HMG COURTLAND PROPERTIES INC
Form 10-K
March 28, 2019

U. S. SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

x Annual Report pursuant to Section 13 or 15(d) of the Securities and Exchange Act of 1934

For the fiscal year ended December 31, 2018

o Transition Report pursuant to Section 13 or 15(d) of the Securities and Exchange Act of 1934

Commission file number: 1-7865

HMG/COURTLAND PROPERTIES, INC.

(Name of Registrant in its Charter)

Delaware (State or other jurisdiction of incorporation or organization)	59-1914299 (I.R.S. Employer Identification Number)
1870 S. Bayshore Drive, Coconut Grove (Miami), Florida (Address of principal executive offices)	33133 (Zip Code)

Issuer's telephone number, including area code: (305) 854-6803

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

Title of class	Name of each exchange on which registered:
Common Stock - Par value $1.00 per share	NYSE

Securities registered pursuant to Section 12(g) of the Act: *None*

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act

Yes o No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes o No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act of 1934 during the past 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 x No o

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 (Section 232.05) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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

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

Emerging growth 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 o No x

The aggregate market value of the voting stock held by non-affiliates of the Registrant (excludes shares of voting stock held by directors, executive officers and beneficial owners of more than 10% of the Registrant’s voting stock; however, this does not constitute an admission that any such holder is an “affiliate” for any purpose) based on the closing price of the stock as traded on the NYSE Amex Exchange on the last business day of the Registrant’s most recently completed second fiscal quarter (June 30, 2018) was $6,071,006. The number of shares outstanding of the issuer’s common stock, $1 par value as of the latest practicable date: 1,013,292 shares of common stock, $1 par value, as of March 28, 2019.

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Part I.

Cautionary Statement.

An investment in our common stock involves a high degree of risk. These risks should be considered carefully with the uncertainties described below, and all other information included in this Annual Report on Form 10-K, before deciding whether to purchase our common stock. Additional risks and uncertainties not currently known to management or that management currently deems immaterial may also become important factors that may harm our business, financial condition or results or operations. The trading price of our common stock could decline due to any of these risks and uncertainties and you may lose part or all of your investment.

This Annual Report contains certain statements relating to future results of the Company that are considered "forward-looking statements" within the meaning of the Private Litigation Reform Act of 1995. Actual results may differ materially from those expressed or implied as a result of certain risks and uncertainties, including, but not limited to, changes in political and economic conditions; interest rate fluctuation; competitive pricing pressures within the Company's market; equity and fixed income market fluctuation; technological change; changes in law; changes in fiscal, monetary, regulatory and tax policies; monetary fluctuations as well as other risks and uncertainties detailed elsewhere in this Annual Report or from time-to-time in the filings of the Company with the Securities and Exchange Commission. Such forward-looking statements speak only as of the date on which such statements are made, and the Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events.

Item 1. Description of Business.

HMG/Courtland Properties, Inc. and subsidiaries ("HMG", or the "Company"), is a Delaware corporation organized in 1972. The Company's business is the ownership and management of income-producing commercial properties and it will consider other investments if they offer growth or profit potential.

HMG qualifies under the U.S. Internal Revenue Code for taxation as a real estate investment trust ("REIT"), excluding its 95% owned taxable REIT subsidiary Courtland Investments, Inc. ("CII"), which files a separate tax return.

As previously reported on Form 8-K dated February 20, 2018, JY-TV Associates, LLC, a Florida limited liability company ("JY-TV") ("Seller") an entity one-third owned by HMG, completed the sale of its multi-family residential apartments located in Orlando, Florida pursuant to the previously reported Agreement of Sale (the “Agreement”) to Murano 240, LLC (as per an Assignment and Assumption of Agreement of Sale with Cardone Real Estate Acquisitions, LLC), a Delaware limited liability company, an unrelated entity (“Purchaser”). The final sales price was $50,150,000 and the sales proceeds were received in cash and payment of outstanding debt. The gain on the sale to HMG was approximately $5.5 million, net of the incentive fee.

The Company invests its idle cash in marketable securities and acquires real estate and other investments utilizing available cash or borrowing funds.

The Company’s portfolio of REIT marketable securities consists primarily of preferred equity of large capital publicly traded REITs with a market value of approximately $1.76 million as of December 31, 2018.

The Company’s investments in non-REIT marketable securities include equity and debt securities issued primarily by large capital companies or government agencies with readily determinable fair values in varying industries. This includes real estate investment trusts and mutual funds focusing in commercial real estate activities. Substantially all the Company’s marketable securities investments are in companies listed on major national stock markets, however the overall investment portfolio and some of the Company’s investment strategies could be viewed as risky and the market values of the portfolio may be subject to fluctuations. Consistent with the Company’s overall investment objectives and activities, management classifies all marketable securities as being held in a trading portfolio. Accordingly, all unrealized gains and losses on the Company’s investments in marketable securities are recorded in the Consolidated Statements of Income. Marketable securities are stated at market value as determined by the most recently traded price of each security at the balance sheet date. Information regarding the amounts and types of investments in marketable securities is set forth in Note 3 of the Notes to Consolidated Financial Statements.

The Company may realize gains and losses in its overall investment portfolio from time to time to take advantage of market conditions and/or manage the portfolio’s resources and the Company’s tax liability. The Company may utilize margin for its marketable securities purchases through the use of standard margin agreements with national brokerage firms. The use of available leverage is guided by the business judgment of management. The Company may also use options and futures to hedge concentrated stock positions and index futures to hedge against market risk and enhance the performance of the Company’s portfolio while reducing the overall portfolio’s risk and volatility.

The Company’s other investments consist primarily of nominal equity interests in various privately-held entities, including limited partnerships whose purpose is to invest venture capital funds in growth-oriented enterprises. The Company does not have significant influence over any investee and the Company’s investments typically represent less than 3% of the investee’s ownership. Some of these investments give rise to exposure resulting from the volatility in capital markets. The Company mitigates its risks by diversifying its investment portfolio. Information with respect to the amounts and types of other investments including the nature of the declines in value is set forth in Note 4 of the Notes to Consolidated Financial Statements.

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Reference is made to Item 13. Certain Relationships and Related Transactions and Director Independence for discussion of the Company's organizational structure and related party transactions.

Investment in Affiliate.

The Company's investment in affiliate consists of a 49% equity interest in T.G.I.F. Texas, Inc. ("TGIF"). TGIF was incorporated in Texas and operates solely from the Company's corporate office in Miami, Florida. The Company's CEO, Maurice Wiener, is also the CEO of TGIF. Its assets consist primarily of promissory notes receivable from its shareholders including CII and Mr. Wiener and other investments including marketable debt and equity securities. This investment's carrying value as of December 31, 2018 and 2017 was approximately $1.6 million and $1.8 million, respectively. CII's note payable to TGIF which is due on demand was approximately $1.3 million and $1.5 million as of December 31, 2018 and 2017, respectively. Reference is made to Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Insurance, Environmental Matters and Other:

In the opinion of management, all significant real estate assets of the Company are adequately covered by insurance or are self-insured.

In May 2018, the Company received a Determination of Eligibility under the Brownfields Reuse and Liability Limitation Act (BRELLA) related to environmental remediation of the Company's 6-acre property located in Montpelier, Vermont ("the remediation plan"). Under BRELLA we will receive a Certificate of Completion upon performance of all actions required under the approved corrective action plan developed for the property. Statutory liability protections become effective upon issuance of the Certificate of Completion. Forbearance from state enforcement action is in effect during the BRELLA provided that all required activities are being implemented in good faith.

On October 17, 2018, the Company received approval from the Vermont Department Environmental Conservation (VTDEC) of its corrective action plan relating to the remediation plan. The estimated costs to remediate the property is $458,000. The Company owns approximately 70% of the property and we have recorded as expense our portion, $319,000, of the anticipated remediation costs as of December 31, 2018. The remediation work is expected to begin in the summer of 2019.

We are not aware of any federal, state or local environmental laws or regulations that will materially affect our earnings or competitive position or result in material capital expenditures. However, we cannot predict the effect of possible future environmental legislation or regulations on our operations.

Competition and the Company's Market

The Company competes for suitable opportunities for real estate investments with other real estate investment trusts, foreign investors, pension funds, insurance companies and other investors. The Company also competes with other real estate investors and borrowers for available sources of financing.

In addition, to the extent the Company leases properties it must compete for tenants with other lessors offering similar facilities. Tenants are sought by providing modern, well-maintained facilities at competitive rentals. The Company has attempted to facilitate successful leasing of its properties by investing in facilities that have been developed according to the specifications of tenants and special local needs.

Employees.

The Company's management is provided in accordance with its Advisory Agreement (the "Agreement") with HMGA, Inc. ("the Adviser"), as described below under "Terms of the Agreement". Reference is also made to Item 13. Certain Relationships and Related Transactions, and Director Independence.

Terms of the Advisory Agreement. Under the terms of the Agreement, the Adviser serves as the Company's investment adviser and, under the supervision of the directors of the Company, administers the day-to-day operations of the Company. All officers of the Company who are officers of the Adviser are compensated solely by the Adviser for their services. The Agreement is renewable annually upon the approval of a majority of the directors of the Company who are not affiliated with the Adviser and a majority of the Company's shareholders. The contract may be terminated at any time on 120 days written notice by the Adviser or upon 60 days written notice by a majority of the unaffiliated directors of the Company or the holders of a majority of the Company's outstanding shares.

On June 28, 2018, the shareholders of the Company approved the renewal of the Advisory Agreement between the Company and the Adviser for a term commencing January 1, 2019 and expiring December 31, 2019.

The Adviser is majority owned by Mr. Wiener. The officers and directors of the Adviser are as follows: Maurice Wiener, Chairman of the Board, Chief Executive officer and President and Carlos Camarotti, Vice President - Finance and Assistant Secretary.

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Advisory Fees. For the years ended December 31, 2018 and 2017, the Company and its subsidiaries incurred Adviser fees of approximately $1,300,000 and $703,000, respectively. This consisted of $660,000 in regular compensation for 2018 and 2017, and $640,000 and $43,000 in incentive fee compensation for 2018 and 2017, respectively.

Item 2. Description of Property.

Executive offices (Coconut Grove, Florida). The principal executive offices of the Company and the Adviser are located at 1870 South Bayshore Drive, Coconut Grove, Florida, 33133, in premises owned by the Company's subsidiary CII and is primarily leased to the Adviser pursuant to a lease agreement originally dated December 1, 1999. In December 2018, the lease was renewed for one year with two one-year extension options with an increase in rent of 5% per year. The lease (as extended) provides for base rent of $58,344 per year beginning on December 1, 2018 and payable in equal monthly installments during the term of the lease which expires on December 1, 2019. The Adviser, as tenant, pays utilities, certain maintenance and security expenses relating to the leased premises.

The Company regularly evaluates potential real estate acquisitions for future investment or development and would utilize funds currently available or from other resources to implement its strategy.

Item 3. Legal Proceedings.

None.

