CRACKER BARREL OLD COUNTRY STORE, INC
Form 10-Q
February 21, 2012

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 January 27, 2012

OR

o 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: 001-25225

Cracker Barrel Old Country Store, Inc.
(Exact name of registrant as specified in its charter)

Tennessee (State or other jurisdiction of incorporation or organization)	62-0812904 (I.R.S. Employer Identification Number)
305 Hartmann Drive, P.O. Box 787 Lebanon, Tennessee (Address of principal executive offices)	37088-0787 (Zip code)

Registrant's telephone number, including area code: (615) 444-5533

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 þ No ¨

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

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

Large accelerated filer x Accelerated filer ¨

Non-accelerated filer ¨ Smaller reporting company ¨

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

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date.

22,993,634 Shares of Common Stock
Outstanding as of February 15, 2012

CRACKER BARREL OLD COUNTRY STORE, INC.

FORM 10-Q

For the Quarter Ended January 27, 2012

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PART I – FINANCIAL INFORMATION

ITEM 1. Financial Statements

CRACKER BARREL OLD COUNTRY STORE, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share data)
(Unaudited)

	January 27, 2012	July 29, 2011*
ASSETS		
Current Assets:		
Cash and cash equivalents	$119,385	$52,274
Property held for sale	884	950
Accounts receivable	16,991	12,279
Income taxes receivable	--	7,898
Inventories	127,176	141,547
Prepaid expenses and other current assets	14,707	9,000
Deferred income taxes	21,494	21,967
Total current assets	300,637	245,915
Property and equipment	1,707,752	1,673,873
Less: Accumulated depreciation and amortization of capital leases	692,518	664,709
Property and equipment – net	1,015,234	1,009,164
Other assets	54,458	55,805
Total assets	$1,370,329	$1,310,884
LIABILITIES AND SHAREHOLDERS’ EQUITY		
Current Liabilities:		
Accounts payable	$93,592	$99,679
Current maturities of long-term debt and other long-term obligations	9,490	123
Income taxes payable	5,173	--
Accrued interest expense	10,059	7,857
Deferred revenue	54,895	32,630
Other current liabilities	122,475	126,814
Total current liabilities	295,684	267,103
Long-term debt	540,715	550,143
Interest rate swap liability	45,050	51,604
Other long-term obligations	101,401	105,661
Deferred income taxes	67,084	68,339
Commitments and Contingencies (Note 13)		
Shareholders’ Equity:		
Preferred stock – 100,000,000 shares of $.01 par value authorized; no shares issued	--	--
Common stock – 400,000,000 shares of $.01 par value authorized; 22,992,183 shares issued and outstanding at January 27, 2012, and 22,840,974 shares issued and outstanding at July 29, 2011	230	228
Additional paid-in capital	15,317	7,081
Accumulated other comprehensive loss	(31,670)	(38,032)

Retained earnings	336,518	298,757
Total shareholders' equity	320,395	268,034
Total liabilities and shareholders' equity	$1,370,329	$1,310,884

See Notes to unaudited Condensed Consolidated Financial Statements.

* This Condensed Consolidated Balance Sheet has been derived from the audited Consolidated Balance Sheet as of July 29, 2011, as filed in the Company's Annual Report on Form 10-K for the fiscal year ended July 29, 2011.

CRACKER BARREL OLD COUNTRY STORE, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(In thousands, except share data)
(Unaudited)

	Quarter Ended		Six Months Ended	
	January 27, 2012	January 28, 2011	January 27, 2012	January 28, 2011
Total revenue	$ 673,234	$ 640,277	$1,271,671	$1,238,968
Cost of goods sold	235,391	219,390	421,698	399,143
Gross profit	437,843	420,887	849,973	839,825
Labor and other related expenses	234,933	7,512		
Other	242	319	851	758
NET INCOME	12,097	17,861	36,821	35,617
Net income attributable to noncontrolling interest in joint ventures	(129)	(132)	(390)	(398)
NET INCOME ATTRIBUTABLE TO EASTGROUP PROPERTIES, INC. COMMON STOCKHOLDERS	11,968	17,729	36,431	35,219
Other comprehensive income (loss) - cash flow hedges	(5,140)	1,063	(4,553)	(1,714)
TOTAL COMPREHENSIVE INCOME	$6,828	18,792	31,878	33,505
BASIC PER COMMON SHARE DATA FOR NET INCOME ATTRIBUTABLE TO EASTGROUP PROPERTIES, INC. COMMON STOCKHOLDERS				
Net income attributable to common stockholders	$0.37	0.56	1.14	1.13
Weighted average shares outstanding	32,126	31,515	32,068	31,156
DILUTED PER COMMON SHARE DATA FOR NET INCOME ATTRIBUTABLE TO EASTGROUP PROPERTIES, INC. COMMON STOCKHOLDERS				
Net income attributable to common stockholders	$0.37	0.56	1.13	1.13
Weighted average shares outstanding	32,248	31,644	32,160	31,256

See accompanying Notes to Consolidated Financial Statements (unaudited).

EASTGROUP PROPERTIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
(IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)
(UNAUDITED)

	Common Stock	Additional Paid-In Capital	Distributions in Excess of Earnings	Accumulated Other Comprehensive Loss	Noncontrolling Interest in Joint Ventures	Total
BALANCE, DECEMBER 31, 2014	$3	874,335	(300,852)	(2,357)	4,486	575,615
Net income	—	—	36,431	—	390	36,821
Net unrealized change in fair value of interest rate swaps	—	—	—	(4,553)	—	(4,553)
Common dividends declared – $1.74 per share	—	—	(56,455)	—	—	(56,455)
Stock-based compensation, net of forfeitures	—	6,565	—	—	—	6,565
Issuance of 106,751 shares of common stock, common stock offering, net of expenses	—	6,233	—	—	—	6,233
Issuance of 3,391 shares of common stock, dividend reinvestment plan	—	193	—	—	—	193
Withheld 32,409 shares of common stock to satisfy tax withholding obligations in connection with the vesting of restricted stock	—	(2,041)	—	—	—	(2,041)
Distributions to noncontrolling interest	—	—	—	—	(513)	(513)
BALANCE, SEPTEMBER 30, 2015	$3	885,285	(320,876)	(6,910)	4,363	561,865

See accompanying Notes to Consolidated Financial Statements (unaudited).

