Limoneira CO
Form 10-Q
September 09, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

FOR THE QUARTERLY PERIOD ENDED July 31, 2015

OR

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

FOR THE TRANSITION PERIOD FROM ______ TO ______

Commission File Number: 001-34755

Limoneira Company

(Exact name of Registrant as Specified in its Charter)

Delaware	**77-0260692**
(State or Other Jurisdiction of	**(I.R.S. Employer**
Incorporation or Organization)	**Identification No.)**

1141 Cummings Road, Santa Paula, CA	**93060**
(Address of Principal Executive Offices)	**(Zip Code)**

Registrant's telephone number, including area code: (805) 525-5541

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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. x Yes ¨ No

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

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

¨ Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company

(Do not check if a smaller reporting company)

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

As of August 31, 2015, there were 14,128,830 shares outstanding of the registrant’s common stock.

LIMONEIRA COMPANY

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Cautionary Note on Forward-Looking Statements.

This Quarterly Report on Form 10-Q contains both historical and forward-looking statements. Forward-looking statements in this 10-Q are subject to a number of risks and uncertainties, some of which are beyond the Company's control. The potential risks and uncertainties that could cause our actual financial condition, results of operations and future performance to differ materially from those expressed or implied include:

- *changes in laws, regulations, rules, quotas, tariff, and import laws;*
- *weather conditions, including freezes and droughts that affect the production, transportation, storage, import and export of fresh produce;*
- *market responses to industry volume pressures;*
- *increased pressure from crop disease, insects and other pests;*
- *disruption of water supplies or changes in water allocations;*
- *product and raw materials supplies and pricing;*
- *energy supply and pricing;*
- *changes in interest and current exchange rates;*
- *availability of financing for land development activities;*
- *general economic conditions for residential and commercial real estate development;*
- *political changes and economic crisis;*
- *international conflict;*

- *acts of terrorism;*
- *labor disruptions, strikes, shortages or work stoppages;*
- *loss of important intellectual property rights; and*
- *other factors disclosed in our public filings with the Securities and Exchange Commission.*

The Company's actual results, performance, prospects or opportunities could differ materially from those expressed in or implied by the forward-looking statements. Additional risks of which the Company is not currently aware or which the Company currently deems immaterial could also cause the Company's actual results to differ, including those discussed in the section entitled "Risk Factors" included elsewhere in this Quarterly Report on Form 10-Q and in our Annual Report on Form 10-K for the fiscal year ended October 31, 2014. Although we believe the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance, or achievements. You should not place undue reliance on these forward-looking statements, which apply only as of the date of this Quarterly Report on Form 10-Q. Except as required by law, we undertake no obligation to update these forward-looking statements, even if our situation changes in the future.

The terms the "Company," "Limoneira", "we," "our" and "us" as used throughout this Quarterly Report on Form 10-Q refer to Limoneira Company and its consolidated subsidiaries, unless otherwise indicated.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Limoneira Company

Consolidated Balance Sheets (unaudited)

	July 31, 2015	October 31, 2014
Assets		
Current assets:		
Cash	$32,000	$92,000
Accounts receivable, net	7,626,000	7,236,000
Cultural costs	2,859,000	3,691,000
Prepaid expenses and other current assets	3,986,000	3,849,000
Income taxes receivable	-	1,143,000
Total current assets	14,503,000	16,011,000
Property, plant and equipment, net	122,007,000	105,433,000
Real estate development	94,923,000	88,088,000
Equity in investments	3,344,000	3,638,000
Investment in Calavo Growers, Inc.	27,255,000	24,270,000
Note receivable	819,000	2,084,000
Other assets	8,125,000	8,114,000
Total assets	$270,976,000	$247,638,000
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	$5,457,000	$6,363,000
Growers payable	6,066,000	5,839,000
Accrued liabilities	7,219,000	7,539,000
Fair value of derivative instrument	764,000	809,000
Current portion of long-term debt	585,000	583,000
Total current liabilities	20,091,000	21,133,000
Long-term liabilities:		
Long-term debt, less current portion	84,215,000	67,771,000
Deferred income taxes	23,294,000	21,792,000
Other long-term liabilities	5,708,000	6,282,000

Total liabilities	133,308,000	116,978,000
Commitments and contingencies	-	-
Series B Convertible Preferred Stock – $100 par value (50,000 shares authorized: 30,000 shares issued and outstanding at July 31, 2015 and October 31, 2014) (8.75% coupon rate)	3,000,000	3,000,000
Series B-2 Convertible Preferred Stock – $100 par value (10,000 shares authorized: 9,300 shares issued and outstanding at July 31, 2015 and October 31, 2014) (4% dividend rate on liquidation value of $1,000 per share)	9,331,000	9,331,000
Stockholders' equity:		
Series A Junior Participating Preferred Stock	-	-
Common stock – $.01 par value (19,900,000 shares authorized: 14,128,830 and 14,078,077 shares issued and outstanding at July 31, 2015 and October 31, 2014, respectively)	141,000	140,000
Additional paid-in capital	90,394,000	89,770,000
Retained earnings	27,356,000	23,308,000
Accumulated other comprehensive income	7,446,000	5,111,000
Total stockholders' equity	125,337,000	118,329,000
Total liabilities and stockholders' equity	$270,976,000	$247,638,000

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

Limoneira Company

Consolidated Statements of Operations (unaudited)