Item 4. Mine Safety Disclosures.

Not applicable to the Company.

Part II.

Item 5. Market for Registrant's Common Equity and Related Stockholder Matters and Issuer Purchases of Equity Securities.

The high and low per share closing sales prices of the Company's stock on the NYSE Exchange (ticker symbol: HMG) for each quarter during the past two years were as follows:

	High	Low
March 31, 2018	$18.45	$12.59
June 30, 2018	$15.40	$12.64
September 30, 2018	$15.65	$13.88
December 31, 2018	$14.75	$13.60
March 31, 2017	$11.38	$10.15
June 30, 2017	$11.45	$10.49
September 30, 2017	$12.00	$10.35
December 31, 2017	$14.45	$10.60

On December 14, 2018 the Company declared a capital gain dividend of $0.50 per share which was payable on January 9, 2019 to all shareholders of record as of December 28, 2018.

On March 7, 2018 the Company declared a capital gain dividend of $2.50 per share which was payable on March 30, 2018 to all shareholders of record as of March 21, 2018.

There were no dividends declared for the year ended December 31, 2017.

On December 19, 2016 the Company declared a return of capital dividend of $.50 per share which was paid on January 9, 2017 to all shareholders of record as of December 29, 2016.

The Company's policy has been to pay dividends as are necessary for it to qualify for taxation as a REIT under the Internal Revenue Code.

As of March 8, 2019, there were approximately 456 shareholders of record of the Company's common stock.

The following table illustrates securities currently authorized for issuance under the Company's equity compensation plan, the 2011 Stock Option Plan:

	Number of securities to be issued upon exercise of outstanding options	Weighted-average exercise price of outstanding options	Number of securities remaining available for future issuance under equity compensation plans
Equity compensation plan approved by shareholders	1,600	$ 15.30	47,608
Equity compensation plan not approved by shareholders	—	—	—
Total	1,600	$ 15.30	47,608

In January and March 2018 three directors and one officer exercised options to purchase a total of 10,900 shares at $9.31 per share.

The following table summarizes stock option activity during the year ended December 31, 2018:

	Options Outstanding	Weighted Average Exercise Price
Outstanding at January 1, 2018	12,500	$ 9.31
Exercised (including 1,600 shares exchanged via re-load option)	(12,500)	(9.31)
Forfeited	-	-
Expired unexercised	-	-
Granted (via re-load option)	1,600	15.30
Outstanding at December 31, 2018	1,600	$ 15.30

As of December 31, 2018, the options outstanding and exercisable had no intrinsic value.

The following table summarizes stock option activity during the year ended December 31, 2017:

	Options Outstanding	Weighted Average Exercise Price
Outstanding at January 1, 2017	12,500	$ 9.31
Forfeited	-	-
Expired unexercised	-	-
Granted	-	-
Outstanding at December 31, 2017	12,500	$ 9.31

As previously reported on December 14, 2018, HMG announced that its Board of Directors has authorized the purchase of up to $500,000 of HMG common stock on the open market or through privately negotiated transactions. The program will be in place through December 31, 2021. During the years ended December 31, 2018 and 2017, there were no shares purchased as part of this publicly announced program.

Item 6. Selected Financial Data:

Not applicable to the Company.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Critical Accounting Policies and Estimates.

The preparation of our consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions in applying our critical accounting policies that affect the reported amounts of assets and liabilities and the disclosure (if any) of contingent assets and liabilities at the date of the consolidated financial statements and the reported amount of revenues and expenses during the reporting period. Our estimates and assumptions concern, among things, potential impairment of our other investments and other long-lived assets, uncertainties for Federal and state income tax and allowance for potential doubtful accounts. We evaluate those estimates and assumptions on an ongoing basis based on historical experience and on various other factors which we believe are reasonable under the circumstances. Note 1 of the consolidated financial statements, included elsewhere on this Form 10-K, includes a summary of the significant accounting policies and methods used in the preparation of the Company's consolidated financial statements. The Company believes the following critical accounting policies affect the significant judgments and estimates used in the preparation of the Company's consolidated financial statements:

Marketable Securities. Consistent with the Company's overall investment objectives and activities, management has classified its entire marketable securities portfolio as trading. As a result, all unrealized gains and losses on the Company's investment portfolio are included in the Consolidated Statements of Income. Our investments in trading equity and debt marketable securities are carried at fair value and based on quoted market prices or other observable inputs. Marketable securities are subject to fluctuations in value in accordance with market conditions.

Other Investments. The Company's other investments consist primarily of nominal equity interests in various privately-held entities, including limited partnerships whose purpose is to invest venture capital funds in growth-oriented enterprises. The Company does not have significant influence over any investee and the Company's investment typically represents less than 3% of the investee's ownership. These investments generally do not meet the criteria of accounting under the equity method and are carried at cost less distributions and other than temporary unrealized losses. These investments do not have available quoted market prices, so we must rely on valuations and related reports and information provided to us by those entities for the purposes of determining other-than-temporary declines. These valuations are by their nature subject to estimates which could change significantly from period to period. The Company regularly reviews the underlying assets in its other investment portfolio for events, that may indicate the investment has suffered other-than-temporary decline in value including. These events include but are not limited to bankruptcies, closures and declines in estimated fair value. When a decline is deemed other-than-temporary, we permanently reduce the cost basis component of the investments to its estimated fair value, and the loss is recorded as a component of income from other investments. As such, any recoveries in the value of the investments will not be recognized until the investments are sold.

We believe our estimates of each of these items historically have been adequate. However, due to uncertainties inherent in the estimation process, it is reasonably possible that the actual resolution of any of these items could vary significantly from the estimate and, accordingly, there can be no assurance that the estimates may not materially change in the near term.

Real Estate. Land, buildings and improvements, furniture, fixtures and equipment are recorded at cost. Tenant improvements, which are included in buildings and improvements, are stated at cost. Expenditures for ordinary maintenance and repairs are expensed to operations as they are incurred. Renovations and/or replacements, which improve or extend the life of the asset are capitalized and depreciated over the shorter of their estimated useful lives, or the remaining lease term (if leased).

Depreciation is computed utilizing the straight-line method over the estimated useful lives of ten to forty years for buildings and improvements and five to ten years for furniture, fixtures and equipment. Tenant improvements are amortized on a straight-line basis over the shorter of the term of the related leases or the assets useful life.

The Company is required to make subjective assessments as to the useful lives of its properties for purposes of determining the amount of depreciation to reflect on an annual basis with respect to those properties. These assessments have a direct impact on the Company’s net income. Should the Company lengthen the expected useful life of a particular asset, it would be depreciated over more years, and result in less depreciation expense and higher annual net income.

Assessment by the Company of certain other lease related costs must be made when the Company has a reason to believe that the tenant will not be able to execute under the term of the lease as originally expected.

The Company periodically reviews the carrying value of certain of its properties and long-lived assets in relation to historical results, current business conditions and trends to identify potential situations in which the carrying value of assets may not be recoverable. If such reviews indicate that the carrying value of such assets may not be recoverable, the Company would estimate the undiscounted sum of the expected future cash flows of such assets or analyze the fair value of the asset, to determine if such sum or fair value is less than the carrying value of such assets to ascertain if a permanent impairment exists. If a permanent impairment exists, the Company would determine the fair value by using quoted market prices, if available, for such assets, or if quoted market prices are not available, the Company would discount the expected future cash flows of such assets and would adjust the carrying value of the asset to fair value.

Judgments as to impairments and assumptions used in projecting future cash flow are inherently imprecise.

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Results of Operations:

For the year ended December 31, 2018, the Company reported net income of approximately $4.1 million ($4.07 per share). For the year ended December 31, 2017, the Company reported a net loss of approximately $314,000 ($0.31 per share).

Revenues:

Total revenues for the years ended December 31, 2018 and 2017 were approximately $73,000 and $68,000, respectively. This is primarily comprised of rental revenue from the leasing of the corporate offices to the Adviser.

Expenses:

Total expenses for the year ended December 31, 2018 as compared to that of 2017 increased by approximately $227,000 (or 15%).

Operating expenses of rental and other properties increased by approximately $232,000 (or 116%). This increase was primarily relating to the projected costs to remediate the Company's Montpelier, Vermont property as previously disclosed in Form 10-Q for the period ended September 30, 2018. This increase in expenses was partially offset by decreased repairs and maintenance at the Company's corporate headquarters in Miami, Florida.

General and administrative expenses for the year ended December 31, 2018 as compared to that of 2017 decreased by approximately $36,000 (or 14%) primarily due to decreased dues and subscriptions incurred by Courtland Investments, Inc.

Interest expense for the year ended December 31, 2018 as compared to that of 2017 increased by approximately $20,000 (or 30%) primarily due to increased broker margin balances and increased interest rates.

Other Income:

Net realized and unrealized gains from investments in marketable securities:

Net gain (loss) from investments in marketable securities, including marketable securities distributed by partnerships in which the Company owns minority positions, for the years ended December 31, 2018 and 2017, is as follows:

	2018	2017
Net realized gain from sales of marketable securities	$51,000	$62,000
Net unrealized (loss) gain from marketable securities	(454,000)	199,000
Total net (loss) gain from investments in marketable securities	$(403,000)	$261,000

Net realized gain from sales of marketable securities consisted of approximately $240,000 of gains net of $189,000 of losses for the year ended December 31, 2018. The comparable amounts in fiscal year 2017 were approximately $364,000 of gains net of $302,000 of losses.

Consistent with the Company's overall current investment objectives and activities, the entire marketable securities portfolio is classified as trading (as defined by U.S generally accepted accounting principles). Unrealized gains or losses from marketable securities are recorded as other income in the Consolidated Statements of Income.

Investment gains and losses on marketable securities may fluctuate significantly from period to period in the future and could have a significant impact on the Company's net earnings. However, the amount of investment gains or losses on marketable securities for any given period has no predictive value and variations in amount from period to period have no practical analytical value.

Investments in marketable securities give rise to exposure resulting from the volatility of capital markets. The Company attempts to mitigate its risk by diversifying its marketable securities portfolio.

Equity loss in residential real estate partnership:

As previously reported on Form 8-K dated February 20, 2018, JY-TV Associates, LLC, a Florida limited liability company ("JY-TV") ("Seller") an entity one-third owned by HMG, completed the sale of its multi-family residential apartments located in Orlando, Florida pursuant to the previously reported Agreement of Sale (the "Agreement") to Murano 240, LLC (as per an Assignment and Assumption of Agreement of Sale with Cardone Real Estate Acquisitions, LLC), a Delaware limited liability company, an unrelated entity ("Purchaser"). The final sales price was $50,150,000 and the sales proceeds were received in cash and payment of outstanding debt. The gain on the sale to

HMG was approximately $5.5 million, net of the incentive fee.

