

CADIZ INC  
Form 10-Q  
November 08, 2013

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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 September 30, 2013

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 0-12114

Cadiz Inc.

(Exact name of registrant specified in its charter)

DELAWARE  
(State or other jurisdiction of  
incorporation or organization)

77-0313235  
(I.R.S. Employer  
Identification No.)

550 South Hope Street, Suite 2850  
Los Angeles, California  
(Address of principal executive offices)

90071  
(Zip Code)

Registrant's telephone number, including area code: (213) 271-1600

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 the definitions 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  Smaller Reporting Company

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Indicate by check mark whether the Registrant is a shell company (as defined in Exchange Act Rule 12b-2).  
Yes \_\_\_ No

As of November 5, 2013, the Registrant had 16,152,756 shares of common stock, par value \$0.01 per share, outstanding.

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Cadiz Inc.

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Cadiz Inc.

## Consolidated Statements of Operations and Comprehensive Loss (Unaudited)

| (\$ in thousands except per share data)                    | For the Three Months |                             |
|--|----------------------|-----------------------------|
|  | 2013                 | Ended September 30,<br>2012 |
| Revenues   | \$ 182               | \$ 287                      |
| Costs and expenses:  |                      |                             |
| Cost of sales  | 292                  | 293                         |
| General and administrative                                 | 2,934                | 2,965                       |
| Depreciation   | 63                   | 97                          |
| Total costs and expenses                                   | 3,289                | 3,355                       |
| Operating loss   | (3,107 )             | (3,068 )                    |
| Interest expense, net                                      | (1,689 )             | (1,665 )                    |
| Loss before income taxes                                   | (4,796 )             | (4,733 )                    |
| Income tax provision                                       | 1                    | 3                           |
| Net loss and comprehensive loss applicable to common stock | \$ (4,797 )          | \$ (4,736 )                 |
| Basic and diluted net loss per common share                | \$ (0.31 )           | \$ (0.31 )                  |
| Basic and diluted weighted average shares outstanding      | 15,453               | 15,439                      |

See accompanying notes to the consolidated financial statements.

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Cadiz Inc.

## Consolidated Statements of Operations and Comprehensive Loss (Unaudited)

| (\$ in thousands except per share data)                    | 2013         | For the Nine Months<br>Ended September 30,<br>2012 |
|--|--------------|--|
| Revenues   | \$ 190       | \$ 324   |
| Costs and expenses:  |              |  |
| Cost of sales  | 292          | 295  |
| General and administrative                                 | 9,629        | 8,683  |
| Depreciation   | 191          | 285  |
| Total costs and expenses                                   | 10,112       | 9,263  |
| Operating loss   | (9,922 )     | (8,939 )   |
| Interest expense, net                                      | (5,715 )     | (4,821 )   |
| Loss on extinguishment of debt and debt refinancing        | (1,055 )     | -  |
| Loss before income taxes                                   | (16,692 )    | (13,760 )  |
| Income tax provision                                       | 5            | 8  |
| Net loss and comprehensive loss applicable to common stock | \$ (16,697 ) | \$ (13,768 )                                       |
| Basic and diluted net loss per common share                | \$ (1.08 )   | \$ (0.89 )   |
| Basic and diluted weighted average shares outstanding      | 15,451       | 15,438   |

See accompanying notes to the consolidated financial statements.

Cadiz Inc.

## Consolidated Balance Sheets (Unaudited)

| (\$ in thousands except share data)  | September 30,<br>2013 | December 31,<br>2012 |
|--|-----------------------|----------------------|
| <b>ASSETS</b>  |                       |                      |
| Current assets:  |                       |                      |
| Cash and cash equivalents  | \$ 5,141              | \$ 1,685             |
| Accounts receivable  | 356                   | 260                  |
| Inventories  | 217                   | -                    |
| Prepaid expenses and other   | 471                   | 404                  |
| <b>Total current assets</b>  | <b>6,185</b>          | <b>2,349</b>         |
| Property, plant, equipment and water programs, net   | 43,883                | 44,074               |
| Goodwill   | 3,813                 | 3,813                |
| Debt issuance costs  | 1,122                 | 81                   |
| Other assets   | 2,975                 | 201                  |
| <b>Total Assets</b>  | <b>\$ 57,978</b>      | <b>\$ 50,518</b>     |
| <b>LIABILITIES AND STOCKHOLDERS' DEFICIT</b>   |                       |                      |
| Current liabilities:   |                       |                      |
| Accounts payable   | \$ 963                | \$ 957               |
| Accrued liabilities  | 1,224                 | 1,395                |
| Current portion of long-term debt  | 11                    | 11                   |
| <b>Total current liabilities</b>   | <b>2,198</b>          | <b>2,363</b>         |
| Long-term debt, net  | 87,090                | 63,250               |
| Deferred revenue   | 750                   | 750                  |
| Other long-term liabilities  | 923                   | 923                  |
| <b>Total Liabilities</b>   | <b>90,961</b>         | <b>67,286</b>        |
| Stockholders' deficit:   |                       |                      |
| Common stock - \$.01 par value; 70,000,000 shares<br>authorized; shares issued and outstanding – 15,452,756 at<br>September 30, 2013 and 15,438,961 at December 31, 2012 | 154                   | 154                  |
| Additional paid-in capital   | 301,521               | 301,039              |
| Accumulated deficit  | (334,658 )            | (317,961 )           |
| <b>Total stockholders' deficit</b>   | <b>(32,983 )</b>      | <b>(16,768 )</b>     |
| <b>Total Liabilities and Stockholders' Deficit</b>   | <b>\$ 57,978</b>      | <b>\$ 50,518</b>     |

See accompanying notes to the consolidated financial statements.





Cadiz Inc.

## Consolidated Statements of Cash Flows (Unaudited)

| (\$ in thousands)  | For the Nine Months<br>Ended September 30, |           |
|--|--|-----------|
|  | 2013                                       | 2012      |
| <b>Cash flows from operating activities:</b>                                 |  |           |
| Net loss   | \$ (16,697 )                               | (13,768 ) |
| Adjustments to reconcile net loss to net cash used for operating activities: |  |           |
| Depreciation   | 191  | 285       |
| Amortization of debt discount and issuance costs                             | 1,418                                      | 2,196     |
| Interest expense added to loan principal                                     | 4,297                                      | 2,628     |
| Loss on early extinguishment of debt and debt refinancing                    | 835  | -         |
| Compensation charge for stock and share options                              | 483  | 314       |
| Changes in operating assets and liabilities:                                 |  |           |
| Increase in accounts receivable  | (96 )                                      | (233 )    |
| Increase in inventories  | (217 )                                     | (316 )    |
| Increase in prepaid expenses and other                                       | (67 )                                      | (606 )    |
| (Increase) decrease in other assets  | (2,774 )                                   | 31        |
| Increase in accounts payable   | 173  | 76        |
| (Decrease ) increase in accrued liabilities                                  | (172 )                                     | 974       |
| Increase in deferred revenue   | -  | 250       |
| Net cash used for operating activities                                       | (12,626 )                                  | (8,169 )  |
| <b>Cash flows from investing activities:</b>                                 |  |           |
| Additions to property, plant and equipment                                   | (167 )                                     | (1,449 )  |
| Increase in restricted cash  | -  | (428 )    |
| Net cash used for investing activities                                       | (167 )                                     | (1,877 )  |
| <b>Cash flows from financing activities:</b>                                 |  |           |
| Proceeds from issuance of long-term debt                                     | 17,500                                     | 56        |
| Debt issuance costs  | (1,243 )                                   | -         |
| Principal payments on long-term debt   | (8 )                                       | (7 )      |
| Net cash provided by financing activities                                    | 16,249                                     | 49        |
| Net increase (decrease) in cash and cash equivalents                         | 3,456                                      | (9,997 )  |
| Cash and cash equivalents, beginning of period                               | 1,685                                      | 11,370    |
| Cash and cash equivalents, end of period                                     | \$ 5,141                                   | \$ 1,373  |

See accompanying notes to the consolidated financial statements.

Cadiz Inc.

## Consolidated Statement of Stockholders' Deficit (Unaudited)

(\$ in thousands except per share data)

|                                  | Common<br>Shares | Stock<br>Amount | Additional<br>Paid-in<br>Capital | Accumulated<br>Deficit | Total<br>Stockholders'<br>Deficit |
|----------------------------------|------------------|-----------------|----------------------------------|------------------------|-----------------------------------|
| Balance as of December 31, 2012  | 15,438,961       | \$154           | \$301,039                        | \$ (317,961 )          | \$ (16,768 )                      |
| Stock awards                     | 13,795           | -               | -                                | -                      | -                                 |
| Stock-based compensation expense | -                | -               | 482                              | -                      | 482                               |
| Net loss and comprehensive loss  | -                | -               | -                                | (16,697 )              | (16,697 )                         |
| Balance as of September 30, 2013 | 15,452,756       | \$154           | \$301,521                        | \$ (334,658 )          | \$ (32,983 )                      |

See accompanying notes to the consolidated financial statements.

