New Home Co Inc.
Form 10-K
February 14, 2018

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

(Mark One)
ý ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2017 or
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ______to ______
Commission File Number 001-36283

The New Home Company Inc.
(Exact Name of Registrant as Specified in Its Charter)

| | |
|---|---|
| Delaware | 27-0560089 |
| (State or other Jurisdiction of Incorporation or Organization) | (I.R.S. Employer Identification No.) |

85 Enterprise, Suite 450
Aliso Viejo, California 92656
(Address of principal executive offices) (Zip Code)
Registrant's telephone number, including area code (949) 382-7800

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

| Title of each class | Name of each exchange on which registered |
|---|---|
| Common Stock, par value $0.01 per share | New York Stock Exchange |

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No ý
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No ý
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 ý No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No ¨
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements

incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Large accelerated filer | ¨ | Non-accelerated filer (Do not check if smaller reporting company) | ¨ | Accelerated filer | ý | Smaller reporting company | ¨ |
| | | | | | | Emerging growth company | ý |

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ý
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes ¨ No ý
The aggregate market value of the registrant's common stock held by non-affiliates of the registrant on June 30, 2017, based on the closing price of $11.47 as reported by the New York Stock Exchange was $157,024,380.
There were 20,876,837 shares of the registrant's common stock issued and outstanding as of February 12, 2018.
DOCUMENTS INCORPORATED BY REFERENCE:
The information required by Part III of this Report, to the extent not set forth herein, is incorporated herein by reference from the registrant's definitive proxy statement relating to the Annual Meeting of Stockholders to be held in 2018, which definitive proxy statement shall be filed with the Securities and Exchange Commission within 120 days after the end of the fiscal year to which this Report relates.

ANNUAL REPORT ON FORM 10-K
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2017

CAUTIONARY NOTE CONCERNING FORWARD-LOOKING STATEMENTS

This annual report on Form 10-K and other materials we have filed or will file with the Securities and Exchange Commission (the "SEC") (as well as information included in oral statements or other written statements made or to be made by us) contains or may contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act, as amended. All statements contained in this annual report on Form 10-K other than statements of historical fact, including statements regarding our future results of operations and financial position, our business strategy and plans, and our objectives for future operations, are forward-looking statements. These forward-looking statements are frequently accompanied by words such as "believe," "may," "will," "estimate," "continue," "anticipate," "intend," "expect," "goal," "could," "can," "might," "should," "plan" and similar expressions. We have based these forward-looking statements largely on our current expectations and projections about future events and trends that we believe may affect our financial condition, results of operations, business strategy, short-term and long-term business operations and objectives, and financial needs. Such statements may include, but are not limited to information related to: anticipated operating results; home deliveries; the ability to acquire land and pursue real estate opportunities; the ability to gain approvals and open new communities; the ability to sell homes and properties; the ability to deliver homes from backlog; the ability to secure materials and subcontractors; joint ventures in which we are involved; anticipated results from our investments in unconsolidated entities; the ability to produce the liquidity and obtain capital necessary to expand and take advantage of opportunities; financial resources and condition; changes in revenues; changes in profitability; changes in margins; changes in accounting treatment; cost of sales; selling, general and administrative expenses; interest expense; inventory write-downs; dividends; community openings; seasonality; home warranty claims and reserves; unrecognized tax benefits; anticipated effective tax rates; seasonality; dividends; sales paces and prices; effects of home buyer cancellations; growth and expansion; and legal proceedings, claims and reserves.

From time to time, forward-looking statements also are included in other reports on Forms 10-Q and 8-K, in press releases, in presentations, on our website and in other materials released to the public. Any or all of the forward-looking statements included in this report and in any other reports or public statements made by us are not guarantees of future performance and may turn out to be inaccurate. This can occur as a result of incorrect assumptions or as a consequence of known or unknown risks and uncertainties. Many factors mentioned in this report or in other reports or public statements made by us, such as market conditions, government regulation and the competitive environment, will be important in determining our future performance. New risks emerge from time to time. It is not possible for our management to predict all risks, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. Consequently, actual results may differ materially from those that might be anticipated from our forward-looking statements.
Forward-looking statements speak only as of the date they are made, and we undertake no obligation to revise or publicly release any revision to these forward-looking statements, except as required by law. Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements.
For a discussion of factors that we believe could cause our actual results to differ materially from expected and historical results, see "Item 1A - Risk Factors" and Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" in this annual report on Form 10-K. This discussion is provided as permitted by the Private Securities Litigation Reform Act of 1995, and all of our forward-looking statements are expressly qualified in their entirety by the cautionary statements contained or referenced in this section.

# PART I

## Item 1. Business

As used in this annual report on Form 10-K, unless the context otherwise requires or indicates, references to "the Company," "our company," "we," "our" and "us" (1) for periods prior to the completion of our formation transactions, refer to The New Home Company LLC and its subsidiaries and affiliates, which we sometimes refer to as "TNHC LLC," and (2) following the completion of our formation transactions, refer to The New Home Company Inc. and its subsidiaries. The New Home Company LLC was formed on June 25, 2009 as a Delaware limited liability company. On January 30, 2014, in connection with our initial public offering, The New Home Company LLC was converted into a Delaware corporation and renamed The New Home Company Inc., which we refer to as our formation transaction. You should read the following in conjunction with the section titled "Risk Factors", which is included in Part I, Item 1A in this annual report on Form 10-K.

### Our Company

We are a new generation homebuilder focused on the design, construction and sale of innovative and consumer-driven homes in major metropolitan areas within select growth markets in California and Arizona, including coastal Southern California, the San Francisco Bay area, metro Sacramento and the greater Phoenix area.

We were founded in August 2009, towards the end of an unprecedented downturn in the U.S. homebuilding industry. In January 2014, we completed our initial public offering of shares of our common stock. We believe our management team has extensive and complementary construction, design, marketing, development and entitlement expertise, as well as strong relationships with key land sellers within each of our local markets, and a reputation for quality building, which provide a competitive advantage in being able to acquire land, participate in and create masterplans, obtain entitlements and build quality homes.

We are organized into two reportable segments: homebuilding and fee building. Our homebuilding operations are comprised of divisions in Northern California, Southern California and our newest division in Arizona, which was established during 2015. Our primary business focus is building and selling homes for our own account; however, we also have a meaningful fee building business. For financial information about our segments, see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Note 14 to the Consolidated Financial Statements.

### Homebuilding Operations

We are currently focused on identifying unique sites and creating communities that allow us to design, construct and sell consumer-driven, single-family detached and attached homes in major metropolitan areas in Southern California, the San Francisco Bay area, metro Sacramento and the greater Phoenix area. We seek sites where we are rewarded for thoughtful land planning and architecture, and additional defining characteristics of our markets include barriers to entry, job growth, high employment to building permit ratios and increasing populations, which can create growing demand for new housing. We perform extensive consumer research that helps us create land plans and design homes that meet the needs and desires of our targeted buyers. We believe our approach to market research and construction expertise across an extensive product offering allows us the flexibility to pursue a wide array of land acquisition opportunities and appeals to a broad range of potential homebuyers, including entry-level, move-up, move-down and luxury customers. The homes that we and our unconsolidated joint ventures build range in price from approximately $360,000 to over $9 million, with home sizes ranging from approximately 700 to 6,200 square feet. Homebuilding revenue contributed to 75%, 73% and 65% of total revenue for the years ended December 31, 2017, 2016 and 2015, respectively. For the years ended December 31, 2017, 2016 and 2015, the average sales price of homes delivered from our communities was approximately $1.6 million, $2.0 million and $1.9 million, respectively. We believe that customer-focused community creation and product development, our reputation for high quality construction, as well as exemplary customer service, are key components of the lifestyle connection we seek to establish with each homebuyer and enhances our overall financial performance.

Additionally, we strive to enhance the home-buying experience and buyers’ personal investment in their homes by actively engaging them in the selection of design options and upgrades. We believe that our on-site design studios, which allow buyers to personalize our home offerings with dedicated designers who are knowledgeable about the attributes of the homes offered in the community, are a key source of competitive differentiation. We believe that the active participation of buyers in selecting options and upgrades results in buyers becoming more personally invested in their homes, which leads to fewer cancellations. In addition to our on-site design studios, we also believe our emphasis on customer care provides us a competitive advantage. Our commitment to customer satisfaction is a key element of company culture, which fosters an environment where team members can innovate.

We seek to maximize returns and reduce exposure to land risk through the use of land options, joint ventures and other flexible land acquisition and development arrangements. The Company owned approximately 946 lots and had options to purchase an additional 1,806 lots as of December 31, 2017. We believe our lot option and joint venture strategy is a key factor in allowing us to leverage our entity-level capital and returns on equity, participate in and develop larger masterplan communities, and establish a homebuilding platform focused on high-growth, land-constrained markets. In addition, we believe that our professional reputation and long-standing relationships with key land sellers, including masterplan community developers, brokers and other builders, as well as our institutional investors and joint venture partners, enable us to acquire well-positioned land parcels in our existing markets as well as new target markets.