EASTGROUP PROPERTIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)
(UNAUDITED)

	Nine Months Ended September 30,	
	2015	2014
OPERATING ACTIVITIES		
Net income	$36,821	35,617
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	54,358	52,101
Stock-based compensation expense	5,185	4,005
Gain on sales of land and real estate investments	(3,026)	(7,610)
Changes in operating assets and liabilities:		
Accrued income and other assets	3,559	2,373
Accounts payable, accrued expenses and prepaid rent	6,765	8,658
Other	(87)	(53)
NET CASH PROVIDED BY OPERATING ACTIVITIES	103,575	95,091
INVESTING ACTIVITIES		
Real estate development	(75,768)	(80,748)
Purchases of real estate	—	(41,751)
Real estate improvements	(17,753)	(12,931)
Proceeds from sales of land and real estate investments	5,156	17,269
Repayments on mortgage loans receivable	87	118
Changes in accrued development costs	159	7,483
Changes in other assets and other liabilities	(6,333)	(15,705)
NET CASH USED IN INVESTING ACTIVITIES	(94,452)	(126,265)
FINANCING ACTIVITIES		
Proceeds from unsecured bank credit facilities	273,253	251,033
Repayments on unsecured bank credit facilities	(229,508)	(255,465)
Repayments on secured debt	(73,031)	(43,268)
Proceeds from unsecured debt	75,000	75,000
Debt issuance costs	(1,767)	(434)
	(56,549)	(52,231)

Distributions paid to stockholders (not including dividends accrued on unvested restricted stock)		
Proceeds from common stock offerings	6,233	59,110
Proceeds from dividend reinvestment plan	189	154
Other	(2,612)	(2,410)
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	(8,792)	31,489
INCREASE IN CASH AND CASH EQUIVALENTS	331	315
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	11	8
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$342	323
SUPPLEMENTAL CASH FLOW INFORMATION		
Cash paid for interest, net of amount capitalized of $3,903 and $3,682 for 2015 and 2014, respectively	$25,958	26,788

See accompanying Notes to Consolidated Financial Statements (unaudited).

EASTGROUP PROPERTIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(1) BASIS OF PRESENTATION

The accompanying unaudited financial statements of EastGroup Properties, Inc. ("EastGroup" or "the Company") have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In management's opinion, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The financial statements should be read in conjunction with the financial statements contained in the 2014 annual report on Form 10-K and the notes thereto. Certain reclassifications have been made in the 2014 consolidated financial statements to conform to the 2015 presentation.

(2) PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of EastGroup Properties, Inc., its wholly owned subsidiaries and its investment in any joint ventures in which the Company has a controlling interest. At September 30, 2015 and December 31, 2014, the Company had a controlling interest in two joint ventures: the 80% owned University Business Center and the 80% owned Castilian Research Center. The Company records 100% of the joint ventures' assets, liabilities, revenues and expenses with noncontrolling interests provided for in accordance with the joint venture agreements. The equity method of accounting is used for the Company's 50% undivided tenant-in-common interest in Industry Distribution Center II. All significant intercompany transactions and accounts have been eliminated in consolidation.

(3) USE OF ESTIMATES

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and revenues and expenses during the reporting period and to disclose material contingent assets and liabilities at the date of the financial statements. Actual results could differ from those estimates.

(4) REAL ESTATE PROPERTIES

EastGroup has one reportable segment – industrial properties. These properties are concentrated in major Sunbelt markets of the United States, primarily in the states of Florida, Texas, Arizona, California and North Carolina, have similar economic characteristics and also meet the other criteria permitting the properties to be aggregated into one reportable segment.

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows (including estimated future expenditures necessary to substantially complete the asset) expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized for the amount by which the carrying amount of the asset exceeds the fair value of the asset. As of September 30, 2015 and December 31, 2014, the Company determined that no impairment charges on the Company's real estate properties were necessary.

Depreciation of buildings and other improvements is computed using the straight-line method over estimated useful lives of generally 40 years for buildings and 3 to 15 years for improvements. Building improvements are capitalized, while maintenance and repair expenses are charged to expense as incurred. Significant renovations and improvements that improve or extend the useful life of the assets are capitalized. Depreciation expense was $14,945,000 and $44,503,000 for the three and nine months ended September 30, 2015, respectively, and $14,504,000 and $42,571,000 for the same periods in 2014.

EASTGROUP PROPERTIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

The Company's real estate properties and development at September 30, 2015 and December 31, 2014 were as follows:

	September 30, 2015	December 31, 2014
	(In thousands)	
Real estate properties:		
Land	$289,039	283,116
Buildings and building improvements	1,329,723	1,284,961
Tenant and other improvements	341,409	326,896
Development	204,981	179,973
	2,165,152	2,074,946
Less accumulated depreciation	(642,142)	(600,526)
	$1,523,010	1,474,420

(5) DEVELOPMENT

During the period in which a property is under development, costs associated with development (i.e., land, construction costs, interest expense, property taxes and other direct and indirect costs associated with development) are aggregated into the total capitalized costs of the property. Included in these costs are management's estimates for the portions of internal costs (primarily personnel costs) deemed directly or indirectly related to such development activities. The internal costs are allocated to specific development properties based on construction activity. As the property becomes occupied, depreciation commences on the occupied portion of the building, and costs are capitalized only for the portion of the building that remains vacant. When the property becomes 80% occupied or one year after completion of the shell construction (whichever comes first), capitalization of development costs, including interest expense, property taxes and internal personnel costs, ceases. The properties are then transferred to Real estate properties, and depreciation commences on the entire property (excluding the land).