For the year ended December 31, 2018 (through the date of sale) JY-TV Associates LLC reported a net loss from operations of approximately $411,000, which includes depreciation and amortization expense of $447,000 and interest expense of $159,000. The Company's portion of the 2018 loss from operations was approximately $137,000. For the year ended December 31, 2017 JY-TV Associates LLC reported a net loss of approximately $671,000, which includes depreciation and amortization expense of $1,556,000 and interest expense of $1,123,000. The Company's portion of the 2017 loss was approximately $224,000.

Income from other investments is summarized below (excluding other than temporary impairment losses):

	2018	2017
Partnerships owning real estate and related investments (a)	$217,000	$224,000
Venture capital funds – diversified businesses (a)	63,000	270,000
Venture capital funds – technology businesses	34,000	27,000
Investment in 49% owned affiliate and other (b)	74,000	70,000
Total income from other investments	$388,000	$591,000

(a) The gains in 2018 and 2017 consist of various cash distributions from investments owning diversified businesses and real estate and related investments which made cash distributions from the sale or refinancing of operating companies or properties.

(b) This gain represents income from the Company's 49% owned affiliate, T.G.I.F. Texas, Inc. ("TGIF"). In 2018 and 2017 TGIF declared and paid a cash dividend of which the Company's portion was approximately $193,000 each year. These dividends were recorded as reduction in the investment carrying value as required under the equity method of accounting for investments.

Other than temporary impairment ("OTTI") losses from other investments:

There were no OTTI losses for the year ended December 31, 2018 and 2017.

Income or loss from other investments may fluctuate significantly from period to period in the future and could have a significant impact on the Company's net earnings. However, the amount of investment gain or loss from other investments for any given period has no predictive value and variations in amount from period to period have no practical analytical value.

Interest, dividend and other income

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Interest, dividend and other income for the year ended December 31, 2018 as compared with 2017 decreased by approximately $86,000 (or 18%). This was primarily due to a decreased dividend income as a result of the sale of the majority of our REIT common equity marketable securities in July 2017.

Benefit from (provision for) income taxes:

The Company qualifies as a real estate investment trust and distributes its taxable ordinary income to stockholders in conformity with requirements of the Internal Revenue Code and is not required to report deferred items due to its ability to distribute all taxable income. In addition, net operating losses can be carried forward to reduce future taxable income but cannot be carried back. Distributed capital gains on sales of real estate as they relate to REIT activities are not subject to taxes; however, undistributed capital gains may be subject to corporate tax.

The benefit from income taxes for the year ended December 31, 2018 was approximately $39,000 and is primarily attributable to deferred tax benefit relating to CII. The provision for income taxes for the year ended December 31, 2017 was approximately $11,000 and was primarily attributable to deferred tax expense of $14,000 less current federal tax benefit of $3,000 relating to estimated tax payment applied to future taxes due to no prohibited REIT income tax due in 2017.

As of December 31, 2018, the Company, excluding its taxable REIT subsidiary, CII, is expected to utilize approximately $1.7 million in tax net operating loss carryover (NOL) generated from 2017 and prior years.

The Company's 95%-owned taxable REIT subsidiary, CII, files a separate income tax return and its operations are not included in the REIT's income tax return.

For CII, the Company follows the liability method of accounting for income taxes. Under this method, deferred tax liabilities and assets are recognized for the expected future tax consequences of temporary differences between the carrying amount and the tax basis of assets and liabilities at each year-end based on enacted tax laws and statutory tax rates applicable to the periods in which the differences are expected to affect taxable income. As a result of timing differences associated with the carrying value of other investments, unrealized gains and losses of marketable securities, depreciable assets and the future benefit of a net operating loss, as of December 31, 2018, and 2017 the Company has recorded a net deferred tax liability of $48,000 and $84,000, respectively.

As of December 31, 2018, CII has an estimated NOL of approximately $893,000 which has been fully reserved due to CII historically having tax losses.

Effect of Inflation.

Inflation affects the costs of maintaining the Company's investments.

Liquidity, Capital Expenditure Requirements and Capital Resources.

The Company's material commitments primarily consist of a note payable to the Company's 49% owned affiliate, T.G.I.F. Texas, Inc. ("TGIF") of approximately $1.3 million due on demand (see Item 13. Certain Relationships and Related Transactions and Director Independence), and contributions committed to other investments of approximately $1 million due upon demand. The $9.86 million in margin is primarily related to the purchase of US T-bills at quarter end. The T-bills were sold in January 2019 and the related margin was repaid. The purchase of T-bills at each fiscal quarter end is for the purposes of qualifying for the REIT asset test. The funds necessary to meet the other obligations are expected from the proceeds from the sales of investments, distributions from investments and available cash and equivalents ($19.7 million at December 31, 2018).

A summary of the Company's contractual cash obligations at December 31, 2018 is as follows:

	Payments Due by Period				
Contractual Obligations	Total	Less than 1 year	1 – 3 years	4 – 5 years	After 5 years
Note payable	$1,340,000	$1,340,000	—	—	—
Other investments commitments	1,039,000	1,039,000	—	—	—
Total	$2,379,000	$2,379,000	—	—	—

The timing of amounts due under commitments for other investments is determined by the managing partners of the individual investments.

Material Changes in Operating, Investing and Financing Cash Flows.

The Company's cash flows are generated primarily from its dividends, interest and sales proceeds of marketable securities, distributions from investments and borrowings.

For the year ended December 31, 2018, net cash used in operating activities was approximately $1,722,000, primarily consisting of net loss before income taxes and other income of approximately $1,617,000, plus interest, dividends and other income of approximately $387,000 less changes in assets and liabilities of approximately $407,000.

For the year ended December 31, 2018, net cash provided by investing activities was approximately $9.3 million and consisted primarily of proceeds from the sale of multi-family residential real estate in Orlando, Florida of $7.6 million, net proceeds from the sale of marketable securities of $2.9 million, distributions from other investments of $1.5 million, proceeds from collections of mortgage loans of $500,000 and a dividend from TGIF of $193,000. These sources of funds were partially offset by $1.5 million of purchases of marketable securities, $1.4 million of contributions to other investments and additions to mortgage loans and notes receivable of $750,000.

For the year ended December 31, 2018, net cash provided by financing activities was approximately $6.9 million and consisted primarily of margin borrowings to purchase US T-bills at the end of each fiscal quarter of approximately $9.6 million and proceeds from the exercise of stock options by directors and officer of approximately $92,000. These sources of funds were partially offset by dividend paid of approximately $2.5 million and $210,000 of repayment of note payable to TGIF.

Item 7A. Quantitative and Qualitative Disclosures About Market Risks.

Not Applicable to the Company.

Item 8. Financial Statements and Supplementary Data

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of HMG/Courtland Properties, Inc. and Subsidiaries

Opinion on the Consolidated Financial Statements

We have audited the accompanying consolidated balance sheets of HMG/Courtland Properties, Inc. (a Delaware corporation) and Subsidiaries (the “Company”) as of December 31, 2018 and 2017, and the related consolidated statements of income, changes in stockholders’ equity and cash flows for each of the years then ended, and the related notes (collectively referred to as the consolidated financial statements). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2018 and 2017, and the results of operations and its cash flows for each of the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Basis for Opinion

These consolidated financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company’s consolidated financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform an audit of its internal control over financial reporting. As part of our audits, we are required to obtain an understanding of internal control over financial reporting, but not for the purposes of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audits provide a reasonable basis for our opinion.

We have served as the Company's auditor since December 31, 2010.

/s/ Cherry Bekaert LLP
Coral Gables, Florida
March 28, 2019

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HMG/COURTLAND PROPERTIES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS AS OF DECEMBER 31, 2018 AND 2017

	December 31, 2018	December 31, 2017
ASSETS		
Investment properties, net of accumulated depreciation:		
Office building and other commercial property	$ 875,198	$ 857,464
Total investment properties, net	875,198	857,464
Cash and cash equivalents	19,738,174	5,223,995
Investments in marketable securities	3,075,718	4,549,745
Other investments	6,039,456	6,412,120
Investment in affiliate	1,637,985	1,757,607
Loans, notes and other receivables	1,796,926	1,561,750
Investment in residential real estate partnership	6,187	1,685,978
Other assets	267,290	108,020
TOTAL ASSETS	$ 33,436,934	$ 22,156,679
LIABILITIES		
Note payable to affiliate	$ 1,340,000	$ 1,550,000
Margin payable	9,857,918	267,198
Dividends payable	506,646	-
Accounts payable, accrued expenses and other liabilities	370,632	119,171
Amounts due to the Adviser for incentive fee	40,426	43,279
Deferred income tax payable	47,888	84,153
TOTAL LIABILITIES	12,163,510	2,063,801
COMMITMENTS AND CONTINGENCIES	—	—
STOCKHOLDERS' EQUITY		
Excess common stock, $1 par value; 100,000 shares authorized: no shares issued	—	—
Common stock, $1 par value; 1,050,000 shares authorized, 1,046,393 and 1,035,493 shares issued as of December 31, 2018 and December 31, 2017, respectively	1,046,393	1,035,493
Additional paid-in capital	24,157,986	24,076,991
Less: Treasury shares at cost 33,101 shares	(340,281)	(340,281)
Undistributed gains from sales of properties, net of losses	54,642,764	52,208,753
Undistributed losses from operations	(58,473,807)	(57,120,990)
Total stockholders' equity	21,033,055	19,859,966
Noncontrolling interest	240,369	232,912
TOTAL EQUITY	21,273,424	20,092,878
TOTAL LIABILITIES AND EQUITY	$ 33,436,934	$ 22,156,679

See notes to the consolidated financial statements

HMG/COURTLAND PROPERTIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

	2018	2017
REVENUES		
Real estate rentals and related revenue	$72,598	$68,321
Total revenues	72,598	68,321
EXPENSES		
Operating expenses:		
Rental and other properties	431,614	199,799
Adviser's base fee	660,000	660,000
General and administrative	219,830	255,750
Professional fees and expenses	193,341	181,580
Directors' fees and expenses	81,494	82,076
Depreciation and Amortization expense	15,398	15,398
Interest expense	88,822	68,577
Total expenses	1,690,499	1,463,180
Loss before other income, income taxes and gain on sale of real estate	(1,617,901)	(1,394,859)
Net realized and unrealized (losses) gains from investments in marketable securities	(403,432)	260,656
Equity loss in residential real estate partnership	(136,889)	(223,736)
Income from other investments	387,671	591,250
Interest, dividend and other income	386,523	472,621
Total other income	233,873	1,100,791
Loss before income taxes and gain on sale of real estate	(1,384,028)	(294,068)
Benefit from (provision for) income taxes	38,668	(10,653)
Net loss before gain on sale of real estate	(1,345,360)	(304,721)
Gain on sale of real estate, net of incentive fee	5,473,887	-
Net income (loss)	4,128,527	(304,721)
Gain from noncontrolling interest	(7,457)	(9,503)
Net income (loss) attributable to the Company	$4,121,070	$(314,224)
Weighted average common shares outstanding-basic and diluted:	1,011,839	1,002,392
Net income (loss) per common share:		

Basic and diluted income (loss) per share	$4.07	$(0.31)

See notes to the consolidated financial statements

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HMG/COURTLAND PROPERTIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