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Cadiz Inc.

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Notes To The Consolidated Financial Statements (Unaudited)

## NOTE 1 – DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Consolidated Financial Statements have been prepared by Cadiz Inc., also referred to as “Cadiz” or “the Company”, without audit and should be read in conjunction with the Consolidated Financial Statements and notes thereto included in the Company’s Form 10-K for the year ended December 31, 2012.

### Basis of Presentation

The foregoing Consolidated Financial Statements include the accounts of the Company and contain all adjustments, consisting only of normal recurring adjustments, which management considers necessary for a fair statement of the Company’s financial position, the results of its operations and its cash flows for the periods presented and have been prepared in accordance with generally accepted accounting principles in the United State of America (“U.S. GAAP”).

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes. Actual results could differ from those estimates and such differences may be material to the financial statements. The results of operations for the nine months ended September 30, 2013, are not necessarily indicative of results for the entire fiscal year ending December 31, 2013.

### Liquidity

The financial statements of the Company have been prepared using accounting principles applicable to a going concern, which assumes realization of assets and settlement of liabilities in the normal course of business. The Company incurred losses of \$16.7 million for the nine months ended September 30, 2013, and \$13.8 million for the nine months ended September 30, 2012. The Company had working capital of \$4.0 million at September 30, 2013, and used cash in operations of \$12.6 million for the nine months ended September 30, 2013, and \$8.2 million for the nine months ended September 30, 2012.

Cash requirements during the nine months ended September 30, 2013, primarily reflect: (i) certain administrative costs related to the Company’s water project development efforts; (ii) litigation costs; and (iii) a \$3.3 million cash payment in March 2013 related to the lease agreement with the Arizona & California Railroad Company to use a portion of the railroad’s right-of-way to construct and operate a water conveyance pipeline. Currently, the Company’s sole focus is the development of its land and water assets.

In June 2006, the Company raised \$36.4 million through the private placement of a five-year zero coupon convertible term loan with Peloton Partners LLP (“Peloton”), as administrative agent, and an affiliate of Peloton and another investor, as lenders (the “Term Loan”). In April 2008, the Company was advised that Peloton’s interest in the Term Loan had been assigned to an affiliate of Lampe, Conway & Company LLC (“Lampe Conway”), and Lampe Conway subsequently replaced Peloton as administrative agent of the loan. In June 2009, the Company completed arrangements to amend the Term Loan and extend its maturity to June of 2013. This facility was further modified as to certain of its conversion features in October 2010, in connection with a new \$10 million working capital facility with its existing lenders. In October 2012, the Company increased the capacity of its existing Term Loan facility with an additional \$5 million facility.



On March 5, 2013, the Company completed arrangements with its senior lenders to refinance its then existing \$66 million Term Loan. Under the terms of the new arrangements, the existing lenders held \$30 million of non-convertible secured debt at the time of the transaction, with the balance of the Company's outstanding debt of approximately \$36 million held in a convertible bond instrument. Further, the Company increased the capacity of the convertible bond instrument with an additional \$17.5 million to be used for working capital purposes. See Note 2, "Long-Term Debt". In July 2013, the majority of the \$30 million of non-convertible secured debt was acquired in a private transaction by MSD Credit Opportunity Master Fund, L.P. ("MSD Credit"). In October 2013, the Company completed arrangements with MSD Credit to increase the secured debt facility by \$10 million to fund additional working capital ("New Term Loan"). See Note 8, "Subsequent Events".

On July 31, 2013, the Company filed a new shelf registration statement on Form S-3 registering the issuance of up to \$40 million in shares of the Company's common stock, preferred stock, warrants, subscription rights, units and certain debt instruments in one or more public offerings.

The \$10 million in additional working capital raised in October 2013, as discussed above, together with our existing cash resources, provides the Company with sufficient funds to meet its expected working capital needs until mid-2015. Based upon the Company's current and anticipated usage of cash resources, and depending on its progress toward implementation of the Cadiz Valley Water Conservation, Recovery and Storage Project ("Water Project" or "Project"), it may require additional working capital during 2015. The Company will evaluate the amount of cash needed, and the manner in which such cash will be raised, on an ongoing basis. The Company may meet any future cash requirements through a variety of means, including equity or debt placements, or through the sale or other disposition of assets. Equity placements would be undertaken only to the extent necessary, so as to minimize the dilutive effect of any such placements upon our existing stockholders. Limitations on the Company's liquidity and ability to raise capital may adversely affect it. Sufficient liquidity is critical to meet its resource development activities. Although the Company currently expects its sources of capital to be sufficient to meet its near-term liquidity needs, there can be no assurance that its liquidity requirements will continue to be satisfied. If the Company cannot raise needed funds, it might be forced to make substantial reductions in its operating expenses, which could adversely affect its ability to implement its current business plan and ultimately its viability as a company.

#### Principles of Consolidation

The consolidated financial statements include the accounts of Cadiz Inc. and all subsidiaries. All significant intercompany transactions and balances have been eliminated in consolidation.

#### Supplemental Cash Flow Information

No cash payments, including interest, are due on the corporate term debt or the convertible bond prior to their maturities.

The Company recorded non-cash additions to fixed assets of \$923,000 at September 30, 2013, and \$1,090,000 at December 31, 2012, which were accrued at the respective period ends, for costs directly attributable to the development of the Water Project.

#### Recent Accounting Pronouncements

##### Offsetting Assets and Liabilities

In December 2011 and December 2012, the FASB issued accounting standards updates modifying the disclosure requirements about the nature of an entity's rights of offsetting assets and liabilities in the consolidated balance sheet under master netting agreements and related arrangements associated with financial and derivative instruments. The guidance requires increased disclosure of the gross and net recognized assets and liabilities, collateral positions and narrative descriptions of setoff rights. The adoption of this pronouncement did not have a material impact on the Company's Consolidated Financial Statements and accompanying disclosures.

##### Presentation of Items Reclassified Out of Accumulated Other Comprehensive Income

In February 2013, the FASB issued an accounting standards update which requires disclosure related to items reclassified out of accumulated other comprehensive income (AOCI). The guidance requires entities to present separately, for each component of other comprehensive income (OCI), current period reclassifications and the remainder of the current period OCI. In addition, for certain current period reclassifications, an entity is required to disclose the effect of the item reclassified out of AOCI on the respective line item of net income. The adoption of this pronouncement did not have a material impact on the Company's Consolidated Financial Statements and accompanying disclosures.

##### Joint and Several Liabilities

In February 2013, the FASB issued an accounting standard update which modifies the requirements for the recognition, measurement, and disclosure of obligations resulting from joint and several liability arrangements for which the total amount of the obligation is fixed at the reporting date. The guidance requires companies to measure these obligations as the sum of the amount the company has agreed with co-obligors to pay and any additional amount it expects to pay on behalf of one or more co-obligors. This guidance is effective for all fiscal years, and interim periods within those years, beginning after December 15, 2013. The Company does not expect this guidance to have a material impact on its Consolidated Financial Statements and accompanying disclosures.

##### Presentation of Unrecognized Tax Benefits

In July 2013, the FASB issued an accounting standards update which will require an unrecognized tax benefit be presented on the balance sheet as a reduction of a deferred tax asset for a net operating loss ("NOL") or tax credit carryforward under certain circumstances. The guidance is effective for all fiscal years, and interim periods within those years, beginning December 15, 2013. The Company does not expect this guidance to have a material impact on the consolidated financial statements.

## NOTE 2 – LONG-TERM DEBT

At September 30, 2013 and December 31, 2012, the carrying amount of the Company's outstanding debt is summarized as follows (in thousands):

|   | September 30,<br>2013 | December 31,<br>2012 |
|---|-----------------------|----------------------|
| Zero coupon secured convertible term loan     | \$ -                  | \$ 65,262            |
| Senior secured debt due March 5, 2016         |                       |                      |
| Interest accrues at 8% per annum              | 31,412                | -                    |
| Convertible bond instrument due March 5, 2018 |                       |                      |
| Interest accrues at 7% per annum              | 55,647                | -                    |
| Other loans                                   | 42                    | 50                   |
| Debt discount, net of accumulated accretion   | -                     | (2,051 )             |
|   | 87,101                | 63,261               |
| Less current portion                          | 11                    | 11                   |
|   | \$ 87,090             | \$ 63,250            |

The carrying value of the Company's debt approximates fair value. The fair value of the Company's debt (Level 2) is determined based on an estimation of discounted future cash flows of the debt at rates currently quoted or offered to the Company for similar debt instruments of comparable maturities by its lenders.

