

REX AMERICAN RESOURCES Corp
Form 10-Q
August 31, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended July 31, 2016

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

For the transition period from _____ to _____

Commission File Number 001-09097

REX AMERICAN RESOURCES CORPORATION

(Exact name of registrant as specified in its charter)

Delaware **31-1095548**
(State or other jurisdiction of **(I.R.S. Employer**
incorporation or organization) **Identification Number)**

7720 Paragon Road, Dayton, Ohio **45459**
(Address of principal executive offices) **(Zip Code)**

(937) 276-3931

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T 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 definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) 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

At the close of business on August 30, 2016 the registrant had 6,582,029 shares of Common Stock, par value \$.01 per share, outstanding.

REX AMERICAN RESOURCES CORPORATION AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION**Item 1. Financial Statements**

REX AMERICAN RESOURCES CORPORATION AND SUBSIDIARIES

Consolidated Condensed Balance Sheets

Unaudited

	July 31, 2016 (In Thousands)	January 31, 2016
Assets		
Current assets:		
Cash and cash equivalents	\$ 134,651	\$ 135,765
Restricted cash	110	54
Accounts receivable	15,833	13,666
Inventory	23,633	17,178
Refundable income taxes	1,562	5,254
Prepaid expenses and other	6,956	6,407
Deferred taxes, net	1,036	1,036
Total current assets	183,781	179,360
Property and equipment, net	189,006	189,976
Other assets	6,395	6,642
Equity method investments	38,622	38,707
Total assets	\$417,804	\$414,685
Liabilities and equity:		
Current liabilities:		
Accounts payable, trade	\$7,056	\$10,212
Accrued expenses and other current liabilities	8,346	9,423
Total current liabilities	15,402	19,635
Long-term liabilities:		
Deferred taxes	38,304	38,304
Other long-term liabilities	1,158	987
Total long-term liabilities	39,462	39,291
Equity:		
REX shareholders' equity:		
Common stock	299	299
Paid-in capital	145,721	144,844
Retained earnings	486,888	475,874
Treasury stock	(313,849)	(309,754)
Total REX shareholders' equity	319,059	311,263

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Noncontrolling interests	43,881	44,496
Total equity	362,940	355,759
Total liabilities and equity	\$417,804	\$414,685

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

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REX AMERICAN RESOURCES CORPORATION AND SUBSIDIARIES**Consolidated Condensed Statements Of Operations**

Unaudited

	Three Months Ended July 31,		Six Months Ended July 31,	
	2016	2015	2016	2015
	(In Thousands, Except Per Share Amounts)			
Net sales and revenue	\$115,707	\$113,480	\$215,929	\$218,677
Cost of sales	98,423	95,204	190,223	191,274
Gross profit	17,284	18,276	25,706	27,403
Selling, general and administrative expenses	(5,206)	(6,456)	(9,233)	(10,909)
Equity in income of unconsolidated affiliates	1,186	5,063	1,419	6,543
Gain on sale of investment	—	10,385	192	10,385
Gain on disposal of property and equipment, net	185	12	185	495
Interest and other income	97	107	257	325
Income before income taxes	13,546	27,387	18,526	34,242
Provision for income taxes	(4,517)	(8,676)	(6,031)	(11,092)
Net income	9,029	18,711	12,495	23,150
Net income attributable to noncontrolling interests	(853)	(2,344)	(1,481)	(2,856)
Net income attributable to REX common shareholders	\$8,176	\$16,367	\$11,014	\$20,294
Weighted average shares outstanding – basic and diluted	6,586	7,580	6,590	7,737
Basic and diluted net income per share attributable to REX common shareholders	\$1.24	\$2.16	\$1.67	\$2.62

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

REX AMERICAN RESOURCES CORPORATION AND SUBSIDIARIES**Consolidated Condensed Statements Of Equity****Unaudited**

(In Thousands)

	REX Shareholders							
	Common Shares Issued		Treasury		Paid-in Capital	Retained Earnings	Noncontrolling Interests	Total Equity
	Shares	Amount	Shares	Amount				
Balance at January 31, 2016	29,853	\$ 299	23,204	\$(309,754)	\$ 144,844	\$ 475,874	\$ 44,496	\$ 355,759
Net income						11,014	1,481	12,495
Treasury stock acquired			88	(4,353)				(4,353)
Stock based compensation expense			(22)	258	877			1,135
Noncontrolling interests distribution and other	—	—	—	—	—	—	(2,096)	(2,096)
Balance at July 31, 2016	29,853	\$ 299	23,270	\$(313,849)	\$ 145,721	\$ 486,888	\$ 43,881	\$ 362,940
Balance at January 31, 2015	29,853	\$ 299	21,954	\$(239,557)	\$ 144,791	\$ 444,438	\$ 42,993	\$ 392,964
Net income						20,294	2,856	23,150
Treasury stock acquired			764	(46,190)				(46,190)
Stock based compensation expense			(3)	2	10			12
Noncontrolling interests distribution and other	—	—	—	—	—	—	(507)	(507)
Balance at July 31, 2015	29,853	\$ 299	22,715	\$(285,745)	\$ 144,801	\$ 464,732	\$ 45,342	\$ 369,429