	Common Stock		Additional	Undistributed Gains from Sales of Properties	Undistributed Losses from	Treasury Stock		Total Stockholders'
	Shares	Amount	Paid-In Capital	Net of Losses	Operations	Shares	Cost	Equity
Balance as of January 1, 2017	1,035,493	$1,035,493	$24,076,991	$52,208,754	$(56,806,767)	$33,101	(340,281)	20,174,190
Net loss					(314,224)			(314,224)
Balance as of December 31, 2017	1,035,493	1,035,493	24,076,991	52,208,754	(57,120,991)	33,101	(340,281)	19,859,966
Net income				5,473,887	(1,352,817)			4,121,070
Dividend paid - $2.50 per share				(2,533,230)				(2,533,230)
Dividend payable - $.50 per share				(506,646)				(506,646)
Stock options exercised, net of 1,600 re-load shares	10,900	10,900	80,995					91,895
Balance as of December 31, 2018	1,046,393	1,046,393	24,157,986	54,642,765	(58,473,808)	33,101	(340,281)	21,033,055

See notes to the consolidated financial statements

HMG/COURTLAND PROPERTIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss) attributable to the Company	$4,121,070	($314,224)
Adjustments to reconcile net income (loss) attributable to the Company to net cash used in operating activities:		
Depreciation expense	15,398	15,398
Income from other investments, excluding impairment losses	(387,671)	(591,250)
Equity loss from operations of residential real estate partnership	136,889	223,736
Gain on sale of real estate, net of incentive fee	(5,473,887)	(10,970)
Net losses (gains) from investments in marketable securities	403,432	(260,656)
Net gain attributable to noncontrolling interest	7,457	9,503
Deferred income tax (benefit) expense	(36,265)	7,826
Changes in assets and liabilities:		
Other assets and other receivables	(119,479)	166,845
Accounts payable, accrued expenses and other liabilities	(388,771)	(34,326)
Total adjustments	(5,842,897)	(473,894)
Net cash used in operating activities	(1,721,827)	(788,118)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net proceeds from sales and redemptions of securities	2,883,616	7,074,127
Investments in marketable securities	(1,513,021)	(3,612,553)
Distribution from investment in residential real estate partnership	7,625,000	130,000
Distributions from other investments	1,831,307	1,520,666
Contributions to other investments	(1,440,436)	(2,060,530)
Proceeds from collections of mortgage loans and notes receivables	500,000	78,000
Distribution from affiliate	193,286	193,286
Purchases and improvements of properties	-	(34,872)
Proceeds from sale of real estate	(33,131)	37,327
Additions in mortgage loans and notes receivable	(750,000)	-
Net cash provided by investing activities	9,296,621	3,325,451
CASH FLOWS FROM FINANCING ACTIVITIES:		
Margin borrowings	9,590,720	218,395
Dividends paid	(2,533,230)	(501,196)
Repayment of note payable to affiliate	(210,000)	(50,000)
Stock options exercised	91,895	-
Net cash provided by (used in) financing activities	6,939,385	(332,801)

Net increase in cash and cash equivalents	14,514,179	2,204,532
Cash and cash equivalents at beginning of the year	5,223,995	3,019,463
Cash and cash equivalents at end of the year	$19,738,174	$ 5,223,995
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid during the year for interest	$89,000	$ 69,000
NONCASH INVESTING AND FINANCING ACTIVITIES:		
Dividends declared but not paid during the year	$506,646	$ -

See notes to the consolidated financial statements

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HMG/COURTLAND PROPERTIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2018 and 2017

1. DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Business and Consolidation. The consolidated financial statements include the accounts of HMG/Courtland Properties, Inc. ("we" or the "Company") and entities in which the Company owns a majority voting interest or controlling financial interest. The Company was organized in 1972 and (excluding its 95% owned subsidiary Courtland Investments, Inc., which files a separate tax return) qualifies for taxation as a real estate investment trust ("REIT") under the Internal Revenue Code. The Company's business is the ownership and management of income-producing commercial properties and its management considers other investments if such investments offer growth or profit potential. The Company's recurring operating revenue is from property rental operations of its corporate offices.

All material transactions and balances with consolidated and unconsolidated entities have been eliminated in consolidation or as required under the equity method.

The Company's consolidated subsidiaries are described below:

Courtland Investments, Inc. ("CII"). In March 2016, this 95% owned corporation of the Company amended its Certificate of Incorporation so that, as amended, the holders of Class A and Class B common stock of CII shall have and possess the exclusive right to notice of and to vote at any meeting of the stockholders and any adjournment thereof, and the exclusive right to express consent to corporate action in writing without a meeting. Class A and Class B shareholders of CII shall have equal voting rights. CII is the Company's taxable REIT subsidiary which files a separate tax return. CII's operations are not part of the REIT tax return.

HMG Orlando, LLC ("HMGO"). This wholly owned limited liability company was formed in August 2014. In September 2014 HMGO acquired a one-third equity membership interest in JY-TV Associates, LLC a Florida limited liability company ("JY-TV") and entered into the Amended and Restated Operating Agreement of JY-TV (the "Agreement"). JY-TV was formed in 2014 for the sole purpose of purchasing and constructing two hundred forty (240) unit rental apartments on approximately 9.5 acres in Orlando, Florida. The other two initial members of JY-TV are not related to the Company. The construction on the rental apartments was completed in September 2016, with partial occupancy commencing in June 2016. On February 20, 2018 JY-TV sold the apartments to an unrelated third party.

260 River Corp ("260"). This wholly owned corporation of the Company owns an approximate 70% interest in a vacant commercially zoned building located on 5.4 acres in Montpelier, Vermont. Development of this property is being considered after completing the environmental remediation of the land.

HMG Bayshore, LLC ("HMGBS"). This is a wholly owned Florida limited liability company which owns an investment in an entity which invests in mortgages secured by real estate.

HMG Atlanta, LLC ("HMGATL"). This is a wholly owned Florida limited liability company which owns a 1.5% interest in an entity which owns and operates two residential real estate properties located in north east Atlanta, Georgia.

Baleen Associates, Inc. ("Baleen"). This corporation is wholly owned by CII and its sole asset is a 50% interest in a partnership which operates an executive suite rental business in Coconut Grove, Florida.

Preparation of Financial Statements. The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Income Taxes. The Company qualifies as a real estate investment trust and distributes its taxable ordinary income to stockholders in conformity with requirements of the Internal Revenue Code and is not required to report deferred items due to its ability to distribute all taxable income. In addition, net operating losses can be carried forward to reduce future taxable income but cannot be carried back. Distributed capital gains on sales of real estate as they relate to REIT activities are not subject to taxes; however, undistributed capital gains are taxed as capital gains. State income taxes are not significant. The Company's 95%-owned taxable REIT subsidiary, CII, files a separate income tax return and its operations are not included in the REIT's income tax return. The Company accounts for income taxes in accordance with ASC Topic 740, "Accounting for Income Taxes" ("ASC Topic 740"). This requires a Company to use the asset and liability method of accounting for income taxes. Under this method, deferred income taxes are recognized for the tax consequences of "temporary differences" by applying enacted statutory tax rates applicable to future years to differences between the financial statement carrying amounts and the tax bases of existing assets and liabilities. The effect on deferred income taxes of a change in tax rates is recognized in income in the period that includes the enactment date. Deferred taxes only pertain to CII.

The Company follows the provisions of ASC Topic 740-10, "Accounting for Uncertainty in Income Taxes" which clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with ASC Topic 740, and prescribes a recognition threshold and measurement process for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This topic also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition.

Based on our evaluation, we have concluded that there are no significant uncertain tax positions requiring recognition in our consolidated financial statements. Our evaluation was performed for the tax years ended December 31, 2018 and 2017. The Company's federal income tax returns since 2014 are subject to examination by the Internal Revenue Service, generally for a period of three years after the returns were filed.

We may from time to time be assessed interest or penalties by major tax jurisdictions, although any such assessments historically have been minimal and immaterial to our financial results. In the event we have received an assessment for interest and/or penalties, it has been classified in the consolidated financial statements as selling, general and administrative expense.

Depreciation. Depreciation of the corporate offices properties held for investment is computed using the straight-line method over its estimated useful life of 39.5 years. Depreciation expense for the corporate offices for each of the years ended December 31, 2018 and 2017 was approximately $15,000.

Fair Value of Financial Instruments. The Company records its financial assets and liabilities at fair value, which is defined under the applicable accounting standards as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measure date. The Company uses valuation techniques to measure fair value, maximizing the use of observable outputs and minimizing the use of unobservable inputs. The standard describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value which are the following:

- Level 1 – Quoted prices in active markets for identical assets or liabilities.
- Level 2 – Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 – Inputs include management's best estimate of what market participants would use in pricing the asset or liability at the measurement date. The inputs are unobservable in the market and significant to the instrument's valuation.

An investment's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

The carrying value of financial instruments including other receivables, notes and advances due from related parties (if any), accounts payable and accrued expenses and mortgages and notes payable approximate their fair values at December 31, 2018 and 2017, due to their relatively short terms or variable interest rates.

Cash equivalents are classified within Level 1 or Level 2 of the fair value hierarchy because they are valued using quoted market prices, broker or dealer quotations, or alternative pricing sources with reasonable levels of transparency. Other investments which are measured by investees at net asset value per share or its equivalent are also classified within Level 2.

The valuation of other investments not included above requires significant judgment by the Company's management due to the absence of quoted market values, inherent lack of liquidity and long-term nature of such assets and have been classified within Level 3. Such investments are valued initially based upon transaction price. Valuations are reviewed periodically utilizing available market data and additional factors to determine if the carrying value of these investments should be adjusted. In determining valuation adjustments, emphasis is placed on market participants' assumptions and market-based information over entity-specific information.

Marketable Securities. The entire marketable securities portfolio is classified as trading consistent with the Company's overall investment objectives and activities. Accordingly, all unrealized gains and losses on the Company's marketable securities investment portfolio are included in the Consolidated Statements of Income.

Gross gains and losses on the sale of marketable securities are based on the first-in first-out method of determining cost.

Marketable securities from time to time are pledged as collateral pursuant to broker margin requirements. As of December 31, 2018, there was no such margin balance outstanding. As of December 31, 2017, there was approximately $267,000 of marketable securities pledged as collateral pursuant to margin agreements.

Treasury bills, from time to time, are pledged as collateral pursuant to broker margin requirements. As of December 31, 2018, there was approximately $9.9 million in margin such margin balances outstanding. As of December 31, 2017, there was no such margin balance outstanding.

Notes and other receivables. Management periodically performs a review of amounts due on its notes and other receivable balances to determine if they are impaired based on factors affecting the collectability of those balances. Management's estimates of collectability of these receivables requires management to exercise significant judgment about the timing, frequency and severity of collection losses, if any, and the underlying value of collateral, which may affect recoverability of such receivables. As of December 31, 2018, and 2017, the Company had no allowances for bad debt.