Fee Building Operations

While our primary business focus is building and selling homes for our own account, we also have a meaningful fee building business. We believe our fee building business complements our homebuilding business in what we believe to be among the most attractive masterplan communities in Southern California. Our fee building segment also includes our management fee revenues that we receive for serving as the managing member or other similar role in our joint ventures. One of our wholly owned subsidiaries is usually the general contractor for our and our unconsolidated joint ventures' projects and retains subcontractors for home construction and land development.

The following table shows the percentage of each segment's revenue in relation to our consolidated total revenues for the years ended December 31, 2017, 2016 and 2015. For additional information related to geographic location of our homebuilding revenues, see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations."

| | Year Ended December 31, (dollars in thousands) | | | | | |
|---|---|---|---|---|---|---|
| | 2017 | % of Total Revenues | 2016 | % of Total Revenues | 2015 | % of Total Revenues |
| Homebuilding | $560,842 | 75 % | $507,949 | 73 % | $280,209 | 65 % |
| Fee building | 190,324 | 25 % | 186,507 | 27 % | 149,890 | 35 % |
| Total revenues | $751,166 | 100 % | $694,456 | 100 % | $430,099 | 100 % |

Summary of Owned and Controlled Lots

As of December 31, 2017, we owned or controlled an aggregate of 2,752 lots, plus another 920 lots pursuant to our fee building contracts. The following table presents certain information with respect to our wholly owned and fee building lots as of December 31, 2017. See Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Lots Owned and Controlled" for further detail.

| | December 31, | | | | | | |
|---|---|---|---|---|---|---|---|
| | 2017 | Change Amount | % | 2016 | Change Amount | % | 2015 |
| Lots Owned | 946 | 356 | 60 % | 590 | 178 | 43 % | 412 |
| Lots Controlled[1] | 1,806 | 820 | 83 % | 986 | 80 | 9 % | 906 |
| Lots Owned and Controlled - Wholly Owned | 2,752 | 1,176 | 75 % | 1,576 | 258 | 20 % | 1,318 |
| Fee Building[2] | 920 | (15) | (2)% | 935 | (487) | (34)% | 1,422 |
| Total Lots Owned and Controlled | 3,672 | 1,161 | 46 % | 2,511 | (229) | (8)% | 2,740 |

(1) Includes lots that we control pursuant to option contracts, purchase contracts or non-binding letters of intent that are subject to customary conditions and have not yet closed. There can be no assurance that such acquisitions will occur.

(2) Lots owned by third party property owners for which we perform general contracting services.

6

Backlog

At December 31, 2017 and 2016, homes under contract, but not yet delivered ("backlog") totaled 153 and 79, respectively, with an estimated sales value of $162.3 million and $187.3 million, respectively. We expect to deliver all of the homes in backlog at December 31, 2017 during 2018 under their existing home order contracts or through the replacement of an existing contract with a new home order contract. The estimated backlog sales value at December 31, 2017 may be impacted by, among other things, subsequent home order cancellations, incentives provided, and/or options and upgrades selected.

Acquisition Process

Our land acquisition strategy focuses on purchasing entitled finished, or partially improved land sufficient for construction of homes over a two- to three-year period from the initiation of homebuilding activity. We also selectively acquire parcels that require land development activities. Our acquisition process generally includes the following steps aimed at reducing development and market cycle risk:

- review of the status of entitlements and other governmental processing, including title reviews;
- identification of target buyer and appropriate housing product;
- determination of land plan to accommodate desired housing product;
- completion of environmental reviews and third-party market studies;
- preparation of detailed budgets for all cost categories;
- completion of due diligence on the land parcel prior to committing to the acquisition;
- utilization of options, joint ventures and other land acquisition arrangements, if appropriate and available;
- limitation on the size of an acquisition relative to the Company's pro forma capitalization; and
- centralized acquisition procedure through a tiered internal management committee, Executive Committee and full Board approval process.

Before purchasing a land parcel, we engage and work closely with outside architects and consultants to design our homes and communities.

We also differentiate our acquisition strategy based on whether the land is in a masterplan community, or part of a larger development. For land which is not part of a larger development or masterplan, we generally enter into a purchase agreement with the land owner and deliver a deposit, which becomes nonrefundable upon the expiration of a specified due diligence period. The closing is generally tied to the date on which we have obtained development entitlements for the land. For land which is part of a larger development being developed by a master developer, we generally enter into a purchase agreement with the master developer and pay a deposit that becomes nonrefundable upon expiration of the due diligence period. The closing in master developments is generally tied to the issuance of final land development entitlements and completion of certain infrastructure and other improvements by the master developer. In master developments we may acquire all of the land at the closing or we may acquire the land in "phases". In master developments we may be required to (a) pay to the master developer a share of our net profit in excess of a specified margin and/or (b) grant the master developer the right to repurchase the land if we fail to develop the land in accordance with applicable development requirements or wish to sell the land in bulk. Our acquisition-development financing is generally obtained using one or more of the following: (i) proceeds from the sale of Senior Notes, (ii) through unsecured lines of credit; (iii) secured acquisition-development loans; (iv) equity obtained from joint venture partners and/or (v) land bank arrangements with providers who take title to the land at closing subject to agreements which obligate us to perform all development activities with respect to the land and provide us with an option to purchase the land.

Construction, Marketing and Sales Process

We typically develop communities in phases based upon projected sales. We seek to control the timing of construction of subsequent phases in the same community based on sales demand in prior phases and the number of qualified potential homebuyers that exist on our priority buyer list. Our construction process is driven by sales contracts that generally precede the start of the construction of homes. The determination that a potential home buyer is qualified to obtain the financing necessary to complete the purchase is an integral part of our process. Once qualified, our on-site design centers, with designers dedicated to a specific community, work with the buyer to tailor the home to meet the buyer's needs.

Land Development and Construction

We customarily acquire improved or unimproved land zoned for residential use. To control larger land parcels or gain access to highly desirable parcels, we sometimes form land development joint ventures with third parties in order to provide us with a pipeline of land to acquire from the joint venture when the lots are developed. If we purchase raw land or partially developed land, we will perform development work that may include negotiating with governmental agencies and local communities to obtain any necessary zoning, environmental and other regulatory approvals and permits, and constructing, as necessary, roads, water, sewer and drainage systems and recreational facilities like parks, community centers, pools, and hiking and biking trails.

The design of our homes must conform to zoning requirements, building codes and energy efficiency laws. As a result, we contract with a number of architects and other consultants in connection with the design process. We act as a general contractor (and certain of our wholly owned subsidiaries hold the general contractor's licenses in California and Arizona) with our supervisory employees coordinating most of the land development and construction work on a project. Independent architectural design, engineering and other consulting firms are generally engaged on a project-by-project basis to assist in project planning and community and home design, and subcontractors and trade partners are engaged to perform all of the physical development and construction work. Although we do not have long-term contractual commitments with our subcontractors, trade partners, suppliers or laborers, we maintain strong and long-standing relationships with many of our subcontractors and trade partners. We believe that our relationships with subcontractors and trade partners have been enhanced through involving them prior to the start of a new community, maintaining our schedules and making timely payment. By dealing fairly, we believe we are able to keep our key subcontractors and trade partners loyal to us.

Sales and Marketing

In connection with the sale and marketing of our homes, we make extensive use of advertising and other promotional activities, including through our website (www.NWHM.com), social-media, brochures, direct mail and other community-specific collateral materials. The information contained in, or that can be accessed through our website, is not incorporated by reference and is not a part of this annual report on Form 10-K.

We primarily sell our homes through our own sales representatives and at times, through the use of outside brokers. One of our wholly owned subsidiaries holds the corporate broker's licenses in California and Arizona. Our in-house sales force works from sales offices located in model homes or sales centers close to, or within each community. Sales representatives assist potential buyers by providing them with floor plan, price and community amenity information, construction timetables and tours of model homes.

Generally, we build model homes at each project and have them professionally decorated and landscaped to display design features and options available for purchase in the design center. We believe that model homes play a significant role in helping homebuyers understand the efficiencies and value provided by each floor plan type. Structural changes in design from the model homes, other than those predetermined, are not generally permitted, but homebuyers may select various other optional construction and design amenities. Our on-site design centers are an integral part of this process. The specific options selected for each community are based upon the price of the home and anticipated buyer preferences. Options include structural (room configurations or pre-determined additional square footage), electrical, plumbing and finish options (flooring, cabinets, fixtures). In certain communities, we also offer turn-key landscape options. Each design center is managed by our own designers dedicated to the specific community.

We typically sell homes using sales contracts that include cash deposits by the purchasers. Before entering into sales contracts, we pre-qualify many of our customers through a preferred mortgage provider. However, purchasers can generally cancel sales contracts if they are unable to sell their existing homes, if they fail to qualify for financing, or under certain other circumstances. For our communities, the cancellation rate of buyers who contracted to buy a home but did not close escrow as a percentage of overall orders was 9%, 12% and 10% during the years ended December 31, 2017, 2016 and 2015, respectively. Cancellation rates are subject to a variety of factors, including those beyond our control, such as adverse economic or housing market conditions and increases in mortgage interest rates.