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

REX AMERICAN RESOURCES CORPORATION AND SUBSIDIARIES**Consolidated Condensed Statements Of Cash Flows****Unaudited**

	Six Months Ended July 31,	
	2016	2015
	(In Thousands)	
Cash flows from operating activities:		
Net income including noncontrolling interests	\$12,495	\$23,150
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, impairment charges and amortization	9,748	9,430
Income from equity method investments	(1,419)	(6,543)
Gain on disposal of real estate and property and equipment, net	(185)	(495)
Dividends received from equity method investees	1,504	5,638
Gain on sale of investment	(192)	(10,385)
Deferred income tax	—	(8,644)
Stock based compensation expense	40	10
Changes in assets and liabilities:		
Accounts receivable	(4,250)	(2,754)
Inventories	(6,455)	(5,188)
Other assets	2,989	192
Accounts payable, trade	(3,087)	261
Other liabilities	169	(2,110)
Net cash provided by operating activities	11,357	2,562
Cash flows from investing activities:		
Capital expenditures	(9,334)	(5,865)
Restricted cash	(56)	(203)
Restricted investments and deposits	409	250
Proceeds from sale of investment	2,275	45,476
Proceeds from sale of real estate and property and equipment, net	1,028	1,935
Other	12	12
Net cash (used in) provided by investing activities	(5,666)	41,605
Cash flows from financing activities:		
Dividend payments to and purchases of stock from noncontrolling interests holders	(2,096)	(507)
Treasury stock acquired	(4,709)	(43,250)
Net cash used in financing activities	(6,805)	(43,757)
Net (decrease) increase in cash and cash equivalents	(1,114)	410
Cash and cash equivalents, beginning of period	135,765	137,697
Cash and cash equivalents, end of period	\$134,651	\$138,107
Non cash investing activities – Accrued capital expenditures	\$1,350	\$370
Non cash financing activities – Accrued treasury stock repurchases	\$—	\$2,938
Non cash financing activities – Equity awards issued	\$1,095	\$—

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

REX AMERICAN RESOURCES CORPORATION AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

July 31, 2016

Note 1. Consolidated Condensed Financial Statements

The consolidated condensed financial statements included in this report have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission and include, in the opinion of management, all adjustments necessary to state fairly the information set forth therein. Any such adjustments were of a normal recurring nature. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted pursuant to such rules and regulations, although the Company believes that the disclosures are adequate to make the information presented not misleading. Financial information as of January 31, 2016 included in these financial statements has been derived from the audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended January 31, 2016 (fiscal year 2015). It is suggested that these unaudited consolidated condensed financial statements be read in conjunction with the consolidated financial statements and the notes thereto included in the Company's Annual Report on Form 10-K for the year ended January 31, 2016. The results of operations for the interim periods are not necessarily indicative of the results to be expected for the year.

Basis of Consolidation – The consolidated condensed financial statements in this report include the operating results and financial position of REX American Resources Corporation and its wholly and majority owned subsidiaries. All intercompany balances and transactions have been eliminated. The Company includes the results of operations of One Earth Energy, LLC (“One Earth”) in its Consolidated Condensed Statements of Operations on a delayed basis of one month.

Nature of Operations – The Company operates in one reportable segment, alternative energy, and has equity investments in three ethanol limited liability companies, two of which are majority ownership interests.

Note 2. Accounting Policies

The interim consolidated condensed financial statements have been prepared in accordance with the accounting policies described in the notes to the consolidated financial statements included in the Company's fiscal year 2015 Annual Report on Form 10-K. While management believes that the procedures followed in the preparation of interim financial information are reasonable, the accuracy of some estimated amounts is dependent upon facts that will exist

or calculations that will be accomplished at fiscal year-end. Examples of such estimates include accrued liabilities, such as management bonuses, and the provision for income taxes. Any adjustments pursuant to such estimates during the quarter were of a normal recurring nature. Actual results could differ from those estimates.

Revenue Recognition

The Company recognizes sales from the production of ethanol, distillers grains and non-food grade corn oil when title transfers to customers, generally upon shipment from the ethanol plant or upon loading of the rail car used to transport the products.