(6) BUSINESS COMBINATIONS AND ACQUIRED INTANGIBLES

Upon acquisition of real estate properties, the Company applies the principles of Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 805, Business Combinations, which requires that acquisition-related costs be recognized as expenses in the periods in which the costs are incurred and the services are received. The Codification also provides guidance on how to properly determine the allocation of the purchase price among the individual components of both the tangible and intangible assets based on their respective fair values. Goodwill is recorded when the purchase price exceeds the fair value of the assets and liabilities acquired. Factors considered by management in allocating the cost of the properties acquired include an estimate of carrying costs during the expected lease-up periods considering current market conditions and costs to execute similar leases. The allocation to tangible assets (land, building and improvements) is based upon management's determination of the value of the property as if it were vacant using discounted cash flow models. The Company determines whether any financing assumed is above or below market based upon comparison to similar financing terms for similar properties. The cost of the properties acquired may be adjusted based on indebtedness assumed from the seller that is determined to be above or below market rates.

The purchase price is also allocated among the following categories of intangible assets: the above or below market component of in-place leases, the value of in-place leases, and the value of customer relationships. The value allocable to the above or below market component of an acquired in-place lease is determined based upon the present value (using a discount rate reflecting the risks associated with the acquired leases) of the difference between (i) the contractual amounts to be paid pursuant to the lease over its remaining term, and (ii) management's estimate of the amounts that would be paid using fair market rates over the remaining term of the lease. The amounts allocated to above and below market leases are included in Other Assets and Other Liabilities, respectively, on the Consolidated Balance Sheets and are amortized to rental income over the remaining terms of the respective leases. The total amount of intangible assets is further allocated to in-place lease values and customer relationship values based upon management's assessment of their respective values. These intangible assets are included in Other Assets on the Consolidated Balance Sheets and are amortized over the remaining term of the existing lease or the anticipated life of the customer relationship, as applicable.

Amortization expense for in-place lease intangibles was $944,000 and $3,129,000 for the three and nine months ended September 30, 2015, respectively, and $1,215,000 and $3,548,000 for the same periods in 2014. Amortization of above and below market leases increased rental income by $94,000 and $326,000 for the three and nine months ended September 30, 2015, respectively, and $119,000 and $295,000 for the same periods in 2014.

EastGroup did not acquire any operating properties during the nine months ended September 30, 2015. During 2014, the Company acquired Ridge Creek Distribution Center III in Charlotte, North Carolina; Colorado Crossing Distribution Center in Austin, Texas; and Ramona Distribution Center in Chino, California. The Company purchased these properties for a total cost of $51,652,000, of which $47,477,000 was allocated to Real estate properties. The Company allocated $10,822,000 of the total purchase price to land using third party land valuations for the Charlotte, Austin and Chino markets. The market values are considered to be Level 3 inputs as defined by ASC 820, Fair Value Measurements and Disclosures (see Note 18 for additional information on ASC 820). Intangibles associated with the purchase of real estate were allocated as follows: $5,074,000 to in-place lease intangibles, $4,000 to above market leases (both included in Other Assets on the Consolidated Balance Sheets), and $903,000 to below market leases (included in Other Liabilities on the Consolidated Balance Sheets). These costs are amortized over the remaining lives of the associated leases in place at the time of acquisition. The Company paid cash of $48,805,000 for the properties and intangibles acquired, assumed a mortgage of $2,617,000 and recorded a premium of $230,000 to adjust the mortgage loan assumed to fair value.

EastGroup did not have any acquisition-related costs for the three and nine months ended September 30, 2015. During the three months ended September 30, 2014, the Company did not recognize any acquisition-related costs; the Company expensed acquisition-related costs of $160,000 during the nine months ended September 30, 2014.

The Company periodically reviews the recoverability of goodwill (at least annually) and the recoverability of other intangibles (on a quarterly basis) for possible impairment. In management’s opinion, no impairment of goodwill or other intangibles existed at September 30, 2015 and December 31, 2014.

(7) REAL ESTATE HELD FOR SALE/DISCONTINUED OPERATIONS

The Company considers a real estate property to be held for sale when it meets the criteria established under ASC 360, Property, Plant and Equipment, including when it is probable that the property will be sold within a year. Real estate properties held for sale are reported at the lower of the carrying amount or fair value less estimated costs to sell and are not depreciated while they are held for sale.

In April 2014, the FASB issued Accounting Standards Update (ASU) 2014-08, Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360), Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity, which amended the requirements for reporting discontinued operations. Under ASU 2014-08, a disposal of a component of an entity or a group of components of an entity is required to be reported in discontinued operations if the disposal represents a strategic shift that has (or will have) a major effect on an entity's operations and financial results when the component or group of components meets the criteria to be classified as held for sale or when the component or group of components is disposed of by sale or other than by sale. In addition, this ASU requires additional disclosures about both discontinued operations and the disposal of an individually significant component of an entity that does not qualify for discontinued operations presentation in the financial statements. The Company adopted the provisions of ASU 2014-08 as of January 1, 2014, and has applied the provisions prospectively.

EastGroup sold a small parcel of land in New Orleans during the first quarter of 2015 for gross proceeds of $170,000 and recognized a gain of $123,000. During the second quarter of 2015, EastGroup sold one operating property, the last of its three Ambassador Row Warehouses in Dallas containing 185,000 square feet, for $5,250,000 and recognized a gain of $2,903,000.

During the year ended December 31, 2014, EastGroup sold five operating properties (442,000 square feet) for $21,381,000 and recognized gains of $9,188,000. In addition, the Company sold a small parcel of land in Orlando for $141,000 and recognized a gain of $98,000.