Customer Financing

At each of our communities, we seek to assist many of our homebuyers in obtaining financing by arranging with preferred mortgage lenders to offer qualified buyers a variety of financing options. Most homebuyers utilize long-term mortgage financing to purchase a home, and mortgage lenders will usually make loans only to qualified borrowers.

Quality Control and Customer Service

We pay particular attention to the product design process and carefully consider quality and choice of materials in order to attempt to eliminate building deficiencies. The quality and workmanship of the subcontractors and trade partners we employ are monitored using our personnel and third-party consultants. We make regular inspections and evaluations of our subcontractors and trade partners to seek to ensure that our standards are met.

We maintain a quality control and customer service staff whose role includes providing a positive experience for each customer throughout the pre-sale, sale, building, delivery and post-delivery periods. These employees are also responsible for providing after-sales customer service, including the coordination of warranty requests. Our quality and service initiatives include taking homebuyers on a comprehensive tour of their home during construction and prior to delivery. In addition, we generally use a third party, Eliant, to survey our homebuyers in order to improve our standards of quality and customer satisfaction.

Insurance and Warranty Program

We provide a limited one-year warranty to our homeowners covering workmanship and materials. In addition, we generally provide a more limited warranty, which generally ranges from a minimum of two years up to the period covered by the applicable statute of repose, that covers certain defined construction defects. The limited warranty covering construction defects is transferable to subsequent buyers and provides for the resolution of unresolved construction-related disputes through binding arbitration. Additionally, we have dedicated customer service staff that work with our homebuyers and coordinate with subcontractors and trade partners, as necessary, during the warranty period. We maintain reserves to cover the resolution of our potential liabilities associated with known and anticipated warranty and construction defect related claims and litigation. While our subcontractors who perform our homebuilding work generally provide us with an indemnity for claims relating to their workmanship and materials, we also purchase general liability insurance that covers development and construction activity at each of our communities. Our subcontractors are usually covered by these programs through an owner-controlled insurance program, or "OCIP." Consultants such as engineers and architects are generally not covered by the OCIP but are required to maintain their own insurance. In general, we maintain insurance, subject to deductibles and self-insured amounts, to protect us against various risks associated with our activities, including, among others, general liability, "all-risk" property, construction defects, workers’ compensation, automobile, and employee fidelity. Our warranty reserves include expected costs associated with the deductibles and self-insured amounts. For a further discussion of the risks associated with our warranty and insurance program, please see the risk factor under the heading "Risks Related to Our Business - We are subject to construction defect and warranty claims arising in the ordinary course of business that can be significant."

Seasonality and Cycles

We have experienced seasonal variations in our quarterly operating results and capital requirements in each of our reportable segments. We typically take orders for more homes in the first half of the fiscal year than in the second half, which creates additional working capital requirements in the second and third quarters to build our inventories to satisfy the deliveries in the second half of the year. Our revenues and cash flows (exclusive of the amount and timing of land purchases) from homebuilding operations are generally higher in the second half of the calendar year, particularly in the fourth quarter. We expect this seasonal pattern to continue over the long-term, although it may be affected by volatility in the homebuilding industry. The homebuilding industry is cyclical. We continue to make substantial investments in land, which is likely to utilize a significant portion of our cash resources, so long as we believe such investments will yield results that meet our investment criteria.

Labor and Raw Materials

Typically, all the raw materials and most of the components used in our business are readily available in the United States. Most are standard items carried by major suppliers. Increases in the cost of building materials and subcontracted labor may reduce gross margins from home sales to the extent that market conditions prevent the recovery of increased costs through higher home sales prices. From time to time and to varying degrees, we may experience shortages in the availability of building materials and/or labor in each of our markets. These shortages and delays may result in delays in the delivery of homes under construction, reduced gross margins from home sales, or both. We continue to monitor the supply markets to achieve favorable prices.

Joint Ventures

Our joint venture strategy has assisted in leveraging our entity-level capital and establishing a homebuilding and land development platform focused on high-growth, land-constrained markets. We own interests in our unconsolidated joint ventures that generally range from 5% to 35%. We also earn management fees from such joint ventures.

We serve as the administrative member, manager or managing member of each of our six homebuilding and four land development joint ventures. We do not, however, exercise control over the joint ventures, as the joint venture agreements generally provide our respective partners with the right to consent to certain actions. Under most joint venture agreements, certain major decisions must be approved by the applicable joint venture's executive committee, which is comprised of both our representatives and representatives of our joint venture partners. In addition, some of our joint venture agreements grant both partners a buy-sell right pursuant to which, subject to certain exceptions, either partner may initiate procedures requiring the other partner to choose between selling its interest to the other partner or buying the other partner's interest. Additional information related to our unconsolidated joint ventures is set forth in Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Off-Balance Sheet Arrangements and Contractual Obligations."

Fee Building Services

Although our primary business focus is building and selling homes for our own account, we also selectively provide general contracting services to build homes for independent third-party property owners. We refer to these projects as "fee building projects." For the year ended December 31, 2017, 97% of our fee building revenue represents fee building billings and 3% represents management fees from unconsolidated joint ventures. Our services with respect to fee building projects typically include design, development and construction. We earn revenue on our fee building projects either as a flat fee for the project or as a percentage of the cost or revenue of the project depending upon the terms of the agreement with our customer. For the years ended December 31, 2017, 2016 and 2015, fee building revenue contributed to 25%, 27% and 35%, respectively, of total revenue. The Company's fee building revenues have historically been concentrated with a small number of customers. We have several fee building agreements with Irvine Pacific, LP and revenues from this customer totaled 25%, 26%, and 32% of our total consolidated revenues for the years ended December 31, 2017, 2016 and 2015, respectively. Our billings to this customer are dependent upon such customer's decision to proceed with construction and the agreements can be canceled at any time. We cannot predict whether these agreements will continue in the future or the current pace of construction, and the loss of these billings could have a material adverse effect on our results of operations. See Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Fee Building" and Note 1 "Revenue Recognition - Fee Building" to the Consolidated Financial Statements for further discussion of this revenue concentration.

Government Regulation and Environmental Matters

We are subject to numerous local, state and federal statutes, ordinances, rules and regulations concerning zoning, development, building design, construction and similar matters, which impose restrictive zoning and density requirements, the result of which is to limit the number of homes that can be built within the boundaries of a particular area. Communities that are not entitled may be subjected to periodic delays, changes in use, less intensive development or elimination of development in certain specific areas due to government regulations. We may also be subject to periodic delays or may be precluded entirely from developing in certain communities due to building moratoriums or "slow-growth" or "no-growth" initiatives that could be implemented in the future. Local governments also have broad discretion regarding the imposition of development fees and exactions for communities in their jurisdiction. Communities for which we have received land use and development entitlements or approvals may still require a variety of other governmental approvals and permits during the development process and can also be impacted adversely by unforeseen health, safety and welfare issues, which can further delay these communities or prevent their development.

We are also subject to a variety of local, state and federal statutes, ordinances, rules and regulations concerning the environment. The particular environmental laws which apply to any given homebuilding site vary according to multiple factors, including the site's location, its environmental conditions and the present and former uses of the site, as well as adjoining properties. Environmental laws and conditions may result in delays, may cause us to incur substantial compliance and other costs, and can prohibit or severely restrict homebuilding activity in environmentally sensitive regions or areas. In addition, in those cases where an endangered or threatened species is involved, environmental rules and regulations can result in the restriction or elimination of development in identified environmentally sensitive areas. Legislation related to climate change and energy efficiency can impose stricter building standards, which may increase our cost to build. From time to time, the EPA and similar federal or state agencies review homebuilders' compliance with environmental laws and may levy fines and penalties for failure to strictly comply with applicable environmental laws or impose additional requirements for future compliance as a result of past failures. Any such actions taken with respect to us may increase our costs. Further, we expect that increasingly stringent requirements will be imposed on homebuilders in the future. Environmental regulations can also have an adverse impact on the availability and price of certain raw materials such as lumber. California is especially susceptible to restrictive government regulations and environmental laws.

Under various environmental laws, current or former owners of real estate, as well as certain other categories of parties, may be required to investigate and clean up hazardous or toxic substances or petroleum product releases, and may be held liable to a governmental entity or to third parties for related damages, including for bodily injury, and for investigation and clean-up costs incurred by such parties in connection with the contamination. A mitigation system may be installed during the construction of a home if a cleanup does not remove all contaminants of concern or to address a naturally occurring condition such as methane. Some buyers may not want to purchase a home with a mitigation system.

We use and our business relies upon general contractors' licenses and corporate real estate broker's licenses in order to build and sell homes.

For a further discussion of the impact of govern regulations on our business, including the impact of environmental regulations, please see the risk factors included under the heading "Risks Related to Laws and Regulations."