Cost of Sales

Cost of sales includes direct production costs and certain overhead costs such as depreciation, property taxes and utilities related to producing ethanol and related by-products.

Selling, General and Administrative Expenses

The Company includes non-production related costs such as professional fees, selling charges and certain payroll in selling, general and administrative expenses.

Financial Instruments

Certain of the forward grain purchase and ethanol, distillers grains and non-food grade corn oil sale contracts are accounted for under the “normal purchases and normal sales” scope exemption of Accounting Standards Codification (“ASC”) 815, “*Derivatives and Hedging*” because these arrangements are for purchases of grain that will be delivered in quantities expected to be used by the Company and sales of ethanol, distillers grains and non-food grade corn oil quantities expected to be produced by the Company over a reasonable period of time in the normal course of business. During fiscal year 2015, the Company began to carry a portion of its forward grain purchase contracts at fair value.

The Company uses derivative financial instruments (exchange-traded futures contracts) to manage a portion of the risk associated with changes in commodity prices, primarily related to corn. The Company monitors and manages this exposure as part of its overall risk management policy. As such, the Company seeks to reduce the potentially adverse effects that the volatility of these markets may have on its operating results. The Company may take hedging positions in these commodities as one way to mitigate risk. While the Company attempts to link its hedging activities to purchase and sales activities, there are situations in which these hedging activities can themselves result in losses. The Company does not hold or issue derivative financial instruments for trading or speculative purposes. The changes in fair value of these derivative financial instruments are recognized in current period earnings as the Company does not use hedge accounting.

Income Taxes

The Company applies an effective tax rate to interim periods that is consistent with the Company's estimated annual tax rate as adjusted for discrete items impacting the interim periods. The Company provides for deferred tax liabilities and assets for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis and operating loss and tax credit carryforwards. The Company provides for a valuation allowance if, based on the weight of available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized. The Company paid income taxes of approximately \$1,010,000 and \$19,680,000 during the six months ended July 31, 2016 and 2015, respectively. The Company received no refunds of income taxes during the six months ended July 31, 2016. The Company received refunds of state income taxes of approximately \$100,000 during the six months ended July 31, 2015.

As of July 31, 2016 and January 31, 2016, total unrecognized tax benefits were approximately \$987,000. Accrued penalties and interest were approximately \$171,000 at July 31, 2016. There were no accrued penalties and interest at January 31, 2016. If the Company were to prevail on all unrecognized tax benefits recorded, the provision for income taxes would be reduced by approximately \$987,000. In addition, the impact of penalties and interest would also benefit the effective tax rate. Interest and penalties associated with unrecognized tax benefits are recorded within income tax expense. On a quarterly basis, the Company accrues for the effects of open uncertain tax positions and the related potential penalties and interest.

Inventories

Inventories are carried at the lower of cost or market on a first-in, first-out basis. Inventory includes direct production costs and certain overhead costs such as depreciation, property taxes and utilities related to producing ethanol and related by-products. Inventory is permanently written down for instances when cost exceeds estimated net realizable value; such write-downs are based primarily upon commodity prices as the market value of inventory is often dependent upon changes in commodity prices. There were no significant permanent write-downs of inventory at July 31, 2016 and January 31, 2016. Fluctuations in the write-down of inventory generally relate to the levels and composition of such inventory at a given point in time. The components of inventory are as follows as of the dates presented (amounts in thousands):

	July 31, 2016	January 31, 2016
Ethanol and other finished goods	\$5,469	\$3,105
Work in process	2,912	2,652
Grain and other raw materials	15,252	11,421
Total	\$23,633	\$17,178

Property and Equipment

Property and equipment is recorded at cost. Depreciation is computed using the straight-line method. Estimated useful lives are 15 to 40 years for buildings and improvements, and 2 to 20 years for fixtures and equipment.

In accordance with ASC 360-10 "*Impairment or Disposal of Long-Lived Assets*", the carrying value of long-lived assets is assessed for recoverability by management when changes in circumstances indicate that the carrying amount may not be recoverable, based on an analysis of undiscounted future expected cash flows from the use and ultimate disposition of the asset. There were no impairment charges in the first six months of fiscal year 2016 and approximately \$125,000 of impairment charges in the first six months of fiscal year 2015, included in cost of sales in the accompanying Consolidated Condensed Statement of Operations. The impairment charges are related to unfavorable changes in real estate conditions in local markets. Impairment charges result from the Company's

management performing cash flow analysis and represent management's estimate of the excess of net book value over fair value.