	Three months ended		**Nine months ended**	
	July 31, 2015	**2014**	**July 31, 2015**	**2014**
Revenues:				
Agribusiness	$28,466,000	$35,173,000	$82,268,000	$83,481,000
Rental operations	1,311,000	1,182,000	3,769,000	3,483,000
Real estate development	34,000	121,000	62,000	196,000
Total revenues	29,811,000	36,476,000	86,099,000	87,160,000
Costs and expenses:				
Agribusiness	17,471,000	17,805,000	63,308,000	58,730,000
Rental operations	907,000	796,000	2,471,000	2,231,000
Real estate development	325,000	420,000	806,000	1,021,000
Impairment of real estate development assets	-	435,000	-	435,000
Selling, general and administrative	3,270,000	3,640,000	10,053,000	10,326,000
Total costs and expenses	21,973,000	23,096,000	76,638,000	72,743,000
Operating income	7,838,000	13,380,000	9,461,000	14,417,000
Other income (expense):				
Interest (expense) income, net	(45,000)	20,000	(102,000)	59,000
Equity in earnings of investments	205,000	101,000	193,000	132,000
Other income, net	91,000	39,000	353,000	254,000
Total other income	251,000	160,000	444,000	445,000
Income before income tax provision	8,089,000	13,540,000	9,905,000	14,862,000
Income tax provision	(2,776,000)	(4,608,000)	(3,477,000)	(5,036,000)
Net income	5,313,000	8,932,000	6,428,000	9,826,000
Preferred dividends	(159,000)	(171,000)	(477,000)	(302,000)
Net income applicable to common stock	$5,154,000	$8,761,000	$5,951,000	$9,524,000
Basic net income per common share	$0.36	$0.62	$0.42	$0.68
Diluted net income per common share	$0.36	$0.61	$0.42	$0.68
Dividends per common share	$0.05	$0.05	$0.14	$0.12
Weighted-average common shares outstanding-basic	14,127,000	14,064,000	14,115,000	14,048,000
Weighted-average common shares outstanding-diluted	14,953,000	14,486,000	14,115,000	14,227,000

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

Limoneira Company

Consolidated Statements of Comprehensive Income (unaudited)

	Three months ended		**Nine months ended**	
	July 31, 2015	**2014**	**July 31, 2015**	**2014**
Net income	$5,313,000	$8,932,000	$6,428,000	$9,826,000
Other comprehensive income, net of tax:				
Minimum pension liability adjustment	149,000	117,000	447,000	352,000
Unrealized holding gains on security available-for-sale	1,172,000	1,023,000	1,813,000	1,445,000
Unrealized gains from derivative instruments	87,000	119,000	75,000	370,000
Total other comprehensive income, net of tax	1,408,000	1,259,000	2,335,000	2,167,000
Comprehensive income	$6,721,000	$10,191,000	$8,763,000	$11,993,000

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

Limoneira Company

Consolidated Statements of Cash Flows (unaudited)

	Nine months ended July 31, 2015	2014
Operating activities		
Net income	$6,428,000	$9,826,000
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	2,979,000	2,564,000
Loss on disposals of assets	357,000	408,000
Impairment of real estate development assets	-	435,000
Stock compensation expense	799,000	892,000
Distributed earnings of investments	303,000	52,000
Accrued interest on notes receivable	(36,000)	(59,000)
Donation of common stock	100,000	100,000
Changes in operating assets and liabilities:		
Accounts receivable, net	(394,000)	(4,728,000)
Cultural costs	832,000	1,434,000
Prepaid expenses and other current assets	(137,000)	(57,000)
Income taxes receivable	1,143,000	-
Other assets	208,000	240,000
Accounts payable and growers payable	(2,073,000)	3,208,000
Accrued liabilities	(581,000)	3,339,000
Other long-term liabilities	258,000	121,000
Net cash provided by operating activities	10,186,000	17,775,000
Investing activities		
Capital expenditures	(23,735,000)	(14,185,000)
Business combination	-	(700,000)
Equity investment contributions	(9,000)	(8,000)
Investments in mutual water companies	(293,000)	(293,000)
Net cash used in investing activities	(24,037,000)	(15,186,000)
Financing activities		
Borrowings of long-term debt	93,334,000	40,938,000
Repayments of long-term debt	(76,888,000)	(50,967,000)
Dividends paid – common	(1,903,000)	(1,687,000)
Dividends paid – preferred	(477,000)	(271,000)
Exchange of common stock	(275,000)	(175,000)
Net proceeds from issuance of preferred stock	-	9,300,000

Payments of debt financing costs	-	(106,000)
Net cash provided by (used in) financing activities	13,791,000	(2,968,000)
Net decrease in cash	(60,000)	(29,000)
Cash at beginning of period	92,000	82,000
Cash at end of period	$32,000	$53,000

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Limoneira Company

Consolidated Statements of Cash Flows (unaudited) (continued)

	Nine months ended July 31,	
	2015	2014
Supplemental disclosures of cash flow information		
Cash paid during the period for interest	$1,939,000	$1,730,000
Cash (received) paid during the period for income taxes, net of payments (refunds)	$(640,000)	$2,095,000
Non-cash investing and financing activities:		
Unrealized holding gain on Calavo investment	$(2,985,000)	$(2,400,000)
Capital expenditures accrued but not paid at period-end	$1,654,000	$721,000
Non-cash reduction of note receivable	$1,301,000	$-
Accrued interest on note receivable	$36,000	$59,000
Donation of common stock	$100,000	$100,000
Accrued Series B-2 Convertible Preferred Stock dividends	$31,000	$31,000

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

Limoneira Company

Consolidated Financial Statements (unaudited)

Preface

The preparation of the unaudited interim consolidated financial statements requires management to make use of estimates and assumptions that affect the reported amount of assets and liabilities, revenue and expenses and certain financial statement disclosures. Actual results may differ from these estimates.

