

GYRODYNE CO OF AMERICA INC

Form 10-Q

November 14, 2012

FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

(Mark One)

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

For the quarterly period ended September 30, 2012

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 0-1684

Gyrodyne Company of America, Inc.  
(Exact name of registrant as specified in its charter)

New York  
(State or other jurisdiction of incorporation or organization)

11-1688021  
(I.R.S. Employer Identification No.)

1 Flowerfield, Suite 24, St. James, NY 11780  
(Address and Zip Code of principal executive offices)

(631) 584-5400  
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

No  X

On November 13, 2012, 1,482,680 shares of the Registrant's common stock, par value \$1.00 per share, were outstanding.

Seq. Page 1

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INDEX TO QUARTERLY REPORT OF GYRODYNE COMPANY OF AMERICA, INC.  
 QUARTER ENDED SEPTEMBER 30, 2012

	Seq. Page
Form 10-Q Cover	1
Index to Form 10-Q	2
<b>PART I - FINANCIAL INFORMATION</b>	<b>3</b>
Item 1. Financial Statements.	3
Condensed Consolidated Balance Sheets as of September 30, 2012 (unaudited) and December 31, 2011	3
Condensed Consolidated Statements of Operations (unaudited)	4
Condensed Consolidated Statements of Comprehensive Income (Loss) (unaudited)	5
Condensed Consolidated Statements of Cash Flows (unaudited)	6
Notes to Condensed Consolidated Financial Statements	7
Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations.	14
Item 3. Quantitative and Qualitative Disclosures About Market Risk.	22
Item 4. Controls and Procedures.	22
<b>PART II - OTHER INFORMATION</b>	<b>22</b>
Item 1. Legal Proceedings.	22
Item 6. Exhibits.	23
<b>SIGNATURES</b>	<b>24</b>
<b>EXHIBIT INDEX</b>	<b>25</b>

## PART I - FINANCIAL INFORMATION

## Item 1. Financial Statements.

GYRODYNE COMPANY OF AMERICA, INC.  
AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS

	September 30, 2012 (Unaudited)	December 31, 2011
<b>ASSETS</b>		
<b>REAL ESTATE</b>		
Rental property:		
Land	\$5,163,093	\$5,163,093
Building and improvements	33,158,756	32,855,932
Machinery and equipment	343,272	338,275
	38,665,121	38,357,300
Less accumulated depreciation	6,054,011	5,381,026
	32,611,110	32,976,274
Land held for development:		
Land	558,466	558,466
Land development costs	1,689,242	1,607,600
	2,247,708	2,166,066
Total real estate, net	34,858,818	35,142,340
Cash and cash equivalents	171,899,892	10,375,994
Investment in marketable securities	4,881,745	-
Rent receivable, net of allowance for doubtful accounts of \$60,000 and \$103,000, respectively	101,564	83,942
Deferred rent receivable	199,655	137,220
Prepaid expenses and other assets	1,048,316	1,002,250
Prepaid pension costs	1,068,310	1,064,843
Total Assets	\$214,058,300	\$47,806,589
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>LIABILITIES:</b>		
Accounts payable	\$617,341	\$333,936
Accrued liabilities	502,517	456,166
Deferred rent liability	81,867	83,047
Tenant security deposits payable	466,322	486,861
Mortgage loans payable	20,682,314	21,143,780
Deferred income taxes	62,964,000	1,315,000
Total Liabilities	85,314,361	23,818,790
Commitments and contingencies		
<b>STOCKHOLDERS' EQUITY:</b>		
	1,723,888	1,723,888

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Common stock, \$1 par value; authorized 4,000,000 shares; 1,723,888 shares issued; 1,482,680 shares outstanding		
Additional paid-in capital	17,753,504	17,747,069
Accumulated other comprehensive income	349,418	292,031
Balance of undistributed income	110,454,826	5,762,508
	130,281,636	25,525,496
Less cost of shares of common stock held in treasury; 241,208	(1,537,697 )	(1,537,697 )
Total Stockholders' Equity	128,743,939	23,987,799
Total Liabilities and Stockholders' Equity	\$214,058,300	\$47,806,589

See notes to condensed consolidated financial statements

Seq. Page 3

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## GYRODYNE COMPANY OF AMERICA, INC.

AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
(UNAUDITED)

	Nine Months Ended September 30		Three Months Ended September 30,	
	2012	2011	2012	2011
<b>Revenues</b>				
Rental income	\$3,348,005	\$3,691,533	\$1,059,576	\$1,224,553
Rental income - tenant reimbursements	429,668	456,936	137,037	152,222
Total	3,777,673	4,148,469	1,196,613	1,376,775
<b>Expenses</b>				
Rental expenses	1,733,083	1,777,307	582,901	562,898
General and administrative expenses	1,731,825	1,343,816	779,563	436,088
Depreciation	672,985	616,936	225,229	208,126
Total	4,137,893	3,738,059	1,587,693	1,207,112
<b>Other Income (Expense):</b>				
Interest income	64,292	541	22,514	398
Interest expense	(764,322 )	(918,763 )	(251,305 )	(305,680 )
Total	(700,030 )	(918,222 )	(228,791 )	(305,282 )
<b>Net Loss before Condemnation Income and Provision for Income Taxes</b>				
Income (expense) on condemnation	100,030,852	(238,990 )	(17,839 )	(17,299 )
Interest income on condemnation	67,370,716	-	104,928	-
<b>Net Income (Loss) before Provision for Income Taxes</b>				
Provision for Income Taxes	166,341,318	(746,802 )	(532,782 )	(152,918 )
Net Income (Loss)	\$104,692,318	\$(746,802 )	\$(532,782 )	\$(152,918 )
<b>Net income (loss) per common share:</b>				
Basic and diluted	\$70.61	\$(0.58 )	\$(0.36 )	\$(0.12 )
<b>Weighted average number of common shares outstanding:</b>				
Basic and diluted	1,482,680	1,292,862	1,482,680	1,298,415

See notes to condensed consolidated financial statements

GYRODYNE COMPANY OF AMERICA, INC.  
AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)  
(UNAUDITED)

	Nine Months Ended September 30,		Three Months Ended September 30,	
	2012	2011	2012	2011
Net Income (loss)	\$ 104,692,318	\$(746,802)	\$(532,782)	\$(152,918)
Other comprehensive income:				
Unrealized gain on investments	57,387	-	42,945	-
Recognition of unrealized gain on interest rate swap	-	107,718	-	37,479
Other comprehensive income	57,387	107,718	42,945	37,479
Comprehensive income (loss)	\$ 104,749,705	\$(639,084)	\$(489,837)	\$(115,439)

See notes to condensed consolidated financial statements

Seq. Page 5

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GYRODYNE COMPANY OF AMERICA, INC.  
AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)

	Nine Months Ended September 30,	
	2012	2011
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net income (loss)	\$ 104,692,318	\$(746,802 )
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	700,357	645,536
Bad debt expense	18,000	18,000
Net periodic pension benefit income	(3,467 )	(31,041 )
Changes in operating assets and liabilities:		
(Increase) decrease in assets:		
Rent receivable	(35,622 )	(99,631 )
Deferred rent receivable	(62,435 )	(30,120 )
Prepaid expenses and other assets	(67,327 )	39,926
Increase (decrease) in liabilities:		
Accounts payable	283,405	(90,007 )
Accrued liabilities	46,351	111,088
Deferred rent liability	(1,180 )	149,553
Tenant security deposits	(20,539 )	17,751
Deferred income taxes	61,649,000	-
Total adjustments	62,506,543	731,055
Net cash provided by (used in) operating activities	167,198,861	(15,747 )
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchase of building improvements and equipment	(311,461 )	(761,319 )
Land development costs	(81,642 )	(120,736 )
Purchases of marketable securities	(5,350,518 )	-
Principal repayments on investment in marketable securities	526,159	-
Net cash used in investing activities	(5,217,462 )	(882,055 )
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Principal payments on mortgage loans payable	(461,466 )	(439,562 )
Loan origination fees paid	(2,471 )	(10,500 )
Proceeds from escrow	-	250,000
Issuance of common shares, net	-	9,987,476
Proceeds from other equity transactions, net	6,436	-
Net cash (used in) provided by financing activities	(457,501 )	9,787,414
Net increase in cash and cash equivalents	161,523,898	8,889,612
Cash and cash equivalents at beginning of period	10,375,994	2,141,522
Cash and cash equivalents at end of period	\$ 171,899,892	\$ 11,031,134



Supplemental cash flow information:

Interest paid	\$770,028	918,763
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See notes to condensed consolidated financial statements

Seq. Page 6

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## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

### 1. The Company:

Gyrodyne Company of America, Inc. (“Gyrodyne” or the “Company”) is a self-managed and self-administered real estate investment trust (“REIT”) formed under the laws of the State of New York. The Company manages its business as one segment. The Company’s primary business is the investment in and the acquisition, ownership and management of a geographically diverse portfolio of medical office and industrial properties and development of industrial and residential properties, located in the Northeast and mid – Atlantic regions of the United States. Substantially all of the Company’s rental properties are subject to net leases in which the tenant must reimburse Gyrodyne for a portion, all of or substantially all of the costs and/ or cost increases for utilities, insurance, repairs and maintenance, and real estate taxes. Certain leases provide that the Company is responsible for certain operating costs.