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The Company tests for recoverability of an asset group by comparing its carrying amount to its estimated undiscounted future cash flows. If the carrying amount of an asset group exceeds its estimated undiscounted future cash flows, the Company recognizes an impairment charge for the amount by which the asset group's carrying amount exceeds its fair value, if any. The Company generally determines the fair value of the asset group using a discounted cash flow model based on market participant assumptions (for income producing asset groups) or by obtaining appraisals based on the market approach and comparable market transactions (for non-income producing asset groups).

Investments

The method of accounting applied to long-term investments, whether consolidated, equity or cost, involves an evaluation of the significant terms of each investment that explicitly grant or suggest evidence of control or influence over the operations of the investee and also includes the identification of any variable interests in which the Company is the primary beneficiary. The Company consolidates the results of two majority owned subsidiaries, One Earth and NuGen. The results of One Earth are included on a delayed basis of one month lag as One Earth has a fiscal year end of December 31. NuGen has the same fiscal year as the parent, and therefore, there is no lag in reporting the results of NuGen. The Company accounts for investments in a limited liability company in which it has a less than 20% ownership interest, using the equity method of accounting when the factors discussed in ASC 323, "*Investments-Equity Method and Joint Ventures*" are met. The excess of the carrying value over the underlying equity in the net assets of equity method investees is allocated to specific assets and liabilities. Any unallocated excess is treated as goodwill and is recorded as a component of the carrying value of the equity method investee. Investments in businesses that the Company does not control but for which it has the ability to exercise significant influence over operating and financial matters are accounted for using the equity method. The Company accounts for its investments in Big River Resources, LLC ("Big River") and Patriot Holdings, LLC ("Patriot") (through May 31, 2015 – see Note 10 for a discussion of the sale of the Company's equity interest in Patriot) using the equity method of accounting and includes the results of these entities on a delayed basis of one month as they have a fiscal year end of December 31.

The Company periodically evaluates its investments for impairment due to declines in market value considered to be other than temporary. Such impairment evaluations include general economic and company-specific evaluations. If the Company determines that a decline in market value is other than temporary, then a charge to earnings is recorded in the Consolidated Condensed Statements of Operations and a new cost basis in the investment is established.

Comprehensive Income

The Company has no components of other comprehensive income, and therefore, comprehensive income equals net income.

Accounting Changes and Recently Issued Accounting Standards

In March 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2016-09, “*Improvements to Employee share-Based Payment Accounting*”. This standard simplifies the accounting treatment for excess tax benefits and deficiencies, forfeitures, and cash flow considerations related to share-based compensation. This standard is effective for annual and interim periods beginning after December 15, 2016. The Company has not determined the effect of this standard on its consolidated financial statements and related disclosures.

In January 2016, the FASB issued ASU 2016-01. “*Recognition and Measurement of Financial Assets and Financial Liabilities*”. This standard provides guidance for the recognition, measurement, presentation and disclosure of financial instruments. This ASU is effective for annual and interim periods beginning after December 15, 2017, and early adoption is not permitted. The Company has not determined the effect of this standard on its consolidated financial statements and related disclosures.

In February 2016, the FASB issued ASU 2016-02 “*Leases*”. This standard requires that virtually all leases will be recognized by lessees on their balance sheet as a right-of-use asset and a corresponding lease liability, including leases currently accounted for as operating leases. The Company will be required to adopt this standard effective February 1, 2019. The Company has not determined the effect of this standard on its consolidated financial statements and related disclosures.

Note 3. Leases

At July 31, 2016, the Company has lease agreements, as lessee, for rail cars and a natural gas pipeline. All of the leases are accounted for as operating leases. The following table is a summary of future minimum rentals on such leases (amounts in thousands):

Years Ended January 31,	Minimum Rentals
Remainder of 2017	\$ 3,669
2018	6,575
2019	5,845
2020	4,341
2021	2,778
Thereafter	4,169
Total	\$ 27,377

Note 4. *Fair Value*

The Company applies ASC 820, “*Fair Value Measurements and Disclosures*”, (“ASC 820”) which provides a framework for measuring fair value under accounting principles generally accepted in the United States of America. This accounting standard defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

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The Company determines the fair market values of its financial instruments based on the fair value hierarchy established by ASC 820 which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair values which are provided below. The Company carries certain cash equivalents, investments and derivative instruments at fair value.

The fair values of derivative assets and liabilities traded in the over-the-counter market are determined using quantitative models that require the use of multiple market inputs including interest rates, prices and indices to generate pricing and volatility factors, which are used to value the position. The predominance of market inputs are actively quoted and can be validated through external sources, including brokers, market transactions and third-party pricing services. Estimation risk is greater for derivative asset and liability positions that are either option-based or have longer maturity dates where observable market inputs are less readily available or are unobservable, in which case interest rate, price or index scenarios are extrapolated in order to determine the fair value. The fair values of derivative assets and liabilities include adjustments for market liquidity, counterparty credit quality, the Company's own credit standing and other specific factors, where appropriate. The fair values of property and equipment are determined by using various models that discount future expected cash flows.

