ 240	89	% \$ 212
2016	\$ 236	89	% \$ 210

The Hotel's revenues increased by 2.7% this quarter as compared to the previous comparable quarter. Average daily rate increased by \$4 and RevPAR increased by \$2 for the three months ended December 31, 2017 compared to the three months ended December 31, 2016. Average occupancy was 89% for both quarters.

### **Real Estate Operations**

Real estate revenues for the three months ended December 31, 2017 and 2016 remained relatively consistent at \$3,625,000 and \$3,605,000, respectively. Real estate operating expenses increased for the three months ended December 31, 2017 comparing to the three months ended December 31, 2016 primarily due to increase in real estate taxes. All of Company's properties are managed in-house. Management continues to review and analyze the Company's real estate operations to improve occupancy and rental rates and to reduce expenses and improve efficiencies.

### **Investment Transactions**

The Company had a net loss on marketable securities of \$1,178,000 for the three months ended December 31, 2017 compared to a net loss on marketable securities of \$3,290,000 for the three months ended December 31, 2016. As of December 31, 2017 and 2016, approximately 16% and 41%, respectively, of the investment in marketable securities balance above is comprised of the common stock of Comstock Mining, Inc. (Comstock). As the result, the change in the market price of the common stock of Comstock will have a significant impact on the gain (loss) on marketable securities. For the three months ended December 31, 2017, the Company had a net realized gain of \$181,000 and a net unrealized loss of \$1,359,000. For the three months ended December 31, 2016, the Company had a net realized loss of \$107,000 and a net unrealized loss of \$3,183,000. Gains and losses on marketable securities may fluctuate significantly from period to period in the future and could have a significant impact on the Company's results of operations. However, the amount of gain or loss on marketable securities for any given period may have no predictive value and variations in amount from period to period may have no analytical value. For a more detailed description of the composition of the Company's marketable securities see the Marketable Securities section below.

The Company and its subsidiaries, Portsmouth and Santa Fe, compute and file income tax returns and prepare discrete income tax provisions for financial reporting. The income tax expense during the three months ended December 31, 2017 and 2016 represents primarily the income tax effect of the pre-tax income at InterGroup and the pretax income of Portsmouth which includes its share in net income of the Hotel.

### Six Months Ended December 31, 2017 Compared to the Six Months Ended December 31, 2016

The Company had a net loss of \$2,802,000 for the six months ended December 31, 2017 compared to net loss of \$414,000 for the six months ended December 31, 2016. The increase in the net loss is primarily attributable to higher operating expenses from the Hotel and real estate.

### Hotel Operations

Net income from Hotel operations was \$1,208,000 for the six months ended December 31, 2017 compared to net income of \$2,473,000 for the six months ended December 31, 2016. The decrease in net income is primarily due to increased operating expenses. The increase in revenues were offset by increased franchise fees, legal fees and union wages during the six months ended December 31, 2017 compared to December 31, 2016.

The following table sets forth a more detailed presentation of Hotel operations for the six months ended December 31, 2017 and 2016.

For the six months ended December 31,	2017	2016
Hotel revenues:		
Hotel rooms	\$22,552,000	\$22,795,000
Food and beverage	3,373,000	2,955,000
Garage	1,516,000	1,324,000
Other operating departments	183,000	368,000
Total hotel revenues	27,624,000	27,442,000
Operating expenses excluding depreciation and amortization	(21,332,000)	(19,867,000)
Operating income before loss on disposal of assets, interest, depreciation and amortization	6,292,000	7,575,000
Interest expense - mortgage	(3,703,000 )	(3,579,000 )
Depreciation and amortization expense	(1,381,000 )	(1,523,000 )
Net income from Hotel operations	\$1,208,000	\$2,473,000

Edgar Filing: INTERGROUP CORP - Form 10-Q

For the six months ended December 31, 2017, the Hotel had operating income of \$6,292,000 before interest, depreciation and amortization on total operating revenues of \$27,624,000 compared to operating income of \$7,575,000 before interest, depreciation and amortization on total operating revenues of \$27,442,000 for the six months ended December 31, 2016. Room revenues decreased by \$243,000 for the six months ended December 31, 2017 compared to the six months ended December 31, 2016 primarily as the result of the decrease in group business and the decrease in the average daily rate. Food and beverage revenue increased by \$418,000 as the result of an increase in the catering and banquet services from the decrease in the group business. Garage revenues increased by \$192,000 as a result of freeing parking spaces that were utilized as storage by previous management as well as additional valet parking income.