The results of operations and gains on sales for the properties sold or held for sale during the periods presented are reported in continuing operations on the Consolidated Statements of Income and Comprehensive Income. The gains on the sales of land are included in Other, and the gains on the sales of operating properties are included in Gain on sales of real estate investments.

EASTGROUP PROPERTIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(8) OTHER ASSETS

A summary of the Company's Other Assets follows:

	September 30, 2015	December 31, 2014
	(In thousands)	
Leasing costs (principally commissions)	$57,711	56,171
Accumulated amortization of leasing costs	(23,375)	(22,951)
Leasing costs (principally commissions), net of accumulated amortization	34,336	33,220
Straight-line rents receivable	25,795	25,013
Allowance for doubtful accounts on straight-line rents receivable	(292)	(102)
Straight-line rents receivable, net of allowance for doubtful accounts	25,503	24,911
Accounts receivable	3,771	4,459
Allowance for doubtful accounts on accounts receivable	(349)	(379)
Accounts receivable, net of allowance for doubtful accounts	3,422	4,080
Acquired in-place lease intangibles	17,920	20,118
Accumulated amortization of acquired in-place lease intangibles	(9,276)	(8,345)
Acquired in-place lease intangibles, net of accumulated amortization	8,644	11,773
Acquired above market lease intangibles	1,444	1,575
Accumulated amortization of acquired above market lease intangibles	(740)	(699)
Acquired above market lease intangibles, net of accumulated amortization	704	876
Loan costs	9,119	8,166
Accumulated amortization of loan costs	(4,655)	(4,454)
Loan costs, net of accumulated amortization	4,464	3,712
Mortgage loans receivable	4,904	4,991
Interest rate swap assets	—	812
Escrow deposits for 1031 exchange	—	698
Goodwill	990	990
Prepaid expenses and other assets	5,642	7,446
Total Other Assets	$88,609	93,509

(9) DEBT

Secured Debt decreased $73,061,000 during the nine months ended September 30, 2015. The decrease primarily resulted from the repayment of a mortgage loan with a balance of $57,450,000, regularly scheduled principal payments of $15,581,000 and mortgage loan premium amortization of $30,000.

Unsecured Debt increased $75,000,000 during the nine months ended September 30, 2015 as a result of the closing of a $75 million unsecured term loan in March 2015. The loan has a seven-year term and requires interest only payments. It bears interest at the annual rate of LIBOR plus an applicable margin (currently 1.4%) based on the Company's senior unsecured long-term debt rating. The Company also entered into an interest rate swap agreement to convert the loan's LIBOR rate component to a fixed interest rate for the entire term of the loan providing a total effective fixed interest rate of 3.031%. See note 13 for additional information on the Company's interest rate swaps.

Unsecured Bank Credit Facilities increased $43,745,000 during the nine months ended September 30, 2015. Until July 30, 2015, EastGroup had $225 million and $25 million unsecured bank credit facilities with margins over LIBOR of 117.5 basis points, facility fees of 22.5 basis points and maturity dates of January 5, 2017. The Company closed on amended credit facilities on July 30, 2015. The amended agreements expand the facilities to $300 million and $35 million, reduce the current applicable margins to 100 basis points and the current applicable facility fees to 20 basis points, and extend the maturity dates to July 30, 2019. The amended $300 million agreement contains an option for a one-year extension (at the Company's election) and a $150 million expansion (with agreement by both parties). The $35 million agreement contains a provision that the credit facility would automatically be extended for one year if the extension option in the $300 million facility is exercised.

Principal payments on long-term debt, including Secured Debt and Unsecured Debt (not including Unsecured Bank Credit Facilities), as of September 30, 2015 are as follows:

Years Ending December 31,	(In thousands)
Remainder of 2015	$29,313
2016	92,807
2017	58,239
2018	141,316
2019	130,569
2020 and beyond	383,471

(10) ACCOUNTS PAYABLE AND ACCRUED EXPENSES

A summary of the Company’s Accounts Payable and Accrued Expenses follows:

	September 30, 2015	December 31, 2014
	(In thousands)	
Property taxes payable	$24,425	15,216
Development costs payable	8,079	7,920
Interest payable	2,337	3,500
Dividends payable on unvested restricted stock	2,002	2,096
Other payables and accrued expenses	11,029	10,707
Total Accounts Payable and Accrued Expenses	$47,872	39,439

(11) OTHER LIABILITIES

A summary of the Company’s Other Liabilities follows:

	September 30, 2015	December 31, 2014
	(In thousands)	
Security deposits	$13,234	12,803
Prepaid rent and other deferred income	8,613	8,971
Acquired below-market lease intangibles	3,298	3,657
Accumulated amortization of below-market lease intangibles	(1,520)	(1,380)
Acquired below-market lease intangibles, net of accumulated amortization	1,778	2,277
Interest rate swap liabilities	7,029	3,314
Prepaid tenant improvement reimbursements	433	212
Other liabilities	223	16

Total Other Liabilities	$31,310	27,593

(12) COMPREHENSIVE INCOME

Total Comprehensive Income is comprised of net income plus all other changes in equity from non-owner sources and is presented on the Consolidated Statements of Income and Comprehensive Income. The components of Accumulated Other Comprehensive Income (Loss) are presented in the Company's Consolidated Statement of Changes in Equity and are summarized below. See Note 13 for information regarding the Company's interest rate swaps.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
	(In thousands)			
ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS):				
Balance at beginning of period	$(1,770)	(1,148)	(2,357)	1,629
Change in fair value of interest rate swaps	(5,140)	1,063	(4,553)	(1,714)
Balance at end of period	$(6,910)	(85)	(6,910)	(85)

(13) DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

The Company is exposed to certain risks arising from both its business operations and economic conditions. The Company principally manages its exposures to a wide variety of business and operational risks through management of its core business activities. The Company manages economic risk, including interest rate, liquidity and credit risk primarily by managing the amount, sources and duration of its debt funding and, to a limited extent, the use of derivative instruments.