To ensure the prudent application of estimates and management judgement in determining the fair value of derivative assets and liabilities, investments and property and equipment, various processes and controls have been adopted, which include: (i) model validation that requires a review and approval for pricing, financial statement fair value determination and risk quantification; and (ii) periodic review and substantiation of profit and loss reporting for all derivative instruments. Financial assets and liabilities measured at fair value on a recurring basis at July 31, 2016 are summarized below (amounts in thousands):

	Level 1	Level 2	Level 3	Fair Value
Commodity futures (1)	\$632	\$—	\$—	\$ 632
Investment in cooperative (2)	—	—	333	333
Total assets	\$632	\$—	\$333	\$ 965
Forward purchase contract liability (3)	\$—	\$695	\$—	\$ 695

Financial assets and liabilities measured at fair value on a recurring basis at January 31, 2016 are summarized below (amounts in thousands):

	Level 1	Level 2	Level 3	Fair Value
Investment in cooperative (2)	\$ —	\$—	\$333	\$ 333
Forward purchase contracts liability (3)	\$ —	\$312	\$—	\$ 312

- (1) Commodity futures are included in “Prepaid expenses and other current assets” on the accompanying Consolidated Condensed Balance Sheets.
- (2) The investment in cooperative is included in “Other assets” on the accompanying Consolidated Condensed Balance Sheets.
- (3) The forward purchase contract liability is included in “Accrued expenses and other current liabilities” on the accompanying Consolidated Condensed Balance Sheets.

The Company determined the fair value of the investment in cooperative by using a discounted cash flow analysis on the expected cash flows. Inputs used in the analysis include the face value of the allocated equity amount, the projected term for repayment based upon a historical trend, and a risk adjusted discount rate based on the expected compensation participants would demand because of the uncertainty of the future cash flows. The inherent risk and uncertainty associated with unobservable inputs could have a significant effect on the actual fair value of the investment.

There were no assets measured at fair value on a non-recurring basis at July 31, 2016 or January 31, 2016.

Note 5. Property and Equipment

The components of property and equipment are as follows for the periods presented (amounts in thousands):

	July 31, 2016	January 31, 2016
Land and improvements	\$21,069	\$21,598
Buildings and improvements	24,280	24,543
Machinery, equipment and fixtures	252,357	237,735
Construction in progress	331	6,094
	298,037	289,970
Less: accumulated depreciation	(109,031)	(99,994)
Total	\$ 189,006	\$ 189,976

Note 6. Other Assets

The components of other assets are as follows for the periods presented (amounts in thousands):

	July 31, 2016	January 31, 2016
Real estate taxes refundable	\$5,186	\$5,091
Deposits	255	664
Other	954	887
Total	\$6,395	\$6,642

Real estate taxes refundable represent amounts due One Earth associated with refunds of previously paid taxes in connection with a tax increment financing arrangement with local taxing authorities. Deposits are with utility and other vendors.

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Note 7. *Accrued Expenses and Other Current Liabilities*

The components of accrued expenses and other current liabilities are as follows for the periods presented (amounts in thousands):

	July 31, 2016	January 31, 2016
Accrued utility charges	\$1,866	\$2,094
Accrued payroll and related items	1,794	3,760
Accrued income taxes	1,140	—
Accrued real estate taxes	2,100	2,564
Other	1,446	1,005
Total	\$8,346	\$9,423

Note 8. *Revolving Lines of Credit*

Effective April 1, 2016, One Earth and NuGen each entered into \$10.0 million revolving loan facilities that mature April 1, 2017. Any borrowings will be secured by the inventory and accounts receivable of One Earth or NuGen, specific to which entity borrows money under these facilities. These revolving loan facilities are recourse only to One Earth and NuGen and not to REX American Resources Corporation or any of its other subsidiaries. Borrowings under these facilities bear interest at the one month LIBOR rate plus 250 basis points. Neither One Earth nor NuGen had outstanding borrowings on the revolving loans during the six months ended July 31, 2016. One Earth and NuGen are also subject to certain financial covenants under the revolving loan facilities, including working capital requirements, should they borrow on the loans.

Note 9. *Derivative Financial Instruments*

The Company is exposed to various market risks, including changes in commodity prices (raw materials and finished goods). To manage risks associated with the volatility of these natural business exposures, the Company enters into commodity agreements and forward purchase (corn) and sale (ethanol, distillers grains and non-food grade corn oil) contracts. The Company does not purchase or sell derivative financial instruments for trading or speculative purposes. The Company does not purchase or sell derivative financial instruments for which a lack of marketplace quotations would require the use of fair value estimation techniques.