Total operating expenses increased by \$1,465,000 for the six months ended December 31, 2017 as compared to the six months ended December 31, 2016 primarily due to the increase in legal fees associated with the Glaser matter, franchise fees, food, beverage and room operating expenses; the increase was offset by reduced advertising and sales costs, repairs and maintenance expense, and other operating department expenses.

The following table sets forth the average daily room rate, average occupancy percentage and room revenue per available room (“RevPAR”) of the Hotel for the six months ended December 31, 2017 and 2016.

<b>Six months</b>	<b>Average</b>	<b>Average</b>	
<b>Ended December 31,</b>	<b>Daily Rate</b>	<b>Occupancy %</b>	<b>RevPAR</b>
2017	\$ 247	91	% \$ 225
2016	\$ 245	93	% \$ 228

The Hotel’s total revenues increased by 0.7% for the six months ended December 31, 2017 as compared to the six months ended December 31, 2016. Average daily rate increased by \$2 and RevPAR decreased by \$3 for the six months ended December 31, 2017 compared to the six months ended December 31, 2016. Average occupancy decreased by 2% during the six months ended December 31, 2017 versus the comparable period.

### **Real Estate Operations**

Real estate revenues for the six months ended December 31, 2017 and 2016 remained relatively consistent at \$7,302,000 and \$7,254,000, respectively. Real estate operating expenses increased for the six months ended December 31, 2017 comparing to the six months ended December 31, 2016 primarily due to increase in real estate taxes. All of Company’s properties are managed in-house. Management continues to review and analyze the Company’s real estate operations to improve occupancy and rental rates and to reduce expenses and improve efficiencies.

### **Investment Transactions**

The Company had a net loss on marketable securities of \$2,200,000 for the six months ended December 31, 2017 compared to a net loss on marketable securities of \$2,136,000 for the six months ended December 31, 2016. For the six months ended December 31, 2017 and 2016, the Company had a net loss of approximately \$2,754,000 and \$2,391,000 related to the Company’s investment in the common stock of Comstock. For the six months ended December 31, 2017, the Company had a net realized loss of \$119,000 and a net unrealized loss of \$2,081,000. For the six months ended December 31, 2016, the Company had a net realized gain of \$312,000 and a net unrealized loss of \$2,448,000. Gains and losses on marketable securities may fluctuate significantly from period to period in the future and could have a significant impact on the Company’s results of operations. However, the amount of gain or loss on marketable securities for any given period may have no predictive value and variations in amount from period to period may have no analytical value. For a more detailed description of the composition of the Company’s marketable securities see the Marketable Securities section below.

During the six months ended December 31, 2017 and 2016, the Company performed an impairment analysis of its other investments and determined that its investments had an other than temporary impairment and recorded impairment losses of \$200,000 and \$44,000 in the respective periods.

The Company and its subsidiaries, Portsmouth and Santa Fe, compute and file income tax returns and prepare discrete income tax provisions for financial reporting. The income tax (expense) benefit during the six months ended December 31, 2017 and 2016 represents primarily the income tax effect of the pre-tax loss at InterGroup and Portsmouth's pretax income (loss) which includes its share in net income of the Hotel.

### **MARKETABLE SECURITIES**

The following table shows the composition of the Company's marketable securities portfolio as of December 31, 2017 and June 30, 2017 by selected industry groups.

- 20 -



As of December 31, 2017 Industry Group	Fair Value	% of Total Investment Securities	
Basic materials	\$2,640,000	20.0	%
Technology	3,039,000	23.0	%
REIT's and real estate ompanies	1,494,000	11.3	%
Corporate Bonds	1,774,000	13.4	%
Energy	472,000	3.6	%
Financial	1,046,000	7.9	%
Other	2,744,000	20.8	%
	\$13,209,000	100.0	%

As of June 30, 2017 Industry Group	Fair Value	% of Total Investment Securities	
Basic materials	\$6,222,000	36.2	%
Technology	4,134,000	24.1	%
REIT's and real estate ompanies	1,820,000	10.6	%
Corporate Bonds	1,683,000	9.8	%
Energy	1,345,000	7.8	%
Other	1,973,000	11.5	%
	\$17,177,000	100.0	%

As of December 31, 2017, 16% of the Company's investment in marketable securities portfolio consists of the common stock of Comstock Mining, Inc. ("Comstock" - NYSE MKT: LODE) which is included in the basic materials industry group.