As of September 30, 2012, the Company had 100% ownership in three medical office parks comprising an aggregate of approximately 131,000 rentable square feet and a multitenant industrial park comprising approximately 128,000 rentable square feet. In addition, the Company has approximately 68 acres of property in St. James, New York, approximately 10 acres of which are utilized by the industrial park, and an estimated 9.32% limited partnership interest in a limited partnership (the “Grove”) which owns an undeveloped Florida property (the “Grove Property”).

The Company has qualified, and expects to continue to qualify as a REIT under Section 856(c)(1) of the Internal Revenue Code of 1986 as amended (the “Code”). Accordingly, the Company generally will not be subject to federal and state income tax, provided that we distribute at least 90% of our REIT taxable income, as defined under the Code, in the form of a dividend to our shareholders each year and comply with various other requirements. As a result of the REIT Modernization Act of 1999, the Company is permitted to participate in certain activities without jeopardizing its REIT status which would have previously been precluded, provided the Company conducts these activities through an entity that elects to be treated as a taxable REIT subsidiary (“TRS”) under the Code. The Company has one TRS, the only asset being its investment in the Grove, which will be subject to federal and state income tax on the income from these activities.

### 2. Basis of Quarterly Presentations:

The accompanying quarterly financial statements have been prepared in conformity with accounting principles generally accepted in the United States (“GAAP”). The financial statements of the Company included herein have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) and, in the opinion of management, reflect all adjustments which are necessary to present fairly the results for the three and nine-month periods ended September 30, 2012 and 2011.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations; however, management believes that the disclosures are adequate to make the information presented not misleading.

This report should be read in conjunction with the audited financial statements and footnotes therein included in the Annual Report on Form 10-K for the year ended December 31, 2011.

The results of operations for the three and nine-month periods ended September 30, 2012 are not necessarily indicative of the results to be expected for the full year.

### 3. Principles of Consolidation:

The accompanying consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

4. Investment in Marketable Securities

The Company determines the appropriate classification of securities at the time of purchase and reassesses the appropriateness of such classification at each reporting date. All marketable securities held by the Company have been classified as available-for-sale and, as a result, are stated at fair value, based on a pricing model that incorporates coupon type, prepayment speeds and the type of collateral backing the securities. Unrealized gains and losses on available-for-sale securities are recorded as a separate component of stockholders' equity. Any realized gains and losses on the sale of securities, as determined on a first-in, first-out basis, will be included in the Consolidated Statements of Operations.

Seq. Page 7

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The Company reviews its investments on a regular basis to evaluate whether or not each security has experienced an other-than-temporary decline in fair value. If it is believed that an other-than-temporary decline exists, the Company will write down the investment to market value and record the related write-down in the Consolidated Statements of Operations.

The historical cost and estimated fair value of investments in marketable securities available for sale as of September 30, 2012 are as follows:

	Amortized Cost	Gross Unrealized Gains	Fair Value
Mortgage-backed Securities	\$ 4,824,358	\$ 57,387	\$ 4,881,745

The Company's investment is in conforming agency fixed rate mortgage pass through securities ("mortgage-backed securities"), each of which contained both AA and AAA ratings, the principal of which is fully guaranteed by agencies of the U.S. Government. At September 30, 2012, marketable securities based on amortized cost, reflect a yield of approximately 2% and an adjusted duration of less than four years. The Company did not have any investments in mortgage-backed securities during the year ended December 31, 2011. The fair value of mortgage-backed securities was estimated based on a Level 2 methodology, additional details of which are discussed further in Note 11 – Fair Value of Financial Instruments. None of the securities with an unrealized loss at September 30, 2012 are considered to be other-than-temporarily impaired, therefore the unrealized loss was reported in the Condensed Consolidated Statement of Comprehensive Income (Loss).

#### 5. Earnings per Share:

Basic earnings per common share are computed by dividing net income (loss) by the weighted average number of shares of common stock outstanding during the period. Diluted earnings per share give effect to stock options and warrants which are considered to be dilutive common stock equivalents. The Company does not have outstanding dilutive common stock equivalents during the periods presented. As a result, the basic and diluted earnings per share is the same. Treasury shares have been excluded from the weighted average number of shares.

During the third quarter ended September 30, 2011, the Company filed a registration statement on Form S-3 with the Securities and Exchange Commission to register a number of shares of the Company's common stock to be offered in a rights offering by the Company to its shareholders. The rights offering resulted in 192,641 common shares being issued.

#### 6. Income Taxes:

The Company files a consolidated U.S. Federal Tax Return that includes all 100% owned subsidiaries. State tax returns are filed on a consolidated or separate basis depending on the applicable laws.

Deferred income tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

The Condemnation litigation with the State of New York concluded in June and the State remitted payment in early July. The following table provides the breakdown of the condemnation proceeds earned through September 30, 2012:

	Condemnation Gross Proceeds	Income Tax Provision
Gross gain from condemnation	\$ 98,685,000	\$ 61,649,000
Interest income on condemnation	67,370,716	-
Reimbursement of condemnation expenses	1,474,941	-
Total	\$ 167,530,657	\$ 61,649,000

In accordance with Section 1033 of the Internal Revenue Code, the Company has deferred recognition of the gain on the condemnation of its real property for income tax purposes. During the quarter ended September 30, 2012, the Company applied for and received an additional approved IRS extension of time to replace the condemned property with like-kind property by April 30, 2014. The previous deadline was April 30, 2013. If the Company replaces the condemned property with like-kind property by April 30, 2014 (or such extended period approved by the Internal Revenue Service at its discretion), recognition of the gain is deferred until the newly acquired property is disposed of. Pending a replacement property acquisition, the Company has recorded a provision for income taxes of \$61,649,000 resulting from the condemnation award. The provision for income taxes is directly resulting from the gain on condemnation of its real property and would reverse into income upon the purchase of like-kind property.

Seq. Page 8

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The Company converted to a REIT in 2007, effective May 1, 2006. As long as Gyrodyne qualifies for REIT status, the Company generally will not be subject to New York State and Federal corporate income taxes on income and gain generated after May 1, 2006. REIT organizations are required to distribute a minimum of 90% of Net Income. As a result, the Company has a contingent liability of approximately \$25 million associated with the net income excluding the real estate gain, which is not a probable liability due to the Company's intent to meet the REIT distribution requirements and is not reflected in the September 30, 2012 financial statements.

#### 7. Mortgage loans Payable:

Mortgage loans payable are comprised of the following:

	September 30, 2012 (Unaudited)	December 31, 2011
Mortgage payable - Port Jefferson Professional Park (a)	\$ 5,033,681	\$ 5,130,831
Mortgage payable - Cortlandt Medical Center (b)	4,375,000	4,532,500
Mortgage payable - Fairfax Medical Center (c)	7,474,537	7,598,188
Mortgage payable - Flowerfield Industrial Park (d)	3,799,096	3,882,261
<b>Total</b>	<b>\$ 20,682,314</b>	<b>\$ 21,143,780</b>

(a) In June 2007, in connection with the purchase of the Port Jefferson Professional Park, the Company assumed a \$5,551,191 mortgage payable to a bank (the "Port Jefferson Mortgage"). The Port Jefferson Mortgage bore interest at 5.75% through February 1, 2012. Effective January 17, 2012, the Company negotiated an interest rate modification from 5.75% to 5% for the 5 year period February 1, 2012 through February 1, 2017 and adjusts to the higher of 5.75% or 275 basis points in excess of the Federal Home Loan Bank's five year Fixed Rate Advance ("Fixed Rate Advance") thereafter. The Port Jefferson Mortgage is payable in monthly installments of principal and interest totaling \$33,439 through February 2012. From March 1, 2012 through February 1, 2022, the minimum monthly installment will be no less than \$31,086 and will vary based upon the Fixed Rate Advance. In February 2022, a balloon payment is due of approximately \$3,560,000. The Port Jefferson Mortgage is collateralized by the Port Jefferson Professional Park in Port Jefferson Station, New York.

(b) In June 2008, in connection with the purchase of the Cortlandt Medical Center in Cortlandt Manor, New York, the Company borrowed \$5,250,000 from a bank (the "Cortlandt Mortgage"). The Cortlandt Mortgage originally bore interest at a per annum rate of 225 basis points above the one month LIBOR rate (4.71% at inception) through July 1, 2018, subject to monthly adjustment. The Cortlandt Mortgage is payable in monthly installments with a fixed principal payment of \$17,500 plus interest, through June 1, 2018. In July 2018, a balloon payment is due of approximately \$3,168,000. The Cortlandt Mortgage is collateralized by the Cortlandt Medical Center. As part of the terms and conditions of the Cortlandt Mortgage, reacting to an increase in the LIBOR rate, the Company exercised an option to enter into an interest rate swap agreement in November 2008 with the bank holding the mortgage, thereby fixing the interest rate at 5.66% through November 1, 2011. Following the expiration of the Interest Rate Swap Agreement, the Cortlandt Mortgage interest rate is variable and floating based on the one month Libor rate plus 225 basis points, which equates to approximately 2.5% at September 30, 2012, and December 31, 2011, respectively. The Company continues to have an option to enter into an interest rate swap agreement but does not plan to hedge any variable interest rate risk for 2012.