The following table provides information about the fair values of the Company's derivative financial instruments and the line items on the Consolidated Condensed Balance Sheets in which the fair values are reflected (in thousands):

	Asset Derivatives Fair Value at July 31, 2016		Liability Derivatives Fair Value at July 31, 2015	
Commodity futures (1)	\$632	\$448	\$—	\$—
Forward purchase contracts (2)	\$—	\$—	\$695	\$469
Total				

(1) Commodity futures are included in other prepaid expense and other current assets. These futures contracts are for approximately 1.3 million and approximately 1.6 million bushels of corn at July 31, 2016 and 2015, respectively.

(2) Forward purchase contracts are included in accrued expenses and other current liabilities. These contracts are for purchases of approximately 0.9 million and approximately 1.1 million bushels of corn at July 31, 2016 and 2015, respectively.

As of July 31, 2016, all of the derivative financial instruments held by the Company were subject to enforceable master netting arrangements. The Company's accounting policy is to offset positions amounts owed or owing with the same counterparty. As of July 31, 2016, the gross positions of the enforceable master netting agreements are not significantly different from the net positions presented in the table above. Depending on the amount of an unrealized loss on a derivative contract held by the Company, the counterparty may require collateral to secure the Company's derivative contract position. As of July 31, 2016, the Company was required to maintain collateral with the counterparty in the amount of approximately \$110,000 to secure the Company's derivative liability position.

See Note 4 which contains fair value information related to derivative financial instruments.

Gains of approximately \$1,136,000 and \$59,000 for the second quarters of fiscal years 2016 and 2015, respectively, on the Company's derivative financial instruments were included in cost of sales on the Consolidated Condensed Statements of Operations. Gains of approximately \$1,625,000 and \$75,000 for the first six months of fiscal years 2016 and 2015, respectively, on the Company's derivative financial instruments were included in cost of sales on the Consolidated Condensed Statements of Operations.

Note 10. Investments

The following table summarizes equity method investments at July 31, 2016 and January 31, 2016 (dollars in thousands):

Entity	Ownership Percentage	Carrying Amount July 31, 2016	Carrying Amount January 31, 2016
Big River	9.7 %	\$ 38,622	\$ 38,707

The following table summarizes income recognized from equity method investments for the periods presented (dollars in thousands):

	Three Months Ended July 31, 2016		Six Months Ended July 31, 2016	
	2016	2015	2016	2015
Big River	\$1,186	\$2,589	\$1,419	\$3,596
Patriot (sold June 1, 2015)	—	2,474	—	2,947
Total	\$1,186	\$5,063	\$1,419	\$6,543

Undistributed earnings of the equity method investee totaled approximately \$18.6 million and \$18.7 million at July 31, 2016 and January 31, 2016, respectively. During the first six months of fiscal years 2016 and 2015, the Company received dividends from equity method investees of approximately \$1.5 million and \$5.6 million, respectively.

Summarized financial information for each of the Company's equity method investees is presented in the following table for the periods presented (amounts in thousands):

	Three Months Ended July 31, 2016		Three Months Ended July 31, 2015	
	Patriot (1)	Big River	Patriot (1)	Big River
Net sales and revenue	\$—	\$210,974	\$52,375	\$223,191
Gross profit	\$—	\$17,057	\$10,605	\$38,463

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Income from continuing operations	\$—\$12,216	\$9,321	\$26,663
Net income	\$—\$12,216	\$9,321	\$26,663

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	Six Months Ended July 31, 2016		Six Months Ended July 31, 2015	
	Patriot (1)	Big River	Patriot (1)	Big River
Net sales and revenue	\$—	\$394,545	\$115,614	\$407,998
Gross profit	\$—	\$22,928	\$14,424	\$49,267
Income from continuing operations	\$—	\$14,620	\$11,100	\$37,040
Net income	\$—	\$14,620	\$11,100	\$37,040

(1) The Company's equity interest in Patriot was sold June 1, 2015, results are for the two and five month periods ended May 31, 2015.

Big River has debt agreements that limit amounts Big River can pay in the form of dividends or advances to owners. The restricted net assets of Big River at July 31, 2016 and January 31, 2016 are approximately \$303.3 million and \$306.3 million, respectively.

On June 1, 2015, Patriot and a subsidiary of CHS Inc. ("CHS") completed a merger that resulted in CHS acquiring 100% of the ownership interest in Patriot. During the first quarter of fiscal year 2016, the Company received proceeds of approximately \$2.3 million as partial payment for certain escrow holdbacks and adjustments to the purchase price. As a result, the Company recognized approximately \$0.2 million as gain on sale of investment during the first quarter of fiscal year 2016. At July 31, 2016, the Company has approximately \$2.3 million in accounts receivable on the accompanying Consolidated Condensed Balance Sheet related to estimated escrow proceeds that were recognized as income. The Company expects that a determination of the final payment of escrowed proceeds to be received will occur by December 1, 2016.