The unaudited interim consolidated financial statements for the three months and nine months ended July 31, 2015 and 2014 and balance sheet as of July 31, 2015 included herein have not been audited by an independent registered public accounting firm, but in management's opinion, all adjustments (consisting of normal recurring adjustments) necessary to make a fair statement of the financial position at July 31, 2015 and the results of operations and the cash flows for the periods presented herein have been made. The results of operations for the three and nine months ended July 31, 2015 are not necessarily indicative of the operating results expected for the full fiscal year.

The consolidated balance sheet at October 31, 2014 included herein has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by U.S. generally accepted accounting principles ("GAAP") for complete financial statements.

The unaudited interim consolidated financial statements included herein have been prepared pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (the "SEC"). Although we believe the disclosures made are adequate to make the information presented not misleading, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules or regulations. These unaudited interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Form 10-K for the fiscal year ended October 31, 2014.

Limoneira Company

Notes to Consolidated Financial Statements (unaudited)

1. Business

Limoneira Company, a Delaware corporation (the “Company”), engages primarily in growing citrus and avocados, picking and hauling citrus, and packing, marketing and selling lemons. The Company is also engaged in residential rentals and other rental operations and real estate development activities.

The Company markets and sells lemons directly to foodservice, wholesale and retail customers throughout the United States, Canada, Asia and other international markets. The Company is a member of Sunkist Growers, Inc. (“Sunkist”), an agricultural marketing cooperative, and sells its oranges, specialty citrus and other crops to Sunkist-licensed and other third-party packinghouses.

The Company sells all of its avocado production to Calavo Growers, Inc. (“Calavo”), a packing and marketing company listed on the NASDAQ Global Select Market under the symbol CVGW. Calavo’s customers include many of the largest retail and food service companies in the United States and Canada. The Company’s avocados are packed by Calavo, sold and distributed under Calavo brands to its customers.

The unaudited interim consolidated financial statements include the accounts of the Company and the accounts of all the subsidiaries and investments in which a controlling interest is held by the Company. The unaudited interim consolidated financial statements represent the consolidated balance sheets, consolidated statements of operations, consolidated statements of comprehensive income and consolidated statements of cash flows of the Company and its wholly-owned subsidiaries. The Company’s subsidiaries include: Limoneira International Division, LLC, Limoneira Mercantile, LLC, Windfall Investors, LLC, Templeton Santa Barbara, LLC, and Associated Citrus Packers, Inc. All significant intercompany balances and transactions have been eliminated in consolidation. The Company considers the criteria established under the Financial Accounting Standards Board – Accounting Standards Code (“FASB ASC”) 810, *Consolidations* and the effect of variable interest entities, in its consolidation process. These unaudited consolidated financial statements should be read in conjunction with the notes thereto included in this quarterly report.

2. Summary of Significant Accounting Policies

Reclassifications and Adjustments

Certain reclassifications have been made to the prior years' consolidated financial statements to conform to the July 31, 2015 presentation.

Immaterial Classification Error - An immaterial error in the classification of an equity method investee's distributions was corrected in the July 31, 2014 consolidated financial statements which resulted in the reclassification of an equity method investee's distributions from investing to operating cash flows in the amount of $184,000 in the consolidated statement of cash flows. The Company has evaluated the materiality of this error both qualitatively and quantitatively in accordance with Staff Accounting Bulletin No. 99, Materiality, and determined that this error was not material to our previously reported consolidated financial statements as of October 31, 2014 and prior.

Other Reclassifications - Equity in earnings of investments were reclassified as a component of other income (expense) from a separate line item following the income tax provision on the statement of operations.

Recent Accounting Pronouncements

Financial Accounting Standards Board – Accounting Standards Update ("FASB ASU") 2014-09, Revenue from Contracts with Customers (Topic 606).

In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers (Topic 606)." This ASU affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets unless those contracts are within the scope of other standards (e.g., insurance contracts or lease contracts). This ASU will supersede the revenue recognition requirements in Topic 605, Revenue Recognition, and most industry-specific guidance. This ASU also supersedes some cost guidance included in Subtopic 605-35, Revenue Recognition – Construction-Type and Production-Type Contracts. In addition, the existing requirements for the recognition of a gain or loss on the transfer of nonfinancial assets that are not in a contract with a customer (e.g., assets within the scope of Topic 360, Property, Plant, and Equipment, and tangible assets within the scope of Topic 350, Intangibles – Goodwill and Other) are amended to be consistent with the guidance on recognition and measurement (including the constraint on revenue) in this ASU.

Limoneira Company

Notes to Consolidated Financial Statements (unaudited) (continued)

2. Summary of Significant Accounting Policies (continued)

The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should apply the following steps:

· Identify the contract(s) with a customer.

· Identify the performance obligations in the contract.

· Determine the transaction price.

· Allocate the transaction price to the performance obligations in the contract.

· Recognize revenue when (or as) the entity satisfies a performance obligation.

The amendments in this ASU are effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early application is not permitted. The Company is evaluating the effect this ASU may have on its consolidated financial statements.

FASB Accounting Standards Update No. 2015-03, Interest—Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs

The amendments in this ASU require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this ASU.

The amendments are effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

FASB Accounting Standards Update No. 2015-11, Inventory (Topic 330): Simplifying the Measurement of Inventory

The amendments in this ASU do not apply to inventory that is measured using last-in, first-out (LIFO) or the retail inventory method. The amendments apply to all other inventory, which includes inventory that is measured using first-in, first-out (FIFO) or average cost.