Specifically, the Company has entered into derivative instruments to manage exposures that arise from business activities that result in the payment of future known and uncertain cash amounts, the value of which are determined by interest rates. The Company's derivative instruments, described below, are used to manage differences in the amount, timing and duration of the Company's known or expected cash payments principally related to certain of the Company's borrowings.

The Company's objective in using interest rate derivatives is to change variable interest rates to fixed interest rates by using interest rate swaps. Interest rate swaps designated as cash flow hedges involve the receipt of variable-rate amounts from a counterparty in exchange for the Company making fixed-rate payments over the life of the agreements without exchange of the underlying notional amount.

As of September 30, 2015, the Company had five interest rate swaps outstanding, all of which are used to hedge the variable cash flows associated with unsecured loans. The Company executed an $80,000,000 interest rate swap associated with an $80,000,000 unsecured loan during the third quarter of 2012. During the third quarter of 2013, the Company entered into two forward starting interest rate swaps totaling $75,000,000 which are hedging an unsecured loan which closed in December 2013. During the third quarter of 2014, the Company executed a $75,000,000 interest rate swap associated with a $75,000,000 unsecured loan. During the first quarter of 2015, EastGroup executed a $75,000,000 interest rate swap associated with a $75,000,000 unsecured loan. All of the aforementioned interest rate swaps convert the related loans' LIBOR rate components to fixed interest rates for the entire terms of the loans, and the Company has concluded that each of the hedging relationships is highly effective.

The effective portion of changes in the fair value of derivatives designated and qualifying as cash flow hedges is recorded in Other Comprehensive Income (Loss) and is subsequently reclassified into earnings in the period that the hedged forecasted transaction affects earnings. The ineffective portion of the change in fair value of the derivatives, which is immaterial for the periods reported, is recognized directly in earnings (included in Other on the Consolidated Statements of Income and Comprehensive Income).

Amounts reported in Other Comprehensive Income (Loss) related to derivatives will be reclassified to Interest Expense as interest payments are made on the Company's variable-rate debt. The Company estimates that an additional $3,828,000 will be reclassified from Other Comprehensive Income (Loss) as an increase to Interest Expense over the next twelve months.

The Company's valuation methodology for over-the-counter (“OTC”) derivatives is to discount cash flows based on Overnight Index Swap (“OIS”) rates. Uncollateralized or partially-collateralized trades are discounted at OIS, but include appropriate economic adjustments for funding costs (i.e., a LIBOR-OIS basis adjustment to approximate uncollateralized cost of funds) and credit risk. As of January 15, 2015, the Company began calculating its derivative valuations using mid-market prices; prior to that date, the Company used bid-market prices. The change in valuation methodology is considered a change in accounting estimate and is the result of recent developments in the marketplace. Management has assessed the impact of the change for all periods presented and has deemed the impact to be immaterial.

As of September 30, 2015 and December 31, 2014, the Company had the following outstanding interest rate derivatives that are designated as cash flow hedges of interest rate risk:

Interest Rate Derivative	Notional Amount as of September 30, 2015	Notional Amount as of December 31, 2014
	(In thousands)	
Interest Rate Swap	$80,000	$80,000
Interest Rate Swap	$75,000	$75,000
Interest Rate Swap	$75,000	—
Interest Rate Swap	$60,000	$60,000
Interest Rate Swap	$15,000	$15,000

The table below presents the fair value of the Company's derivative financial instruments as well as their classification on the Consolidated Balance Sheets as of September 30, 2015 and December 31, 2014. See Note 18 for additional information on the fair value of the Company's interest rate swaps.

	Derivatives As of September 30, 2015		Derivatives As of December 31, 2014	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
	(In thousands)			
Derivatives designated as cash flow hedges:				
Interest rate swap assets	Other Assets	$—	Other Assets	$812
Interest rate swap liabilities	Other Liabilities	7,029	Other Liabilities	3,314

The table below presents the effect of the Company's derivative financial instruments on the Consolidated Statements of Income and Comprehensive Income for the three and nine months ended September 30, 2015 and 2014:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
	(In thousands)			
DERIVATIVES IN CASH FLOW HEDGING RELATIONSHIPS				
Interest Rate Swaps:				
Amount of income (loss) recognized in Other Comprehensive Income (Loss) on derivatives	$(6,261)	287	(7,723)	(3,635)
Amount of loss reclassified from Accumulated Other Comprehensive Loss into Interest Expense	(1,121)	(776)	(3,170)	(1,921)

See Note 12 for additional information on the Company's Accumulated Other Comprehensive Loss resulting from its interest rate swaps.

Derivative financial agreements expose the Company to credit risk in the event of non-performance by the counterparties under the terms of the interest rate hedge agreements. The Company believes it minimizes the credit risk by transacting with financial institutions the Company regards as credit-worthy.

The Company has an agreement with its derivative counterparties containing a provision stating that the Company could be declared in default on its derivative obligations if the Company defaults on any of its indebtedness, including default where repayment of the indebtedness has not been accelerated by the lender.

As of September 30, 2015, the Company had no derivatives in an asset position; the fair value of derivatives in a liability position related to the Company's derivative agreements was $7,029,000. If the Company breached any of the contractual provisions of the derivative contracts, it could be required to settle its obligation under the agreements at the swap termination value. As of September 30, 2015, the swap termination value of derivatives in a liability position was a liability in the amount of $7,149,000.

EASTGROUP PROPERTIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(14) EARNINGS PER SHARE

The Company applies ASC 260, Earnings Per Share, which requires companies to present basic and diluted earnings per share (EPS). Basic EPS represents the amount of earnings for the period attributable to each share of common stock outstanding during the reporting period. The Company's basic EPS is calculated by dividing Net Income Attributable to EastGroup Properties, Inc. Common Stockholders by the weighted average number of common shares outstanding. The weighted average number of common shares outstanding does not include any potentially dilutive securities or any unvested restricted shares of common stock. These unvested restricted shares, although classified as issued and outstanding, are considered forfeitable until the restrictions lapse and will not be included in the basic EPS calculation until the shares are vested.