Pursuant to the Company's loan agreements, annual maturities of long-term debt outstanding on September 30, 2013, are as follows:

| 12 Months<br>Ending September 30 | (in thousands) |
|----------------------------------|----------------|
| 2014                             | 11             |
| 2015                             | 11             |
| 2016                             | 31,424         |
| 2017                             | 8              |
| 2018                             | 55,647         |
|                                  | \$ 87,101      |

In June 2006, the Company raised \$36.4 million through the private placement of a five-year zero coupon convertible term loan with Peloton Partners LLP ("Peloton"), as administrative agent, and an affiliate of Peloton and another investor, as lenders (the "Term Loan"). In April 2008, the Company was advised that Peloton's interest in the Term Loan had been assigned to an affiliate of Lampe, Conway & Company LLC ("Lampe Conway"), and Lampe Conway subsequently replaced Peloton as administrative agent of the loan. In June 2009, the Company completed arrangements to amend the Term Loan and extend its maturity to June 2013. This facility was further modified as to certain of its conversion features in October 2010, in connection with a new \$10 million working capital facility with its existing lenders. In October 2012, the Company increased the capacity of its existing Term Loan facility with an additional \$5 million facility. As a result of this transaction, the Company issued warrants to lenders to purchase shares of common stock. The value of the warrants totaled approximately \$533 thousand and was recorded as additional debt discount with a corresponding amount recorded as additional paid-in capital.





On March 5, 2013, the Company completed arrangements with its senior lenders to refinance the Company's existing \$66 million corporate term debt. The new arrangements established two separate debt instruments, a \$30 million senior secured mortgage loan due in three years, and a new \$53.5 million convertible bond due in five years, with no principal or interest payments due on either instrument until maturity. The new debt instruments replaced all existing term debt as of March 5, 2013, and provided \$17.5 million in new working capital to fund the Company's current operations, including pre-construction activities related to the Project.

The major components of the refinancing included:

- A \$30 million senior term loan secured by the underlying assets of the Company, including landholdings and infrastructure (the "Senior Secured Debt"). The instrument accrues interest at 8% per annum and requires no principal or interest payments before maturity on March 5, 2016. Prepayment would be mandatory following any asset sale or voluntarily at the Company's option, subject to a premium. The Senior Secured Debt has a senior position to any other Company debt instrument.
- A \$53.5 million convertible bond (the "Convertible Bond"). The Convertible Bond provides for convertibility into the Company's common stock at a price of \$8.05 per share. Interest accrues at 7% per annum, with no principal or interest payments required before maturity on March 5, 2018. This instrument has a junior position to the Senior Secured Debt.
- \$17.5 million in new working capital provided as part of the Convertible Bond issuance to fund Company operations.

The new credit facility does not constitute a troubled debt restructuring and was accounted for as a debt extinguishment under ASC 470-50. The fair value of the new credit facility was recorded at face value. The Company recorded a loss on extinguishment of debt in the amount of \$1.06 million which consisted of the write-off of unamortized debt discount, unamortized debt issuance costs and fees paid to the lenders.

The Company incurred \$1.2 million of legal expenses and placement agent fees related to the negotiation and documentation of the refinancing which will be amortized over the life of the Convertible Bond.

In July 2013, the majority interest of the Senior Secured Debt was acquired in a private transaction by MSD Credit Opportunity Master Fund, L.P. ("MSD Credit"). In October 2013, the Company completed arrangements with MSD Credit to increase the Senior Secured Debt facility by \$10 million to fund additional working capital. See Note 8, "Subsequent Events".

Both the Senior Secured Debt and the Convertible Bond contain representations, warranties and covenants that are typical for agreements of this type, including restrictions that would limit the Company's ability to incur additional indebtedness, incur liens, pay dividends or make restricted payments, dispose of assets, make investments and merge or consolidate with another person. However, while there are affirmative covenants, there are no financial maintenance covenants and no restrictions on the Company's ability to issue additional common stock to fund future working capital needs. The debt covenants were negotiated by the parties with a view towards the Company's operating and financial condition as it existed at the time the agreements were executed. At September 30, 2013, the Company was in compliance with its debt covenants.

#### NOTE 3 – COMMON STOCK

On January 9, 2013, Cadiz revised its existing agreement with the law firm of Brownstein Hyatt Farber Schreck LLP ("Brownstein"). Under this agreement, Brownstein provides certain legal and advisory services to the Company, including the services of Mr. Scott Slater, the Company's Chief Executive Officer. As previously disclosed, the Company had agreed to pay to Brownstein an amount of up to 1% of the net present value of the Water Project as incentive compensation in consideration of the services provided by Brownstein under the original agreement.

The revised agreement replaced the net present-value-based incentive compensation provisions of the original agreement with an agreement to issue up to a total of 400,000 shares of the Company's common stock, with 100,000 shares earned upon the achievement of each of four enumerated milestones as follows:

- i. 100,000 shares earned upon the execution of the revised agreement;
- ii. 100,000 shares earned upon receipt by the Company of a final judicial order dismissing all legal challenges to the Final Environmental Impact Report for the Project;
- iii. 100,000 shares earned upon the signing of binding agreements for more than 51% of the Project's annual capacity;  
and
- iv. 100,000 shares earned upon the commencement of construction of all of the major facilities contemplated in the Final Environmental Impact Report necessary for the completion and delivery of the Project.

All shares earned upon achievement of any of the four milestones will be payable three years from the date earned. The agreement also provides for base cash compensation payments to Brownstein of \$25,000 per month.

In accordance with ASC 505, the Company recognized stock compensation in the amount of \$373,000 for the first of the four milestones which was satisfied on January 9, 2013. Because the shares are payable three years from the date earned, the fair value of these shares was estimated by discounting the current market price of the Company's common stock by the fair value of a protective put using the Black-Scholes model.

#### NOTE 4 – STOCK-BASED COMPENSATION PLANS AND WARRANTS

The Company has issued options pursuant to its 2003 Management Equity Incentive Plan, 2007 Management Equity Incentive Plan, and 2009 Equity Incentive Plan. The Company has also granted stock awards pursuant to its 2007 Equity Incentive Plan, 2009 Equity Incentive Plan and Outside Director Compensation Plan, as described below.

##### 2003 Management Equity Incentive Plan

In December 2003, concurrently with the completion of the Company's then current financing arrangements with ING, the Company's board of directors authorized the adoption of a Management Equity Incentive Plan. As of September 30, 2013, a total of 315,000 common stock options remain outstanding under this plan.

##### Outside Director Compensation Plan

The Cadiz Inc. Outside Director Compensation Plan was approved by Cadiz stockholders in November 2006. Under the plan, each outside director receives \$30,000 of cash compensation and receives a deferred stock award consisting of shares of the Company's common stock with a value equal to \$20,000 on June 30 of each year. The award accrues on a quarterly basis, with \$7,500 of cash compensation and \$5,000 of stock earned for each fiscal quarter in which a director serves. The deferred stock award vests automatically on the January 31 which first follows the award date.

##### 2007 Management Equity Incentive Plan

The 2007 Management Equity Incentive Plan was approved by stockholders at the 2007 Annual Meeting. As of September 30, 2013, a total of 10,000 common stock options remain outstanding under this plan.

##### 2009 Equity Incentive Plan

The 2009 Equity Incentive Plan was approved by stockholders at the 2009 Annual Meeting. The plan provides for the grant and issuance of up to 850,000 shares and options to the Company's employees and consultants. The plan became effective when the Company filed a registration statement on Form S-8 on December 18, 2009. All options issued under the 2009 Equity Incentive Plan have a ten-year term with vesting periods ranging from issuance date to 24 months. To date, 537,500 common stock options have been issued under this plan and all remained outstanding as of September 30, 2013.

All options that have been issued under the above plans have been issued to officers, employees and consultants of the Company. In total, options to purchase 862,500 shares were unexercised and outstanding on September 30, 2013, under the three equity incentive plans.

The Company recognized stock-option-related compensation costs of \$39,000 and \$239,000 in the nine months ended September 30, 2013 and 2012, respectively. No options were exercised during the nine months ended September 30, 2013.

### Stock Awards to Directors, Officers, and Consultants

The Company has granted stock awards pursuant to its 2007 Management Equity Incentive Plan, 2009 Equity Incentive Plan and Outside Director Compensation Plan.

Awards of 240,000 common shares were issued under the 2007 Management Equity Incentive Plan. A 150,000-share award was issued that vested in three equal installments on January 1, 2008, January 1, 2009, and January 1, 2010. The remaining award of 90,000 shares was issued as shares that vested in May 2009 consistent with the terms of the agreements pursuant to which those executives provide services to the Company.