(c) In March 2009, in connection with the purchase of the Fairfax Medical Center in Fairfax, Virginia by Virginia Healthcare Center, LLC ("VHC"), a wholly-owned subsidiary of the Company, VHC borrowed \$8,000,000 from a bank (the "Fairfax Mortgage"). The Fairfax Mortgage bears interest at 5.875% through April 10, 2014 and thereafter adjusts to the higher of 5.50% or 300 basis points over the weekly average yield on five-year United States Treasury

securities. The Fairfax Mortgage is collateralized by a Deed of Trust and Security Agreement establishing a first trust lien upon the land, buildings and improvements as well as a Collateral Assignment of Leases and Rents and matures on April 10, 2019. In April 2019, a balloon payment is due of approximately \$6,120,000. The payment of the indebtedness evidenced by the Fairfax Mortgage and the performance by VHC of its obligations thereunder have been guaranteed by the Company.

Seq. Page 9

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(d) On December 29, 2010, the Company closed on a mortgage loan with a bank for \$4,000,000. A portion of the proceeds was used to retire the outstanding line of credit with the Company's previous lender of \$1,750,000. The mortgage loan has a maturity date of January 2, 2031 and a floating interest rate of prime plus 100 basis points with a floor of 5%, to be adjusted once annually on its anniversary date. The interest rate is 5% at September 30, 2012. The mortgage loan is subject to a 20 year amortization schedule requiring monthly payments of principal and interest due on the first of each month beginning February 1, 2011. The mortgage loan is secured by approximately 35.1 acres of the Flowerfield Industrial Park including the respective buildings and related leases. In the event of collection from New York State under the State of New York Court of Claims ruling on the Company's condemnation case (Index No. 112279), the lender had the option to require the Company to repay all or a part of the balance outstanding. In early July, following the receipt of the condemnation proceeds, the lender communicated that it will not exercise its option to require the Company to repay a portion or all of the loan other than under its regularly scheduled amortization terms.

#### 8. Retirement Plans:

The Company sponsors a Defined Benefit Retirement Plan for substantially all of its employees and records net periodic pension benefit / cost pro rata throughout the year. The following table provides the components of net periodic pension benefit cost for the plan for the three and nine-months ended September 30, 2012 and 2011 including the required and expected contributions:

	Nine Months Ended September 30,		Three Months Ended September 30,	
	2012	2011	2012	2011
<b>Pension Benefits</b>				
Service Cost	\$ 137,136	\$ 95,921	\$ 45,712	\$ 31,974
Interest Cost	135,130	117,668	45,043	39,223
Expected Return on Plan Assets	(289,543 )	(243,728 )	(96,515 )	(81,243 )
Amortization of prior service costs	16,932	-	5,644	-
Amortization of Actuarial Loss	(3,122 )	(902 )	(1,040 )	(301 )
Net Periodic Pension Benefit	\$ (3,467 )	\$ (31,041 )	\$ (1,156 )	\$ (10,347 )
<b>(Income) Cost After Curtailments and Settlements</b>				
Minimum required contribution	\$ -	\$ -	\$ -	\$ -
Expected contribution	\$ -	\$ -	\$ -	\$ -

During the three and nine-months ended September 30, 2012, the Company did not make any contribution to the plan. The Company does not have a minimum required contribution for the December 31, 2012 plan year, and is not expecting to make a contribution for the related plan year.

#### 9. Commitments and Contingencies:

Lease revenue commitments - The approximate future minimum revenues from rental property under the terms of all noncancellable tenant leases, assuming no new or renegotiated leases are executed for such premises, are as follows:

Twelve Months Ending September 30,	Amount
2013	\$ 3,682,000
2014	2,679,000



2015	2,034,000
2016	1,728,000
2017	1,244,000
Thereafter	2,587,000
	\$ 13,954,000

Other commitments and contingencies As of September 30, 2012, other commitments and contingencies are summarized in the below table:

Employment agreement with severance commitment contingencies	\$ 163,000
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Employment agreements - The Company has a compensation arrangement with its Chief Financial Officer.

Seq. Page 10

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10. Recent Accounting Pronouncements:

In May 2011, the FASB issued ASU 2011-04, "Fair Value Measurement (Topic 820), Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS". The amendment results in a consistent definition of fair value and ensures the fair value measurement and disclosure requirements are similar between GAAP and International Financial Reporting Standards ("IFRS"). This amendment changes certain fair value measurement principles and enhances the disclosure requirements particularly for Level 3 fair value measurements. This amendment is effective for the Company on January 1, 2012. The adoption did not have a material effect on the Company's consolidated financial position or results of operations.

In June 2011, the Financial Accounting Standards Board ("FASB") issued ASU 2011-05, "Comprehensive Income (Topic 220), Presentation of Comprehensive Income". ASU 2011-05 amends the presentation of other comprehensive income and the Statement of Consolidated Operations. Under this amendment, entities will be required to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. Regardless of which reporting option is selected, the Company is required to present on the face of the financial statements, reclassification adjustments for items that are reclassified from other comprehensive income to net income in the statements where the components of net income and the components of other comprehensive income are presented. The current option to report other comprehensive income and its components in the statement of changes in equity has been eliminated. This amendment is effective for the Company on January 1, 2012 and full retrospective application is required. The amendment did not have a material impact on its financial statements.

Affecting certain sections covered under ASU 2011-05, in December, 2011, the FASB issued ASU 2011-12, "Comprehensive Income (Topic 220)", Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items out of Accumulated Other Comprehensive Income in ASU 2011-05". The pronouncement is effective for fiscal years and interim periods beginning January 1, 2012 with retrospective application for all comparative periods presented. The Company's adoption of the new standard did not have a material effect on the Company's consolidated financial position or results of operations.

In September 2011, the Financial Accounting Standards Board ("FASB") issued ASU 2011-08, "Intangibles – Goodwill and Other (Topic 350), Testing Goodwill for Impairment". ASU 2011-08 amends the required annual impairment testing of goodwill by providing an entity an option to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, after assessing the totality of events and circumstances, an entity determines it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test under Topic 350-24 and Topic 350-20-35-9 is unnecessary. However, if an entity concludes otherwise, then it is required to perform the impairment testing under Topic 350-24 by calculating the fair value of the reporting unit and comparing the results with the carrying amount. If the fair value exceeds the carrying amount, then the entity must perform the second step test of measuring the amount of the impairment test under Topic 350-20-35-9. An entity has the option to bypass the qualitative assessment and proceed directly to the two step goodwill impairment test. Additionally, the entity has the option to resume with the qualitative testing in any subsequent period. The amendment is effective for the Company on January 1, 2012. The adoption did not have a material effect on the Company's consolidated financial position or results of operations.

In December 2011, the FASB issued ASU 2011-11, "Balance Sheet (Topic 210), Disclosures about Offsetting Assets and Liabilities". The guidance in this update requires the Company to disclose information about offsetting and related arrangements to enable users of its financial statements to understand the effect of those arrangements on its financial position. The pronouncement is effective for fiscal years and interim periods beginning on or after January 1, 2013 with retrospective application for all comparative periods presented. The Company's adoption of the new standard is

not expected to have a material effect on the Company's consolidated financial position or results of operations.

In July, 2012, the FASB issued ASU 2012-02, "Intangibles – Goodwill and Other (Topic)". ASU 2012-02 amends the required annual impairment testing of indefinite-lived intangible assets by providing an entity an option to first assess qualitative factors to determine whether it is more likely than not that the fair value of the indefinite-lived asset is less than its carrying amount. If, after assessing the totality of events and circumstances, an entity determines it is not more likely than not that the fair value of the indefinite-lived asset is less than its carrying amount, then performing the two-step impairment test under Topic 350-30 is unnecessary. However, if an entity concludes otherwise, then it is required to perform the impairment testing under Topic 350-30-35-18F by calculating the fair value of the reporting unit and comparing the results with the carrying amount. If the fair value exceeds the carrying amount, then the entity must perform the second step test of measuring the amount of the impairment test under Topic 350-30-35-19. An entity has the option to bypass the qualitative assessment and proceed directly to the two step goodwill impairment test. Additionally, the entity has the option to resume with the qualitative testing in any subsequent period. The pronouncement is effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012 and early adoption is permitted. The Company's adoption of the new standard is not expected to have a material effect on the Company's consolidated financial position or results of operations.

Seq. Page 11

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## 11. Fair Value of Financial Instruments:

Assets and Liabilities Measured at Fair-Value – The Company follows authoritative guidance on fair value measurements, which defines fair-value, establishes a framework for measuring fair-value, and expands disclosures about fair-value measurements. The guidance applies to reported balances that are required or permitted to be measured at fair-value under existing accounting pronouncements.

The Company follows authoritative guidance on the fair value option for financial assets, which permits companies to choose to measure certain financial instruments and other items at fair-value in order to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently. However, we have not elected to measure any additional financial instruments and other items at fair-value (other than those previously required under other GAAP rules or standards) under the provisions of this standard.

The guidance emphasizes that fair-value is a market-based measurement, not an entity-specific measurement. Therefore, a fair-value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair-value measurements, the guidance establishes a fair-value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity's own assumptions about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy). In instances where the determination of the fair-value measurement is based on inputs from different levels of the fair-value hierarchy, the level in the fair-value hierarchy within which the entire fair-value measurement falls is based on the lowest level input that is significant to the fair-value measurement in its entirety. Our assessment of the significance of a particular input to the fair-value measurement in its entirety requires judgment, and considers factors specific to the asset or liability.