## Bonds and Other Obligations

In connection with the development of our communities, we are frequently required to provide performance, maintenance and other bonds and letters of credit in support of our related obligations with respect to such developments. The amount of such obligations outstanding at any time varies in accordance with our pending development activities. In the event any such bonds or letters of credit are drawn upon, we would be obligated to reimburse the issuer of such bonds or letters of credit. As of December 31, 2017, we had approximately $52.1 million and $0 of outstanding performance bonds and letters of credit, respectively, primarily related to our obligations to local governments to construct roads and other improvements in various developments.

## Competition

The homebuilding industry is fragmented and highly competitive. We compete with numerous other residential construction companies, including large national and regional firms, for customers, land, financing, raw materials, skilled labor, and employees. A number of our primary competitors are significantly larger, have a longer operating history and may have greater resources or lower cost of capital than us. We compete for customers primarily on the basis of home design and location, price, customer satisfaction, construction quality, reputation, and the availability of mortgage financing. We also compete for sales with individual resales of existing homes and with available rental housing. As part of our strategy to expand our product offerings to include more affordably-priced homes to reach a deeper pool of qualified buyers and in connection with growing our overall community count, our average sales price of homes in backlog has declined from $2.4 million at December 31, 2016 to $1.1 million at December 31, 2017. We anticipate that we will continue to build more affordably-priced homes. We believe there is more competition among homebuilding companies in more affordable product offerings than in the luxury and move-up segments, however, we also believe this is a prudent strategy as there is a larger population of qualified buyers in more affordable price points. For risks associated with the competition we face, please see the risk factor under the heading "Risks Related to Our Business - We may not be able to compete effectively against competitors in the homebuilding industry".

## Employees

As of December 31, 2017, we had 281 employees, 104 of whom were executive, management and administrative personnel located in our offices, 55 of whom were sales and marketing personnel and 122 were involved in field construction. Although none of our employees are covered by collective bargaining agreements, certain of the third party subcontractors and trade partners engaged by us are represented by labor unions or are subject to collective bargaining arrangements. We believe that relations with our employees, subcontractors and trade partners are good.

## Our Offices and Available Information

Our principal executive offices are located at 85 Enterprise, Suite 450, Aliso Viejo, California 92656. Our main telephone number is (949) 382-7800. Our internet website is www.NWHM.com. Our common stock is listed on the New York Stock Exchange (NYSE: NWHM). We will make available through the "Investors" section of our website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to these reports filed or furnished pursuant to Section 13(d) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonably practicable after filing with, or furnishing to, the SEC. Copies of these reports, and any amendment to them, are available free of charge upon request. We provide information about our business and financial performance, including our corporate profile, on our Investor Relations website. Additionally, we webcast our earnings calls and certain events we participate in with members of the investment community on our Investor Relations website. Further corporate governance information, including our code of ethics and business conduct, corporate governance guidelines, and board committee charters, is also available on our Investor Relations website. The information contained in, or that can be accessed through our website is not incorporated by reference and is not part of this annual report on Form 10-K.

Item 1A. Risk Factors

You should carefully consider the following risk factors, which address the material risks concerning our business, together with the other information contained in this annual report on Form 10-K. If any of the risks discussed in this annual report on Form 10-K occur, our business, prospects, liquidity, financial condition and results of operations could be materially and adversely affected, in which case the trading price of our common stock could decline significantly and you could lose part or all of your investment. Some statements in this annual report, including statements in the following risk factors, constitute forward-looking statements. Please refer to the initial section of this annual report entitled "Cautionary Note Concerning Forward-Looking Statements."

Risks Related to Our Business

Our geographic concentration could materially and adversely affect us if the homebuilding industry or the availability of land parcels in our current markets declines.

Our current business involves the design, construction and sale of innovative single-family detached and attached homes in planned communities in major metropolitan areas in coastal Southern California, the San Francisco Bay area, metro Sacramento and the greater Phoenix area. Because our operations are concentrated in these areas, a prolonged economic downturn affecting one or more of these areas, or affecting any sector of employment on which the residents of such area are dependent, could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations, and a disproportionately greater impact on us than other homebuilders with more diversified operations. During the downturn from 2008 to 2011, land values, the demand for new homes and home prices declined substantially in California. Accordingly, our sales, results of operations, financial condition and business could be negatively impacted by a decline in the economy, one or more significant job sectors or the homebuilding industry in the Western U.S. regions in which our operations are concentrated.

In addition, our ability to acquire land parcels for new single-family homes may be adversely affected by changes in the general availability of land parcels, the willingness of land sellers to sell land parcels at reasonable prices, competition for available land parcels, availability of financing to acquire land parcels, zoning and other market conditions. The availability of land parcels in our California markets at reasonable prices is limited. If the supply of land parcels appropriate for development of single-family homes is limited because of these factors, or for any other reason, our ability to grow could be significantly limited, and the number of homes that we build and sell could decline.

The homebuilding industry is cyclical and affected by changes in general economic, real estate and other business conditions that could reduce the demand for new homes and, as a result, adversely impact our results of operations, financial condition and cash flows.

The residential homebuilding industry is cyclical and is highly sensitive to changes in general economic, real estate and other business conditions such as levels of employment, consumer confidence and income, availability of mortgage financing for homebuyers, interest rate levels, demographic trends, homebuyer preferences for specific designs or locations, real estate taxes, inflation and supply of and demand for new and existing homes. The foregoing conditions, among others, are complex and interrelated. Periods of prolonged economic downturn, high unemployment levels, increases in the rate of inflation and uncertainty in the U.S. economy, have historically contributed to decreased demand for housing, declining sales prices and increasing pricing pressure. In the event that one or more of such economic and business conditions occur, we could experience declines in the market value of our inventory and demand for our homes, which could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations. Federal government actions and new legislation related to economic stimulus, taxation, spending levels and borrowing limits, along with the related political debates, conflicts and compromises associated with such actions, may negatively impact the financial markets and consumer confidence.

Such events could hurt the U.S. economy and the housing market and, in turn, could adversely affect the operating results of our business. Adverse economic conditions outside the U.S., such as Asia or Canada, may also adversely affect the demand for our homes to the extent such conditions impact the amount of potential homebuyers from such regions in our markets.

In addition, an important segment of our customer base consists of first and second "move-up" buyers, who often purchase homes contingent upon the sale of their existing homes. During recessionary periods, these buyers may face difficulties selling their homes, which may in turn adversely affect our sales. Moreover, during such periods, we may need to reduce our sales prices and offer greater incentives to buyers to compete for sales that may result in reduced margins.

Our long-term growth depends upon our ability to successfully identify and acquire desirable land parcels for residential buildout for reasonable prices.

Our future growth depends upon our ability to successfully identify and acquire attractive land parcels for development of our single-family homes at reasonable prices and with terms that meet our underwriting criteria. Our ability to acquire land parcels for new single-family homes may be adversely affected by changes in the general availability of land parcels, the willingness of land sellers to sell land parcels at reasonable prices, competition for available land parcels, availability of financing to acquire land parcels, zoning and other market conditions. We currently depend primarily on the California markets and availability of land parcels in that market at reasonable prices is limited. If the supply of land parcels appropriate for development of single-family homes is limited because of these factors, or for any other reason, our ability to grow could be significantly limited, and the number of homes that we build and sell could decline. Additionally, our ability to begin new projects could be impacted if we elect not to purchase land parcels under option contracts. To the extent that we are unable to purchase land parcels timely or enter into new contracts for the purchase of land parcels at reasonable prices, our home sales revenue and results of operations could be adversely impacted.

Labor and raw material shortages and price fluctuations could delay or increase the cost of home construction, which could materially and adversely affect us.

The residential construction industry experiences serious labor and raw material shortages from time to time, including shortages in qualified tradespeople, and supplies of insulation, drywall, cement, steel and lumber. These labor and raw material shortages can be more severe during periods of strong demand for housing or during periods where the regions in which we operate experience natural disasters that have a significant impact on existing residential and commercial structures. The cost of labor and raw materials may also increase during periods of shortage or high inflation. During the downturn in 2008 to 2011, a large number of qualified trade partners went out of business or otherwise exited the market into new fields. A reduction in available trade partners exacerbates labor shortages as demand for new housing increases. Shortages and price increases could cause delays in and increase our costs of home construction, which we may not be able to recover by raising home prices due to market demand and because the price for each home is typically set months prior to its delivery pursuant to the agreement of sale with the home buyer, which in turn could have a material adverse effect on our business, prospects, financial condition and results of operations.

Our business and results of operations depend on the availability and skill of subcontractors at reasonable rates.