Equity investments. Investments in which the Company does not have a majority voting or financial controlling interest but has the ability to exercise influence are accounted for under the equity method of accounting, even though the Company may have a majority interest in profits and losses. The Company follows ASC Topic 323-30 in accounting for its investments in limited partnerships. This guidance requires the use of the equity method for limited partnership investments of more than 3 to 5 percent.

The Company has no voting or financial controlling interests in its other investments which include entities that invest venture capital funds in growth-oriented enterprises. These other investments are carried at cost less adjustments for other than temporary declines in value.

Income (loss) per common share. Net income (loss) per common share (basic and diluted) is based on the net income (loss) divided by the weighted average number of common shares outstanding during each year. Diluted net loss per share includes the dilutive effect of options to acquire common stock. Common shares outstanding include issued shares less shares held in treasury. There were 1,600 and 12,500 stock options outstanding as of December 31, 2018 and 2017, respectively. The 2018 and 2017 options were not included in the diluted earnings per share computation as their effect would have been de minimums or anti-dilutive.

Gain on sales of properties. Gain on sales of properties is recognized when the minimum investment requirements have been met by the purchaser and title passes to the purchaser.

In February 2018, JY-TV sold its residential apartments located in Orlando, Florida for cash. The Company’s portion of the gain on sale of real estate for this property was approximately $5.5 million (or $5.40 per share), net of incentive fee.

In July 2017 CII sold a 20,000 square foot undeveloped residential parcel of land located in Paxton, Massachusetts for approximately $44,000 and recognized a gain of approximately $10,000.

Cash and cash Equivalents. For purposes of the consolidated statements of cash flows, the Company considers all highly liquid investments with an original maturity of three months or less to be cash and cash equivalents.

Concentration of Credit Risk. Financial instruments that potentially subject the Company to concentration of credit risk are cash and cash equivalent deposits in excess of federally insured limits, marketable securities, other receivables and notes and mortgages receivable. From time to time the Company may have bank deposits in excess of federally insured limits (presently $250,000). The Company evaluates these excess deposits and transfers amounts to brokerage accounts and other banks to mitigate this exposure. As of December 31, 2018, we had no bank deposits in excess of federally insured limits. As of December 31, 2017, we had approximately $52,000 of deposits in excess of federally insured limits. The Company has not experienced any losses in such accounts and believes that it is not exposed to any significant credit risk on cash.

Other intangible assets:

Deferred loan costs, when applicable, are amortized on a straight-line basis over the life of the loan. This method approximates the effective interest rate method.

Noncontrolling Interest. Noncontrolling interest represents the noncontrolling or minority partners' proportionate share of the equity of the Company's majority owned subsidiaries. A summary for the years ended December 31, 2018 and 2017 is as follows:

	2018	2017
Noncontrolling interest balance at beginning of year	$233,000	$223,000
Noncontrolling partners' interest in operating gains of CII	7,000	10,000
Noncontrolling interest balance at end of year	$240,000	$233,000

Revenue recognition. CII is the lessor of the Company's principal executive offices and the Adviser corporate offices. This lease agreement is classified as an operating lease and accordingly all rental revenue is recognized as earned based upon total fixed cash flow over the initial term of the lease, using the straight-line method. In December 2018, the lease was renewed for one year with two one-year extension options expiring on December 1, 2021, with an increase of 5% in rent for each year extended. Beginning in December 2018 the base rent is $58,344 per year payable in equal monthly installments plus sales tax during the term of the lease. The Adviser, ral income tax regardless of the source of such income, or (d) a trust if (i) such trust has validly elected to be treated as a U.S. person for U.S. federal income tax purposes or (ii) a U.S. court is able to exercise primary supervision over the administration of such trust and one or more U.S. persons have the authority to control all substantial decisions of such trust.

Non-U.S. Holders

For purposes of this summary, a non-U.S. Holder is a beneficial owner of units, warrants, or common shares other than a U.S. Holder. This summary does not address the U.S. federal income tax consequences to non-U.S. Holders of the acquisition of units purchased pursuant to this U.S. Preliminary Placement Memorandum, the exercise, disposition, and lapse of warrants, or the acquisition, ownership, and disposition of common shares. Accordingly, a non-U.S. Holder should consult its own financial advisor, legal counsel, or accountant regarding the U.S. federal income, U.S. state and local, and foreign tax consequences (including the potential application of and operation of any income tax treaties) of the acquisition of units purchased pursuant to this U.S. Preliminary Placement Memorandum, the exercise, disposition, and lapse of warrants, and the acquisition, ownership, and disposition of common shares.

U.S. Holders Subject to Special U.S. Federal Income Tax Rules Not Addressed

This summary does not address the U.S. federal income tax consequences applicable to U.S. Holders that are subject to special provisions under the Code, including the following U.S. Holders: (a) U.S. Holders that are tax-exempt organizations, qualified retirement plans, individual retirement accounts, or other tax-deferred accounts; (b) U.S. Holders that are financial institutions, insurance companies, real estate investment trusts, or regulated investment companies; (c) U.S. Holders that are dealers in securities or currencies or U.S. Holders that are traders in securities that elect to apply a mark-to-market accounting method; (d) U.S. Holders that have a functional currency other than the U.S. dollar; (e) U.S. Holders that are liable for the alternative minimum tax under the Code; (f) U.S. Holders that own units, warrants, or common shares as part of a straddle, hedging transaction, conversion transaction, constructive sale, or other

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arrangement involving more than one position; (g) U.S. Holders that acquired units, warrants, or common shares in connection with the exercise of employee stock options or otherwise as compensation for services; (h) U.S. Holders that hold units, warrants, or common shares other than as a capital asset within the meaning of Section 1221 of the Code; or (i) U.S. Holders that own (directly, indirectly, or constructively) 10% or more of the total combined voting power of the outstanding shares of the Corporation. U.S. Holders that are subject to special provisions under the Code, including U.S. Holders described immediately above, should consult their own financial advisor, legal counsel or accountant regarding the U.S. federal income tax consequences of the acquisition of units purchased pursuant to this U.S. Preliminary Placement Memorandum, the exercise, disposition, and lapse of warrants, and the acquisition, ownership, and disposition of common shares.

If an entity that is classified as a partnership for U.S. federal income tax purposes holds units, warrants, or common shares, the U.S. federal income tax consequences to such partnership and the partners of such partnership generally will depend on the activities of the partnership and the status of such partners. Partners of entities that are classified as partnerships for U.S. federal income tax purposes should consult their own financial advisor, legal counsel or accountant regarding the U.S. federal income tax consequences of the acquisition of units purchased pursuant to this U.S. Preliminary Placement Memorandum, the exercise, disposition, and lapse of warrants, and the acquisition, ownership, and disposition of common shares.

Tax Consequences Other than U.S. Federal Income Tax Consequences Not Addressed

This summary does not address the U.S. state and local, U.S. federal estate and gift, or foreign tax consequences to U.S. Holders of the acquisition of units purchased pursuant to this U.S. Preliminary Placement Memorandum, the exercise, disposition, and lapse of warrants, or the acquisition, ownership, and disposition of common shares. Each U.S. Holder should consult its own financial advisor, legal counsel, or accountant regarding the U.S. state and local, U.S. federal estate and gift, and foreign tax consequences of the acquisition of units purchased pursuant to this U.S. Preliminary Placement Memorandum, the exercise, disposition, and lapse of warrants, and the acquisition, ownership, and disposition of common shares.

U.S. Federal Income Tax Consequences of the Acquisition of Units

For U.S. federal income tax purposes, the acquisition of a unit by a U.S. Holder will be treated as the acquisition of an investment unit consisting of two components: one common share and one-half of one warrant. The purchase price for each unit will be allocated between these two components in proportion to their relative fair market values on the date that the unit is purchased by the U.S. Holder. This allocation of the purchase price for each unit will establish a U.S. Holder s initial tax basis in the common share and the one-half of one warrant that comprise each unit for U.S. federal income tax purposes.

For this purpose, the Corporation will allocate U.S.$ 1 of the purchase price for each unit to the common share and U.S.$ 1 of the purchase price for each unit to the one-half of one warrant. The IRS will not be bound by the Corporation s allocation of the purchase price for each unit between the common share and the one-half of one warrant, and accordingly, the IRS may allocate the purchase price for each unit between the common share and the one-half of one warrant in a manner that is different than the allocation set forth above. Each U.S. Holder should consult its own financial advisor, legal counsel, or accountant regarding the allocation of the purchase price for each unit between the common share and the one-half of one warrant.

U.S. Federal Income Tax Consequences of the Exercise and Disposition of Warrants

Exercise of Warrants

A U.S. Holder should not recognize gain or loss on the exercise of a warrant and related receipt of a common share (except if cash is received in lieu of the issuance of a fractional common share). A U.S. Holder s initial tax basis in the common share received on the exercise of a warrant should be equal to the sum of (a) such U.S. Holder s tax basis in such warrant plus (b) the exercise price paid by such U.S. Holder on the exercise of such warrant. A U.S. Holder s holding period for the common share received on the exercise of a warrant should begin on the date that such warrant is exercised by such U.S. Holder.

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Disposition of Warrants

A U.S. Holder will recognize gain or loss on the sale or other taxable disposition of a warrant in an amount equal to the difference, if any, between (a) the amount of cash plus the fair market value of any property received and (b) such U.S. Holder s tax basis in the warrant sold or otherwise disposed of. Subject to the passive foreign investment company rules discussed below, any such gain or loss generally will be a capital gain or loss (provided that the common share to be issued on the exercise of such warrant would have been a capital asset within the meaning of Section 1221 of the Code if acquired by the U.S. Holder), which will be long-term capital gain or loss if the warrant is held for more than one year.

Expiration of Warrants Without Exercise

Upon the lapse or expiration of a warrant, a U.S. Holder will recognize a loss in an amount equal to such U.S. Holder s tax basis in the warrant. Any such loss generally will be a capital loss (provided that the common share to be issued on the exercise of such warrant would have been a capital asset if acquired by the U.S. Holder). Any such capital loss will be short-term capital loss or long-term capital loss, depending on whether the warrants are held for more than one year. Deductions for capital losses are subject to complex limitations under the Code.

Certain Adjustments to the Warrants

Under Section 305 of the Code, an adjustment to the number of common shares that will be issued on the exercise of the warrants, or an adjustment to the exercise price of the warrants, may be treated as a constructive distribution to a U.S. Holder of the warrants if, and to the extent that, such adjustment has the effect of increasing such U.S. Holder s proportionate interest in the earnings and profits or assets of the Corporation, depending on the circumstances of such adjustment (for example, if such adjustment is to compensate for a distribution of cash or other property to shareholders of the Corporation). (See more detailed discussion of the rules applicable to distributions made by the Corporation at Distributions on Common Shares below).