The following table represents the carrying value and fair value of the Company's financial assets and liabilities as of September 30, 2012 and December 31, 2011, respectively.

Description	September 30, 2012		December 31, 2011	
	Carrying Value	Fair Value (Level 2)	Carrying Value	Fair Value (Level 2)
<b>I n v e s t m e n t i n</b>				
Marketable Securities	\$ 4,881,745	\$ 4,881,745	N/A	N/A

During 2012, the Company invested in mortgage backed securities with both AA and AAA ratings fully guaranteed by US government agencies (the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation). The fair values of mortgage backed securities originated by US government agencies are based on a pricing model that incorporates coupon type, prepayment speeds and the type of collateral backing the securities. A discount rate is applied to the cashflows in the model to arrive at the fair value. Market quotes, current yields, and their spreads to benchmark indices are obtained for each type of security. With this data, a yield curve is derived for each category of mortgage backed securities. Each security is priced by discounting the cashflow stream by the appropriate yield found on the yield curve. As the significant inputs used to derive the value of the mortgage-backed securities are observable market inputs, the fair value of these securities are included in the Level 2 fair value hierarchy.

The Company estimates that fair value approximates carrying value for cash equivalents, rents receivable, prepaid and other assets, and accounts payable due to the relatively short maturity of the instruments.

The Company determined the fair value of its mortgage loans payable approximates book value. The Company based its decision by looking at current rates available based on the Company's estimate for nonperformance and liquidity risk, the Company's loan to value ratio, the maturity of the debt and the underlying security for the debt.

Seq. Page 12

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The Grove investment is a distressed asset operating in a distressed environment where an orderly transaction is not available. The Grove's lender, Prudential Industrial Properties, LLC ("Prudential"), commenced a foreclosure action against the Grove by filing a complaint in the Circuit Court of Palm Beach County to foreclose upon the Grove Property, alleging that the Grove has defaulted on its loan from Prudential and that the Grove is indebted to Prudential in the amount of over \$37 million in principal and over \$8 million in interest and fees. The facts and circumstances of the Grove make it unreasonable to present a fair value utilizing a Level 3 methodology, the lowest methodology which allows for broad assumptions; therefore, in accordance with the exception rules for thinly traded/lack of marketability of distressed assets, the Company is not presenting a fair value. The Company is accounting for the investment under the equity method. As of September 30, 2012, the carrying value of the Company's investment was \$0.

12. Risk Management – Use of Derivative Instruments:

The Company entered into the Interest Rate Swap ("Swap") agreement on the mortgage of the Cortlandt Medical Center in November 2008, fixing the interest rate at 5.66% through November 1, 2011.

The Swap was considered a derivative instrument. The Company utilized the Swap agreement to minimize its interest rate exposure on the Cortlandt Medical Center mortgage. The principal objective of this agreement was to limit the risks and/or costs associated with the Company's operating structure as well as to hedge the specific transaction. The Company had only one interest rate swap agreement with the purpose of hedging against a rise in LIBOR on the mortgage for the Cortlandt Medical Center. The counterparty to the arrangement was the bank which holds the mortgage for the Cortlandt Medical Center. The Company was potentially exposed to credit losses in the event of non-performance by the counterparty. However, the Company did not expect the counterparty to fail to meet its obligations due to the same party holding both the Mortgage and the Swap Agreement. The Company did not hedge credit or property value market risks through derivative financial instruments.

The Company formally assessed both at inception of the hedge, and on an ongoing basis, whether such derivatives are highly-effective in offsetting changes in cash flows of the hedged item. If management determined that a derivative is not highly-effective as a hedge, or if a derivative ceases to be a highly-effective hedge, the Company would discontinue hedge accounting prospectively. The related ineffectiveness would be charged to the Statement of Operations.

The valuation of these instruments was determined utilizing widely accepted valuation techniques including discounted cash flow analysis on the expected cash flows for the derivative. This analysis includes the contractual terms of the derivative through the maturity date, and utilizes observable market based inputs including interest rate curves and implied volatilities. The fair value of the interest rate swap was based on market standard methodology of netting the discounted future inflows and outflows.

Following the expiration of the Interest Rate Swap Agreement, the Company's interest rate adjusted to 2.5% (225 basis points above the one month Libor rate (.25% on September 30, 2012 and December 31, 2011). As part of the terms and conditions of the Cortlandt Mortgage, the Company has the option to enter into a new Interest Rate Swap Agreement throughout the term of the loan. Based on the current economic environment the Company has not entered into a new Interest Rate Swap Agreement.

13. Accumulated Other Comprehensive Income (Loss):

Accumulated other comprehensive income as of September 30, 2012 and December 31, 2011 was \$349,418 and \$292,031, respectively. The balances were comprised of the following:

December 31, 2011

	September 30, 2012	
Unrecorded gain on investments	\$ 57,387	\$ -
Unrecorded income on pension	292,031	292,031
Accumulated other comprehensive income	\$ 349,418	\$ 292,031

#### 14. Condemnation:

In early July, the Company received \$167,530,657 from the State of New York (the "State") in payment of the judgments in the Company's favor in the condemnation litigation with the State. The amount received consisted of \$98,685,000 in additional damages, \$1,474,941 in costs, disbursements and expenses, and \$67,370,716 in interest.

Seq. Page 13

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The \$167.5 million payment brings to a resolution the Company's case for just compensation, commenced in 2006 for the 245.5 acres of its Flowerfield property in St. James and Stony Brook, New York (the "Property") taken by the State. The State had paid the Company \$26,315,000 for the Property in March 2006, which the Company elected, under New York's eminent domain law, to treat as an advance payment while it pursued its claim for just compensation. The Court of Claims ruled in the Company's favor in June 2010 when it awarded the Company \$125,000,000, thereby requiring the State to pay an additional \$98,685,000 plus statutory interest of nine percent from the date of taking on November 2, 2005 to the date of payment. That judgment, as well as a related judgment for costs, disbursements and expenses, was affirmed by the Appellate Division and the Court of Appeals.

The original advance payment of \$26,315,000 was successfully reinvested in like-kind property under Section 1033 of the Internal Revenue Code, thereby deferring income tax on the related gain. In accordance with Section 1033, the Company has deferred recognition of the gain on the condemnation of its real property for income tax purposes. If the Company replaces the condemned property with like-kind property by April 30, 2014 (or such extended period if requested and approved by the Internal Revenue Service at its discretion), recognition of the gain is deferred until the newly acquired property is disposed of.

15. Reclassifications:

Certain amounts in the prior period have been reclassified to conform to the classification used in the current period.

16. Subsequent Events:

The Company is in the process of evaluating the impact of Hurricane Sandy on its real estate holdings and fourth quarter financial results. Currently, the Company cannot conclude on the probable and or estimable impact if any, on its real estate holdings or its results of operations.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

When we use the terms "Gyrodyne," the "Company," "we," "us," and "our," we mean Gyrodyne Company of America, Inc. and all entities owned by us, including non-consolidated entities, except where it is clear that the term means only the parent company. References herein to our Quarterly Report are to this Quarterly Report on Form 10-Q for the three and nine-months ended September 30, 2012.

Forward Looking Statements. The statements made in this Form 10-Q that are not current or historical facts contain "forward-looking information" within the meaning of the Private Securities Litigation Reform Act of 1995, and Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, both as amended, which can be identified by the use of forward-looking terminology such as "may," "will," "anticipates," "expects," "projects," "estimates," "believes," "seeks," "could," "should," or "continue," the negative thereof, other variations or comparative terminology. Important factors, including certain risks and uncertainties, with respect to such forward-looking statements that could cause actual results to differ materially from those reflected in such forward-looking statements include, but are not limited to, risks and uncertainties relating to the process of exploring strategic alternatives, as well as statements regarding the evaluation of strategic alternatives, the effect of economic and business conditions, including risks inherent in the real estate markets of Suffolk and Westchester Counties in New York, Palm Beach County in Florida and Fairfax County in Virginia, risks and uncertainties relating to Gyrodyne's undeveloped property in St. James, New York, and other risks detailed from time to time in the Company's SEC reports. These and other matters the Company discusses in this Quarterly Report, or in the documents it incorporates by reference into this Quarterly Report, may cause actual results to differ from those the Company describes. The Company assumes no obligation to update or revise any forward-looking information, whether as a result of new information, future events or otherwise.



Overview:

General: We are a self-managed and self-administered real estate investment trust formed under the laws of the State of New York. We operate primarily in one segment. The Company's primary business is the investment in and the acquisition, ownership and management of a geographically diverse portfolio of medical office and industrial properties and development of industrial and residential properties. Substantially all of our rental properties are subject to net leases in which the tenant must reimburse Gyrodyne for a portion of or all or substantially all of the costs and /or cost increases for utilities, insurance, repairs and maintenance, and real estate taxes.

As of September 30, 2012, the Company had 100% ownership, directly or indirectly, in three medical office parks, comprising an aggregate of approximately 131,000 rentable square feet and a multitenant industrial park comprising approximately 128,000 rentable square feet. In addition, the Company has approximately 68 acres of property located in St. James, New York, approximately 10 of which are utilized by the industrial park and the balance remains undeveloped. Furthermore, the Company has an estimated 9.32% limited partnership in a limited partnership which owns an undeveloped Florida property called "the Grove Property".