Substantially all of our construction work is done by third-party subcontractors with us acting as the general contractor. Accordingly, the timing and quality of our construction depend on the availability and skill of our subcontractors. We do not have long-term contractual commitments with any subcontractors, and there can be no assurance that skilled subcontractors will continue to be available at reasonable rates and in the areas in which we conduct our operations. Certain of the subcontractors engaged by us are represented by labor unions or are subject to collective bargaining arrangements that require the payment of prevailing wages that are higher than normally expected on a residential construction site. A strike or other work stoppage involving any of our subcontractors could also make it difficult for us to retain subcontractors for our construction work. In addition, union activity could result in higher costs to retain our subcontractors. In addition, the enactment of federal, state or local statutes, ordinances, rules or regulations requiring the payment of prevailing wages on private residential developments would materially increase our costs of development and construction. Access to qualified labor at reasonable rates may also be affected by other circumstances beyond our control, including: (i) shortages of qualified tradespeople, such as carpenters, roofers, drywallers, electricians and plumbers; (ii) high inflation; (iii) changes in laws relating to employment and union organizing activity; (iv) changes in trends in labor force migration; and (v) increases in contractor, subcontractor and professional services costs. The inability to contract with skilled contractors and subcontractors at reasonable rates on a timely basis could materially and adversely affect our business prospects, liquidity, financial condition and results of operations. The inability to contract with skilled subcontractors at reasonable costs on a timely basis could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

In addition, despite our quality control efforts, we may discover that our subcontractors were engaging in improper construction practices or installing defective materials in our homes. When we discover these issues, we, generally through our subcontractors, repair the homes in accordance with our new home warranty and as required by law. Reserves are established based on market practices, our historical experiences and our judgment of the qualitative risks associated with the types of homes built. However, the cost of satisfying our warranty and other legal obligations in these instances may be significantly higher than our reserves, and we may be unable to recover the cost of repair from such subcontractors. Regardless of the steps we take, we can in some instances be subject to fines, litigation, or other penalties, and our reputation and our financial condition may be adversely affected.

We could be responsible for employment-related liabilities with respect to our contractors' employees.

Although contractors are independent of the homebuilders that contract with them under normal management practices and the terms of trade contracts and subcontracts within the homebuilding industry, on October 14, 2017, California's governor signed into law Assembly Bill 1701, which would require general contractors to assume and be liable for unpaid wage, fringe or other benefit payments or contributions that subcontractors owe their employees. Assembly Bill 1701 imposes such liability under California Labor Code Section 218.7 for private works contracts entered on or after January 1, 2018. We are, and may become in the future, subject to similar measures and legislation, such as California Labor Code Section 2810.3, that requires us to share liability with our contractors for the payment of wages and the failure to secure valid workers' compensation insurance coverage. While the Company ordinarily negotiates with its subcontractors to obtain broad indemnification rights, there is no guarantee that it will be able to recover from its subcontractors for actions brought against the Company by its subcontractors' employees or unions representing such employees and such liability could have a material and adverse effect on our financial performance. Even if we are successful in obtaining indemnification from our subcontractors, we may sustain additional administrative costs as a result of such legislation which could materially and adversely affect our financial performance. In addition, despite the fact that our subcontractors are independent from us, if regulatory agencies reclassify the employees of contractors as employees of homebuilders, homebuilders using contractors could be responsible for wage and hour labor laws, workers' compensation and other employment-related liabilities of their contractors. Governmental rulings that make us responsible for labor practices by our subcontractors could create substantial exposures for us in situations that are not within our control.

If the market value of our land or housing inventory decreases, our results of operations could be adversely affected due to the illiquid nature of real estate investments and by impairments.

The market value of our land and housing inventories depends on market conditions. We acquire land for expansion into new markets and for replacement of land inventory and expansion within our current markets. There is an inherent risk that the value of the land owned or controlled by us may decline after purchase. The risks inherent in purchasing and developing land parcels increase as consumer demand for housing decreases. As a result, we may buy and develop land parcels on which homes cannot be profitably built and sold. The valuation of property is inherently subjective and based on the individual characteristics of each property. When market conditions drive land values down, land we have purchased or option agreements we have previously entered into may become less desirable because we may not be able to build and sell homes profitably, at which time we may elect to sell the land or, in the case of options contracts, to forego pre-acquisition costs and forfeit deposits and terminate the agreements. Factors such as changes in regulatory requirements and applicable laws (including in relation to building regulations, taxation and planning), political conditions, the condition of financial markets, both local and national economic conditions, the financial condition of customers, potentially adverse tax consequences, and interest and inflation rate fluctuations subject the market value of land owned, controlled or optioned by us to uncertainty. Moreover, all valuations are made on the basis of assumptions that may not prove to reflect economic or demographic reality. If housing demand decreases below what we anticipated when we acquired our inventory, our results of operations and financial conditions may be adversely affected and we may not be able to recover our costs when we sell and build houses. Land parcels, building lots and housing inventories are illiquid assets, and we may not be able to dispose of them efficiently or at all if we or the housing market and general economy are in financial distress. In addition, inventory carrying costs can be significant and can result in losses in a poorly performing project or market. We regularly review the value of our land holdings and continue to review our holdings on a periodic basis. Material impairments in the value of our inventory may be required, and we may in the future sell land or homes at significantly lower margins or at a loss, if we are able to sell them at all, which could adversely affect our results of operations and financial condition.

We may not be able to compete effectively against competitors in the homebuilding industry.

We operate in a very competitive environment which is characterized by competition from a number of other homebuilders in each market in which we operate. Additionally, there are relatively low barriers to entry into our business. We compete with numerous large national and regional homebuilding companies and with smaller local homebuilders and land developers for, among other things, home buyers, desirable land parcels, financing, raw materials and skilled management and labor resources. Our competitors may independently develop land and construct homes that are superior or substantially similar to our products. As part of our strategy to expand our product offerings to include more affordably-priced homes to reach a deeper pool of qualified buyers and in connection with growing our overall community count, our average sales price of homes in backlog has declined to $1.1 million at December 31, 2017 from $2.4 million at December 31, 2016. We anticipate that we will continue to build more affordably-priced homes. We believe there is more competition among homebuilding companies in more affordable product offerings than in the luxury and move-up segments. Increased competition could hurt our business, as it could prevent us from acquiring attractive land parcels on which to build homes or make such acquisitions more expensive, hinder our market share expansion and cause us to increase our selling incentives or reduce our prices. In past housing cycles, an oversupply of homes available for sale and heavy discounting of home prices by some of our competitors have adversely affected demand for homes in the market as a whole and could do so again in the future. We also compete with the resale, or "previously owned," home market. If we are unable to compete effectively in our markets, our business could decline disproportionately to our competitors, and our results of operations and financial condition could be adversely affected.

We may be at a competitive disadvantage with regard to certain of our large national and regional homebuilding competitors whose operations are more geographically diversified than ours, as these competitors may be better able to withstand any future regional downturn in the housing market. We compete directly with a number of large national and regional homebuilders that may have longer operating histories and greater financial and operational resources than we do. Many of these competitors also have longstanding relationships with subcontractors, local governments and suppliers in the markets in which we operate or in which we may operate in the future. This may give our competitors an advantage in securing materials and labor at lower prices, marketing their products and allowing their homes to be delivered to customers more quickly and at more favorable prices. This competition could reduce our market share and limit our ability to expand our business as we have planned.

If we are unable to develop our communities successfully or within expected timeframes, our results of operations could be adversely affected.

Before a community generates any revenue, time and material expenditures are required to acquire land, obtain development approvals and construct significant portions of project infrastructure, amenities, model homes and sales facilities. It can take several years from the time we acquire control of a property to the time we make our first home sale on the site. Our ability to process a significant number of transactions (which include, among other things, evaluating the site purchase, designing the layout of the development, sourcing materials and subcontractors and managing contractual commitments) efficiently and accurately is important to our success. Errors by employees, failure to comply with regulatory requirements and conduct of business rules, failings or inadequacies in internal control processes, equipment failures, natural disasters or the failure of external systems, including those of our suppliers or counterparties, could result in delays and operational issues that could adversely affect our business, financial condition and operating results and our relationships with our customers. Delays in the development of communities also expose us to the risk of changes in market conditions for homes. A decline in our ability to develop and market our communities successfully and to generate positive cash flow from these operations in a timely manner could have a material adverse effect on our business and results of operations and on our ability to service our debt and to meet our working capital requirements.

Increases in our cancellation rate could have a negative impact on our home sales revenue and homebuilding margins.

In connection with the sale of a home we collect a deposit from the homebuyer that is a small percentage of the total purchase price. In California, upon a home order cancellation, the homebuyer’s escrow deposit is generally returned to the homebuyer (other than with respect to certain design-related deposits, which we generally retain). Home order cancellations can result from a number of factors, including declines or slow appreciation in the market value of homes, increases in the supply of homes available to be purchased, increased competition, higher mortgage interest rates, and changes in homebuyers' financial condition or personal circumstances. In addition, as part of our strategy, we intend to increase the number of homes we build at more affordable price points. Our cancellation rate may increase as we sell to a more diverse credit quality of buyers. Home order cancellations negatively impact our financial and operating results due to a negative impact on the number of homes closed, net new home orders, home sales revenue and results of operations, as well as the number of homes in backlog.

A large proportion of our fee building revenue is from one customer.