Diluted EPS represents the amount of earnings for the period attributable to each share of common stock outstanding during the reporting period and to each share that would have been outstanding assuming the issuance of common shares for all dilutive potential common shares outstanding during the reporting period. The Company calculates diluted EPS by dividing Net Income Attributable to EastGroup Properties, Inc. Common Stockholders by the weighted average number of common shares outstanding plus the dilutive effect of unvested restricted stock. The dilutive effect of unvested restricted stock is determined using the treasury stock method.

Reconciliation of the numerators and denominators in the basic and diluted EPS computations is as follows:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2015	2014	2015	2014
	(In thousands)			
BASIC EPS COMPUTATION FOR NET INCOME ATTRIBUTABLE TO EASTGROUP PROPERTIES, INC. COMMON STOCKHOLDERS				
Numerator – net income attributable to common stockholders	$11,968	17,729	36,431	35,219
Denominator – weighted average shares outstanding	32,126	31,515	32,068	31,156
DILUTED EPS COMPUTATION FOR NET INCOME ATTRIBUTABLE TO EASTGROUP PROPERTIES, INC. COMMON STOCKHOLDERS				
Numerator – net income attributable to common stockholders	$11,968	17,729	36,431	35,219
Denominator:				
Weighted average shares outstanding	32,126	31,515	32,068	31,156
Unvested restricted stock	122	129	92	100
Total Shares	32,248	31,644	32,160	31,256

(15) STOCK-BASED COMPENSATION

EastGroup applies the provisions of ASC 718, Compensation - Stock Compensation, to account for its stock-based compensation plans. ASC 718 requires that the compensation cost relating to share-based payment transactions be recognized in the financial statements and that the cost be measured on the fair value of the equity or liability instruments issued.

Stock-based compensation cost for employees was $1,855,000 and $6,035,000 for the three and nine months ended September 30, 2015, respectively, of which $410,000 and $1,231,000 were capitalized as part of the Company's development costs. For the three and nine months ended September 30, 2014, stock-based compensation cost for employees was $1,324,000 and $4,741,000, respectively, of which $267,000 and $1,099,000 were capitalized as part of the Company’s development costs.

Stock-based compensation expense for directors was $133,000 and $381,000 for the three and nine months ended September 30, 2015, respectively, and $124,000 and $363,000 for the same periods of 2014.

In the second quarter of 2015, the Company’s Board of Directors approved an equity compensation plan for its executive officers based upon certain annual performance measures (primarily funds from operations (FFO) per share and total shareholder return). Any shares issued pursuant to this compensation plan will be determined by the Compensation Committee in its discretion and issued in the first quarter of 2016. The number of shares to be issued on the grant date could range from zero to 49,366. These shares will vest 20% on the date shares are determined and awarded and generally will vest 20% per year on each January 1 for the subsequent four years.

EASTGROUP PROPERTIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Also in the second quarter of 2015, EastGroup's Board of Directors approved a long-term equity compensation plan for the Company's executive officers. The awards will be based on the results of the Company's total shareholder return, both on an absolute basis for 2015 as well as on a relative basis compared to the NAREIT Equity Index, NAREIT Industrial Index and Russell 2000 Index over the five-year period ending December 31, 2015. Any shares issued pursuant to this equity compensation plan will be determined by the Compensation Committee in its discretion and issued in the first quarter of 2016. The number of shares to be issued on the grant date could range from zero to 51,432. These shares will vest 25% on the date shares are determined and awarded and generally will vest 25% per year on each January 1 for the subsequent three years.

Notwithstanding the foregoing, shares issued to the Company's Chief Executive Officer, David H. Hoster II, will become fully vested on the date shares are determined and awarded and shares issued to the Company's Chief Financial Officer, N. Keith McKey, will become fully vested no later than April 6, 2016.

Following is a summary of the total restricted shares granted, forfeited and delivered (vested) to participants with the related weighted average grant date fair value share prices. Of the shares that vested in the first nine months of 2015, the Company withheld 32,409 shares to satisfy the tax obligations for those participants who elected this option as permitted under the applicable equity plan. As of the vesting dates, the aggregate fair value of shares that vested during the first nine months of 2015 was $6,664,000.

Award Activity:	Three Months Ended September 30, 2015		Nine Months Ended September 30, 2015	
	Shares	Weighted Average Grant Date Fair Value	Shares	Weighted Average Grant Date Fair Value
Unvested at beginning of period	261,010	$52.69	266,223	$49.81
Granted	—	—	100,622	61.07
Forfeited	—	—	—	—
Vested	—	—	(105,835)	53.40
Unvested at end of period	261,010	$52.69	261,010	$52.69

(16) RISKS AND UNCERTAINTIES

The state of the overall economy can significantly impact the Company's operational performance and thus impact its financial position. Should EastGroup experience a significant decline in operational performance, it may affect the Company's ability to make distributions to its shareholders, service debt, or meet other financial obligations.

(17) RECENT ACCOUNTING PRONOUNCEMENTS

EastGroup has evaluated all ASUs recently released by the FASB through the date the financial statements were issued and determined that ASU 2014-09 and ASU 2015-03 apply to the Company.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers, which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The effective date of ASU was extended by one year by ASU 2015-14, Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date. The new standard is effective for the Company on January 1, 2018. The standard permits the use of either the retrospective or cumulative effect transition method. The Company is evaluating the effect that ASU 2014-09 will have on its consolidated financial statements and related disclosures beginning with the Form 10-Q for the period ended March 31, 2018. The Company has not yet selected a transition method nor has it determined the effect of the standard on its ongoing financial reporting.