An entity should measure in scope inventory at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. Subsequent measurement is unchanged for inventory measured using LIFO or the retail inventory method.

The amendments in this ASU more closely align the measurement of inventory in GAAP with the measurement of inventory in International Financial Reporting Standards.

For public business entities, the amendments are effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. For all other entities, the amendments are effective for fiscal years beginning after December 15, 2016, and interim periods within fiscal years beginning after December 15, 2017. The amendments should be applied prospectively with earlier application permitted as of the beginning of an interim or annual reporting period. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

Limoneira Company

Notes to Consolidated Financial Statements (unaudited) (continued)

3. Fair Value Measurements

Under the FASB ASC 820, *Fair Value Measurement and Disclosures*, a fair value measurement is determined based on the assumptions that a market participant would use in pricing an asset or liability. A three-tiered hierarchy draws distinctions between market participant assumptions based on (i) observable inputs such as quoted prices in active markets (Level 1), (ii) inputs other than quoted prices in active markets that are observable either directly or indirectly (Level 2) and (iii) unobservable inputs that require the Company to use present value and other valuation techniques in the determination of fair value (Level 3).

The following table sets forth the Company's financial assets and liabilities as of July 31, 2015 and October 31, 2014, which are measured on a recurring basis during the period, segregated by level within the fair value hierarchy:

July 31, 2015

	Level 1	Level 2	Level 3	Total
Assets at fair value:				
Available-for-sale securities	$27,255,000	$–	$ –	$27,255,000
Liabilities at fair value:				
Derivative	$–	$1,662,000	$ –	$1,662,000

October 31, 2014

	Level 1	Level 2	Level 3	Total
Assets at fair value:				
Available-for-sale securities	$24,270,000	$–	$ –	$24,270,000
Liabilities at fair value:				
Derivative	$–	$1,782,000	$ –	$1,782,000

Available-for-sale securities consist of marketable securities in Calavo common stock. The Company currently owns 500,000 shares, representing approximately 2.9% of Calavo's outstanding common stock. These securities are measured at fair value by quoted market prices. Calavo's stock price at July 31, 2015 and October 31, 2014 was $54.51 and $48.54 per share, respectively.

The derivative consists of an interest rate swap, the fair value of which is estimated using industry-standard valuation models. Such models project future cash flows and discount the future amounts to a present value using market-based observable inputs.

4. Accounts Receivable

The Company grants credit in the course of its operations to customers, cooperatives, companies and lessees of the Company's facilities. The Company performs periodic credit evaluations of its customers' financial condition and generally does not require collateral. The Company provides allowances on its receivables, as required, based on accounts receivable aging and certain other factors. As of July 31, 2015 and October 31, 2014 the allowances totaled $163,000 and $442,000, respectively.

5. Concentrations

Lemons procured from third-party growers were 25% and 23% of lemon supply in the three months ended July 31, 2015 and 2014, respectively and 35% and 20% of lemon supply in the nine months ended July 31, 2015 and 2014, respectively.

The Company sells all of its avocado production to Calavo.

Limoneira Company

Notes to Consolidated Financial Statements (unaudited) (continued)

6. Real Estate Development Assets

Real estate development assets consist of the following:

	July 31, 2015	October 31, 2014
East Areas 1 and 2	$58,532,000	$55,016,000
Templeton Santa Barbara, LLC	11,039,000	11,039,000
Windfall Investors, LLC	25,352,000	22,033,000
	$94,923,000	$88,088,000

East Areas 1 and 2

In fiscal year 2005, the Company began capitalizing the costs of two real estate development projects east of Santa Paula, California, for the development of 550 acres of land into residential units, commercial buildings and civic facilities. During the three months ended July 31, 2015 and 2014, the Company capitalized $1,434,000 and $827,000, respectively, of costs related to these projects. During the nine months ended July 31, 2015 and 2014, the Company capitalized $3,516,000 and $2,333,000, respectively, of costs related to these projects. Additionally, in relation to these projects, the Company incurred expenses of $4,000 in each of the three months ended July 31, 2015 and 2014 and $12,000 and $13,000 in the nine months ended July 31, 2015 and 2014, respectively.

On August 24, 2010, the Company entered into an amendment (the "Amendment") to a Real Estate Advisory Management Consultant Agreement (the "Consultant Agreement") with Parkstone Companies, Inc. (the "Consultant") dated April 1, 2004, that includes provisions for the Consultant to earn a success fee (the "Success Fee") upon the annexation by the City of Santa Paula, California of East Area I. Under the terms of the Amendment, the Company agrees to pay the Success Fee in an amount equal to 4% of the incremental Property Value under a formula defined in the Amendment. The Success Fee is due and payable 120 days following the earlier to occur of (a) the sale of all or any portion of East Area I, including any unrelated third party material investment in the property, (b) the determination of an appraised value of the East Area I or (c) the second anniversary of the property annexation (each a "Success Fee Event").

The Success Fee, if any, shall be paid in cash, shares of the Company's common stock, or any combination of the forgoing at the sole discretion of the Company. The Success Fee is based on the calculated value of the property, which can vary over time until the settlement date. Accordingly, the Success Fee will be "marked to market" periodically to recognize the potential variability in the property value. Changes in the value, if any, will be recorded to capitalized development costs and additional paid in capital ("APIC"). To the extent that it becomes probable that cash will be used in the settlement rather than stock, such amount of cash will be classified as a liability rather than APIC.