With the exception of the receipt of the condemnation proceeds, our revenues and cash flows are generated predominantly from property rent receipts. Growth in revenues and cash flows has been and remains directly correlated to our ability to (1) re-lease suites that are vacant or may become vacant at favorable rates and (2) successfully complete the liquidity events in our strategic plan and / or the reinvestment under Section 1033 of the condemnation proceeds.

Seq. Page 14

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Our properties are concentrated in New York State and Northern Virginia. We compete with a large number of real estate property owners and developers, some of which may be willing to accept lower returns on their investments. The principal factors of competition are rents charged, attractiveness of location, the quality of the property and breadth and quality of services provided. Our success depends upon, among other factors, trends of the national, regional and local economies, financial condition and operating results of current and prospective tenants and customers, availability and cost of capital, construction and renovation costs, taxes, governmental regulations, legislation and population trends. See "Part I" in our Annual Report on Form 10-K for the year ended December 31, 2011 for additional information regarding these factors.

The economic recession and illiquidity and volatility in the financial and capital markets from 2008 to present has continued to negatively affect substantially all businesses, including ours. Although signs of an economic recovery beginning in 2010 through early 2012 have emerged, it is not possible for us to quantify the timing and impact of the recovery on our future financial results. The length and depth of the economic recession combined with the slow economic recovery has continued to negatively impact the real estate industry. Additionally, the Company stated in its 2010 through 2012 periodic filings that it believes the full impact of the economic downturn has not yet been fully absorbed by the real estate market, partially attributable to the Company's belief that lease commitments, by their very nature, expire over time resulting in the vacancy impact of an economic slowdown occurring over a similar period of time as tenants cannot reduce their space demands until their leases expire. The continuation of negative absorption rates into the first quarter in many regions across the country, including Long Island, continue to confirm the impact of the economic volatility.

**Fiscal Cliff:** Under current legislation, beginning January 1, 2013, there will be a combination of an increase in tax rates and a significant reduction in government spending, often referred to as the pending fiscal cliff. The fiscal cliff may impact entitlement programs (i.e. Medicare, Medicaid) that may indirectly impact our medical office properties. Furthermore, such reductions combined with potential reductions in funding to the State University at Stony Brook and public funding related projects or businesses that may impact the tenants at our industrial park, which include Stony Brook University.

**Global Credit and Financial Crisis:** The continued concerns about the impact of a widespread and long term global credit and financial crisis have contributed to market volatility and diminishing expectations for the real estate industry, including the potential downward pressure on our common stock price. As a result, our business continues to be impacted by factors including (1) increased challenges in re-leasing space, and (2) potential risks stemming from late rental receipts, tenant defaults and tenant bankruptcies.

**Health Care Legislation:** The Federal health care legislation enacted in 2010 will potentially affect medical office real estate due to the direct impact on its tenant base. While the impact is not expected to be immediate due to the multi-year phase in period of the legislation, medical professionals are reviewing their real estate options which include remaining status quo, increasing tenant space to address a higher volume of patients as well as combining practices with other professionals. As a result, our business could be impacted by factors including (1) difficulty transitioning doctors to longer term leases, (2) difficulty raising rates and (3) increased challenges in re-leasing space.

As of September 30, 2012, the average effective rental revenue per square foot adjusted for tenant improvements was \$19.33 compared to \$20.22 on December 31, 2011. The Company defines the effective revenue per square foot as the annual rate per square foot stated in the lease reduced by the average annual tenant improvement allowance provided for in such leases.

**Business Strategy:** We have focused our business strategy to strike a balance between preserving capital and improving the market value of our portfolio to meet our long term goal of executing on a liquidity event or series of liquidity events. Included within this strategy were, and except for the last item, continue to be our objectives:

- actively managing our portfolio to improve our operating cash flow;
  - pursuing the re-zoning effort of the Flowerfield property to maximize its value;
  - limiting our use of capital to that which preserves the market value of our real estate portfolio;
  - maximizing our working capital without materially increasing our debt service requirements; and
- diligently managing the condemnation lawsuit which was concluded June 5, 2012 with the related payment received in July 2012.

We believe these objectives strengthen our business and enhance its value.

Following the receipt of the condemnation proceeds in early July, the Board of Directors established a committee to pursue strategic alternatives, including managing the process of selecting legal and financial advisors and making recommendations to the Board of Directors. As part of the process, on August 10, 2012 the Company retained Skadden, Arps, Slate, Meagher & Flom, LLP and on August 23, 2012 the Company retained Rothschild Inc. as financial advisors.

Seq. Page 15

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### Third Quarter 2012 Transaction Summary

The following summarizes our significant transactions and other activity during the three months ended September 30, 2012.

**Investments** – The Company received principal distributions during the third quarter of approximately \$341,000 from its first quarter investment of \$5.4 million in conforming agency fixed rate mortgage pass through securities with both AA and AAA ratings fully guaranteed by US government agencies (the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation). The portfolio is currently generating a yield of approximately 2%.

**Leasing** – During the three months ended September 30, 2012, the Company executed 4 lease renewals encompassing approximately 3,000 square feet, and approximately \$54,000 in annual revenue. In addition, the Company entered into 5 new leases encompassing approximately 12,000 square feet and \$150,000 in annual revenue. The increase in revenue from its new leases and contractual annual increases was offset by 1 lease termination encompassing approximately 3,000 square feet and approximately \$79,000 in annual revenue. The Company generated a decrease in net deferred revenue of approximately \$32,000.

The new leases and lease extensions signed during the third quarter included tenant improvement allowances which the Company estimates at a cost of approximately \$5,000, and approximately \$20,000 of rent abatements. There were lease commissions incurred by the Company during the third quarter of approximately \$34,000 affiliated with total lease commitment revenues over the term of the respected leases of \$1,422,050.

The continued economic volatility for small businesses and medical practitioners have impacted property management firms, including the Company's ability to renew leases at comparable rates if at all, without providing either rent abatements or comparable other lease incentives. During 2011 through September 2012, medical office parks and industrial parks experienced degradation in both rental rates and occupancy. Rental revenues were \$1,059,576 and \$1,101,161 for the three months ended September 30, 2012, and June 30, 2012, respectively, a quarter over quarter decrease of \$41,585. Although the Company successfully reduced the quarterly rate of degradation to \$41,585 compared to the second quarter reduction of \$86,106, the continued, albeit slower degradation in revenue is a reflection of the continuing challenges to maintain both rental rates and occupancy during the slow economic recovery.

Re-tenanting vacant space, renewing tenants, and transitioning tenants to longer term leases has resulted in total lease commitments as of September 30, 2012 and June 30, 2012 of \$13,954,000 and \$13,847,000, respectively, an increase of \$106,000. During the third quarter the Company did not offer significant tenant improvements to attract new tenants. However, if the challenges on reletting space continues, the Company may offer tenant improvements in exchange for signing long term lease commitments.

**Condemnation lawsuit** – In early July, the Company received \$167,530,657 from the State of New York (the "State") in payment of the Judgments in the Company's favor in the condemnation litigation with the State. The amount received consisted of \$98,685,000 in additional damages, \$1,474,941 in costs, disbursements and expenses, and \$67,370,716 in interest.

The \$167.5 million payment brings to a successful resolution the Company's case for just compensation, commenced in 2006 for the 245.5 acres of its Flowerfield property in St. James and Stony Brook, New York (the "Property") taken by the State. The State had paid the Company \$26,315,000 for the Property at the time of the taking, which the Company elected, under New York's eminent domain law, to treat as an advance payment while it pursued its claim for just compensation. The Court of Claims ruled in the Company's favor in June 2010 when it awarded the Company \$125,000,000, thereby requiring the State to pay an additional \$98,685,000 plus statutory interest of nine percent from

the date of taking on November 2, 2005 to the date of payment. That Judgment, as well as a related Judgment for costs, disbursements and expenses, was affirmed by the Appellate Division and the Court of Appeals.

The Company recorded the income of \$167,425,729 less condemnation costs incurred in its financial statements for the quarter ended June 30, 2012, including the interest through June 30, 2012. As a result of the payment being received in early July, the interest of \$104,928 for the first three days in July was reflected in the financial statements for the third quarter ending September 30, 2012.

#### The Grove

On March 18, 2011, the Grove's lender, Prudential Industrial Properties, LLC ("Prudential"), commenced a foreclosure action against the Grove by filing a complaint in the Circuit Court of Palm Beach County to foreclose upon the Grove Property, alleging that the Grove has defaulted on its loan from Prudential and that the Grove is indebted to Prudential in the amount of over \$37 million in principal and over \$8 million in interest and fees. The Grove continues to operate while its management attempts to negotiate a resolution acceptable to all parties. The Company is a limited partner in the Grove and is not a guarantor of any debt related to the Grove. The investment is held in a taxable REIT subsidiary where the Company has a \$1,315,000 deferred tax liability related to the Grove. The deferred tax liability represents taxable losses not yet recorded pursuant to the Equity Method of Accounting.