In April 2015, the FASB issued ASU 2015-03, Simplifying the Presentation of Debt Issuance Costs, which requires 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. For public business entities, the ASU is effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. Entities should apply the new guidance on a retrospective basis, wherein the balance sheet of each individual period presented should be adjusted to reflect the period-specific effects of applying the new guidance. Upon transition, entities are required to comply with the applicable disclosures for a change in an accounting principle. EastGroup plans to adopt ASU 2015-03 effective January 1, 2016; as such, the Company plans to present debt issuance costs as a direct deduction from the carrying amounts of its debt liabilities and to provide all necessary disclosures beginning with the Form 10-Q for the period ended March 31, 2016.

In August 2015, the FASB issued ASU 2015-15, Interest - Imputation of Interest: Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements, which adds comments from the Securities and Exchange

Commission (SEC) addressing ASU 2015-03, as discussed above, and debt issuance costs related to line-of-credit arrangements. The SEC commented it would not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the line-of-credit arrangement. EastGroup plans to adopt ASU 2015-15 in connection with its adoption of ASU 2015-03 effective January 1, 2016. The Company does not anticipate the adoption of ASU 2015-15 will have a material impact on the Company's financial condition or results of operations.

(18) FAIR VALUE OF FINANCIAL INSTRUMENTS

ASC 820, Fair Value Measurements and Disclosures, defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820 also provides guidance for using fair value to measure financial assets and liabilities. The Codification requires disclosure of the level within the fair value hierarchy in which the fair value measurements fall, including measurements using quoted prices in active markets for identical assets or liabilities (Level 1), quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in markets that are not active (Level 2), and significant valuation assumptions that are not readily observable in the market (Level 3).

The following table presents the carrying amounts and estimated fair values of the Company’s financial instruments in accordance with ASC 820 at September 30, 2015 and December 31, 2014.

	September 30, 2015		December 31, 2014	
	Carrying Amount [(1)]	Fair Value	Carrying Amount [(1)]	Fair Value
	(In thousands)			
Financial Assets:				
Cash and cash equivalents	$342	342	11	11
Cash held in escrow for 1031 exchange	—	—	698	698
Mortgage loans receivable	4,904	4,973	4,991	5,055
Interest rate swap assets	—	—	812	812
Financial Liabilities:				
Secured debt	380,715	402,425	453,776	478,659
Unsecured debt	455,000	430,709	380,000	364,295
Unsecured bank credit facilities	143,146	143,184	99,401	99,638
Interest rate swap liabilities	7,029	7,029	3,314	3,314

(1) Carrying amounts shown in the table are included in the Consolidated Balance Sheets under the indicated captions, except as explained in the notes below.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

Cash and cash equivalents: The carrying amounts approximate fair value due to the short maturity of those instruments.
Cash held in escrow for 1031 exchange (included in Other Assets on the Consolidated Balance Sheets): The carrying amounts approximate fair value due to the short maturity of those instruments.
Mortgage loans receivable (included in Other Assets on the Consolidated Balance Sheets): The fair value is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities (Level 2 input).

Interest rate swap assets (included in Other Assets on the Consolidated Balance Sheets): The instruments are recorded at fair value based on models using inputs, such as interest rate yield curves, LIBOR swap curves and OIS curves, observable for substantially the full term of the contract (Level 2 input). See Note 13 for additional information on the Company's interest rate swaps.

Secured debt: The fair value of the Company’s secured debt is estimated by discounting expected cash flows at the rates currently offered to the Company for debt of the same remaining maturities, as advised by the Company’s bankers (Level 2 input).

Unsecured debt: The fair value of the Company’s unsecured debt is estimated by discounting expected cash flows at the rates currently offered to the Company for debt of the same remaining maturities, as advised by the Company’s bankers (Level 2 input).

Unsecured bank credit facilities: The fair value of the Company’s unsecured bank credit facilities is estimated by discounting expected cash flows at current market rates (Level 2 input).

Interest rate swap liabilities (included in Other Liabilities on the Consolidated Balance Sheets): The instruments are recorded at fair value based on models using inputs, such as interest rate yield curves, LIBOR swap curves and OIS curves, observable for substantially the full term of the contract (Level 2 input). See Note 13 for additional information on the Company's interest rate swaps.

(19) SUBSEQUENT EVENTS

In October 2015, EastGroup issued $75 million of senior unsecured private placement notes with two insurance companies. The 10-year notes have a weighted average interest rate of 3.98% with semi-annual interest payments. The notes will not be and have not been registered under the Securities Act of 1933, as amended, and may not be offered or sold in the United States absent registration or an applicable exemption from the registration requirements.

EastGroup is currently under contract to purchase 335,000 square feet of business distribution buildings in Austin, Texas, in two separate transactions for a total purchase price of approximately $31.6 million. The transactions are expected to close during the fourth quarter of 2015.

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

OVERVIEW

EastGroup's goal is to maximize shareholder value by being the leading provider in its markets of functional, flexible and quality business distribution space for location sensitive customers (primarily in the 5,000 to 50,000 square foot range). The Company develops, acquires and operates distribution facilities, the majority of which are clustered around major transportation features in supply constrained submarkets in major Sunbelt regions. The Company's core markets are in the states of Florida, Texas, Arizona, California and North Carolina.

The Company believes its current operating cash flows and unsecured bank credit facilities provide the capacity to fund the operations of the Company. The Company also believes it can issue common and/or preferred equity and obtain financing from financial institutions and insurance companies, as evidenced by the issuance of $75 million of senior unsecured private placement notes in October 2015. The continuous common equity program provided net proceeds to the Company of $6,233,000 in the first nine months of 2015. EastGroup's financing and equity issuances are further described in Liquidity and Capital Resources.