The following table shows the net gain or loss on the Company's marketable securities and the associated margin interest and trading expenses for the respective periods:

For the three months ended December 31,	2017	2016
Net loss on marketable securities	\$(1,178,000)	\$(3,290,000)
Impairment loss on other investments	(200,000 )	(24,000 )
Dividend and interest income	48,000	68,000
Margin interest expense	(162,000 )	(159,000 )
Trading and management expenses	(151,000 )	(132,000 )
	\$(1,643,000)	\$(3,537,000)



For the six months ended December 31,	2017	2016
Net loss on marketable securities	\$(2,200,000)	\$(2,136,000)
Impairment loss on other investments	(200,000 )	(44,000 )
Dividend and interest income	131,000	110,000
Margin interest expense	(352,000 )	(303,000 )
Trading and management expenses	(274,000 )	(250,000 )
	\$(2,895,000)	\$(2,623,000)

## FINANCIAL CONDITION AND LIQUIDITY

The Company's cash flows are primarily generated from its Hotel operations, and general partner management fees and limited partnership distributions from Justice Investors, its real estate operations and from the investment of its cash in marketable securities and other investments.

On December 18, 2013, the Partnership completed an Offer to Redeem any and all limited partnership interests not held by Portsmouth. As a result, Portsmouth, which prior to the Offer to Redeem owned 50% of the then outstanding limited partnership interests now controls approximately 93% of the voting interest in Justice and is now its sole General Partner.

To fund the redemption of limited partnership interests and to repay the prior mortgage of \$42,940,000, Justice obtained a \$97,000,000 mortgage loan and a \$20,000,000 mezzanine loan. The mortgage loan is secured by the Partnership's principal asset, the Hotel. The mortgage loan bears an interest rate of 5.275% per annum and matures in January 2024. Beginning in February 2017, the loan began to amortize over a thirty-year period thru its maturity date. As additional security for the mortgage loan, there is a limited guaranty executed by the Company in favor of mortgage lender. The mezzanine loan is secured by the Operating membership interest held by Mezzanine and is subordinated to the Mortgage Loan. The mezzanine loan initially bears interest at 9.75% per annum and matures in January 2024. As additional security for the mezzanine loan, there is a limited guaranty executed by the Company in favor of mezzanine lender. The outstanding balance of the senior loan and the mezzanine loans as of September 30, 2017 were \$96,028,399 and \$20,000,000 respectively. Effective May 12, 2017, InterGroup agreed to become an additional guarantor under the limited guaranty and an additional indemnitor under the environmental indemnity for Justice Investors limited partnership's \$97,000,000 mortgage loan and the \$20,000,000 mezzanine loan.

On July 2, 2014, the Partnership obtained from InterGroup (a related party) an unsecured loan in the principal amount of \$4,250,000 at 12% per year fixed interest, with a term of 2 years, payable interest only each month. InterGroup received a 3% loan fee. The loan may be prepaid at any time without penalty. The loan was extended to December 31, 2018.

In April 2017, Portsmouth obtained from InterGroup an unsecured short-term loan in the amount of \$1,000,000 at 5% per year fixed interest, with a term of five months and maturing September 6, 2017. The short-term loan was extended to September 15, 2017 and paid off on September 13, 2017.

Despite an uncertain economy, the Hotel has continued to generate strong revenue growth. While the debt service requirements related the loans and the legal settlement may create some additional risks for the Company and its ability to generate cash flows in the future, management believes that cash flows from the operations of the Hotel and the garage will continue to be sufficient to meet all of the Partnership's current and future obligations and financial requirements.

The Company has invested in short-term, income-producing instruments and in equity and debt securities when deemed appropriate. The Company's marketable securities are classified as trading with unrealized gains and losses recorded through the consolidated statements of operations.

Management believes that its cash, marketable securities, and the cash flows generated from those assets and from the partnership management fees, will be adequate to meet the Company's current and future obligations. Additionally, management believes there is significant appreciated value in the Hotel property to support additional borrowings, if necessary.

## OFF-BALANCE SHEET ARRANGEMENTS

The Company has no off balance sheet arrangements.