Of the total 850,000 shares reserved under the 2009 Equity Incentive Plan, a grant of 115,000 restricted shares of common stock became effective on January 14, 2010, and a grant of 140,000 restricted shares of common stock became effective on January 10, 2011, consistent with the terms of the agreements pursuant to which those executives provide services to the Company and which contemplate that such executives will participate in the Company's long-term incentive plans. The recipients of these restricted shares have a contractual agreement not to sell any of these shares for a period of three years following the effective date. Of the remaining 595,000 shares reserved under the 2009 Equity Incentive Plan, 42,265 shares of common stock were awarded to directors, 537,500 were issued as options as described above and 15,235 are available for future grants as of September 30, 2013.

Under the Outside Director Compensation Plan, 92,265 shares have been awarded for the plan years ended June 30, 2003, through June 30, 2013. Of the 92,265 shares awarded, 72,782 shares have vested and been issued. The remaining 19,483 shares will vest on January 31, 2014.

### Stock Purchase Warrants Issued to Non-Employees

The Company accounts for equity securities issued to non-employees in accordance with the provisions of ASC 505.

On November 30, 2011, the Company raised \$6 million with a private placement of 666,667 shares of Common Stock at a price of \$9 per share. For every three (3) shares of Common Stock issued, the Company issued one (1) Common Stock purchase warrant entitling the holder to purchase, commencing 90 days from the date of the issuance and prior to December 8, 2014, one (1) share of Common Stock at an exercise price of \$13 per share.

On October 30, 2012, the Company increased the capacity of its then existing Term Loan facility with an additional \$5 million facility. Concurrently with the funding of the facility, the Company issued warrants to the lenders to purchase an aggregate of 250,000 shares of its common stock. These warrants have an exercise price of \$10 per share and must be exercised not later than two years from the date of issuance.

As of September 30, 2013, 472,222 warrants remain outstanding.

#### NOTE 5 – INCOME TAXES

As of September 30, 2013, the Company had net operating loss (“NOL”) carryforwards of approximately \$197 million for federal income tax purposes and \$107 million for California state income tax purposes. Such carryforwards expire in varying amounts through the year 2033. Use of the carryforward amounts is subject to an annual limitation as a result of ownership changes.

As of September 30, 2013, the Company possessed unrecognized tax benefits totaling approximately \$2.8 million. None of these, if recognized, would affect the Company's effective tax rate because the Company has recorded a full valuation allowance against these assets.

The Company's tax years 2010 through 2012 remain subject to examination by the Internal Revenue Service, and tax years 2009 through 2012 remain subject to examination by California tax jurisdictions. In addition, the Company's loss carryforward amounts are generally subject to examination and adjustment for a period of three years for federal tax purposes and four years for California purposes, beginning when such carryovers are utilized to reduce taxes in a future tax year.

Because it is more likely than not that the Company will not realize its net deferred tax assets, it has recorded a full valuation allowance against these assets. Accordingly, no deferred tax asset has been reflected in the accompanying consolidated balance sheets.

#### NOTE 6 – NET LOSS PER COMMON SHARE

Basic earnings per share (“EPS”) is computed by dividing the net loss by the weighted-average common shares outstanding. Options, deferred stock units, warrants and the zero coupon term loan convertible into or exercisable for certain shares of the Company's common stock were not considered in the computation of diluted EPS because their inclusion would have been antidilutive. Had these instruments been included, the fully diluted weighted average shares outstanding would have increased by approximately 6,485,000 and 3,194,000 for the three months ended September 30, 2013 and 2012, respectively, and 8,142,000 and 3,170,000 for the nine months ended September 30, 2013 and 2012, respectively.

#### NOTE 7 - CONTINGENCIES

In California, third parties have the ability to file litigation challenging the approval of a water project. As a result, the Company is and expects to continue to be party to various legal proceedings arising in the general course of its business, including, in particular, the development of the Water Project.

The Company is currently named as a real party in interest in six (6) lawsuits related to the Water Project approvals granted last year by the Santa Margarita Water District and County of San Bernardino in accordance with the California Environmental Quality Act (“CEQA”). The six lawsuits have been brought by two plaintiffs and have been coordinated in Orange County Superior Court. The cases seek various forms of relief, but are primarily focused on causing a reconsideration of the environmental documents and limitation of the Project approvals. The cases are scheduled to proceed to administrative trial in December 2013. The Company cannot predict the outcome of any of the proceedings. Three (3) additional cases filed last year have been dismissed and are no longer pending, including one case dismissed in October 2013.

There are no other material legal proceedings pending to which the Company is a party or of which any of the Company's property is the subject.

#### NOTE 8 – SUBSEQUENT EVENTS

On October 30, 2013, the Company entered into an agreement (“Credit Agreement”) with its new majority senior lender, MSD Credit Opportunity Master Fund, L.P. (“MSD Credit”), to increase its existing \$30 million senior secured mortgage loan by \$10 million to fund additional working capital. MSD Credit previously acquired the majority interest of the \$30 million portion of the debt in a private transaction. The new \$10 million tranche accrues interest at 8% and requires no principal or interest payments prior to maturity on June 30, 2017. The new \$10 million and the original \$30 million (“Senior Secured Debt”) are both secured by the underlying assets of the Company, including all landholdings and infrastructure. The Credit Agreement also now provides that in the case of certain asset sales unrelated to the Water Project, the Company would retain for working capital purposes up to 50% of the first \$10 million of sales, with the remainder requiring mandatory prepayment of the Senior Secured Debt. In addition, as part of this transaction, the Company issued 700,000 shares of Cadiz Inc. common stock to MSD Credit subject to certain restrictions on resale.

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

In connection with the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, the following discussion contains trend analysis and other forward-looking statements. Forward-looking statements can be identified by the use of words such as "intends", "anticipates", "believes", "estimates", "projects", "forecasts", "expects", "plans" and "proposes". Although we believe that the expectations reflected in these forward-looking statements are based on reasonable assumptions, there are a number of risks and uncertainties that could cause actual results to differ materially from these forward-looking statements. These include, among others, our ability to maximize value from our California land and water resources; and our ability to obtain new financings as needed to meet our ongoing working capital needs. See additional discussion under the heading "Risk Factors" in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2012.

### Overview

We are a land and water resource development company with 45,000 acres of land in three separate areas of eastern San Bernardino County, California. Virtually all of this land is underlain by high-quality, naturally recharging groundwater resources, and is situated in proximity to the Colorado River and the Colorado River Aqueduct ("CRA"), a major source of imported water for Southern California. Our main objective is to realize the highest and best use of these land and water resources in an environmentally responsible way.

For more than 20 years, we have maintained an agricultural development at our 34,000-acre property in the Cadiz Valley, relying upon groundwater from the underlying aquifer system for irrigation. In 1993, we secured permits to develop agriculture on up to 9,600 acres of the Cadiz Valley property and withdraw more than one million acre-feet of groundwater from the underlying aquifer system. Since that time, we have maintained various levels of agriculture at the property and this operation has provided our principal source of revenue.

In addition to our sustainable agricultural operations, we believe that the long-term value of our land assets can best be derived through the development of a combination of water supply and storage projects at our properties. The primary factor driving the value of such projects is continuing pressure on water supplies throughout California, including environmental and regulatory restrictions on each of the State's three main water sources: the State Water Project, the CRA and the Los Angeles Aqueduct. Southern California's water providers rely on imports from these systems for a majority of their water supplies, but deliveries from all three into the region have been below capacity over the last several years. Availability of supplies in California also differs greatly from year to year due to natural hydrological variability. For example, State Water Project deliveries were limited to just 35% of capacity for 2013 due to ongoing environmental restrictions and below average snowpack in Northern California. Southern California water providers are seeking new, reliable supply solutions to address ongoing limitations of traditional water supplies and to plan for long-term water needs, but cost-effective alternatives and solutions are limited.

At present, our water development efforts are primarily focused on the Cadiz Valley Water Conservation, Recovery and Storage Project (“Water Project” or “Project”), which will capture and conserve millions of acre-feet of native groundwater currently being lost to evaporation from the aquifer system beneath our Cadiz Valley property and deliver it to water providers throughout Southern California (see “Water Resource Development”). We believe that the ultimate implementation of this Water Project will create the primary source of our future cash flow and, accordingly, our working capital requirements relate largely to the development activities associated with this Water Project.

We also continue to explore additional uses of our land and water resource assets, including additional agricultural opportunities and the development of a land conservation bank on our properties outside the Water Project area.

In addition to these development efforts, we will also pursue strategic investments in complementary business or infrastructure to meet our objectives. We cannot predict with certainty when or if these objectives will be realized.