U.S. Federal Income Tax Consequences of the Acquisition, Ownership, and Disposition of Common Shares

Distributions on Common Shares

General Taxation of Distributions

Subject to the passive foreign investment company rules discussed below, a U.S. Holder that receives a distribution, including a constructive distribution, with respect to the common shares will be required to include the amount of such distribution in gross income as a dividend (without reduction for any Canadian income tax withheld from such distribution) to the extent of the current or accumulated earnings and profits of the Corporation. To the extent that a distribution exceeds the current and accumulated earnings and profits of the Corporation, such distribution will be treated (a) first, as a tax-free return of capital to the extent of a U.S. Holder s tax basis in the common shares and, (b) thereafter, as gain from the sale or exchange of such common shares. (See more detailed discussion at Disposition of Common Shares below). Dividends paid on the common shares generally will not be eligible for the dividends received deduction.

Reduced Tax Rates for Certain Dividends

For taxable years beginning before January 1, 2011, a dividend paid by the Corporation generally will be taxed at the preferential tax rates applicable to long-term capital gains if (a) the Corporation is a qualified foreign corporation (as defined below), (b) the U.S. Holder receiving such dividend is an individual, estate, or trust, and (c) such dividend is paid on common shares that have been held by such U.S. Holder for at least 61 days during the 121-day period beginning 60 days before the ex-dividend date.

The Corporation generally will be a qualified foreign corporation under Section 1(h)(11) of the Code (a **QFC**) if (a) the Corporation is eligible for the benefits of the Canada-U.S. Tax Convention, or (b) the common shares are readily tradable on an established securities market in the U.S. However, even if the Corporation satisfies one or more of such requirements, the Corporation will not be treated as a QFC if the Corporation is a passive foreign investment company (as defined below) for the taxable year during which the Corporation pays a dividend or for the preceding taxable year.

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As discussed below, the Corporation anticipates that it may qualify as a passive foreign investment company for the taxable year ending December 31, 2007 and subsequent taxable years, depending on the assets and income of the Corporation over the course of the taxable year ending December 31, 2007. (See more detailed discussion at Additional Rules that May Apply to U.S. Holders Passive Foreign Investment Corporation below). Accordingly, there can be no assurances that the Corporation will be a QFC for the current or any future taxable year or that the Corporation will be able to certify that it is a QFC in accordance with the certification procedures issued by the Treasury and the IRS.

If the Corporation is not a QFC, a dividend paid by the Corporation to a U.S. Holder, including a U.S. Holder that is an individual, estate, or trust, generally will be taxed at ordinary income tax rates (and not at the preferential tax rates applicable to long-term capital gains). The dividend rules are complex, and each U.S. Holder should consult its own financial advisor, legal counsel, or accountant regarding the dividend rules.

Distributions Paid in Foreign Currency

The amount of a distribution paid to a U.S. Holder in foreign currency generally will be equal to the U.S. dollar value of such distribution based on the exchange rate applicable on the date of receipt. A U.S. Holder that does not convert foreign currency received as a distribution into U.S. dollars on the date of receipt generally will have a tax basis in such foreign currency equal to the U.S. dollar value of such foreign currency on the date of receipt. Such a U.S. Holder generally will recognize ordinary income or loss on the subsequent sale or other taxable disposition of such foreign currency (including an exchange for U.S. dollars).

Disposition of Common Shares

A U.S. Holder will recognize gain or loss on the sale or other taxable disposition of common shares in an amount equal to the difference, if any, between (a) the amount of cash plus the fair market value of any property received and (b) such U.S. Holder s tax basis in the common shares sold or otherwise disposed of. Subject to the passive foreign investment company rules discussed below, any such gain or loss generally will be capital gain or loss, which will be long-term capital gain or loss if the common shares are held for more than one year. Gain or loss recognized by a U.S. Holder on the sale or other taxable disposition of common shares generally will be treated as U.S. source for purposes of applying the U.S. foreign tax credit rules. (See more detailed discussion at Foreign Tax Credit below).

Preferential tax rates apply to long-term capital gains of a U.S. Holder that is an individual, estate, or trust. There are currently no preferential tax rates for long-term capital gains of a U.S. Holder that is a corporation. Deductions for capital losses are subject to significant limitations under the Code.

Foreign Tax Credit

A U.S. Holder that pays (whether directly or through withholding) Canadian income tax with respect to dividends received on the common shares generally will be entitled, at the election of such U.S. Holder, to receive either a deduction or a credit for such Canadian income tax paid. Generally, a credit will reduce a U.S. Holder s U.S. federal income tax liability on a dollar-for-dollar basis, whereas a deduction will reduce a U.S. Holder s income subject to U.S. federal income tax. This election is made on a year-by-year basis and applies to all foreign taxes paid (whether directly or through withholding) by a U.S. Holder during a taxable year.

Complex limitations apply to the foreign tax credit, including the general limitation that the credit cannot exceed the proportionate share of a U.S. Holder s U.S. federal income tax liability that such U.S. Holder s foreign source taxable income bears to such U.S. Holder s worldwide taxable income. In applying this limitation, a U.S. Holder s various items of income and deduction must be classified, under complex rules, as either foreign source or U.S. source. In addition, this limitation is calculated separately with respect to specific categories of income. Dividends received on the common shares generally will constitute foreign source income and generally will be categorized as passive income. The foreign tax credit rules are complex, and each U.S. Holder should consult its own financial advisor, legal counsel, or accountant regarding the foreign tax credit rules.

Information Reporting; Backup Withholding Tax

Payments made within the U.S., or by a U.S. payor or U.S. middleman, of dividends on, or proceeds arising from the sale or other taxable disposition of, common shares generally will be subject to information reporting and backup withholding tax, at the rate of 28%, if a U.S. Holder (a) fails to furnish such U.S. Holder s correct U.S. taxpayer identification number (generally on Form W-9), (b) furnishes an incorrect U.S. taxpayer identification number, (c) is notified by the IRS that such U.S. Holder has previously failed to properly report items subject to backup withholding tax, or (d) fails to certify, under penalty of perjury, that such U.S. Holder has furnished its correct U.S. taxpayer identification number and that the IRS has not notified such U.S. Holder that it is subject to backup withholding tax. However, U.S. Holders that are corporations generally are excluded from these information reporting and backup withholding tax rules. Any amounts withheld under the U.S. backup withholding tax rules will be allowed as a credit against a U.S. Holder s U.S. federal income tax liability, if any, or will be refunded, if such U.S. Holder furnishes required information to the IRS. Each U.S. Holder should consult its own financial advisor, legal counsel, or accountant regarding the information reporting and backup withholding tax rules.

Information Filing Required by Certain U.S. Holders

A U.S. Holder may be required to file Form 926 with the IRS if (a) immediately after acquiring the units pursuant to this U.S. Preliminary Placement Memorandum, such U.S. Holder owns, directly or indirectly, at least 10% of the total voting power or the total value of the outstanding shares of the Corporation or (b) the purchase price of the units, when aggregated with all other transfers of cash by such U.S. Holder (or any person related to such U.S. Holder) to the Corporation within the preceding 12 month period, exceeds U.S.$100,000. A U.S. Holder that fails to properly and timely file Form 926 with the IRS generally will be subject to a penalty equal to 10% of the purchase price for the units (subject to a maximum penalty of U.S.$100,000, unless the failure to file is due to intentional disregard). Each U.S. Holder should consult its own financial advisor, legal counsel, or accountant regarding the information reporting requirements that may apply with respect to the acquisition of the units.

Additional Rules that May Apply to U.S. Holders

If the Corporation is a passive foreign investment company (as defined below), the preceding sections of this summary may not describe the U.S. federal income tax consequences to U.S. Holders of the acquisition, ownership, and disposition of common shares.

Passive Foreign Investment Corporation

The Corporation generally will be a passive foreign investment company under Section 1297 of the Code (a **PFIC**) if, for a taxable year, (a) 75% or more of the gross income of the Corporation for such taxable year is passive income or (b) on average, 50% or more of the assets held by the Corporation either produce passive income or are held for the production of passive income, based on the fair market value of such assets (or on the adjusted tax basis of such assets, if the Corporation is not publicly traded and either is a controlled foreign corporation or makes an election). Passive income includes, for example, dividends, interest, certain rents and royalties, certain gains from the sale of stock and securities, and certain gains from commodities transactions. Active business gains arising from the sale of commodities generally are excluded from passive income if substantially all of a foreign corporation s commodities are (a) stock in trade of such foreign corporation or other property of a kind which would properly be included in inventory of such foreign corporation, or property held by such foreign corporation primarily for sale to customers in the ordinary course of business, (b) property used in the trade or business of such foreign corporation that would be subject to the allowance for depreciation under Section 167 of the Code, or (c) supplies of a type regularly used or consumed by such foreign corporation in the ordinary course of its trade or business.

For purposes of the PFIC income test and asset test described above, if the Corporation owns, directly or indirectly, 25% or more of the total value of the outstanding shares of another corporation, the Corporation will be treated as if it (a) held a proportionate share of the assets of such other corporation and (b) received directly a proportionate share of the income of such other corporation. In addition, for purposes of the PFIC income test and asset test described above, passive income does not include any interest, dividends, rents, or royalties that are received or accrued by the Corporation from a related person (as defined in Section 954(d)(3) of the Code), to the extent such items are properly allocable to the income of such related person that is not passive income.

In addition, if the Corporation is a PFIC and owns shares of another foreign corporation that also is a PFIC, under certain indirect ownership rules, a disposition of the shares of such other foreign corporation or a distribution received from such other foreign corporation generally will be treated as an indirect disposition by a U.S. Holder or an indirect

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distribution received by a U.S. Holder, subject to the rules of Section 1291 of the Code discussed below. To the extent that gain recognized on the actual disposition by a U.S. Holder of the common shares or income recognized by a U.S. Holder on an actual distribution received on the common shares was previously subject to U.S. federal income tax under these indirect ownership rules, such amount generally should not be subject to U.S. federal income tax.

The Corporation anticipates that it may qualify as a PFIC for the taxable year ending December 31, 2007 and for subsequent taxable years. Whether the Corporation will, in fact, qualify as a PFIC for the taxable year ending December 31, 2007 will depend on the assets and income of the Corporation over the course of the taxable year ending December 31, 2007 and, as a result, cannot be predicted with certainty as of the date of this U.S. Preliminary Private Placement Memorandum. Each U.S. Holder should consult its own financial advisor, legal counsel, or accountant regarding whether the Corporation will qualify as a PFIC for the taxable year ending December 31, 2007 and in subsequent taxable years.

Default PFIC Rules Under Section 1291 of the Code

If the Corporation is a PFIC, the U.S. federal income tax consequences to a U.S. Holder of the acquisition, ownership, and disposition of common shares will depend on whether such U.S. Holder makes an election to treat the Corporation as a qualified electing fund or QEF under Section 1295 of the Code (a **QEF Election**) or a mark-to-market election under Section 1296 of the Code (a **Mark-to-Market Election**). A U.S. Holder that does not make either a QEF Election or a Mark-to-Market Election will be referred to in this summary as a Non-Electing U.S. Holder.