Note 11. Income Taxes

The effective tax rate on consolidated pre-tax income was 33.3% for the three months ended July 31, 2016, and 31.7% for the three months ended July 31, 2015. The effective tax rate on consolidated pre-tax income was 32.6% for the six months ended July 31, 2016, and 32.4% for the six months ended July 31, 2015. The fluctuation in the effective tax rate primarily relates to the impact of noncontrolling interests.

The Company files a U.S. federal income tax return and income tax returns in various states. In general, the Company is no longer subject to U.S. federal, state or local income tax examinations by tax authorities for years ended January 31, 2010 and prior. A reconciliation of the beginning and ending amount of unrecognized tax benefits, including interest and penalties, is as follows (amounts in thousands):

Unrecognized tax benefits, January 31, 2016	\$987
Changes for prior years' tax positions	171
Changes for current year tax positions	—
Unrecognized tax benefits, July 31, 2016	\$1,158

Note 12. Commitments and Contingencies

The Company is involved in various legal actions arising in the normal course of business. After taking into consideration legal counsels' evaluations of such actions, management is of the opinion that their outcome will not have a material adverse effect on the Company's Consolidated Condensed Financial Statements.

One Earth and NuGen have combined forward purchase contracts for approximately 8.2 million bushels of corn, the principal raw material for their ethanol plants. They expect to take delivery of the grain through December 2016.

One Earth and NuGen have combined sales commitments for approximately 37.2 million gallons of ethanol, approximately 61,000 tons of distillers grains and approximately 9.9 million pounds of non-food grade corn oil. They expect to deliver the ethanol, distillers grains and non-food grade corn oil through September 2016.

Note 13. Net Sales and Revenue

The following table summarizes sales for each product and service group for the periods presented (amounts in thousands):

Product or Service Category	Three Months Ended		Six Months Ended	
	July 31, 2016	2015	July 31, 2016	2015
Ethanol	\$90,933	\$86,990	\$168,564	\$165,562
Dried distillers grains	18,946	21,585	36,000	41,836
Non-food grade corn oil	4,738	4,049	8,584	8,008
Modified distillers grains	983	696	2,547	3,001
Other	107	160	234	270

Total	\$115,707	\$113,480	\$215,929	\$218,677
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Note 14. *Related-Party Transactions*

During the second quarters of fiscal year 2016 and 2015, One Earth and NuGen purchased approximately \$36.0 million and approximately \$38.0 million, respectively, of corn from minority equity investors and board members of those subsidiaries. Such purchases totaled approximately \$80.4 million and approximately \$76.3 million for the six months ended July 31, 2016 and 2015, respectively.

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

At July 31, 2016, we had equity investments in three ethanol limited liability companies, two of which we have a majority ownership interest in. The following table is a summary of ethanol gallons shipped at our plants:

Entity	Trailing 12 Months Ethanol Gallons Shipped	REX's Current Effective Ownership Interest	Current Effective Ownership of Trailing 12 Months Ethanol Gallons Shipped
One Earth Energy, LLC	117.0	M 75.0	% 87.8 M
NuGen Energy, LLC	121.1	M 99.5	% 120.5 M
Big River Resources, LLC:			
Big River Resources W Burlington, LLC	107.7	M 9.7	% 10.4 M
Big River Resources Galva, LLC	125.0	M 9.7	% 12.1 M
Big River United Energy, LLC	126.1	M 5.4	% 6.8 M
Big River Resources Boyceville, LLC	57.9	M 9.7	% 5.6 M
Total	654.8	M	243.2 M

Our ethanol operations are highly dependent on commodity prices, especially prices for corn, ethanol, distillers grains, non-food grade corn oil and natural gas. As a result of price volatility for these commodities, our operating results can fluctuate substantially. The price and availability of corn is subject to significant fluctuations depending upon a number of factors that affect commodity prices in general, including crop conditions, weather, federal policy and foreign trade. Because the market price of ethanol is not always directly related to corn prices (for example, crude and other energy prices can impact ethanol prices), at times ethanol prices may lag movements in corn prices and, in an environment of higher corn prices or lower ethanol prices, reduce the overall margin structure at the plants. As a result, at times, we may operate our plants at negative or marginally positive operating margins.