Seq. Page 16

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## Critical Accounting Policies

Management's discussion and analysis of financial condition and results of operations is based upon our condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America, or GAAP. The condensed consolidated financial statements of the Company include accounts of the Company and all majority-owned and controlled subsidiaries. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions in certain circumstances that affect amounts reported in the Company's condensed consolidated financial statements and related notes. In preparing these financial statements, management has utilized information available including its past history, industry standards and the current economic environment, among other factors, in forming its estimates and judgments of certain amounts included in the condensed consolidated financial statements, giving due consideration to materiality. On a regular basis, we evaluate our assumptions, judgments and estimates. However, application of the critical accounting policies below involves the exercise of judgment and use of assumptions as to future uncertainties and, as a result, actual results could differ from these estimates. In addition, other companies may utilize different estimates, which may impact comparability of the Company's results of operations to those of companies in similar businesses. We believe there have been no material changes to the items that we disclosed as our critical accounting policies under Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our annual report on Form 10-K for the year ended December 31, 2011.

## Revenue Recognition

Rental revenue is recognized on a straight-line basis, which averages minimum rents over the terms of the leases. The excess of rents recognized over amounts contractually due, if any, is included in deferred rents receivable on the Company's balance sheet. Alternatively, rents received in advance of rents recognized, if any, are included in deferred rent liability on the Company's balance sheet. Certain leases also provide for tenant reimbursements of common area maintenance and other operating expenses and real estate taxes. Tenant reimbursements to the Company for expenses where the Company negotiates, manages, contracts and pays the expense on behalf of the tenant are recognized as revenue when they become estimable and collectible. Ancillary and other property related income is recognized in the period earned. The only exception to the straight line basis is for tenants at risk of default. Revenue from tenants where collectability is in question is recognized on a cash basis when the rent is received.

## Real Estate

Rental real estate assets, including land, buildings and improvements, furniture, fixtures and equipment are recorded at cost. Tenant improvements, which are included in buildings and improvements, are also 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 their estimated useful lives.

Depreciation is computed utilizing the straight-line method over the estimated useful life of ten to thirty-nine years for buildings and improvements and three to twenty years for machinery and equipment.

The Company is required to make subjective assessments as to the useful life 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 increased annual net income.

Real estate held for development is stated at the lower of cost or net realizable value. In addition to land, land development and construction costs, real estate held for development includes interest, real estate taxes and related development and construction overhead costs which are capitalized during the development and construction period. Net realizable value represents estimates, based on management's present plans and intentions, of sale price less development and disposition cost, assuming that disposition occurs in the normal course of business.

#### Long Lived Assets

On a periodic basis, management assesses whether there are any indicators that the value of the real estate properties may be impaired. A property's value is considered to be impaired if management's estimate of the aggregate future cash flows (undiscounted and without interest charges) to be generated by the property is less than the carrying value of the property. Such future cash flow estimates consider factors such as expected future operating income, trends and prospects, as well as the effects of demand, competition and other factors. To the extent impairment occurs, the loss will be measured as the excess of the carrying amount of the property over the fair value of the property.

Seq. Page 17

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The Company is required to make subjective assessments as to whether there are impairments in the value of its real estate properties and other investments. These assessments have a direct impact on the Company's net income, since an impairment charge results in an immediate negative adjustment to net income. In determining impairment, if any, the Company has adopted Accounting for the Impairment or Disposal of Long Lived Assets.

#### Assets and Liabilities Measured at Fair-Value

On January 1, 2008, the Company adopted Fair Value Measurements, which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair-value measurements. The guidance for Fair Value Measurements applies to reported balances that are required or permitted to be measured at fair value under existing accounting pronouncements; accordingly, the standard does not require any new fair value measurements of reported balances.

On January 1, 2008, the Company adopted The Fair Value Option for Financial Assets and Financial Liabilities, which permits companies to choose to measure certain financial instruments and other items at fair value in order to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently. However, the Company has not elected to measure any additional financial instruments and other items at fair value (other than those previously required under other GAAP rules or standards) under the provisions of this standard.

The guidance for the Fair Value Option for Financial Assets and Financial Liabilities emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair-value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair-value measurements, the guidance establishes a fair-value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity's own assumptions about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy).

Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access. Level 2 inputs are inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs may include quoted prices for similar assets and liabilities in active markets, as well as inputs that are observable for the asset or liability (other than quoted prices), such as interest rates, foreign exchange rates, and yield curves that are observable at commonly quoted intervals. Level 3 inputs are unobservable inputs for the asset or liability, which are typically based on an entity's own assumptions, as there is little, if any, related market activity. In instances where the determination of the fair-value measurement is based on inputs from different levels of the fair-value hierarchy, the level in the fair-value hierarchy within which the entire fair-value measurement falls is based on the lowest level input that is significant to the fair-value measurement in its entirety. The Company's assessment of the significance of a particular input to the fair-value measurement in its entirety requires judgment, and considers factors specific to the asset or liability.

Income taxes - Effective May 1, 2006, the Company operates as a real estate investment trust (REIT) for federal and state income tax purposes. As a REIT, the Company is generally not subject to income taxes. To maintain its REIT status, the Company is required to distribute at least 90% of its annual REIT taxable income, as defined by the Internal Revenue Code ("IRC"), to its shareholders, among other requirements. If the Company fails to qualify as a REIT in any taxable year, the Company will be subject to federal and state income tax on its taxable income at regular corporate tax rates. Although the Company qualified for taxation as a REIT, the Company may be subject to certain state and local taxes on its income and property and Federal income and excise taxes on its undistributed income.



The Company's investment in the Grove is held in a taxable REIT subsidiary of the Company and is subject to federal and state income taxes. Taxable REIT subsidiaries perform non-customary services for tenants, hold assets that the Company cannot hold directly and generally may engage in any real estate or non-real estate related business. Accordingly, through the investment in the Grove, the Company is subject to corporate federal and state income taxes on the Company's share of the Grove's taxable income.

Deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities, and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. The Company follows the guidance of FASB Accounting Standards Codification, Accounting for Uncertainty in Income Taxes. This guidance, among other things, creates a two-step approach for evaluating uncertain tax positions. Recognition (step one) occurs when an enterprise concludes that a tax position, based solely on its technical merits, is more-likely-than-not to be sustained upon examination. Measurement (step two) determines the amount of benefit that more-likely-than-not will be realized upon settlement. Derecognition of a tax position that was previously recognized would occur when a company subsequently determines that a tax position no longer meets the more-likely-than-not threshold of being sustained. This interpretation specifically prohibits the use of a valuation allowance as a substitute for derecognition of tax positions, and it has expanded disclosure requirements.

#### Recent Development

As disclosed by the Company in its Current Report on Form 8-K filed on July 30, 2012 with the Securities and Exchange Commission, the Company received written notice on July 25, 2012 of the retirement of Stephen V. Maroney from his positions as the Company's President and Chief Executive Officer and as a director, effective August 16, 2012. In the notice, Mr. Maroney indicated that his retirement was a personal decision, which he had delayed in order to oversee the management of the Company's condemnation litigation. In light of the Company's successful resolution of its condemnation litigation, Mr. Maroney determined that he no longer had reason to postpone his plans to retire. Mr. Maroney has served as President and Chief Executive Officer since 1999. On August 17, 2012, the Company's Board of Directors appointed Gary Fitlin, its current Chief Financial Officer and Treasurer as Interim President and Chief Executive Officer while the Company continues its search for a new Chief Executive Officer, which the Board expects to complete as soon as possible.

#### RESULTS OF OPERATIONS

Three Months Ended September 30, 2012 compared with the Three Months Ended September 30, 2011.

Rental revenues are comprised solely of rental income and amounted to \$1,059,576 and \$1,224,553 for the three months ended September 30, 2012 and 2011, respectively, a decrease of \$164,977 or 13%. The Flowerfield Industrial Park, Port Jefferson Professional Park, Cortlandt Manor Medical Center and Fairfax Medical Center all experienced a decrease in revenue; amounting to \$9,118, \$51,774, \$84,107, and \$19,978, respectively. The reduction in revenue at the Flowerfield Industrial Park was primarily related to one tenant which defaulted on its lease. The tenant was evicted as of June 30, 2012 and the Company has a judgment in the amount of \$136,000. Revenue from the judgment will not be recorded until received. The net decrease at the Cortlandt Manor Medical Center was related to a drop in occupancy compared to the prior period due to two terminations representing approximately 9,000 rentable square feet, half of which was retenanted by early October 2012. The Port Jefferson Professional Park's decrease was primarily related to one tenant which did not renew its lease in the fourth quarter of 2011 and a second tenant which did not renew its lease in June 2012, collectively representing approximately 7,000 square feet and \$40,000 in revenue for the quarter. The net decrease at the Fairfax Medical Center was primarily related to various net terminations increasing the vacancy rate by 6,500 square feet over the comparable prior period.

Tenant reimbursements represent expenses negotiated, managed and incurred directly by the Company on behalf of or for the benefit of the tenants. Tenant reimbursements were \$137,037 and \$152,222 for the three months ended September 30, 2012 and 2011, respectively, a decrease of \$15,185 or approximately 10%. The reduction in tenant reimbursements was primarily related to net terminations across the real estate portfolio.

Rental expenses for the three months ended September 30, 2012 and 2011 were \$582,901 and \$562,898, respectively, an increase of \$20,003 or 4%. Approximately \$25,000 of the increase was due to maintenance expenses, partially offset by an approximate \$4,000 reduction in management fees. The increase in maintenance expenses were incurred as part of a plan to reposition the real estate to maximize both occupancy rates and resale value.