A Non-Electing U.S. Holder will be subject to the rules of Section 1291 of the Code with respect to (a) any gain recognized on the sale or other taxable disposition of common shares and (b) any excess distribution paid on the common shares. A distribution generally will be an excess distribution to the extent that such distribution (together with all other distributions received in the current taxable year) exceeds 125% of the average distributions received during the three preceding taxable years (or during a U.S. Holder s holding period for the common shares, if shorter).

Under Section 1291 of the Code, any gain recognized on the sale or other taxable disposition of common shares, and any excess distribution paid on the common shares, must be ratably allocated to each day in a Non-Electing U.S. Holder s holding period for the common shares. The amount of any such gain or excess distribution allocated to prior years of such Non-Electing U.S. Holder s holding period for the common shares (other than years prior to the first taxable year of the Corporation beginning after December 31, 1986 for which the Corporation was not a PFIC) will be subject to U.S. federal income tax at the highest tax applicable to ordinary income in each such prior year. A Non-Electing U.S. Holder will be required to pay interest on the resulting tax liability for each such prior year, calculated as if such tax liability had been due in each such prior year. Such a Non-Electing U.S. Holder that is not a corporation must treat any such interest paid as personal interest, which is not deductible. The amount of any such gain or excess distribution allocated to the current year of such Non-Electing U.S. Holder s holding period for the common shares will be treated as ordinary income in the current year, and no interest charge will be incurred with respect to the resulting tax liability for the current year.

If the Corporation is a PFIC for any taxable year during which a Non-Electing U.S. Holder holds common shares, the Corporation will continue to be treated as a PFIC with respect to such Non-Electing U.S. Holder, regardless of whether the Corporation ceases to be a PFIC in one or more subsequent years. A Non-Electing U.S. Holder may terminate this deemed PFIC status by electing to recognize gain (which will be taxed under the rules of Section 1291 of the Code discussed above) as if such common shares were sold on the last day of the last taxable year for which the Corporation was a PFIC.

QEF Election

A U.S. Holder that makes a QEF Election generally will not be subject to the rules of Section 1291 of the Code discussed above. However, a U.S. Holder that makes a QEF Election will be subject to U.S. federal income tax on such U.S. Holder s pro rata share of (a) the net capital gain of the Corporation, which will be taxed as long-term capital gain to such U.S. Holder, and (b) the ordinary earnings of the Corporation, which will be taxed as ordinary income to such U.S. Holder. Generally, net capital gain is the excess of (a) net long-term capital gain over (b) net short-term capital loss, and ordinary earnings are the excess of (a) earnings and profits over (b) net capital gain. A U.S. Holder that makes a QEF Election will be subject to U.S. federal income tax on such amounts for each taxable year in which the Corporation is a PFIC, regardless of whether such amounts are actually distributed to such U.S. Holder by the Corporation. However, a U.S. Holder that makes a QEF Election may, subject to certain limitations, elect to defer payment of current U.S. federal

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income tax on such amounts, subject to an interest charge. If such U.S. Holder is not a corporation, any such interest paid will be treated as personal interest, which is not deductible.

A U.S. Holder that makes a QEF Election generally (a) may receive a tax-free distribution from the Corporation to the extent that such distribution represents earnings and profits of the Corporation that were previously included in income by the U.S. Holder because of such QEF Election and (b) will adjust such U.S. Holder s tax basis in the common shares to reflect the amount included in income or allowed as a tax-free distribution because of such QEF Election. In addition, a U.S. Holder that makes a QEF Election generally will recognize capital gain or loss on the sale or other taxable disposition of common shares.

The procedure for making a QEF Election, and the U.S. federal income tax consequences of making a QEF Election, will depend on whether such QEF Election is timely. A QEF Election will be treated as timely if such QEF Election is made for the first year in the U.S. Holder s holding period for the common shares in which the Corporation was a PFIC. A U.S. Holder may make a timely QEF Election by filing the appropriate QEF Election documents at the time such U.S. Holder files a U.S. federal income tax return for such first year. However, if the Corporation was a PFIC in a prior year, then in addition to filing the QEF Election documents, a U.S. Holder must elect to recognize (a) gain (which will be taxed under the rules of Section 1291 of the Code discussed above) as if the common shares were sold on the qualification date or (b) if the Corporation was also a CFC, such U.S. Holder s pro rata share of the post-1986 earnings and profits of the Corporation as of the qualification date. The qualification date is the first day of the first taxable year in which the Corporation was a QEF with respect to such U.S. Holder. The election to recognize such gain or earnings and profits can only be made if such U.S. Holder s holding period for the common shares includes the qualification date. By electing to recognize such gain or earnings and profits, such U.S. Holder will be deemed to have made a timely QEF Election. In addition, under very limited circumstances, a U.S. Holder may make a retroactive QEF Election if such U.S. Holder failed to file the QEF Election documents in a timely manner.

A QEF Election will apply to the taxable year for which such QEF Election is made and to all subsequent taxable years, unless such QEF Election is invalidated or terminated or the IRS consents to revocation of such QEF Election. If a U.S. Holder makes a QEF Election and, in a subsequent taxable year, the Corporation ceases to be a PFIC, the QEF Election will remain in effect (although it will not be applicable) during those taxable years in which the Corporation is not a PFIC. Accordingly, if the Corporation becomes a PFIC in another subsequent taxable year, the QEF Election will be effective and the U.S. Holder will be subject to the QEF rules described above during any such subsequent taxable year in which the Corporation qualifies as a PFIC. In addition, the QEF Election will remain in effect (although it will not be applicable) with respect to a U.S. Holder even after such U.S. Holder disposes of all of such U.S. Holder s direct and indirect interest in the common shares. Accordingly, if such U.S. Holder reacquires an interest in the Corporation, such U.S. Holder will be subject to the QEF rules described above for each taxable year in which the Corporation is a PFIC.

Each U.S. Holder should consult its own financial advisor, legal counsel, or accountant regarding the availability of, and procedure for making, a QEF Election. The Corporation will make available to U.S. Holders, upon their request, timely and accurate information as to its status as a PFIC and will use commercially reasonable efforts to provide to a purchaser acquiring common shares pursuant to this Private Placement Memorandum that is a U.S. Holder all information that a U.S. Holder making a QEF Election is required to obtain for U.S. federal income tax purposes.

Under applicable Treasury Regulations, a person that holds an option, warrant, or other right to acquire shares of a PFIC may not make a QEF Election that will apply to either (a) the option, warrant, or other right or (b) the shares of the PFIC subject to the option, warrant, or other right. In addition, under Treasury Regulations, if a person holds an option, warrant, or other right to acquire shares of a PFIC, the holding period with respect to the shares of the PFIC acquired on the exercise of such option, warrant, or other right will include the period that the option, warrant, or other right was held.

Accordingly, a U.S. Holder of the warrants may not make a QEF Election that will apply to either the warrants or the common shares subject to the warrants. The general effect of these special rules is that (a) excess distributions paid on common shares acquired on exercise of the warrants, and gains recognized on the sale or other taxable disposition of common shares acquired on exercise of the warrants, will be spread over a U.S. Holder s entire holding period for such warrants and common shares (pursuant to the rules of Section 1291 of the Code discussed above) and (b) if a U.S. Holder makes a QEF Election on the exercise of the warrants and receipt of the common shares, that election generally will not be a timely QEF Election with respect to such common shares (and the rules of Section 1291 of the Code discussed above will continue to apply). It appears, however, that a U.S. Holder receiving common shares on the exercise of the warrants should be eligible to make an effective QEF Election as of the first day of the taxable year of such U.S. Holder beginning after the receipt of such common shares if such U.S. Holder also makes an election to recognize gain (which will be taxed under the rules of Section 1291 of the Code discussed above) as if such common shares were sold on such date at fair market value. In addition, gain recognized on the sale or other taxable disposition (other than by exercise) of the warrants by a U.S. Holder will be subject to the rules of Section 1291 of the Code discussed above. Each U.S. Holder should consult its own financial advisor, legal counsel, or accountant regarding the application of the PFIC rules to the warrants and the common shares. received on exercise of the warrants.

Mark-to-Market Election

A U.S. Holder may make a Mark-to-Market Election only if the common shares are marketable stock. The common shares generally will be marketable stock if the common shares are regularly traded on a qualified exchange or other market. For this purpose, a qualified exchange or other market includes (a) a national securities exchange that is registered with the Securities and Exchange Commission, (b) the national market system established pursuant to section 11A of the Securities and Exchange Act of 1934, or (c) a foreign securities exchange that is regulated or supervised by a governmental authority of the country in which the market is located, provided that (i) such foreign exchange has trading volume, listing, financial disclosure, surveillance, and other requirements designed to prevent fraudulent and manipulative acts and practices, remove impediments to and perfect the mechanism of a free, open, fair, and orderly market, and protect investors (and the laws of the country in which the foreign exchange is located and the rules of the foreign exchange ensure that such requirements are actually enforced) and (ii) the rules of such foreign exchange effectively promote active trading of listed stocks. If the common shares are traded on such a qualified exchange or other market, the common shares generally will be regularly traded for any calendar year during which the common shares are traded, other than in de minimis quantities, on at least 15 days during each calendar quarter.

A U.S. Holder that makes a Mark-to-Market Election generally will not be subject to the rules of Section 1291 of the Code discussed above. However, if a U.S. Holder makes a Mark-to-Market Election after the beginning of such U.S. Holder s holding period for the common shares and such U.S. Holder has not made a timely QEF Election, the rules of Section 1291 of the Code discussed above will apply to certain dispositions of, and distributions on, the common shares.

A U.S. Holder that makes a Mark-to-Market Election will include in ordinary income, for each taxable year in which the Corporation is a PFIC, an amount equal to the excess, if any, of (a) the fair market value of the common shares as of the close of such taxable year over (b) such U.S. Holder s adjusted tax basis in such common shares. A U.S. Holder that makes a Mark-to-Market Election will be allowed a deduction in an amount equal to the lesser of (a) the excess, if any, of (i) such U.S. Holder s adjusted tax basis in the common shares over (ii) the fair market value of such common shares as of the close of such taxable year or (b) the excess, if any, of (i) the amount included in ordinary income because of such Mark-to-Market Election for prior taxable years over (ii) the amount allowed as a deduction because of such Mark-to-Market Election for prior taxable years.

A U.S. Holder that makes a Mark-to-Market Election generally also will adjust such U.S. Holder s tax basis in the common shares to reflect the amount included in gross income or allowed as a deduction because of such Mark-to-Market Election. In addition, upon a sale or other taxable disposition of common shares, a U.S. Holder that makes a Mark-to-Market Election will recognize ordinary income or loss (not to exceed the excess, if any, of (a) the amount included in ordinary income because of such Mark-to-Market Election for prior taxable years over (b) the amount allowed as a deduction because of such Mark-to-Market Election for prior taxable years).

A Mark-to-Market Election applies to the taxable year in which such Mark-to-Market Election is made and to each subsequent taxable year, unless the common shares cease to be marketable stock or the IRS consents to revocation of such election. Each U.S. Holder should consult its own financial advisor, legal counsel, or accountant regarding the availability of, and procedure for making, a Mark-to-Market Election.