If the Success Fee is paid in shares of common stock, deemed to be an equity award, the amount of common stock paid will be determined using a price per share equal to the average of closing prices of the common stock on the NASDAQ Global Market for the 20 trading days ending on the last trading day prior to the earliest occurring Success Fee Event; provided, however, that the price per share shall be no less than $16.00 per share. Previously recognized capitalized development costs will be adjusted to reflect the calculated value of the property upon settlement. The related APIC amount will be adjusted to common stock to reflect the issuance of common stock. To the extent that it becomes probable that cash will be used in the settlement rather than stock, such amount of cash will be classified as a liability rather than APIC/common stock. As of July 31, 2015, the estimated amount of the Success Fee was zero.

In connection with facilitating the annexation of East Area 1 into the City of Santa Paula, during February 2013, the Company entered into a Capital Improvement Cost Sharing Agreement for Improvements to Santa Paula Creek Channel (the "Cost Sharing Agreement") with the Ventura County Watershed Protection District (the "District"). The Cost Sharing Agreement requires the Company to reimburse the District 28.5% of the costs of the improvements, up to a maximum of $5,000,000. Additionally, the Company is required to pay the cost of preparing a study to determine a feasible scope of work and budget for the improvements. No costs have been incurred to date in relation to this agreement.

Limoneira Company

Notes to Consolidated Financial Statements (unaudited) (continued)

6. Real Estate Development Assets (continued)

Templeton Santa Barbara, LLC

The three real estate development parcels within the Templeton Santa Barbara, LLC project are described as Centennial Square (“Centennial”), The Terraces at Pacific Crest (“Pacific Crest”), and Sevilla. The net carrying values of Centennial, Pacific Crest and Sevilla at July 31, 2015 and October 31, 2014 were $2,983,000, $3,370,000 and $4,686,000, respectively. These projects were idle during the nine months ended July 31, 2015 and, as such, no costs were capitalized.

During the three months ended July 31, 2015 and 2014, the Company capitalized zero and $24,000, respectively, of costs related to these real estate parcels. During the nine months ended July 31, 2015 and 2014, the Company capitalized zero and $197,000, respectively, of costs related to these real estate parcels. Additionally, in relation to these parcels, the Company incurred net expenses of $42,000 and $465,000 in the three months ended July 31, 2015 and 2014, respectively, and $128,000 and $527,000 in the nine months ended July 31, 2015 and 2014, respectively. The net expenses incurred in fiscal year 2014 include a July 31, 2014 impairment charge of $435,000 recognized on the Centennial property.

Windfall Investors, LLC

On November 15, 2009, the Company acquired Windfall Investors, LLC, which included $16,842,000 of real estate development assets. During the three months ended July 31, 2015 and 2014, the Company capitalized $2,597,000 and $673,000, respectively, of costs primarily related to vineyards and water wells for this real estate development project. During the nine months ended July 31, 2015 and 2014, the Company capitalized $3,319,000 and $1,323,000, respectively, of costs primarily related to vineyards and water wells for this real estate development project. Additionally, in relation to this project, the Company incurred net expenses of $245,000 and $265,000, in the three months ended July 31, 2015 and 2014, respectively, and $604,000 and $720,000 in the nine months ended July 31, 2015 and 2014, respectively.

7. Investment in Calavo Growers, Inc.

In June 2005, the Company entered into a stock purchase agreement with Calavo. Pursuant to this agreement, the Company purchased 1,000,000 shares, or approximately 6.9%, of Calavo's common stock for $10,000,000 and Calavo purchased 1,728,570 shares, or approximately 15.1%, of the Company's common stock for $23,450,000. Under the terms of the agreement, the Company received net cash consideration of $13,450,000. The Company has classified its marketable securities investment as available-for-sale.

In fiscal year 2009, the Company sold 335,000 shares of Calavo stock for a total of $6,079,000, recognizing a gain of $2,729,000. In fiscal year 2013, the Company sold 165,000 shares to Calavo pursuant to the 2005 Stock Purchase Agreement for a total of $4,788,000, recognizing a gain of $3,138,000. The Company continues to own 500,000 shares of Calavo common stock.

Changes in the fair value of the available-for-sale securities result in unrealized holding gains or losses for the remaining shares held by the Company. The Company recorded unrealized holding gains of $1,930,000 ($1,172,000 net of tax) and $1,700,000 ($1,023,000 net of tax), during the three months ended July 31, 2015 and 2014, respectively. The Company recorded unrealized holding gains of $2,985,000 ($1,813,000 net of tax) and $2,400,000 ($1,445,000 net of tax), during the nine months ended July 31, 2015 and 2014, respectively.

8. Note Receivable

During fiscal year 2004, the Company sold a parcel of land in Morro Bay, California and in connection with the sale; the Company recorded a note receivable of $1,300,000. Total principal and interest due was $819,000 and $2,084,000 at July 31, 2015 and October 31, 2014, respectively. Interest continues to accrue on the principal balance of the note and was $12,000 and $20,000 in the three months ended July 31, 2015 and 2014, respectively and $36,000 and $59,000 in the nine months ended July 31, 2015 and 2014, respectively.

In July 2015, the holder of the note completed the drilling of three water wells at the Company's Windfall Investors, LLC real estate development property. The fair value of the well drilling services was $1,301,000 and the Company recorded a non-cash reduction of the note receivable comprised of $820,000 in accrued interest and $481,000 of principal.