#### Water Resource Development

The Water Project is designed to capture and conserve billions of gallons of renewable native groundwater currently being lost annually to evaporation from the aquifer system underlying our Cadiz/Fenner Property, and provide a new, reliable water supply in Southern California. By implementing established groundwater management practices, the Water Project will create a sustainable water supply for Project participants without adversely impacting the aquifer system or the desert environment. The total quantity of groundwater to be recovered and conveyed to Project participants will not exceed a long-term annual average of 50,000 acre-feet per year for 50 years. The Project also offers participants the ability to carry-over their annual supply and store it in the groundwater basin from year to year. A second phase of the Project, Phase II, will offer approximately one million acre-feet of storage capacity that can be used to store imported water supplies at the Water Project area.

Facilities required for Phase I of the Project primarily include, among other things:

- High yield wells designed to efficiently recover available native groundwater from beneath the Water Project area;
  - A water conveyance pipeline to deliver water from the well field to the CRA; and
  - An energy source to provide power to the well field, pipeline and pumping plant.

If an imported water storage component of the project is ultimately implemented in Phase II, the following additional facilities would be required, among other things:

- A pumping plant to pump water through the conveyance pipeline from the CRA to the Project well field; and
- Spreading basins, which are shallow settling ponds that will be configured to efficiently percolate water from the ground surface down to the water table using subsurface storage capacity for the storage of water.



In general, several elements are needed to implement such a project: (1) a water conveyance pipeline right-of-way from the Water Project area to a delivery system; (2) storage and supply purchase agreements with one or more public water agencies or private water utilities; (3) environmental/regulatory permits; and (4) construction and working capital. As described below, the first three elements have been progressed on a concurrent basis. The fourth is dependent on actions arising from the completion of the first three.

(1) A Water Conveyance Pipeline Right-of-Way from the Water Project Area to a Delivery System

In September 2008, we secured a right-of-way for the Water Project's water conveyance pipeline by entering into a lease agreement with the Arizona & California Railroad Company ("ARZC") which operates an active shortline railroad extending from Cadiz to Matthie, Arizona. The agreement allows for the use of a portion of the railroad's right-of-way to construct and operate a water conveyance pipeline for a period up to 99 years. The buried pipeline would be constructed parallel to the railroad tracks and be used to convey water between our Cadiz Valley property and the CRA in Rice, California. The ARZC is also a Project participant and would receive water from the Project to serve a variety of railroad purposes, including fire suppression and other safety and maintenance uses. In addition, in September 2013, we entered into a trackage rights agreement with the ARZC that would enable the operation of steam-powered, passenger excursion trains on the line powered by water made available from the pipeline.

The ARZC route was fully analyzed in the Water Project's Final Environmental Impact Report ("FEIR") as part of the California Environmental Quality Act ("CEQA") environmental review process completed in 2012. Pursuant to our lease agreement with ARZC, we made a payment in the amount of \$3.3 million on March 6, 2013, marking the completion of the environmental review period and the commencement of the construction and operation term of the agreement.

We are also exploring the potential to utilize an unused natural gas pipeline (as described in "Existing Pipeline Asset" below), which exists in the Project area and to which we hold an ownership right, as a means to access additional distribution systems. Initial feasibility studies indicate that this pipeline could be used as a component of the Project to distribute water to Project participants or import water for storage at the Project area in Phase II. The potential use of this pipeline by the Project was preliminarily analyzed as part of the Project's FEIR. Additional environmental review would be required prior to converting this line for water distribution.

(2) Storage and Supply Purchase Agreements with One or More Public Water Agencies or Private Water Utilities

In 2010 and 2011, we entered into option and environmental cost-sharing agreements with six water providers seeking water supplies and storage from the Project: Santa Margarita Water District ("SMWD"), Golden State Water Company (a wholly owned subsidiary of American States Water [NYSE: AWR]), Three Valleys Municipal Water District, Suburban Water Systems (a wholly owned subsidiary of SouthWest Water Company), Jurupa Community Services District and California Water Service Company, the third largest investor-owned American water utility. The six water providers serve more than one million customers in cities throughout California's San Bernardino, Riverside, Los Angeles, Orange, Ventura and Imperial Counties.

Under the terms of the agreements with the six water providers, upon completion of the Water Project's California Environmental Quality Act ("CEQA") review and certification of the FEIR, which occurred on July 31, 2012, each agency has the right to acquire an annual supply of 5,000 acre-feet of water at a pre-determined formula competitive with their incremental cost of new water. In addition, the agencies have options to acquire storage rights in the Water Project to allow them to manage their supplies to complement their other water resources.

Following CEQA certification, SMWD was the first participant to approve a Water Purchase and Sale Agreement for 5,000 acre-feet of water effectively converting its earlier option agreement. The structure of the SMWD purchase agreement calls for an annually adjusted water supply payment of up to \$500/AF, including identified income streams, plus its pro rata portion of the capital recovery charge and operating and maintenance costs. The capital recovery charge is calculated by amortizing the total capital investment by the Company over a 30-year term.

Approximately 80% of the water to be conserved annually by the Project is now either under a Water Purchase and Sale Agreement or remains under option. We are currently working with other participating agencies to convert their option agreements to definitive economic agreements.

We are also in discussions with additional water providers interested in acquiring rights to the remaining available Project supplies, as well as with third parties regarding the imported storage aspect of this Project.

(3) Environmental/Regulatory Permits

In order to properly develop and quantify the sustainability of the Water Project, and prior to initiating the formal permitting process for the Water Project, we commissioned consulting firm CH2M HILL to complete a comprehensive study of the water resources at the Project area. Following a year of analysis, CH2M HILL released its study of the aquifer system in February 2010. Utilizing new models produced by the U.S. Geological Survey in 2006 and 2008, the study estimated the total groundwater in storage in the aquifer system to be between 17 and 34 million acre-feet, a quantity on par with Lake Mead, the nation's largest surface reservoir. The study also identified a renewable annual supply of native groundwater in the aquifer system currently being lost to evaporation. CH2M HILL's findings, which were peer reviewed by leading groundwater experts, confirmed that the aquifer system could sustainably support the Water Project.

Further, and also prior to beginning the formal environmental permitting process, we entered into a Memorandum of Understanding with the Natural Heritage Institute ("NHI"), a leading global environmental organization committed to protecting aquatic ecosystems, to assist with our efforts to sustainably manage the development of our Cadiz/Fenner property. As part of this "Green Compact", we will follow stringent plans for groundwater management and habitat conservation, and create a groundwater management plan for the Water Project.

Following release of CH2M Hill's analysis, the Project began a public environmental review process according to CEQA. SMWD served as the Lead Agency for the CEQA review. San Bernardino County, the public agency participating water providers and Metropolitan Water District of Southern California ("Metropolitan") were considered responsible agencies, because they are public agencies that will have a discretionary approval power over the Project. ESA Associates, a leading environmental consulting firm, prepared the environmental review documentation. As discussed in (2), above, we entered into environmental cost-sharing agreements with all participating water providers to create a framework for funding the costs associated with the review.

SMWD released the FEIR in July 2012 following a 17-month public review and comment process. The FEIR summarized that, with the exception of unavoidable short-term construction emissions, by implementing the measures developed in the Project's Groundwater Management, Monitoring and Mitigation Plan ("GMMMP"), the Project will avoid significant impacts to desert resources. On July 31, 2012, the SMWD Board of Directors voted unanimously to certify the FEIR and approve the Project.

Following SMWD's action, the San Bernardino County Board of Supervisors voted on October 1, 2012 to approve the GMMMP for the Project and adopted certain findings under CEQA, becoming the first responsible agency to take an approving action pursuant to the certified EIR. San Bernardino County served as a responsible agency in the CEQA review process as the local government entity responsible for oversight over groundwater resources in the Project area.

Metropolitan will take action as a responsible agency under CEQA prior to construction regarding the terms and conditions of the Project's use of the CRA. Project water supplies will enter Metropolitan's CRA in accordance with its published engineering and design standards and subject to all applicable fees and charges routinely established by Metropolitan for the conveyance of water within its service territory.

(4) Construction and Working Capital

As part of the Water Purchase and Sale Agreement with SMWD referred to in (2), above, the SMWD Board also authorized continued Project implementation efforts with the Company, including final permitting, design and construction.

As described above, construction of Phase I of the Project would primarily consist of well field facilities at the Water Project site, a conveyance pipeline along the right-of-way described in (1), above, from the well field to the CRA, and an energy source to pump water through the conveyance pipeline between the Project well field and the CRA. Existing wells at the Cadiz Valley property currently in use for our agricultural operations will be integrated into the Water Project well field, reducing the number of wells that must be constructed prior to Project implementation.