We expect our ethanol plants to produce approximately 2.8 gallons of denatured ethanol for each bushel of grain processed in the production cycle. We refer to the difference between the price per gallon of ethanol and the price per bushel of grain (divided by 2.8) as the "crush spread". Should the crush spread decline, it is possible that our ethanol plants will generate operating results that do not provide adequate cash flows for sustained periods of time. In such cases, production at the ethanol plants may be reduced or stopped altogether in order to minimize variable costs at individual plants.

We attempt to manage the risk related to the volatility of commodity prices by utilizing forward grain purchase and forward ethanol, distillers grains and corn oil sale contracts as management deems appropriate. We attempt to match quantities of these sale contracts with an appropriate quantity of grain purchase contracts over a given period of time when we can obtain an adequate gross margin resulting from the contracts we have executed. However, the market for future ethanol sales contracts generally lags the spot market with respect to ethanol price. Consequently, we generally execute fixed price contracts for no more than four months into the future at any given time and we may lock in our corn or ethanol price without having a corresponding locked in ethanol or corn price for short durations of time. As a

result of

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the relatively short period of time our contracts cover, we generally cannot predict the future movements in the crush spread for more than four months; thus, we are unable to predict the likelihood or amounts of future income or loss from the operations of our ethanol facilities. We utilize derivative financial instruments, primarily exchange traded commodity future contracts, in conjunction with certain of our grain procurement activities.

Future Energy

During fiscal year 2013, we entered into a joint venture with Hytken HPGP, LLC (“Hytken”) to file and defend patents for eSteam technology relating to heavy oil and oil sands production methods, and to commercially exploit the technology to generate license fees, royalty income and development opportunities. The patented technology is an enhanced method of heavy oil recovery involving zero emissions downhole steam generation. We own 60% and Hytken owns 40% of the entity named Future Energy, LLC.

We have agreed to fund direct patent expenses relating to patent applications and defense, annual annuity fees and maintenance on a country by country basis, with the right to terminate funding and transfer related patent rights to Hytken. We may also fund, through loans, all costs relating to new intellectual property, consultants, and future research and development, pilot field tests and equipment purchases for commercialization stage of the patents. We have paid approximately \$1,684,000 cumulatively, including \$73,000 in fiscal year 2016 for our ownership interest, patent and other expenses.

Critical Accounting Policies and Estimates

During the three months ended July 31, 2016, we did not change any of our critical accounting policies as disclosed in our 2015 Annual Report on Form 10-K as filed with the Securities and Exchange Commission on March 25, 2016. All other accounting policies used in preparing our interim fiscal year 2016 Consolidated Condensed Financial Statements are the same as those described in our Form 10-K.

Fiscal Year

All references in this report to a particular fiscal year are to REX’s fiscal year ended January 31. For example, “fiscal year 2016” means the period February 1, 2016 to January 31, 2017.

Results of Operations**Comparison of Three and Six Months Ended July 31, 2016 and 2015**

The following table summarizes selected data from our consolidated operations for the periods presented:

	Three Months Ended		Six Months Ended	
	July 31, 2016	2015	July 31, 2016	2015
Average selling price per gallon of ethanol	\$1.49	\$1.50	\$1.41	\$1.46
Gallons of ethanol sold (in millions)	60.9	57.9	119.7	113.7
Average selling price per ton of dried distillers grains	\$134.81	\$169.31	\$130.12	\$156.16
Tons of dried distillers grains sold	140,541	127,493	276,662	267,900
Average selling price per pound of non-food grade corn oil	\$0.29	\$0.28	\$0.27	\$0.28
Pounds of non-food grade corn oil sold (in millions)	16.4	14.6	32.2	28.5
Average selling price per ton of modified distillers grains	\$56.60	\$73.95	\$58.54	\$78.48
Tons of modified distillers grains sold	17,370	9,415	43,517	38,246
Average cost per bushel of grain	\$3.73	\$3.64	\$3.63	\$3.65
Average cost of natural gas (per mmbtu)	\$2.71	\$3.42	\$2.96	\$4.13

Net sales and revenue in the quarter ended July 31, 2016 were approximately \$115.7 million compared to approximately \$113.5 million in the prior year's second quarter, representing an increase of approximately \$2.2 million. Net sales and revenue in the first six months of fiscal year 2016 were approximately \$215.9 million compared to approximately \$218.7 million in the in the first six months of fiscal year 2015, representing a decrease of approximately \$2.8 million.

The following table summarizes sales of our consolidated operations for each major product and service group for the periods presented (amounts in thousands):

Product Category	Three Months Ended		Six Months Ended	
	July 31, 2016	2015	July 31, 2016	2015
Ethanol	\$90,933	\$86,990	\$168,564	\$165,562
Dried distillers grains	18,946	21,585	36,000	41,836
Non-food grade corn oil	4,738	4,049	8,584	