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Notes to Consolidated Financial Statements (unaudited) (continued)

9. Other Assets

Other assets consist of the following:

	July 31, 2015	October 31, 2014
Investments in mutual water companies	$4,024,000	$3,731,000
Acquired water and mineral rights	1,536,000	1,536,000
Deferred lease assets and other	1,085,000	1,282,000
Revolving funds and memberships	344,000	355,000
Acquired trade names and trademarks, net	456,000	530,000
Goodwill	680,000	680,000
	$8,125,000	$8,114,000

10. Accrued Liabilities

Accrued liabilities consist of the following:

	July 31, 2015	October 31, 2014
Compensation	$1,514,000	$3,280,000
Property taxes	182,000	500,000
Income taxes	2,969,000	-
Interest	251,000	235,000
Deferred rental income and deposits	808,000	598,000
Lease expense	675,000	1,458,000
Lemon supplier payables	-	624,000
Capital expenditures and other	820,000	844,000

$7,219,000	$7,539,000

11. Long-Term Debt

Long-term debt is comprised of the following:

	July 31, 2015	October 31, 2014
Rabobank revolving credit facility: the interest rate is variable based on the one-month London Interbank Offered Rate (LIBOR), which was 0.19% at July 31, 2015, plus 1.80%. Interest is payable monthly and the principal is due in full in June 2018.	$78,664,000	$61,623,000
Farm Credit West term loan: the interest rate is variable and was 2.75% at July 31, 2015. The loan is payable in quarterly installments through November 2022.	4,367,000	4,756,000
Farm Credit West non-revolving line of credit: the interest rate is variable and was 2.75% at July 31, 2015. Interest is payable monthly and the principal is due in full in May 2018.	492,000	492,000
Farm Credit West term loan: the interest rate is variable and was 2.75% at July 31, 2015. The loan is payable in monthly installments through October 2035.	1,277,000	1,475,000
CNH Capital loans: the interest rate was zero and the loans were paid off in May and July 2015.	-	8,000
Subtotal	84,800,000	68,354,000
Less current portion	585,000	583,000
Total long-term debt, less current portion	$84,215,000	$67,771,000

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Notes to Consolidated Financial Statements (unaudited) (continued)

11. Long-Term Debt (continued)

Interest is capitalized on non-bearing orchards, real estate development projects and significant construction in progress. The Company capitalized interest of $651,000 and $559,000 during the three months ended July 31, 2015 and 2014, respectively, and $1,874,000 and $1,757,000 during the nine months ended July 31, 2015 and 2014, respectively. Capitalized interest is included in property, plant and equipment and real estate development assets in the Company's consolidated balance sheets.

12. Derivative Instrument and Hedging Activities

The Company enters into interest rate swaps to minimize the risks and costs associated with its financing activities. Derivative financial instruments are as follows:

	Notional Amount		Fair Value Liability	
	July 31, 2015	October 31, 2014	July 31, 2015	October 31, 2014
Pay fixed-rate, receive floating-rate forward interest rate swap, beginning July 2013 until June 2018	$40,000,000	$40,000,000	$1,662,000	$1,782,000

In November 2011, the Company entered into a forward interest rate swap agreement with Rabobank International, Utrecht to fix the interest rate at 4.30% on $40,000,000 of its outstanding borrowings under the Rabobank line of credit beginning July 2013 until June 2018. This interest rate swap qualifies as a cash flow hedge and is accounted for as a hedge under the short-cut method. Therefore, the fair value liability is included in fair value of derivative instrument, other long-term liabilities and related accumulated other comprehensive income at July 31, 2015 and October 31, 2014.

13. Basic and Diluted Net Income per Share

Basic net income per common share is calculated using the weighted-average number of common shares outstanding during the period without consideration of the dilutive effect of conversion of preferred stock. Diluted net income per common share is calculated using the weighted-average number of common shares outstanding during the period plus the dilutive effect of conversion of preferred stock. The Series B and Series B-2 convertible preferred shares were included in the computation of diluted net income per common share for the three months ended July 31, 2015 because such shares were dilutive. The Series B and Series B-2 convertible preferred shares were excluded from the computation of diluted net income per common share for the nine months ended July 31, 2015 and 2014 because such shares were anti-dilutive.

14. Related-Party Transactions

The Company rents certain of its residential housing assets to employees on a month-to-month basis. The Company recorded $166,000 and $132,000 of rental revenue from employees in the three months ended July 31, 2015 and 2014, respectively. The Company recorded $459,000 and $405,000 of rental revenue from employees in the nine months ended July 31, 2015 and 2014, respectively. There were no rental payments due from employees at July 31, 2015 and October 31, 2014.

The Company has representation on the boards of directors of the mutual water companies in which the Company has investments. The Company recorded capital contributions and purchased water and water delivery services from such mutual water companies, in aggregate, of $364,000 and $202,000 in the three months ended July 31, 2015 and 2014, respectively. The Company recorded capital contributions and purchased water and water delivery services from such mutual water companies, in aggregate, of $1,067,000 and $947,000 in the nine months ended July 31, 2015 and 2014, respectively. Such amounts are included in agribusiness expense in the Company’s consolidated statements of operations. Payments due to the mutual water companies were, in aggregate, $141,000 and $74,000 at July 31, 2015 and October 31, 2014, respectively.

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Notes to Consolidated Financial Statements (unaudited) (continued)

14. Related-Party Transactions (continued)

The Company has representation on the board of directors of a non-profit cooperative association that provides pest control services for the agricultural industry. The Company purchased services and supplies of $382,000 and $438,000 from the association in the three months ended July 31, 2015 and 2014, respectively. The Company purchased services and supplies of $1,081,000 and $989,000 from the association in the nine months ended July 31, 2015 and 2014, respectively. Such amounts are included in agribusiness expense in the Company’s consolidated statements of operations. Payments due to the association were $7,000 and $177,000 at July 31, 2015 and October 31, 2014, respectively.