The Company’s fee building revenues have historically been concentrated with a small number of customers.  We have several fee building agreements with Irvine Pacific, LP and our billings to this customer are dependent upon such customer’s decision to proceed with construction and the agreements can be canceled at any time. We cannot predict whether these agreements will continue in the future or the current pace of construction, and the loss of these billings could negatively impact our business and our results of operations. See Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Fee Building" and Note 1 "Revenue Recognition - Fee Building" to the accompanying notes to consolidated financial statements included in this annual report on Form 10-K for further discussion of this revenue concentration.

We are subject to construction defect and warranty claims arising in the ordinary course of business that can be significant.

As a homebuilder, we are subject to construction defect, product liability and home warranty claims, arising in the ordinary course of business or otherwise. While we maintain general liability insurance and generally seek to require our subcontractors and design professionals to indemnify us for some portion of the liabilities arising from their work, there can be no assurance that these insurance rights and indemnities will be collectible or adequate to cover any or all construction defect and warranty claims for which we may be liable. Some claims may not be covered by insurance or may exceed applicable coverage limits. We may not be able to renew our insurance coverage or renew it at reasonable rates and may incur significant costs or expenses (including repair costs and litigation expenses) surrounding possible construction defects, product liability claims, soil subsidence or building related claims.  Some claims may arise out of uninsurable events or circumstances not covered by insurance or that are not subject to effective indemnification agreements with our trade partners.

With respect to certain general liability exposures, including construction defects and related claims and product liability claims, interpretation of underlying current and future trends, assessment of claims and the related liability and reserve estimation process require us to exercise significant judgment due to the complex nature of these exposures, with each exposure often exhibiting unique circumstances. Furthermore, once claims are asserted against us for construction defects, it is difficult to determine the extent to which the assertion of these claims will expand. Plaintiffs may seek to consolidate multiple parties in one lawsuit or seek class action status in some of these legal proceedings with potential class sizes that vary from case to case. Consolidated and class action lawsuits can be costly to defend and, if we were to lose any consolidated or certified class action suit, it could result in substantial liability.

We also expend significant resources to repair items in homes we have sold to fulfill the warranties we issued to our homebuyers. Additionally, we are subject to construction defect claims can be costly to defend and resolve in the legal system. Warranty and construction defect matters can also result in negative publicity in the media and on the internet, which can damage our reputation and adversely affect our ability to sell homes.

In addition, we conduct most of our business in California, one of the most highly regulated and litigious jurisdictions in the United States, which imposes a ten year, strict liability tail on many construction liability claims. As a result, our potential losses and expenses due to litigation, new laws and regulations may be greater than those of our competitors who have smaller California operations as a percentage of the total enterprise.

Adverse weather and geological conditions may increase costs, cause project delays and reduce consumer demand for housing, all of which could materially and adversely affect us.

As a homebuilder and land developer, we are subject to the risks associated with numerous weather-related and geologic events, many of which are beyond our control. These weather-related and geologic events include but are not limited to droughts, floods, wildfires, landslides, soil subsidence and earthquakes. The occurrence of any of these events could damage our land parcels and projects, cause delays in the completion of our projects, reduce consumer demand for housing and cause shortages and price increases in labor or raw materials, any of which could harm our sales and profitability. Our California markets are in areas which have historically experienced significant earthquake activity and seasonal wildfires. In addition to directly damaging our land or projects, earthquakes, floods, landslides, wildfires or other geologic events could damage roads and highways providing access to those projects, thereby adversely affecting our ability to market homes in those areas and possibly increasing the costs of completion.

There are some risks of loss for which we may be unable to purchase insurance coverage. For example, losses associated with landslides, earthquakes and other geologic events may not be insurable, and other losses, such as those arising from terrorism, may not be economically insurable. A sizeable uninsured loss could materially and adversely affect our business, prospects, liquidity, financial condition and results of operations.

Power, water and other natural resource shortages or price increases could have an adverse impact on operations.

The markets in which we operate have experienced power and resource shortages, including mandatory periods without electrical power, changes to water availability (including drought conditions) and significant increases in utility and resource costs. These conditions may cause us to incur additional costs and we may not be able to complete construction on a timely basis if they were to continue for an extended period of time. Shortages of natural resources, particularly water and power, may make it more difficult to obtain regulatory approval of new developments. We may incur additional costs and may not be able to complete construction on a timely basis if such power shortages and utility rate increases continue. Furthermore, water restrictions, drought conditions, power shortages and rate increases may adversely affect the regional economies in which we operate, which may reduce demand for housing. Our operations may be adversely impacted if further restrictions, drought conditions, rate increases and/or power shortages occur.

Because of the seasonal nature of our business, our quarterly operating results fluctuate.

As discussed under "Management’s Discussion and Analysis of Financial Condition-Seasonality" we have experienced seasonal fluctuations in our quarterly operating results and capital requirements that can have a material impact on our results and our consolidated financial statements. We typically experience the highest new home order activity in spring and summer, although this activity also highly depends on the number of active selling communities, timing of new community openings and other market factors. Since it typically takes five to ten months to construct a new home, we deliver more homes in the second half of the year as spring and summer home orders convert to home deliveries. Because of this seasonality, home starts, construction costs and related cash outflows have historically been highest in the second and third quarters, and the majority of cash receipts from home deliveries occur during the second half of the year. We expect this seasonal pattern to continue over the long-term, although it may be affected by volatility in the homebuilding industry.

Seasonality also requires us to finance construction activities in advance of the receipt of sales proceeds. In many cases, we may not be able to recapture increased costs by raising prices because prices are established upon signing the purchase contract. Accordingly, there is a risk that we will invest significant amounts of capital in the acquisition and development of land and construction of homes that we do not sell at anticipated pricing levels or within anticipated time frames. If, due to market conditions, construction delays or other causes, we do not complete sales of our homes at anticipated pricing levels or within anticipated time frames, our financial performance and financial conditions could be materially and adversely affected.

We may be unable to obtain suitable bonding for the development of our housing projects.

We are often required to provide bonds to governmental authorities and others to ensure the completion of our projects. As a result of market conditions, surety providers have been reluctant to issue new bonds and some providers are requesting credit enhancements (such as cash deposits or letters of credit) in order to maintain existing bonds or to issue new bonds. If we are unable to obtain required bonds in the future for our projects, or if we are required to provide credit enhancements with respect to our current or future bonds, our business, prospects, liquidity, financial condition and results of operations could be materially and adversely affected.

Inflation could adversely affect our business and financial results.

Inflation could adversely affect us by increasing the costs of land, raw materials and labor needed to operate our business, which in turn requires us to increase our home selling price in an effort to maintain satisfactory housing gross margins. Inflation typically also accompanies higher interests rates, which could adversely impact potential customers’ ability to obtain financing on favorable terms, thereby further decreasing demand. If we are unable to raise the prices of our homes to offset the increasing costs of our operations, our margins could decrease. Furthermore, if we need to lower the price of our homes to meet demand, the value of our land inventory may decrease. Depressed land values may cause us to abandon and forfeit deposits on land option contracts and other similar contracts if we cannot satisfactorily renegotiate the purchase price of the subject land. We may record charges against our earnings for inventory impairments if the value of our owned inventory, including land we decide to sell, is reduced, or for land option contract abandonments if we choose not to exercise land option contracts or other similar contracts, and these charges may be substantial. Inflation may also raise our costs of capital and decrease our purchasing power, making it more difficult to maintain sufficient funds to operate our business.

A major health and safety incident relating to our business could be costly in terms of potential liabilities and reputational damage.

Building sites are inherently dangerous, and operating in the homebuilding industry poses certain inherent health and safety risks to those working at such sites. Due to health and safety regulatory requirements and the number of projects we work on, health and safety performance is critical to the success of all areas of our business. Any failure in health and safety performance may result in penalties for non-compliance with relevant regulatory requirements or litigation, and a failure that results in a major or significant health and safety incident is likely to be costly in terms of potential liabilities incurred as a result. Such a failure could generate significant negative publicity and have a corresponding impact on our reputation, our relationships with relevant regulatory agencies, governmental authorities and local communities, and our ability to win new business, which in turn could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

Negative publicity or poor relations with the residents of our communities could negatively impact sales, which could cause our revenues or results of operations to decline.

Unfavorable media related to our industry, company, brands, marketing, personnel, operations, business performance, or prospects may affect our stock price and the performance of our business, regardless of its accuracy or inaccuracy. Our success in maintaining, extending and expanding our brand image depends on our ability to adapt to a rapidly changing media environment. Adverse publicity or negative commentary on social media outlets, such as blogs, websites or newsletters, could hurt operating results, as consumers might avoid or protest brands that receive bad press or negative reviews. Negative publicity may result in a decrease in our operating results.

In addition, residents of communities we develop may look to us to resolve issues or disputes that may arise in connection with the operation or development of their communities. Efforts made by us to resolve these issues or disputes could be deemed unsatisfactory by the affected residents, and subsequent actions by these residents could adversely affect sales or our reputation.

An information systems interruption or breach in security could adversely affect us.