The construction of these facilities will require capital financing, which is expected to be entirely provided with lower-cost senior debt, secured by the new facility assets. Our existing Convertible Bond provides us the flexibility to incorporate Water Project construction financing by allowing Project financing to be placed ahead of it in terms of priority.

## Existing Pipeline Asset

We currently hold ownership rights to a 96-mile existing idle natural gas pipeline from the Cadiz Valley to Barstow, California, which we intend to convert for the transportation of water.

In September 2011, we entered into an option agreement with El Paso Natural Gas (“EPNG”), a subsidiary of Kinder Morgan Inc., which granted the Company rights to purchase a 220-mile idle pipeline between Bakersfield and Cadiz, California for \$40 million. Initial feasibility studies indicated that, upon conversion, the 30-inch line could transport 20,000 - 30,000 acre-feet of water per year between the Water Project area and various points along the Central and Northern California water transportation network. In February 2012, we made a \$1 million payment to EPNG to extend our option to purchase the 220-mile line until April 2013.

In December 2012, we entered into a new agreement with EPNG dividing the 220-mile pipeline in Barstow, California, with the Company gaining ownership rights to the 96-mile eastern segment between Barstow and the Cadiz Valley and returning to EPNG rights to the 124-mile western segment for its own use. The 96-mile eastern portion from the Cadiz Valley to Barstow was identified as the most critical segment of the line for accessing the state’s water transportation infrastructure. The Barstow area serves as a hub for water delivered from northern and central California to communities in Southern California’s High Desert.

In consideration of the new agreement, EPNG reduced the purchase price of the 96-mile eastern segment to a nominal amount of \$1 (one dollar), plus previous option payments totaling \$1.07 million already made by the Company. The remaining purchase price of \$1 (one dollar) is payable before expiration of the option period in April 2014. In addition, if EPNG files for regulatory approval of any new use of the 124-mile western segment prior to December 2015, EPNG will make an additional payment to the Company of \$10 million, payable on the date the application for regulatory approval is filed.

The 96-mile Cadiz-Barstow route creates significant opportunities for our water resource development efforts. Once converted to water use, the pipeline can be used to directly connect the Water Project area to northern and central California water sources, serving a growing need for additional locations for storage of water south of the Sacramento/San Joaquin Bay Delta region. In addition, the 96-mile pipeline creates new opportunities to deliver water, either directly or via exchange, to potential customers in the High Desert region of San Bernardino and southern Kern County, areas which do not currently have an interconnection point with the Project. When both the 96-mile line and the 43-mile pipeline to the CRA become operational, the Water Project area would create a new link between the CRA and the State Water Project, the two major water delivery systems in California providing flexible opportunities for both supply and storage.

The entire EPNG pipeline was evaluated in the Water Project’s EIR during the CEQA process at a programmatic level. Any use of the line would be conducted in conformity with the Project’s GMMMP and is subject to further CEQA evaluation (see “Water Resource Development” above).

## Agricultural Development

Within the Cadiz/Fenner Property, 9,600 acres have been zoned for agriculture and the Company has developed a total of 1,920 acres of the property for agricultural operations. The infrastructure currently includes seven wells that are interconnected within a portion of this acreage, with total annual production capacity of approximately 13,000 acre-feet of water. Additionally, there are housing and kitchen facilities that support up to 300 employees. If the entire 9,600 acres were developed and irrigated, total water usage would be approximately 40,000 – 50,000 acre-feet per year depending on the crop mix. The underlying groundwater, fertile soil, and desert temperatures are well suited for a wide variety of fruits and vegetables.

Permanent crops currently include 160 acres of vineyard used to produce dried-on-the-vine raisins and 440 acres of lemon orchards. All crops are farmed using sustainable agricultural practices.

We currently derive our agricultural revenues through direct farming and sale of our products into the market or through the lease of our agricultural properties to third parties for farming. The entire organic raisin crop grown at the property is farmed by the Company and we incur all of the costs required to produce and harvest the crop. The harvested raisins are then sold in bulk to a raisin processing facility. Approximately 260 acres of lemons in production are farmed by the Company. We incur all of the costs required to produce this lemon crop. Once harvested, the lemons are shipped in bulk to an independent packing and sales facility.

The remaining 180 acres of lemons are farmed by LA Fresh Foods under a 2009 lease agreement to develop up to 500 acres of lemon orchards. We expect to receive lease income once the lemon orchards reach commercial production through a profit-sharing agreement component of the lease.

In July 2013, we also entered into a lease agreement with Limoneira Company (NASDAQ: LMR) to plant up to 1,280 acres of new lemons at the property over the next five years. In consideration for the lease arrangement, Limoneira will provide an annual base rent and will also provide a profit-sharing payment once the new lemon orchards reach commercial production.

Agricultural revenues will vary from year to year based on the number of acres in development, crop yields, and prices. We do not expect that our agricultural revenues will be material to our overall results of operations once the Water Project is fully operational. However, our agricultural operations are expected to be maintained in complement with the Water Project to provide added value to Project operations.

## Additional Eastern Mojave Properties

We also own approximately 11,000 acres outside of the Cadiz/Fenner Valley area in other parts of the Mojave Desert in eastern San Bernardino County.

Our primary landholding outside of the Cadiz area is approximately 9,000 acres in the Piute Valley. This landholding is located approximately 15 miles from the resort community of Laughlin, Nevada, and about 12 miles from the Colorado River town of Needles, California. Extensive hydrological studies, including the drilling and testing of a full-scale production well, have demonstrated that this landholding is underlain by high-quality groundwater. The aquifer system underlying this property is naturally recharged by precipitation (both rain and snow) within a watershed of approximately 975 square miles and could be suitable for a water supply project, agricultural development or solar energy production. Certain of these properties are located in or adjacent to areas designated by the federal government as Critical Desert Tortoise Habitat and/or Desert Wilderness Areas and are suitable candidates for preservation and conservation.



Additionally, we own acreage located near Danby Dry Lake, approximately 30 miles southeast of our Cadiz/Fenner Valley properties. The Danby Dry Lake property is located approximately 10 miles north of the CRA. Initial hydrological studies indicate that the area has excellent potential for a water supply project and could site certain facilities for the Water Project. Certain of the properties in this area may also be suitable for agricultural development and/or preservation and conservation.

#### Land Conservation Bank

As stated above, some of our properties not currently being developed are located within areas designated by the federal government as Critical Desert Tortoise Habitat and/or Desert Wilderness Areas. We are currently in a permitting process with the California Department of Fish and Wildlife to permit approximately 7,500 acres of these properties for inclusion in a land mitigation or conservation bank, which would provide credits that can be acquired by entities that must mitigate or offset planned development in other areas. For example, this bank could potentially service the mitigation requirements of numerous utility-scale solar development projects being considered throughout Riverside and San Bernardino Counties, including projects within the recently approved federal Riverside-East Solar Energy Zone.

#### Other Opportunities

Over the longer-term, we believe the population of Southern California, Nevada and Arizona will continue to grow, and that, in time, the economics of commercial and residential development or solar energy generation at our properties may become attractive. Moreover, other opportunities in business or infrastructure complementary to our current objectives could provide new opportunities for our business.

We remain committed to the sustainable use of our land and water assets, and will continue to explore all opportunities for environmentally responsible development of these assets. We cannot predict with certainty which of these various opportunities will ultimately be utilized.

#### Results of Operations

##### Three Months Ended September 30, 2013, Compared to Three Months Ended September 30, 2012

We have not received significant revenues from our water resource and real estate development activity to date. Our revenues have been limited to our agricultural operations. As a result, we have historically incurred a net loss from operations. We had revenues of \$182 thousand for the three months ended September 30, 2013, and \$287 thousand for the three months ended September 30, 2012. We incurred a net loss of \$4.8 million in the three months ended September 30, 2013, compared with a \$4.7 million net loss during the three months ended September 30, 2012.

Our primary expenses are our ongoing overhead costs associated with the development of the Water Project (i.e. general and administrative expense) and our interest expense. We will continue to incur non-cash expenses in connection with our management and director equity incentive compensation plans.

**Revenues** We had revenues of \$182 thousand for the three months ended September 30, 2013, and \$287 thousand for the three months ended September 30, 2012. The decrease in revenue in 2013 was primarily due to the smaller raisin crop in 2013 in comparison to the 2012 raisin crop.

**Cost of Sales** Cost of sales was \$292 thousand for the three months ended September 30, 2013, and \$293 thousand for the three months ended September 30, 2012.

**General and Administrative Expenses** General and administrative expenses totaled \$2.9 million during the three months ended September 30, 2013, and \$3.0 million during the three months ended September 30, 2012. Non-cash compensation costs for stock and option awards are included in General and Administrative Expenses.