Other PFIC Rules

Under Section 1291(f) of the Code, the IRS has issued proposed Treasury Regulations that, subject to certain exceptions, would cause a U.S. Holder that had not made a timely QEF Election to recognize gain (but not loss) upon certain transfers of common shares that would otherwise be tax-deferred (e.g., gifts and exchanges pursuant to corporate reorganizations). However, the specific U.S. federal income tax consequences to a U.S. Holder may vary based on the manner in which common shares are transferred.

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Certain additional adverse rules will apply with respect to a U.S. Holder if the Corporation is a PFIC, regardless of whether such U.S. Holder makes a QEF Election. For example under Section 1298(b)(6) of the Code, a U.S. Holder that uses common shares as security for a loan will, except as may be provided in Treasury Regulations, be treated as having made a taxable disposition of such common shares.

The PFIC rules are complex, and each U.S. Holder should consult its own financial advisor, legal counsel, or accountant regarding the PFIC rules and how the PFIC rules may affect the U.S. federal income tax consequences of the acquisition, ownership, and disposition of common shares.

LEGAL MATTERS

Certain legal matters relating to the securities offered hereby will be passed upon on behalf of us by Bennett Jones LLP and Dorsey & Whitney LLP and on behalf of the underwriter by Fasken Martineau DuMoulin LLP and White & Case LLP. The partners and associates of each of Bennett Jones LLP and Fasken Martineau DuMoulin LLP, as a group, beneficially own, directly or indirectly, less than 1% of our securities.

LEGAL PROCEEDINGS

We are not involved in or aware of any present or pending legal proceedings against us involving us jointly or separately as a party.

AUDITORS, TRANSFER AGENT AND REGISTRAR

Our auditors are Ernst & Young LLP, Chartered Accountants, 1000, 440-2nd Avenue S.W., Calgary, Alberta T2P 5E9.

The transfer agent and registrar for our common shares is Computershare Trust Company of Canada at its principal offices in the cities of Calgary, Alberta and Toronto, Ontario.

STATUTORY RIGHTS OF WITHDRAWAL AND RESCISSION

Securities legislation in certain of the provinces of Canada provides purchasers with the right to withdraw from an agreement to purchase securities. This right may be exercised within two business days after receipt or deemed receipt of a prospectus and any amendment. In several of the provinces, securities legislation further provides a purchaser with remedies for rescission or, in some jurisdictions, damages if the prospectus and any amendment contains a misrepresentation or is not delivered to the purchaser, provided that the remedies for rescission or damages are exercised by the purchaser within the time limit prescribed by the securities legislation of the purchaser s province. The purchaser should refer to any applicable provisions of the securities legislation of the purchaser s province for the particulars of these rights or consult with a legal adviser.

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PART II
INFORMATION NOT REQUIRED TO BE DELIVERED TO OFFEREES OR PURCHASERS

Under the *Business Corporations Act* (Alberta), Oncolytics Biotech Inc. (the Corporation) may indemnify a director or officer, a former director or officer, or a person who acts or acted at the Corporation s request as a director or officer or a body corporate of which the Corporation is or was a shareholder or creditor, and the director s or officer s heirs and legal representatives, against all costs, charges and expenses, including an amount paid to settle an action or satisfy a judgment, reasonably incurred by the individual in respect of any civil, criminal or administrative action or proceeding to which the individual is involved because of that association with the Corporation or other entity, and the Corporation may advance moneys to such an individual for the costs, charges and expenses of such a proceeding. The Corporation may not indemnify such an individual unless the individual acted honestly and in good faith with a view to the best interests of the Corporation, or, as the case may be, to the best interests of the other entity for which the individual acted as a director or officer or in a similar capacity at the Corporation s request, and, in the case of a criminal or administrative action or proceeding that is enforced by a monetary penalty, the individual had reasonable grounds for believing that the individual s conduct was lawful. In addition, the individual must repay any moneys advanced by the Corporation if the individual has not fulfilled the conditions set out in the preceding sentence. Such indemnification or advance of moneys may be made in connection with a derivative action only with court approval. Such an individual is entitled to indemnification from the Corporation as a matter of right if the individual was not judged by the court or other competent authority to have committed any fault or omitted to do anything that the individual ought to have done, and the individual fulfilled the conditions set forth above.

In accordance with and subject to the *Business Corporations Act* (Alberta), the by-laws of the Corporation provide that the Corporation shall indemnify a director or officer, a former director or officer, or a person who acts or acted at the Corporation s request as a director or officer, or a body corporate of which the Corporation is or was a shareholder or creditor, and the director s or officer s heirs and legal representatives, against all costs, charges and expenses, including an amount paid to settle an action or satisfy a judgment, reasonably incurred by him in respect of any civil, criminal or administrative action or proceeding to which he is made a party by reason of being or having been a director or officer of the Corporation or other entity if he acted honestly and in good faith with a view to the best interests of the Corporation or, as the case may be, to the best interests of the other entity for which he acted as a director or officer at the Corporation s request, and, in the case of a criminal or administrative action or proceeding that is enforced by monetary penalty, he had reasonable grounds for believing that his conduct was lawful. The Corporation shall also indemnify such person in such other circumstances as the *Business Corporations Act* (Alberta) permits or requires.

The Corporation maintains a directors & officers insurance policy for the benefit of the directors and officers of the Corporation and its subsidiaries against liability incurred by them in their official capacities for which they become obligated to pay to the extent permitted by applicable law.

Insofar as indemnification for liabilities arising under the U.S. Securities Act of 1933, as amended, may be permitted to directors, officers or persons controlling the Corporation pursuant to the foregoing provisions, the Corporation has been informed that, in the opinion of the U.S. Securities and Exchange Commission, such indemnification is against public policy as expressed in the Securities Act and is therefore unenforceable.

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EXHIBITS

Exhibit Number	Description
3.1	Form of Underwriting Agreement dated as of February ___, 2007*
4.1	Renewal Annual Information Form dated March 2, 2006, for the year ended December 31, 2005, incorporated by reference to the Corporation s Annual Report of Form 40-F, filed with the Commission on March 3, 2006
4.2	Audited financial statements, together with the accompanying notes to the financial statements, for the fiscal years ended December 31, 2005 and 2004 and the auditors report thereon addressed to the Corporation s shareholders, incorporated by reference to the Corporation s Annual Report on Form 40-F, filed with the Commission on March 3, 2006
4.3	Management Proxy Circular dated March 24, 2006 relating to the annual and special meeting of shareholders held on April 26, 2006, excluding those portions which are not prescribed by Canadian securities law to be included in the Canadian Prospectus, incorporated by reference to the Corporation s Current Report on Form 6-K, furnished to the Commission on March 31, 2006
4.4	Management s discussion and analysis of financial condition and results of operations dated March 2, 2006, for the year ended December 31, 2005, incorporated by reference to the Corporation s Annual Report on Form 40-F, filed with the Commission on March 3, 2006
4.5	Unaudited interim financial statements as at September 30, 2006 and for the three and nine months ended September 30, 2006, together with the notes thereto, incorporated by reference to the Corporation s Current Report on Form 6-K, furnished to the Commission on November 3, 2006
4.6	Management s discussion and analysis of financial condition and results of operations dated November 2, 2006, for the three and nine months ended September 30, 2006, incorporated by reference to the Corporation s Current Report on Form 6-K, furnished to the Commission on November 3, 2006
4.7	Reconciliation of financial statements as at September 30, 2006 and for the three and nine months ended September 30, 2006, incorporated by reference to the Corporation s Current Report on Form 6-K, furnished to the Commission on February 5, 2007
5.1	Consent of Ernst & Young LLP dated February 5, 2007
5.2	Consent of Bennett Jones LLP dated February 5, 2007
5.3	Consent of Fasken Martineau DuMoulin LLP dated February 5, 2007
6.1	Powers of Attorney (included on the signature pages of this Registration Statement)
7.1	Warrant Indenture, dated as of February ___, 2007, between the Corporation and Computershare Trust Company of Canada, as trustee*

*

To be filed by amendment

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PART III
UNDERTAKING AND CONSENT TO SERVICE OF PROCESS

Item 1. Undertaking

The Registrant undertakes to make available, in person or by telephone, representatives to respond to inquiries made by the Commission staff, and to furnish promptly, when requested to do so by the Commission staff, information relating to the securities registered pursuant to this Form F-10 or to transactions in said securities.

Item 2. Consent to Service of Process

Concurrently with the filing of this Registration Statement on Form F-10, the Registrant is filing with the Commission a written irrevocable consent and power of attorney on Form F-X.

Any change to the name and address of the agent for service of the Registrant will be communicated promptly to the Commission by amendment to Form F-X referencing the file number of this Registration Statement.

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Signatures

Pursuant to the requirements of the Securities Act, the Registrant certifies that it has reasonable grounds to believe that it meets all of the requirements for filing on Form F-10 and has duly caused this Registration Statement to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Calgary, Province of Alberta, Canada, on February 5, 2007.

ONCOLYTICS BIOTECH INC.

By: /s/ Bradley G. Thompson
Bradley G. Thompson
Chief Executive Officer

Each person whose signature appears below constitutes and appoints Bradley G. Thompson and Douglas A. Ball, and each of them, either of whom may act without the joinder of the other, as his true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution, for him and in his name, place and stead, in any and all capacities, to sign any or all amendments (including post-effective amendments) to this Registration Statement and registration statements filed pursuant to Rule 429 under the Securities Act, and to file the same, with all exhibits thereto and other documents in connection therewith, with the U.S. Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, each acting alone, full power and authority to do and perform each and every act and thing requisite and necessary to be done, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, each acting alone, or their substitute or substitutes may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Act, this Registration Statement has been signed by or on behalf of the following persons in the capacities indicated on February 5, 2007:

Signature	Title
/s/ Bradley G. Thompson Bradley G. Thompson	President, Chief Executive Officer and Chairman of the Board (Principal Executive Officer)
/s/ Douglas A. Ball Douglas A. Ball	Chief Financial Officer and Director (Principal Financial and Accounting Officer)
/s/ William A. Cochrane William A. Cochrane	Director
/s/ Ger J. van Amersfoort Ger J. van Amersfoort	Director

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Signature	**Title**
/s/ Robert B. Schultz	Director
Robert B. Schultz	
/s/ Fred A. Stewart	Director
Fred A. Stewart	
/s/ Ed Levy	Director
Ed Levy	
/s/ J. Mark Lievonen	Director
J. Mark Lievonen	
/s/ Jim Dinning	Director
Jim Dinning	

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Authorized representative

Pursuant to the requirements of Section 6(a) of the Securities Act of 1933, the Authorized Representative has signed this Registration Statement, solely in his capacity as the duly authorized representative of Oncolytics Biotech Inc. in the United States, in the State of California, on February 5, 2007.

By:

/s/ Karl Mettinger
Name: Karl Mettinger
Title: Chief Medical Officer

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