General and administrative expenses for the three months ended September 30, 2012 and 2011 were \$779,563 and \$436,088, respectively, an increase of \$343,475 or 79%. The major contributing factor to the increase was approximately \$300,000 of advisory fees incurred to explore strategic alternatives encompassing one or more tax efficient liquidity events, and an increase in compensation and benefits of approximately \$24,000. Approximately \$15,000 of increased compensation was the result of non recurring payments to the former Chief Executive Officer and approximately \$9,000 of the compensation and benefit increase was a non-cash charge directly related to the Company's pension plan.

Depreciation expense for the three months ended September 30, 2012 and 2011 was \$225,229 and \$208,126, respectively, an increase of \$17,103 or 8%. The increase is mainly attributable to the 2011 renovations in the developed property portfolio.

Interest income, not including condemnation related interest, was \$22,514 and \$398 for the three months ended September 30, 2012 and 2011, respectively. The increase in interest income is mainly attributable to the purchase of mortgage-backed securities during February and March of 2012.

Interest expense for the three months ended September 30, 2012 and 2011 was \$251,305 and \$305,680, respectively, a decrease of \$54,375 or 18%. The decrease was attributable primarily to the expiration of the Swap on the Cortlandt Manor mortgage which locked in the rate at 5.66%. Following the expiration of the Swap, the rate adjusted down to Libor plus 225 basis points or approximately 2.5%. In addition, the Company renegotiated the rate on the Port Jefferson mortgage effective March 1, 2012, reducing the rate over the next 5 years from 6% to 5%.

The Company is reporting a net loss before Condemnation Proceeds and Provision for Income Taxes for the three months ended September 30, 2012, and 2011 of \$619,871 and \$135,619, respectively primarily due to the impact of the items discussed above.

The expense from condemnation proceeds was approximately \$17,839 and \$17,299 during the three months ended September 30, 2012, and 2011, respectively.

Interest income on condemnation proceeds of \$104,928 reflects the interest earned during the third quarter following the Company's successful conclusion of its condemnation case for just compensation. The interest was received in early July 2012.

There was no provision or benefit for income tax for the three months ended September 30, 2012 and 2011.

The Company is reporting a net loss of \$532,782 and \$152,918 for the three months ended September 30, 2012 and 2011, respectively, primarily due to the impact of the items discussed above.

Nine Months Ended September 30, 2012 compared with the Nine Months Ended September 30, 2011.

Rental revenues are comprised solely of rental income and amounted to \$3,348,005 and \$3,691,533 for the nine months ended September 30, 2012 and 2011, respectively, a decrease of \$343,528 or 9%. The Flowerfield Industrial Park, Cortlandt Manor Medical Center, Port Jefferson Professional Park and Fairfax Medical Center, all experienced a decrease in revenue; amounting to \$41,432, \$140,145, \$121,015 and \$40,936, respectively. The reduction in revenue at the Flowerfield Industrial Park was primarily related to one tenant who defaulted on the lease. The tenant was evicted as of June 30, 2012 and the Company has a Judgment in the amount of \$136,000. Revenue from the Judgment will not be recorded until received. The reduction in revenue at the Cortlandt Manor Medical Center was primarily related to a drop in occupancy compared to the prior period due to two terminations. The Port Jefferson Professional Park's decrease was primarily related to one tenant which did not renew its lease in the fourth quarter of 2011 and a second tenant which did not renew its lease in June 2012, collectively representing approximately 7,000 square feet and \$120,000 in revenue for the quarter.

Seq. Page 19

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The reduction in revenue at the Fairfax Medical Center was primarily related to one tenant exercising an early termination option during the first quarter of 2011. The option included a fee of \$22,000 which was equivalent to one year's rent with the balance comprised of 1 net termination representing 5,138 square feet.

Tenant reimbursements represent expenses negotiated, managed and incurred directly by the Company on behalf of, or for the benefit of, the tenants. Tenant reimbursements were \$429,688 and \$456,936 for the nine months ended September 30, 2012 and 2011, respectively, a decrease of \$27,248 or 6%. The reduction in tenant reimbursements was primarily related to terminations.

Rental expenses for the nine months ended September 30, 2012 and 2011 were \$1,733,083 and \$1,777,307, respectively, a decrease of \$44,224 or 2%. The Company reduced maintenance expenses by approximately \$13,000. Additionally, approximately \$12,000 of the decrease was due to the Company successfully reducing the real estate taxes for the Port Jefferson Medical Center by \$25,000 which was partially offset by net escalating real estate taxes at the remaining properties of approximately \$13,000. The remaining difference is primarily related to a net reduction in the lease commission amortization expenses of \$16,000 as a result of a prior year write-off of commissions related to an early termination at the Fairfax Medical Center and lower management fees of \$12,000 primarily due to lower revenues. The Company successfully offset over 50% of the escalating insurance costs of approximately \$17,000 with lower utility costs of \$10,000.

General and administrative expenses for the nine months ended September 30, 2012 and 2011 were \$1,731,825 and \$1,343,816, respectively, an increase of \$388,009 or 29%. The major contributing factors to the increase were approximately \$300,000 of legal and financial advisory expenses incurred to explore strategic alternatives encompassing one or more tax efficient liquidity events, and an increase in compensation and benefits of approximately \$66,000. Approximately \$28,000 of the compensation and benefit increase was a non-cash charge directly related to the Company's pension plan and approximately \$24,000 resulted from non-recurring compensation expenses paid to the former chief executive officer.

Depreciation expense for the nine months ended September 30, 2012 and 2011 was \$672,985 and \$616,936, respectively, an increase of \$56,049 or 9%. The increase is mainly attributable to the 2011 renovations in the developed property portfolio.

Interest income, not including condemnation related interest, was \$64,292 and \$541 for the nine months ended September 30, 2012 and 2011, respectively. The increase in interest income is mainly attributable to the purchase of mortgage-backed securities during February and March of 2012 which earned approximately 2%.

Interest expense for the nine months ended September 30, 2012 and 2011 was \$764,322 and \$918,763, respectively, a decrease of \$154,441 or 17%. The decrease was attributable primarily to the expiration of the Swap on the Cortlandt Manor mortgage which locked in the rate at 5.66%. Following the expiration of the Swap, the rate adjusted down to Libor plus 225 basis points or approximately 2.5%. In addition, the Company renegotiated the rate on the Port Jefferson mortgage effective March 1, 2012, reducing the rate over the next 5 years from 6% to 5%.

The Company is reporting a net loss before Condemnation Proceeds and Provision for Income Taxes for the nine months ended September 30, 2012, and 2011 of \$1,060,250 and \$507,812 primarily due to the impact of the items discussed above.

The income (expense) from condemnation proceeds was \$100,030,852 and \$(238,990) for the nine months ended September 30, 2012 and 2011, respectively, an increase of \$100,269,842. The Company successfully concluded its condemnation case during the second quarter resulting in an additional \$98,685,000 for just compensation for the Property and reimbursement of condemnation costs of \$1,474,941. The Company incurred approximately

\$129,000 and \$239,000 in condemnation costs during the nine months ended September 30, 2012, and 2011, respectively.

Interest income on condemnation proceeds of \$67,370,716 resulted from the Company's successful conclusion of its condemnation case for just compensation. The interest was received in early July 2012.

The provision for income tax for the nine months ended September 30, 2012 was \$61,649,000. There was no provision or benefit for income tax for the nine months ended September 30, 2011.

The Company is reporting a net income (loss) of \$104,692,318 and \$(746,802) for the nine months ended September 30, 2012 and 2011, respectively, primarily due to the impact of the items discussed above.

#### LIQUIDITY AND CAPITAL RESOURCES

Cash Flows: We believe that a main focus of management is to effectively manage our balance sheet through cash flow management of our tenant leases, maintaining or improving occupancy, and pursuing and recycling capital. Furthermore, following the collection of the condemnation proceeds, management implemented a strategic shift to balancing the management of FFO with prioritizing the exploration of strategic alternatives which will result in additional advisory fees in excess of \$100,000 per month.

Seq. Page 20

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We generally finance our operations and acquisitions through a combination of cash on hand and debt.

As of September 30, 2012, the Company had cash and cash equivalents, totaling approximately \$171.9 million and investments in U.S. guaranteed mortgage-backed securities of approximately \$4.9 million. The Company anticipates that the combination of its current cash balance and cash flow from continuing operations will be adequate to fund business operations, the debt amortization of our long term mortgages over the next twelve months and expenses associated with creating one or more liquidity events in accordance with our strategic plan. In addition to these ongoing requirements, the fiscal cliff, the continued economic challenges for small businesses, including the lack of available credit to many of our tenant classes who are small businesses, and the uncertainty facing medical tenants brought about by the 2010 Federal health care reform legislation, could adversely affect our operating results. Prior to the receipt of the condemnation proceeds and to address these risks and challenges, during 2011 the Company filed a registration statement on Form S-3 with the Securities and Exchange Commission to register a number of shares of the Company's common stock to be offered in a rights offering by the Company to its shareholders with gross proceeds (if all rights were exercised) of \$9,210,000 or \$10,210,000 if an over-allotment option was exercised. The Company received subscriptions for approximately 294,685 shares, greatly exceeding the maximum shares offered of 173,305, and the Company elected to exercise its over-allotment option to issue an additional 19,336 shares to satisfy over-subscription requests. Shareholders were allocated 100% of their basic subscriptions. The rights offering resulted in 192,641 common shares being issued, and net proceeds (after expenses) raised of \$9,961,476.