The Company's primary revenue is rental income; as such, EastGroup's greatest challenge is leasing space. During the nine months ended September 30, 2015, leases expired on 5,254,000 square feet (15.5% of EastGroup's total square footage of 33,962,000), and the Company was successful in renewing or re-leasing 89% of the expiring square feet. In addition, EastGroup leased 1,183,000 square feet of other vacant space during this period. During the first nine months of 2015, average rental rates on new and renewal leases increased by11.5%. Property net operating income (PNOI) from same properties, defined as operating properties owned during the entire current period and prior year reporting period, increased 1.3% for the quarter ended September 30, 2015, as compared to the same quarter in 2014. For the nine months ended September 30, 2015, PNOI from same properties increased 2.5% as compared to the same period of 2014.

EastGroup's total leased percentage was 96.6% at September 30, 2015, compared to 96.8% at September 30, 2014. Leases scheduled to expire for the remainder of 2015 were 1.8% of the portfolio on a square foot basis at September 30, 2015, and this figure was reduced to 1.1% as of October 16, 2015.

The Company generates new sources of leasing revenue through its development and acquisition programs. EastGroup continues to see targeted development as a contributor to the Company's long-term growth. The Company mitigates risks associated with development through a Board-approved maximum level of land held for development and by adjusting development start dates according to leasing activity.   During the first nine months of 2015, the Company began construction of nine development projects containing 1,024,000 square feet in Orlando, Tampa, San Antonio, Houston, Phoenix and Charlotte. EastGroup also transferred eight properties (748,000 square feet) in Orlando, Phoenix, Charlotte and Houston from its development program to real estate properties with costs of $47.0 million at the date of transfer. As of September 30, 2015, EastGroup's development program consisted of 21 projects (2,077,000 square feet) located in Houston, Dallas, San Antonio, Phoenix, Tampa, Orlando, Denver and Charlotte. The projected total investment for the development projects, which were collectively 37% leased as of October 16, 2015, is $156.8 million, of which $41.7 million remained to be invested as of September 30, 2015.

Typically, the Company initially funds its development and acquisition programs through its $335 million unsecured bank credit facilities (as discussed in Liquidity and Capital Resources). As market conditions permit, EastGroup issues equity and/or employs fixed-rate debt, including variable-rate debt that has been swapped to an effectively fixed rate through the use of interest rate swaps, to replace short-term bank borrowings. In March 2015, Moody's Investor Services affirmed the Company's issuer rating of Baa2 with a stable outlook. Also in March 2015, Fitch Ratings affirmed EastGroup's issuer rating of BBB with a stable outlook. A security rating is not a recommendation to buy, sell or hold securities and may be subject to revision or withdrawal at any time by the assigning rating agency. Each rating should be evaluated independently of any other rating. The Company intends to obtain primarily unsecured fixed-rate debt, including variable-rate debt that has been swapped to an effectively fixed rate through the use of interest rate swaps, in the future. The Company may also access the public debt market in the future as a means to raise capital.

EastGroup has one reportable segment – industrial properties. These properties are primarily located in major Sunbelt regions of the United States, have similar economic characteristics and also meet the other criteria permitting the properties to be aggregated into one reportable segment. The Company's chief decision makers use two primary measures of operating results in making decisions: (1) property net operating income (PNOI), defined as Income from real estate operations less Expenses from real estate operations (including market-based internal management fee expense) plus the Company's share of income and property operating expenses from its less-than-wholly-owned real estate investments, and (2) funds from operations attributable to common stockholders (FFO), defined as net income (loss) attributable to common stockholders computed in accordance with U.S. generally accepted accounting principles (GAAP), excluding gains or losses from sales of depreciable real estate property and impairment losses, plus real estate related depreciation and amortization, and after adjustments for unconsolidated partnerships and joint ventures. The Company calculates FFO based on the National Association of Real Estate Investment Trusts' (NAREIT) definition.

PNOI is a supplemental industry reporting measurement used to evaluate the performance of the Company's real estate investments. The Company believes the exclusion of depreciation and amortization in the industry's calculation of PNOI provides a supplemental indicator of the properties' performance since real estate values have historically risen or fallen with market conditions. PNOI as calculated by the Company may not be comparable to similarly titled but differently calculated measures for other real estate investment trusts (REITs). The major factors influencing PNOI are occupancy levels, acquisitions and sales, development properties that achieve stabilized operations, rental rate increases or decreases, and the recoverability of operating expenses. The Company's success depends largely upon its ability to lease space and to recover from tenants the operating costs associated with those leases.

PNOI is comprised of Income from real estate operations, less Expenses from real estate operations plus the Company's share of income and property operating expenses from its less-than-wholly-owned real estate investments. PNOI was calculated as follows for the three and nine months ended September 30, 2015 and 2014.

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2015	2014	2015	2014
	(In thousands)			
Income from real estate operations	$58,520	55,896	173,922	162,474
Expenses from real estate operations	(16,795)	(15,899)	(49,255)	(46,536)
Noncontrolling interest in PNOI of consolidated 80% joint ventures	(208)	(209)	(628)	(636)
PNOI from 50% owned unconsolidated investment	213	199	629	595
PROPERTY NET OPERATING INCOME	$41,730	39,987	124,668	115,897

Income from real estate operations is comprised of rental income, expense reimbursement pass-through income and other real estate income including lease termination fees. Expenses from real estate operations is comprised of property taxes, insurance, utilities, repair and maintenance expenses, management fees, other operating costs and bad debt expense. Generally, the Company's most significant operating expenses are property taxes and insurance. Tenant leases may be net leases in which the total operating expenses are recoverable, modified gross leases in which some of the operating expenses are recoverable, or gross leases in which no expenses are recoverable (gross leases represent only a small portion of the Company's total leases). Increases in property operating expenses are fully recoverable under net leases and recoverable to a high degree under modified gross leases. Modified gross leases often include base year amounts and expense increases over these amounts are recoverable. The Company's exposure to property operating expenses is primarily due to vacancies and leases for occupied space that limit the amount of expenses that can be recovered.