General and Administrative Expenses, exclusive of stock-based compensation costs, totaled \$2.9 million and \$2.9 million for the three months ended September 30, 2013 and 2012, respectively.

Compensation costs from stock and option awards for the three months ended September 30, 2013 totaled \$29 thousand, compared with \$82 thousand for the three months ended September 30, 2012. The expense reflects the vesting schedules of the stock and option awards under the 2009 Equity Incentive Plan.

**Depreciation** Depreciation expense totaled \$63 thousand for the three months ended September 30, 2013, and \$97 thousand for the three months ended September 30, 2012.

**Interest Expense, net** Net interest expense for each of the three months ended June 30, 2013 and 2012 was \$1.7 million. The following table summarizes the components of net interest expense for the two periods (in thousands):

|                                 | Three Months Ended |          |
|---------------------------------|--------------------|----------|
|                                 | September 30,      |          |
|                                 | 2013               | 2012     |
| Interest on outstanding debt    | \$ 1,633           | \$ 895   |
| Amortization of financing costs | 56                 | 23       |
| Amortization of debt discount   | -                  | 748      |
| Interest income                 | -                  | (1 )     |
|                                 | \$ 1,689           | \$ 1,665 |

See Note 2 to the Consolidated Financial Statements – “Long-Term Debt”.



**Income Taxes** Income tax expense for the three months ended September 30, 2013 was \$1 thousand and \$3 thousand for the three months ended September 30, 2012. See Note 5 to the Consolidated Financial Statements - "Income Taxes".

#### Nine Months Ended September 30, 2013, Compared to Nine Months Ended September 30, 2012

We had revenues of \$190 thousand for the nine months ended September 30, 2013, and \$324 thousand for the nine months ended September 30, 2012. We incurred a net loss of \$16.7 million in the nine months ended September 30, 2013, compared with a \$13.8 million net loss during the nine months ended September 30, 2012. The higher 2013 loss was primarily due to litigation costs, higher stock-based non-cash compensation costs and the loss on extinguishment of debt and debt refinancing.

**Revenues** We had revenues of \$190 thousand for the nine months ended September 30, 2013, and \$324 thousand for the nine months ended September 30, 2012. The decrease in revenue in 2013 was primarily due to a smaller raisin crop in 2013 in comparison to the 2012 raisin crop.

**Cost of Sales** Cost of sales was \$292 thousand during the nine months ended September 30, 2013, and \$295 thousand during the nine months ended September 30, 2012.

**General and Administrative Expenses** General and administrative expenses during the nine months ended September 30, 2013 totaled \$9.6 million compared to \$8.7 million for the nine months ended September 30, 2012. Non-cash compensation costs for stock and option awards are included in General and Administrative Expenses.

Compensation costs from stock and option awards for the nine months ended September 30, 2013, totaled \$482 thousand compared with \$314 thousand for the nine months ended September 30, 2012. The expense reflects the vesting schedules of the stock and option awards under the 2009 equity incentive plan. The higher 2013 expense was primarily due to higher stock non-cash compensation costs related to shares awarded to the Brownstein law firm for certain legal and advisory services to the Company (see Note 3 to the Consolidated Financial Statements - "Common Stock"), partially offset by a decrease in stock based non-cash compensation costs related to stock and options issued in 2011 under the 2009 Equity Incentive Plan.

Other general and administrative expenses, exclusive of stock-based compensation costs, totaled \$9.1 million in the nine months ended September 30, 2013, compared with \$8.4 million for the nine months ended September 30, 2012. The increase in general and administrative expenses in 2013 was primarily due to litigation costs related to the Water Project.

**Depreciation** Depreciation expense totaled \$191 thousand for the nine months ended September 30, 2013, and \$285 thousand for the nine months ended September 30, 2012.

Interest Expense, net Net interest expense totaled \$5.7 million during the nine months ended September 30, 2013, compared to \$4.8 million during the same period in 2012. The following table summarizes the components of net interest expense for the two periods (in thousands):

|                                 | Nine Months Ended<br>September 30, |          |
|---------------------------------|------------------------------------|----------|
|                                 | 2013                               | 2012     |
| Interest on outstanding debt    | \$ 4,297                           | \$ 2,628 |
| Amortization of financing costs | 169                                | 67       |
| Amortization of debt discount   | 1,249                              | 2,129    |
| Interest income                 | -                                  | (3 )     |
|                                 | \$ 5,715                           | \$ 4,821 |

The interest on outstanding debt increased from \$2.6 million to \$4.3 million due to the increase in interest rate on a larger credit facility associated with the debt refinancing. See Note 2 to the Consolidated Financial Statements – “Long-Term Debt”.

Income Taxes Income tax expense was \$5 thousand for the nine months ended September 30, 2013, and \$8 thousand for the nine months ended September 30, 2012. See Note 5 to the Consolidated Financial Statements – “Income Taxes”.

## Liquidity and Capital Resources

### Current Financing Arrangements

As we have not received significant revenues from our development activities to date, we have been required to obtain financing to bridge the gap between the time water resource and other development expenses are incurred and the time that revenue will commence. Historically, we have addressed these needs primarily through secured debt financing arrangements, private equity placements and the exercise of outstanding stock options and warrants. We have also worked with our secured lenders to structure our debt in a way which allows us to continue development of the Water Project and minimize dilution of the ownership interests of common stockholders.

On March 5, 2013, we refinanced our term debt. See Note 2 to the Consolidated Financial Statements – “Long-Term Debt”. The major components of the refinancing included:

- I. A \$30 million senior term loan secured by the underlying assets of the Company (the “Senior Secured Debt”) that accrues interest at 8% per annum and requires no principal or interest payments before maturity in March 2016; and
- II. A \$53.5 million convertible bond (the “Convertible Bond”) that accrues interest at 7% per annum with no principal or interest payments required before maturity in March 2018; and
- III. \$17.5 million in new working capital provided as part of the Convertible Bond issuance.

We believe that by breaking our debt into two components, we now have the flexibility to incorporate project financing for the Water Project, as necessary, into our current debt structure. While the new \$30 million Senior Secured Debt would be required to be repaid by any necessary project financing, the \$53.5 million Convertible Bond has been designed to allow project financing to be placed ahead of it in terms of priority. The \$17.5 million of new working capital provides us with the resources to continue to move through our pre-construction phase, including resolution of outstanding administrative CEQA litigation and the finalization of water supply purchase agreements with all Water Project participants.

On October 30, 2013, we entered into an agreement (“Credit Agreement”) with our new majority senior lender, MSD Credit Opportunity Master Fund, L.P. (“MSD Credit”), to increase our existing \$30 million senior secured mortgage loan by \$10 million to fund additional working capital. MSD Credit previously acquired the majority interest of the \$30 million portion of the debt in a private transaction. The new \$10 million tranche accrues interest at 8% and requires no principal or interest payments prior to maturity on June 30, 2017. The new \$10 million and the original \$30 million are both secured by the underlying assets of the Company, including all landholdings and infrastructure. The Credit Agreement also now provides that in the case of certain asset sales unrelated to the Water Project, the Company would retain for working capital purposes up to 50% of the first \$10 million of sales, with the remainder requiring mandatory prepayment of the Senior Secured Debt. In addition, as part of this transaction, we issued 700,000 shares of Cadiz Inc. common stock to MSD Credit subject to certain restrictions on resale.

Both the Senior Secured Debt and the Convertible Bond contain representations, warranties and covenants that are typical for agreements of this type, including restrictions that would limit our ability to incur additional indebtedness, incur liens, pay dividends or make restricted payments, dispose of assets, make investments and merge or consolidate with another person. However, while there are affirmative covenants, there are no financial maintenance covenants and no restrictions on our ability to issue additional common stock to fund future working capital needs. The debt covenants associated with the new loans were negotiated by the parties with a view towards our operating and financial condition as it existed at the time the agreements were executed. At September 30, 2013, we were in compliance with our debt covenants.

In connection with the October 2012 additional debt facility (See Note 2 to the Consolidated Financial Statements – “Long-Term Debt”), we issued warrants to the lenders to purchase shares of common stock. The value of the warrants totaled approximately \$533 thousand and was recorded as additional debt discount with a corresponding amount recorded as additional paid-in capital.

In 2011, we raised a total of \$15.1 million in working capital through three equity issuances. On July 8, 2011, we sold 363,636 shares of Common Stock at a price of \$11 per share for total proceeds of \$4 million. On November 30, 2011, we raised \$6 million in a private placement of 666,667 shares of Common Stock at a price of \$9 per share. For every three (3) shares of Common Stock issued, we issued (1) Common Stock purchase warrant entitling the holder to purchase, commencing 90 days from the date of the issuance and prior to December 8, 2014, one (1) share of Common Stock at an exercise price of \$13 per share. On December 14, 2011, we sold 570,000 shares of Common Stock at a price of \$9 per share for total proceeds of \$5.1 million.