The Company recorded dividend income of $375,000 and $350,000 in the nine months ended July 31, 2015 and 2014, respectively, on its investment in Calavo, which is included in other income (expense), net in the Company’s consolidated statements of operations. The Company had $3,027,000 and $6,147,000 of avocado sales to Calavo for the three months ended July 31, 2015 and 2014, respectively. The Company had $7,142,000 and $7,320,000 of avocado sales to Calavo for the nine months ended July 31, 2015 and 2014, respectively. Such amounts are included in agribusiness revenues in the Company’s consolidated statements of operations. There was $189,000 and zero receivable by the Company from Calavo at July 31, 2015 and October 31, 2014, respectively. Additionally, the Company leases office space to Calavo and received rental income of $68,000 and $69,000 in the three months ended July 31, 2015 and 2014, respectively. The Company received rental income from Calavo of $204,000 and $207,000 in the nine months ended July 31, 2015 and 2014, respectively. Such amounts are included in rental operations revenues in the Company’s consolidated statements of operations.

Certain members of the Company’s board of directors market lemons through the Company pursuant to its customary marketing agreements. During the three months ended July 31, 2015 and 2014, the aggregate amount of lemons procured from entities owned or controlled by members of the board of directors was $774,000 and $915,000, respectively. During the nine months ended July 31, 2015 and 2014, the aggregate amount was $1,356,000 and $1,311,000, respectively. Such amounts are included in agribusiness expense in the Company’s consolidated statements of operations. Payments due to these board members were $284,000 and $592,000 at July 31, 2015 and October 31, 2014, respectively.

On July 1, 2013, the Company and Cadiz Real Estate, LLC ("Cadiz"), a wholly-owned subsidiary of Cadiz, Inc., entered into a long-term lease agreement (the "Lease") for a minimum of 320 acres, with an option to lease up to an additional 640 acres, located within 9,600 zoned agricultural acres owned by Cadiz in eastern San Bernardino County, California. The initial term of the Lease runs for 20 years and the annual base rental rate will be equal to the sum of $200 per planted acre and 20% of gross revenues from the sale of harvested lemons (less operating expenses) and will not exceed $1,200 per acre per year. The Company has incurred lease expense of $16,000 and $11,000 in the three months ended July 31, 2015 and 2014, respectively and $41,000 and $15,000 in the nine months ended July 31, 2015 and 2014, respectively. A member of the Company's board of directors serves as the CEO, President and a member of the board of directors of Cadiz, Inc. Additionally, this board member is an attorney with a law firm that provided services to the Company $122,000 and $71,000 in the nine months ended July 31, 2015 and 2014, respectively.

On February 3, 2015, the Company entered into a Modification of Lease Agreement (the "Amendment") with Cadiz. The Amendment, among other things, increased by 200 acres the amount of property leased by the Company under the lease agreement dated July 1, 2013. In connection with the Amendment, the Company paid a total of $1,212,000 to acquire existing lemon trees and irrigations systems from Cadiz and a Cadiz tenant.

The Company has representation on the board of directors of Colorado River Growers, Inc. ("CRG"), a non-profit cooperative association of fruit growers engaged in the agricultural harvesting and marketing business in Yuma County, Arizona. The Company paid no harvest and third-party grower expense to CRG in the three months ended July 31, 2014 and 2014 and $5,177,000 and $5,505,000 in the nine months ended July 31, 2015 and 2014, respectively. Such amounts are included in agribusiness expense in the Company's consolidated statements of operations. Additionally, the Company's subsidiary, Associated Citrus Packers, Inc. ("Associated") provided no harvest management and administrative services to CRG in the three months ended July 31, 2015 and 2014 and $305,000 and $295,000 in the nine months ended July 31, 2015 and 2014, respectively. Such amounts are included in agribusiness revenues in the Company's consolidated statements of operations. There was $33,000 and $40,000 receivable by Associated from CRG at July 31, 2015 and October 31, 2014, respectively.

Limoneira Company

Notes to Consolidated Financial Statements (unaudited) (continued)

14. Related-Party Transactions (continued)

The Company has representation on the board of directors of Yuma Mesa Irrigation and Drainage District ("YMIDD"). In December 2013, Associated entered into an agreement, as amended in December 2014, with the YMIDD to participate in a Pilot Fallowing Program in which Associated agreed to forego its water allocation for approximately 300 acres of land in exchange for $750 per acre through December 31, 2016, unless terminated sooner by YMIDD. In relation to this program, during the three months ended July 31, 2015 and 2014 the Company recorded income of $50,000 and $43,000, respectively. In relation to this program, during the nine months ended July 31, 2015 and 2014 the Company recorded income of $151,000 and $111,000, respectively, and recorded losses on orchard disposals of $160,000 and $183,000, respectively. These net amounts are included in other income in the Company's consolidated statements of operations. Additionally, the Company purchased no water from YMIDD in the three months ended July 31, 2015 and 2014 and $68,000 and $62,000 in the nine months ended July 31, 2015 and 2014, respectively. Such amounts are included in agribusiness expenses in the Company's consolidated statements of operations. There were no amounts receivable from or payments due to YMIDD at July 31, 2015 and October 31, 2014.