Privacy, security, and compliance concerns have continued to increase as technology has evolved. We rely on accounting, financial and operational management information systems to conduct our operations. Many of these resources are provided to us or are maintained on our behalf by third-party service providers pursuant to agreements that specify certain security and service level standards. Our ability to conduct our business may be materially and adversely impaired if our computer resources are compromised, degraded, damaged or fail, whether due to a virus or other harmful circumstance, intentional penetration or disruption of our information technology resources by a third-party, natural disaster, hardware or software corruption or failure or error (including a failure of security controls incorporated into or applied to such hardware or software), telecommunications system failure, service provider error or failure, intentional or unintentional personnel actions (including the failure to follow our security protocols), or lost connectivity to its networked resources. Furthermore, as part of our normal business activities, we collect and store certain confidential information, including information about employees, homebuyers, customers, vendors and suppliers. This information is entitled to protection under a number of regulatory regimes. We may share some of this information with vendors who assist us with certain aspects of our business. Our failure to maintain the security of the data which we are required to protect, including via the penetration of our network security and the misappropriation of confidential and personal information, could result in business disruption, damage to our reputation, financial obligations to third parties, fines, penalties, regulatory proceedings and private litigation with potentially large costs, and also result in deterioration in customers confidence in us and other competitive disadvantages, and thus could have a material adverse impact on our financial condition and results of operations.

We may incur a variety of costs to engage in future growth or expansion of our operations or acquisitions of businesses, and the anticipated benefits may never be realized.

As a part of our business strategy, we may consider growth or expansion of our operations in our current markets or in other areas of the country. Any such growth or expansion would be accompanied by risks such as:

- difficulties in assimilating the operations and personnel of acquired companies or businesses;
- potential loss of key employees of the acquired companies or business;
- diversion of our management’s attention from ongoing business concerns;
- our potential inability to maximize our financial and strategic position through the successful expansion or acquisition;
- impairment of existing relationships with employees, contractors, suppliers and customers as a result of the integration of new management personnel and cost-saving initiatives; and
- risks associated with entering markets in which we have limited or no direct experience.

The magnitude, timing and nature of any future acquisition or expansion will depend on a number of factors, including our ability to identify suitable additional markets or acquisition candidates as well as capital resources. We cannot guarantee that any expansion into a new market will be successfully executed, and our failure to do so could harm our current business.

A reduction in our sales absorption levels may force us to incur and absorb additional community-level costs.

We incur certain overhead costs associated with our communities, such as indirect construction costs, property taxes, marketing expenses and costs associated with the upkeep and maintenance of our model and sales complexes. If our sales absorptions pace decreases and the time required to close out our communities is extended, we would likely incur additional overhead costs, which would negatively impact our financial results. Additionally, we incur various land development improvement costs for a community prior to the commencement of home construction. Such costs include infrastructure, utilities, property taxes, interest and other related expenses. Reduction in home absorption rates increases the associated holding costs and extends our time to recover such costs. Declines in the homebuilding market may also require us to evaluate the recoverability of costs relating to land acquired more recently.

Future terrorist attacks against the United States or increased domestic or international instability could have an adverse effect on our operations.

Future terrorist attacks against the United States or any foreign country or increased domestic or international instability could cause consumer unease, which could significantly reduce the number of new contracts signed, and/or increase the number of cancellations of existing contracts, which could adversely affect our business.

Risks Related to Laws and Regulations

Mortgage financing, interest rate increases or changes in federal lending programs or other regulations could lower demand for or impact homebuyers' ability to purchase our homes, which could materially and adversely affect us.

A substantial percentage of purchasers of our homes finance their acquisitions with mortgage financing. Rising interest rates, decreased availability of mortgage financing or of certain mortgage programs, higher down payment requirements, increased monthly mortgage costs, tightened credit requirements and underwriting standards, and an increase in indemnity claims for mortgages may lead to reduced demand for our homes and mortgage loans. Deterioration in credit quality among subprime and other nonconforming loans has caused most lenders to eliminate subprime mortgages and most other loan products that do not conform to Federal National Mortgage Association, or Fannie Mae, Federal Home Loan Mortgage Corporation, or Freddie Mac, Federal Housing Administration, or FHA, or Veterans Administration, or the VA, standards. In addition, as a result of the turbulence in the credit markets and mortgage finance industry during the last downturn, in July 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act was signed into law. This legislation provides for a number of new requirements relating to residential mortgages and mortgage lending practices that reduce the availability of loans to borrowers or increase the costs to borrowers to obtain such loans. Fewer loan products and tighter loan qualifications, in turn, make it more difficult for a borrower to finance the purchase of a new home or the purchase of an existing home from a potential "move-up" buyer who wishes to purchase one of our homes. The foregoing may also hinder our ability to realize our backlog because our home purchase contracts provide customers with a financing contingency. Financing contingencies allow customers to cancel their home purchase contracts in the event that they cannot arrange for adequate financing. As a result, rising interest rates, stricter underwriting standards, and a reduction of loan products, among other similar factors, can decrease our home sales. Any of these factors could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

The federal government has also taken on a significant role in supporting mortgage lending through its conservatorship of Fannie Mae and Freddie Mac, both of which purchase home mortgages and mortgage-backed securities originated by mortgage lenders, and its insurance of mortgages originated by lenders through the FHA and the VA. The availability and affordability of mortgage loans, including interest rates for such loans, could be adversely affected by a curtailment or cessation of the federal government's mortgage-related programs or policies. The FHA may continue to impose stricter loan qualification standards, raise minimum down payment requirements, impose higher mortgage insurance premiums and other costs, or limit the number of mortgages it insures. Due to federal budget deficits, the U.S. Treasury may not be able to continue supporting the mortgage-related activities of Fannie Mae, Freddie Mac, the FHA and the VA at present levels, or it may revise significantly the federal government's participation in and support of the residential mortgage market. Because the availability of Fannie Mae, Freddie Mac, FHA and VA-backed mortgage financing is an important factor in marketing and selling many of our homes, any limitations, restrictions or changes in the availability of such government-backed financing could reduce our home sales, which could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

Changes in tax laws can increase the after tax cost of owning a home, and further tax law changes or government fees could adversely affect demand for the homes we build, increase our costs, or negatively affect our operating results.

Under previous tax law, certain significant expenses of owning a home, including mortgage loan interest costs and real estate taxes, generally are deductible expenses for the purpose of calculating an individual’s federal, and in some cases state, tax liability. However, the Tax Cuts and Jobs Act (the "Tax Act") signed into law on December 22, 2017 may limit these deductions for some individuals starting in 2018. The Tax Act caps individual state and local tax deductions at $10,000 for the aggregate of state and local real property and income taxes or state and local sales taxes. Additionally, the Tax Act reduces the cap on mortgage interest deduction to $750,000 of debt for debt incurred after December 15, 2017 while retaining the $1 million debt cap for debt incurred prior to December 15, 2017. The limits on deductibility of mortgage interest and property taxes may increase the after-tax cost of owning a home for some individuals.

Any increases in personal income tax rates and/or additional tax deduction limits could adversely impact demand for new homes, including homes we build, which could adversely affect our results of operations. Furthermore, increases in real estate taxes and other local government fees, such as fees imposed on developers to fund schools, open space, and road improvements, and/or provide low- and moderate-income housing, could increase our costs and have an adverse effect on our operations. In addition, increases in local real estate taxes as well as the limitation on deductibility of such costs could adversely affect our potential home buyers, who may consider those costs in determining whether to make a new home purchase and decide, as a result, not to purchase one of our homes.

We believe that our recorded tax balances are adequate; however it is not possible to predict the effects of possible changes in the tax laws or changes in their interpretation (including the interpretation of laws included in the newly enacted Tax Act), and whether they could adversely impact our operating results.

New and existing laws and regulations, including environmental laws and regulations, or other governmental actions may increase our expenses, limit the number of homes that we can build or delay the completion of our projects.

We are subject to numerous local, state, federal and other statutes, ordinances, rules and regulations concerning zoning, development, building design, construction and similar matters which impose restrictive zoning and density requirements, which can limit the number of homes that can be built within the boundaries of a particular area. Projects that are not entitled may be subjected to periodic delays, changes in use, less intensive development or elimination of development in certain specific areas due to government regulations. We may also be subject to periodic delays or may be precluded entirely from developing in certain communities due to building moratoriums or "slow-growth" or "no-growth" initiatives that could be implemented in the future. Local governments also have broad discretion regarding the imposition of development fees, assessments and exactions for projects in their jurisdiction. Projects for which we have received land use and development entitlements or approvals may still require a variety of other governmental approvals and permits during the development process and can also be impacted adversely by unforeseen health, safety and welfare issues, which can further delay these projects or prevent their development. As a result, home sales could decline and costs could increase, which could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

We are also subject to a significant number and variety of local, state and federal laws and regulations concerning protection of health, safety, labor standards and the environment. The particular environmental laws which apply to any given property vary according to multiple factors, including the property’s location, its environmental conditions and geographic attributes, the present and former uses of the property, the presence or absence of endangered plants or animals or sensitive habitats, as well as conditions at nearby properties. Environmental laws and conditions may result in delays, may cause us to incur substantial compliance and other costs and can prohibit or severely restrict development and homebuilding activity in environmentally sensitive regions or areas. For example, under certain environmental laws and regulations, third parties, such as environmental groups or neighborhood associations, may challenge the permits and other approvals required for our projects and operations. Any such claims may adversely affect our business, prospects, liquidity, financial condition and results of operations. Insurance coverage for such claims may be limited or non-existent.