As we continue to actively pursue our business strategy, additional financing may continue to be required. See “Outlook”, below. The covenants in the term debt do not prohibit our use of additional equity financing and allow us to retain 100% of the proceeds of any equity financing. We do not expect the loan covenants to materially limit our ability to finance our water development activities.

At September 30, 2013, we had no outstanding credit facilities other than the Senior Secured Debt and the Convertible Bond described above.

**Cash Used for Operating Activities.** Cash used for operating activities totaled \$12.6 million and \$8.2 million for the nine months ended September 30, 2013 and 2012, respectively. The cash was primarily used to fund: (i) general and administrative expenses related to our water project development efforts; (ii) litigation costs; and (iii) a \$3.3 million cash payment in March 2013 related to the lease agreement with the Arizona & California Railroad Company to use a portion of the railroad’s right-of-way to construct and operate a water conveyance pipeline which is reflected in the increase in other assets in the consolidated statement of cash flows.

**Cash Used for Investing Activities.** Cash used for investing activities during the nine months ended September 30, 2013 was \$167 thousand compared with \$1.9 million during the same period in 2012. The 2012 period included additional investments in environmental work related to the Water Project.

**Cash Provided by Financing Activities.** Cash provided by financing activities for the nine months ended September 30, 2013 was \$16.3 million compared with \$49 thousand during the same period in 2012. The 2013 period included \$17.5 million of proceeds as part of the issuance of long-term debt, offset by \$1.2 million in debt issuance costs related to the debt refinancing.

## Outlook

**Short-Term Outlook.** The additional \$10 million working capital facility which closed on October 30, 2013, together with our existing cash resources, provide us with sufficient funds to meet our expected working capital needs until mid-2015. Should we require additional working capital to fund operations, we expect to continue our historical practice of structuring our financing arrangements to match the anticipated needs of our development activities. See “Long-Term Outlook”. No assurances can be given, however, as to the availability or terms of any new financing.

**Long-Term Outlook.** In the longer term, we may need to raise additional capital to finance working capital needs, capital expenditures and any payments due under our Senior Secured Debt or our Convertible Bond at maturity (see “Current Financing Arrangements” above). Our future working capital needs will depend upon the specific measures we pursue in the entitlement and development of our water resources and other developments. Future capital expenditures will depend primarily on the progress of the Water Project.

We will evaluate the amount of cash needed, and the manner in which such cash will be raised, on an ongoing basis. We may meet any future cash requirements through a variety of means, including equity or debt placements, or through the sale or other disposition of assets. Equity placements would be undertaken only to the extent necessary, so as to minimize the dilutive effect of any such placements upon our existing stockholders. Limitations on our liquidity and ability to raise capital may adversely affect us. Sufficient liquidity is critical to meet our resource development activities. Although we currently expect our sources of capital to be sufficient to meet our near-term liquidity needs, there can be no assurance that our liquidity requirements will continue to be satisfied. If the Company cannot raise needed funds, it might be forced to make substantial reductions in its operating expenses, which could adversely affect its ability to implement its current business plan and ultimately its viability as a company.

#### Recent Accounting Pronouncements

See Note 1 to the Consolidated Financial Statements – “Description of Business and Summary of Significant Accounting Policies”.

#### Certain Known Contractual Obligations

| Contractual Obligations<br>(in thousands) | Total      | Payments Due by Period |           |           |               |
|---|------------|------------------------|-----------|-----------|---------------|
|   |            | 1 year or less         | 2-3 years | 4-5 years | After 5 years |
| Long-term debt obligations                | \$ 87,101  | \$ 11                  | \$ 31,435 | \$ 55,655 | \$ -          |
| Interest Expense                          | 27,137     | -                      | 6,767     | 20,370    | -             |
| Operating leases                          | 3,113      | 493                    | 820       | 600       | 1,200         |
|   | \$ 117,351 | \$ 504                 | \$ 39,022 | \$ 76,625 | \$ 1,200      |

\* The above table does not reflect unrecognized tax benefits of \$2.8 million, the timing of which is uncertain. Refer to Note 7 to our Annual Report on Form 10-K for the year ended December 31, 2012.

Long-term debt included in the table above primarily reflects the Senior Secured Debt and the Convertible Bond, which is described above in Item 2, “Management’s Discussion and Analysis of Financial Condition and Results of Operation; Liquidity and Capital Resources”. Operating leases include the lease agreement with the Arizona & California Railroad Company to use a portion of the railroad’s right-of-way to construct and operate a water conveyance pipeline, as described in Item 2, “Water Resource Development”, and the lease of the Company’s executive offices.

#### ITEM 3. Quantitative and Qualitative Disclosures about Market Risk

As of September 30, 2013, all of the Company's indebtedness bore interest at fixed rates; therefore, the Company is not exposed to market risk from changes in interest rates on long-term debt obligations.

#### ITEM 4. Controls and Procedures

##### Disclosure Controls and Procedures

The Company established disclosure controls and procedures to ensure that material information related to the Company, including its consolidated entities, is accumulated and communicated to senior management, including the Chief Executive Officer (the “Principal Executive Officer”) and Chief Financial Officer (the “Principal Financial Officer”) and to its Board of Directors. Based on their evaluation as of September 30, 2013, the Company's Principal Executive Officer and Principal Financial Officer have concluded that the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) are effective to ensure that the information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and such information is accumulated and communicated to management, including the principal executive and principal financial officers as appropriate, to allow timely decisions regarding required disclosures.

### Changes in Internal Controls Over Financial Reporting

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

## PART II - OTHER INFORMATION

### ITEM 1. Legal Proceedings

#### CEQA Claims Challenging Water Project Approvals

As noted in Item 3. Legal Proceedings in the Company's Annual Report on Form 10-K for the year ended December 31, 2012, third parties have the ability in California to file litigation challenging the approval of a project. We are currently named as a real party in interest in six (6) lawsuits related to the Water Project approvals granted last year by the Santa Margarita Water District ("SMWD") and the County of San Bernardino ("County") in accordance with the California Environmental Quality Act ("CEQA"). Three (3) additional cases filed last year have been dismissed and are no longer pending, including one case dismissed in October 2013.

The six remaining lawsuits have been brought by two (2) plaintiffs and challenge three (3) separate Project approvals as follows:

- (1) MOU Approval – two cases filed by Tetra Technologies, Inc. ("Tetra") (NYSE: TTI) challenging the May 2012 approvals of the Memorandum of Understanding between Cadiz, SMWD and the County related to the Project's Groundwater Management, Monitoring & Mitigation Plan (GMMMP).
- (2) EIR Approval – two cases filed by Tetra and Center for Biological Diversity, et al ("CBD") challenging the adequacy of the EIR certified by SMWD on July 31, 2012.
- (3) GMMMP Approval – two cases filed by Tetra and CBD challenging the approval of the GMMMP by the County Board of Supervisors on October 1, 2012.

All six remaining lawsuits have been coordinated in Orange County Superior Court and are before one judge. A trial date for the six cases has been scheduled to begin on December 3, 2013. The cases seek various forms of relief, but are primarily focused on causing a reconsideration of the environmental documents and limitation of the Project approvals.

We cannot predict with certainty the outcome of any of the proceedings.

#### Other Proceedings

There are no other material legal proceedings pending to which we are a party or of which any of our property is the subject.

### ITEM 1A. Risk Factors

Not applicable.

### ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

Not applicable.



ITEM 3. Defaults Upon Senior Securities

Not applicable.

ITEM 4. Mine Safety Disclosures

Not applicable.

ITEM 5. Other Information

Not applicable.

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ITEM 6. Exhibits

The following exhibits are filed or incorporated by reference as part of this Quarterly Report on Form 10-Q.

10.1 Track Utilization Agreement dated September 16, 2013, between Arizona & California Railroad Company and Cadiz Real Estate LLC

31.1 Certification of Scott S. Slater, Chief Executive Officer of Cadiz Inc. pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification of Timothy J. Shaheen, Chief Financial Officer and Secretary of Cadiz Inc. pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1 Certification of Scott S. Slater, Chief Executive Officer of Cadiz Inc. pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

32.2 Certification of Timothy J. Shaheen, Chief Financial Officer and Secretary of Cadiz Inc. pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

SIGNATURE

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.

Cadiz Inc.

By: /s/ Scott S. Slater  
Scott S. Slater  
Chief Executive Officer and President  
(Principal Executive Officer)

November 8, 2013  
Date

By: /s/ Timothy J. Shaheen  
Timothy J. Shaheen  
Chief Financial Officer and Secretary  
(Principal Financial Officer)

November 8, 2013  
Date