The Company has a 1.3% interest in Limco Del Mar, Ltd. ("Del Mar") as a general partner and a 22.1% interest as a limited partner. The Company provides Del Mar with farm management, orchard land development and accounting services, and recognized agribusiness revenue relating to such services of $44,000 and $40,000 in the three months ended July 31, 2015 and 2014, respectively, and $119,000 in the nine months ended July 31, 2015 and 2014. The Company also performed contract lemon packing services for Del Mar and recognized agribusiness revenues relating to such services of $367,000 and $396,000 in the three months ended July 31, 2015 and 2014, respectively and $470,000 and $517,000 in the nine months ended July 31, 2015 and 2014, respectively. Fruit proceeds due to Del Mar were $882,000 and $828,000 at July 31, 2015 and October 31, 2014, respectively, and are included in grower's payable in the Company's consolidated balance sheets. In the three months ended July 31, 2015 and 2014, the Company received no cash distributions and recorded equity in earnings of this investment of $225,000 and $101,000, respectively. In the nine months ended July 31, 2015 and 2014, the Company received cash distributions of $495,000 and $184,000, respectively and recorded equity in earnings of this investment of $412,000 and $132,000, respectively.

On August 14, 2014, the Company's wholly owned subsidiary, Limoneira Chile SpA, invested approximately $1,750,000 for a 35% interest in Rosales S.A. ("Rosales"), a citrus packing, marketing and sales business located in La Serena, Chile. The Company recognized lemon sales of zero and $119,000 to Rosales in the three and nine months ended July 31, 2015, respectively and such amounts are recorded in agribusiness revenues in the Company's consolidated statements of operations. During the three months ended July 31, 2015 and 2014, the aggregate amount of lemons procured from Rosales was $415,000 and $555,000, respectively. During the nine months ended July 31, 2015 and 2014, the aggregate amount procured was $567,000 and $555,000, respectively. Amounts due to Rosales were $259,000 and zero at July 31, 2015 and October 31, 2014. Additionally, the Company recorded equity losses of this investment of $19,000 and $220,000, which includes amortization of fair value basis differences of $52,000 and $156,000 in the three and nine months ended July 31, 2015, respectively. In August 2015 the Company received a cash distribution of $53,000.

15. Income Taxes

There has been no material change to the Company's uncertain tax position for the three and nine month periods ended July 31, 2015. The Company does not expect its unrecognized tax benefits to change significantly over the next 12 months.

The Company's policy is to recognize interest expense and penalties related to income tax matters as a component of income tax expense. The Company has not accrued any interest and penalties associated with uncertain tax positions as of July 31, 2015.

Limoneira Company

Notes to Consolidated Financial Statements (unaudited) (continued)

16. Retirement Plans

The Limoneira Company Retirement Plan (the "Plan") is a noncontributory, defined benefit, single employer pension plan, which provides retirement benefits for all eligible employees of the Company. Benefits paid by the Plan are calculated based on years of service, highest five-year average earnings, primary Social Security benefit and retirement age. Effective June 2004, the Company froze the Plan and no additional benefits accrued to participants subsequent to that date. The Plan is administered by City National Bank and Mercer Human Resource Consulting.

The Plan is funded consistent with the funding requirements of federal law and regulations. There were funding contributions of $125,000 during the three months ended July 31, 2015 and 2014, and $375,000 during the nine months ended July 31, 2015 and 2014.

The net periodic pension costs for the Plan for the three months ended July 31 were as follows:

	2015	2014
Administrative expenses	$34,000	$34,000
Interest cost	213,000	205,000
Expected return on plan assets	(282,000)	(268,000)
Recognized actuarial loss	246,000	195,000
Net periodic benefit cost	$211,000	$166,000

The net periodic pension costs for the Plan for the nine months ended July 31 were as follows:

	2015	2014
Administrative expenses	$102,000	$102,000
Interest cost	639,000	615,000
Expected return on plan assets	(846,000)	(804,000)
Recognized actuarial loss	738,000	585,000

Net periodic pension cost	$633,000	$498,000

17. Other Long-Term Liabilities

Other long-term liabilities consist of the following:

	July 31, 2015	October 31, 2014
Minimum pension liability	$4,474,000	$4,954,000
Fair value of derivative instrument	898,000	973,000
Contingent consideration	300,000	300,000
Other	36,000	55,000
	$5,708,000	$6,282,000

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Notes to Consolidated Financial Statements (unaudited) (continued)

18. Stock-based Compensation

As of July 31, 2015, there are 7,810 shares of common stock issued to employees in connection with a discontinued stock option plan. Such shares are subject to repurchase by the Company and constitute a liability due to the repurchase right. The repurchase obligation of $6,000 is included in other long-term liabilities in the Company's consolidated balance sheets at July 31, 2015 and October 31, 2014.

The Company has a stock-based compensation plan (the "Stock Plan") that allows for the grant of common stock of the Company to members of management based on achievement of certain annual financial performance and other criteria. The number of shares granted is based on a percentage of the employee's base salary divided by the stock price on the grant date. Shares granted under the Stock Plan generally vest over a two year period.

During December 2014, 42,085 shares of common stock were granted to management under the Stock Plan for fiscal year 2014 performance, resulting in total compensation expense of approximately $1,071,000, with $367,000 recognized in the year ended October 31, 2014 and the balance to be recognized over the next two years as the shares vest. During December 2013, 27,091 shares of common stock were granted to management under the Stock Plan for fiscal 2013 performance, resulting in a total compensation expense of approximately $727,000, with $253,000 recognized in the year ended October 31, 2013 and the balance to be recognized over the next two years as the shares vest. During December 2012, 34,721 shares of common stock were granted to management under the Stock Plan for fiscal year 2012 performance, resulting in total compensation expense of approximately $657,000, with $216,000 recognized in the year ended October 31, 2012 and the balance to be recognized over the next two years as the shares vest.

Stock-based compensation expense is included in selling, general and administrative expense and is recognized over the performance and vesting periods as summarized below:

Performance