As of September 30, 2012, approximately \$4.8 million is invested in mortgage-backed securities with both AA and AAA ratings fully guaranteed by US government agencies (the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation).

Net cash provided by (used in) operating activities was \$167,198,861 and \$(15,747) during the nine months ended September 30, 2012 and 2011, respectively. The primary factor impacting cashflow provided by operations in the current period was the conclusion of the condemnation litigation. The Company concluded its condemnation litigation in June 2012 and the State remitted payment of \$167,530,657 in early July including interest, all of which was recorded in 2012. The cash used in operating activities in the prior period was primarily related to condemnation costs of \$238,990 and a reduction in accounts payable of \$90,007.

Net cash used in investing activities was \$5,217,462 and \$882,055 during the nine months ended September 30, 2012 and 2011, respectively. Cash used in investing activities in the current period was primarily attributable to the purchases of securities of approximately \$4.8 million net of principal distributions. The securities are currently generating a yield of approximately 2%. Cash used in investing activities in the prior period was primarily due to property taxes on our undeveloped land, tenant improvements of approximately \$177,000, most of which was contracted for in 2010, and approximately \$385,000 to rebuild and expand the parking lot at Cortlandt Medical Center which had a 100% occupancy rate.

Net cash (used in) provided by financing activities was \$(457,501) and \$9,787,414 during the nine months ended September 30, 2012 and 2011, respectively. The cash used in financing activities in the current period was primarily comprised of scheduled principal payments on the Company's debt service obligations. The cash provided by financing activities in the prior period was primarily comprised of the net capital raised in the Rights Offering of \$9,987,476 offset by scheduled principal payments on the Company's debt service obligations of \$439,562.

Beginning in the second half of 2007, the residential mortgage and capital markets began showing signs of stress, primarily in the form of escalating default rates on sub-prime mortgages, declining residential home values and increasing inventory nationwide. This credit crisis spread to the broader commercial credit markets and has reduced the availability of financing and increased interest rates. The extended weak economy, unemployment and lack of liquidity combined with the impact of the Healthcare Legislation has resulted in an extensive reduction in occupancy

rates and related rental rates across residential, commercial and medical office properties. In certain cases the Company has addressed these challenges to date through various tenant incentives which resulted in the Company's current market rents and related occupancy rates.

The economic climate continues to negatively impact the volume and pricing of real estate transactions which may have recently been exacerbated by concerns over the fiscal cliff. Despite the fact that the Company has invested in medical office buildings, an asset class that has been less vulnerable, if these conditions continue, our portfolio may experience lower occupancy and effective rents, which would result in a corresponding decrease in net income, funds from operations and cash flows. While the Company has been successful maintaining its effective rental rates, its occupancy and revenue commitments have been decreasing which the Company attributes mainly to the challenges of renewing tenants into multi-year leases in the face of an economy that is volatile supplemented by the challenges of attracting new tenants. The Company has recently implemented steps to enhance the real estate portfolio through capital improvements, cosmetic improvements and in certain cases, the offering of tenant improvements, rent abatements or other incentives which, if successful, will improve both resale value and funds from operations.

Seq. Page 21

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## LIMITED PARTNERSHIP INVESTMENT

The Company has a limited partnership investment in the “Grove”, which owns a 3,700+ acre citrus grove located in Palm Beach County, Florida, which is the subject of a plan for mixed-use development. The investment currently represents an estimated 9.32% interest in the Grove. The Company is accounting for the investment under the equity method. As of September 30, 2012, the carrying value of the Company’s investment was \$0. The Company cannot predict what, if any, value it will ultimately realize from this investment.

In November 2010, the Grove made an offering to its partners to invest additional funds in the partnership. The offering had a minimum and maximum aggregate offering amount of \$2 million and \$3 million, respectively, and was due to expire on December 10, 2010. In November 2010, after careful deliberation, the Company informed the Grove that it would not participate in the offering. Subsequently, the Company was informed that the offering would remain open until March 10, 2011. The Company’s non-participation in the offering was expected to dilute its ownership interest to 8.98% from 9.99%, depending on the amount raised in the offering. The Grove completed its offering which closed on March 10, 2011 with a capital raise of \$2 million. The Company has not yet received the dilution impact or any other details following the close of the offering but estimates its new ownership interest will be reduced from 9.99% to 9.32%.

On March 18, 2011, the Grove’s lender, Prudential Industrial Properties, LLC (“Prudential”), commenced a foreclosure action against the Grove by filing a complaint in the Circuit Court of Palm Beach County to foreclose upon the Grove property, alleging that the Grove has defaulted on its loan from Prudential and that the Grove is indebted to Prudential in the amount of over \$37 million in principal and over \$8 million in interest and fees. The Company is a limited partner in the Grove, and is not a guarantor of any debt related to the Grove. The investment is held in a taxable REIT subsidiary where the Company has a \$1,315,000 deferred tax liability related to the Grove. The deferred tax liability represents taxable losses not yet recorded pursuant to the Equity Method of Accounting.

## OFF-BALANCE SHEET ARRANGEMENTS

The Company has no off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on its financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors.

### Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Not required for smaller reporting companies.

### Item 4. Controls and Procedures.

The Company’s management, including the Chief Executive Officer (“CEO”)/Chief Financial Officer (“CFO”), has evaluated the effectiveness of the Company’s disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of September 30, 2012. Based upon that evaluation, the Company’s CEO and CFO concluded that the disclosure controls and procedures were effective, in all material respects, to ensure that information required to be disclosed in the reports the Company files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission and that information is accumulated and communicated to the Company’s management, including the CEO and CFO, to allow timely decisions regarding required disclosure. It should be noted that design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions regardless



of how remote.

There have been no changes in the Company's internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Exchange Act Rule 13a-15 that occurred during the Company's last fiscal quarter that has materially affected, or that is reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II - OTHER INFORMATION

### Item 1. Legal Proceedings

Gyrodyne Company of America, Inc. v. The State of New York

In early July, the Company received \$167,530,657 from the State of New York (the "State") in payment of the judgments in the Company's favor in the condemnation litigation with the State. The amount received consisted of \$98,685,000 in additional damages, \$1,474,941 in costs, disbursements and expenses, and \$67,370,716 in interest.

Seq. Page 22

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The \$167.5 million payment brings to a successful resolution the Company's case for just compensation, commenced in 2006 for the 245.5 acres of its Flowerfield property in St. James and Stony Brook, New York (the "Property") taken by the State. The State had paid the Company \$26,315,000 for the Property in March 2006, which the Company elected, under New York's eminent domain law, to treat as an advance payment while it pursued its claim for just compensation. The Court of Claims ruled in the Company's favor in June 2010 when it awarded the Company \$125,000,000, thereby requiring the State to pay an additional \$98,685,000 plus statutory interest of nine percent from the date of taking on November 2, 2005 to the date of payment. That Judgment, as well as a related Judgment for costs, disbursements and expenses, was affirmed by the Appellate Division and the Court of Appeals.

The Company recorded income of \$167,425,729 including interest through June 30, 2012 in the quarter ended June 30, 2012 and recorded the balance of the interest earned through July 3, 2012 of \$104,928 in the financial statements for the third quarter ended September 30, 2012.

In addition, in the normal course of business, the Company is a party to various legal proceedings. After reviewing all actions and proceedings pending against or involving the Company, management considers the aggregate loss, if any, will not be material to the Company's financial statements.

Items 1A through 5 are not applicable to the Company in the three months ended September 30, 2012.

Item 6. Exhibits.

- 3.1 Restated Certificate of Incorporation of Gyrodyne Company of America, Inc. (1)
- 3.2 Amended and Restated Bylaws of Gyrodyne Company of America, Inc. (2)
- 4.1 Form of Stock Certificate of Gyrodyne Company of America, Inc. (3)
- 4.2 Rights Agreement, dated as of August 10, 2004, by and between Gyrodyne Company of America, Inc. and Registrar and Transfer Company, as Rights Agent, including as Exhibit B the forms of Rights Certificate and of Election to Purchase. (4)
- 10.1 Rothschild Engagement Agreement. (5)
- 31.1 Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer/Chief Financial Officer. (5)
- 32.1 CEO/CFO Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (5)
- 101.INS\*\* XBRL Instance
- 101.SCH\*\*XBRL Taxonomy Extension Schema
- 101.CAL\*\*XBRL Taxonomy Extension Calculation
- 101.DEF\*\*XBRL Taxonomy Extension Definition
- 101.LAB\*\*XBRL Taxonomy Extension Labels
- 101.PRE\*\*XBRL Taxonomy Extension Presentation

(1) Incorporated herein by reference to the Annual Report on Form 10-KSB/A, filed with the Securities and Exchange Commission on September 5, 2001.

Seq. Page 23

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(2) Incorporated herein by reference to Form 8-K, filed with the Securities and Exchange Commission on June 18, 2008.

(3) Incorporated herein by reference to the Quarterly Report on Form 10-Q, filed with the Securities and Exchange Commission on November 13, 2008.

(4) Incorporated herein by reference to Form 8-K, filed with the Securities and Exchange Commission on August 13, 2004.

(5) Filed as part of this report.

\*\* XBRL information is furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.

## SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

GYRODYNE COMPANY OF AMERICA, INC.

Date: November 14, 2012

/s/ Gary Fitlin

By Gary Fitlin

Interim President and Chief Executive Officer

Chief Financial Officer and Treasurer

Seq. Page 24

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