## MATERIAL CONTRACTUAL OBLIGATIONS

The following table provides a summary as of December 31, 2017, the Company's material financial obligations which also including interest payments.

	<b>Total</b>	6 Months 2018	Year 2019	Year 2020	Year 2021	Year 2022	<b>Thereafter</b>
Mortgage and subordinated notes payable	\$ 179,704,000	\$ 1,463,000	\$ 3,980,000	\$ 3,103,000	\$ 15,171,000	\$ 3,078,000	\$ 152,909,000
Other notes payable	5,919,000	184,000	474,000	607,000	567,000	567,000	3,520,000
Interest	54,872,000	5,139,000	9,919,000	9,529,000	9,120,000	8,591,000	12,574,000
<b>Total</b>	<b>\$ 240,495,000</b>	<b>\$ 6,786,000</b>	<b>\$ 14,373,000</b>	<b>\$ 13,239,000</b>	<b>\$ 24,858,000</b>	<b>\$ 12,236,000</b>	<b>\$ 169,003,000</b>

## IMPACT OF INFLATION

Hotel room rates are typically impacted by supply and demand factors, not inflation, since rental of a hotel room is usually for a limited number of nights. Room rates can be, and usually are, adjusted to account for inflationary cost increases. Since Prism has the power and ability under the terms of its management agreement to adjust hotel room rates on an ongoing basis, there should be minimal impact on partnership revenues due to inflation. Partnership revenues are also subject to interest rate risks, which may be influenced by inflation. For the two most recent fiscal years, the impact of inflation on the Company's income is not viewed by management as material.

The Company's residential rental properties provide income from short-term operating leases and no lease extends beyond one year. Rental increases are expected to offset anticipated increased property operating expenses.

## **CRITICAL ACCOUNTING POLICIES AND USE OF ESTIMATES**

Critical accounting policies are those that are most significant to the presentation of our financial position and results of operations and require judgments by management in order to make estimates about the effect of matters that are inherently uncertain. The preparation of these condensed financial statements requires us to make estimates and judgments that affect the reported amounts in our consolidated financial statements. We evaluate our estimates on an on-going basis, including those related to the consolidation of our subsidiaries, to our revenues, allowances for bad debts, accruals, asset impairments, other investments, income taxes and commitments and contingencies. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities. The actual results may differ from these estimates or our estimates may be affected by different assumptions or conditions. There have been no material changes to the Company's critical accounting policies during the six months ended December 31, 2017. Please refer to the Company's Annual Report on Form 10-K for the year ended June 30, 2017 for a summary of the critical accounting policies.

**Item 4. Controls and Procedures.**

**EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES**

The Company's management, with the participation of the Company's Chief Executive Officer and Principal Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the quarterly period covered by this Quarterly Report on Form 10-Q. Based upon such evaluation, the Chief Executive Officer and Principal Financial Officer have concluded that, as of the end of such period, the Company's disclosure controls and procedures are effective in ensuring that information required to be disclosed in this filing is accumulated and communicated to management and is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission rules and forms.

**CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING**

As stated in the Company's Form 10-K for the year ended June 30, 2017, we identified a material weakness in internal controls over financial reporting related to our deferred income taxes and income tax expense during the fourth quarter of fiscal 2017. During the quarter ended September 30, 2017, we hired new tax CPA specialist to perform detailed analysis which was completed for the year ended June 30, 2017. We also assigned our audit committee with oversight responsibilities. The Company has taken steps to remediate the material weakness and improved its internal control over financial reporting during the last quarterly period covered by this Form 10-Q.

**PART II.**

**OTHER INFORMATION**

**Item 5. Exhibits.**

31.1 Certification of Principal Executive Officer of Periodic Report Pursuant to Rule 13a-14(a) and Rule 15d-14(a).

31.2 Certification of Principal Financial Officer of Periodic Report Pursuant to Rule 13a-14(a) and Rule 15d-14(a).

32.1 Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350.

32.2 Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350.

- 24 -



**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

THE INTERGROUP CORPORATION  
(Registrant)

Date: February 2, 2018 by/s/ John V. Winfield  
John V. Winfield, President,  
Chairman of the Board and  
Chief Executive Officer

Date: February 2, 2018 by/s/ Danfeng Xu  
Danfeng Xu, Treasurer  
and Controller

- 25 -