In addition, in those cases where an endangered or threatened species is involved and agency rulemaking and litigation are ongoing, the outcome of such rulemaking and litigation can be unpredictable, and at any time can result in unplanned or unforeseeable restrictions on or even the prohibition of development in identified environmentally sensitive areas. From time to time, the EPA and similar federal, state or local agencies review land developers' and homebuilders' compliance with environmental laws and may levy fines and penalties for failure to strictly comply with applicable environmental laws, including those applicable to control or storm water discharges during construction, or impose additional requirements for future compliance as a result of past failures. Any such actions taken with respect to us may increase our costs and result in project delays. We expect that increasingly stringent requirements will be imposed on land developers and homebuilders in the future. Environmental regulations can also have an adverse impact on the availability and price of certain raw materials such as lumber, and on other building materials.

California is especially susceptible to restrictive government regulations and environmental laws. For example, California imposes notification obligations respecting environmental conditions, sometimes recorded on deeds, and also those required to be delivered to persons accessing property or to home buyers or renters, which may cause some persons, or their financing sources, to view the subject parcels as less valuable or as impaired.

Under various environmental laws, current or former owners of real estate, as well as certain other categories of parties, may be required to investigate and clean up hazardous or toxic substances or petroleum product releases, and may be held liable to a governmental entity or to third parties for related damages, including for bodily injury, and for investigation and clean-up costs incurred by such parties in connection with the contamination.

Legislation relating to energy and climate change could increase our costs to construct homes.

There is a variety of new legislation being enacted, or considered for enactment at the federal, state and local level relating to energy, emissions and climate change. This legislation relates to items such as carbon dioxide emissions control and building codes that impose energy efficiency standards. New building code requirements that impose stricter energy efficiency standards could significantly increase our cost to construct homes. As climate change concerns continue to grow, legislation and regulations of this nature are expected to continue and become more costly to comply with. Similarly, energy-related initiatives affect a wide variety of companies throughout the United States and the world and because our operations are heavily dependent on significant amounts of raw materials, such as lumber, steel, and concrete, they could have an indirect adverse impact on our operations and profitability to the extent the manufacturers and suppliers of our materials are burdened with expensive cap and trade and similar energy-related regulations.

Risks Related to Financing and Indebtedness

Difficulty in obtaining sufficient capital could prevent us from acquiring land for our developments or increase costs and delays in the completion of our development projects.

The homebuilding and land development industry is capital-intensive and requires significant up-front expenditures to acquire land parcels and complete development. We cannot assure you that we will maintain cash reserves and generate sufficient cash flow from operations in an amount to enable us to service our debt or to fund other liquidity needs. Additionally, while we have issued $325 million in aggregate principal amount of 7.25% Senior Notes due 2022 and debt commitments of
$200 million under our revolving credit facility, our ability and capacity to borrow under the credit facility is limited by our asset based borrowing base and our ability to meet the covenants of the facility. In addition, our senior notes contain certain restrictions on our business, including the incurrence of additional debt under certain circumstances. If our senior notes, credit facility and internally generated funds are insufficient to cover our liquidity needs, we may seek additional capital in the form of equity or debt financing from a variety of potential sources, including additional bank financings, formation of joint venture relationships or securities offerings. The availability of borrowed funds, especially for land acquisition and construction financing, may be greatly reduced nationally, and the lending community may require increased amounts of equity to be invested in a project by borrowers in connection with both new loans and the extension of existing loans. If we are required to seek additional financing to fund our operations, continued volatility in these markets may restrict our flexibility to access such financing. If we are not successful in obtaining sufficient capital to fund our planned capital and other expenditures, we may be unable to acquire land for our housing developments or to develop the land and construct homes. Additionally, if we cannot obtain additional financing to fund the purchase of land under our option contracts or purchase contracts, we may incur contractual

penalties and fees. Any difficulty in obtaining sufficient capital for planned development expenditures could also cause project delays, which could increase our costs. Furthermore, if additional funds are raised through the issuance of stock, dilution to stockholders could result. If additional funds are raised through the incurrence of debt, we will incur increased debt servicing costs and may become subject to additional restrictive financial and other covenants. We can give no assurance as to the terms or availability of additional capital. If we are not successful in obtaining or refinancing capital when needed, it could adversely impact our ability to operate our business effectively, which could reduce our sales and earnings, and adversely impact our financial position.

Our level of indebtedness may adversely affect our financial position and prevent us from fulfilling our debt obligations, and we may incur additional debt in the future.

The homebuilding industry is capital-intensive and requires significant up-front expenditures to secure land and pursue development and construction on such land. Accordingly, we incur substantial indebtedness to finance our homebuilding activities. As discussed elsewhere in this filing, including "Management's Discussion and Analysis of Financial Condition and Result of Operations - Liquidity and Capital Resources," the Company has outstanding $325 million in aggregate principal amount of 7.25% Senior Notes due 2022 (the "Notes"). As of December 31, 2017, we had approximately $318.7 million in aggregate principle amount of debt outstanding, net of the unamortized discount of $2.2 million, unamortized premium of $1.8 million and $5.9 million of debt issuance costs. In addition, we have $200 million in debt commitments under our revolving credit facility, of which no indebtedness is outstanding or utilized to provide letters of credit at December 31, 2017 and $200 million is available for borrowing, subject to satisfaction of the financial covenants and borrowing base requirements in our revolving credit facility. Moreover, the terms of the indenture governing the Notes and our revolving credit facility permit us to incur additional debt, in each case, subject to certain restrictions.

Incurring substantial debt subjects us to many risks that, if realized, would adversely affect us, including the risk that:

- our ability to obtain additional financing as needed for working capital, land acquisition costs, building costs, other capital expenditures, or general corporate purposes, or to refinance existing indebtedness before its scheduled maturity, may be limited;
- our debt may increase our vulnerability to adverse economic and industry conditions with no assurance that investment yields will increase with higher financing costs;
- we would be required to dedicate a portion of our cash flow from operations to payments on our debt, thereby reducing funds available for other purposes such as land and lot acquisition, development and construction activities;
- our cash flow from operations may be insufficient to make required payments of principal of and interest on the debt, which would likely result in acceleration of the maturity of such debt;
- we may be put at a competitive disadvantage and reduce our flexibility in planning for, or responding to, changing conditions in our industry, including increased competition; and
- the terms of any refinancing may not be as favorable as the terms of the debt being refinanced.

Our ability to meet our expenses depends, to a large extent, on our future performance, which will be affected by financial, business, economic and other factors. We will not be able to control many of these factors, such as economic conditions in the markets where we operate and pressure from competitors. If we do not have sufficient funds, we may be required to refinance all or part of our existing debt, sell assets or borrow additional funds. We cannot guarantee that we will be able to do so on terms acceptable to us, if at all. If we are unable to refinance our debt on acceptable terms, we may be forced to dispose of our assets on disadvantageous terms, potentially resulting in losses. To the extent we cannot meet any future debt service obligations, we may lose some or all of our assets or property that may be pledged to secure our obligations to foreclosure. Also, debt agreements may contain specific cross-default provisions with respect to specified other indebtedness, giving the lenders the right to declare a default if we are in default under other loans in some circumstances. Defaults under our debt agreements could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

We currently have significant amounts invested in unconsolidated joint ventures with third parties - some of which are affiliated with certain of our board members - in which we have less than a controlling interest. These investments are highly illiquid and have significant risks due to, in part, a lack of sole decision-making authority and reliance on the financial condition and liquidity of our joint venture partners.

We own interests in various joint ventures and as of December 31, 2017, our investments in and advances to our unconsolidated joint ventures was $55.8 million. We have entered into joint ventures in order to acquire land positions, to manage our risk profile and to leverage our capital base. We may enter into additional joint ventures in the future. Such joint venture investments involve risks not otherwise present in wholly owned projects, including the following:

- Control and Partner Dispute Risk. We do not have exclusive control over the development, financing, management and other aspects of the project or joint venture, which may prevent us from taking actions that are in our best interest but opposed by our partners. We cannot exercise sole decision-making authority regarding the project or joint venture, which could create the potential risk of creating impasses on decisions, such as acquisitions or sales. Disputes between us and our partners may result in litigation or arbitration that would increase our expenses and prevent our officers and directors from focusing their time and efforts on our business and could result in subjecting the projects owned by the

22

joint venture to additional risk. Our existing joint venture agreements contain, and any future joint venture agreements may contain, buy-sell provisions pursuant to which one partner may initiate procedures requiring the other partner to choose between buying the other partner’s interest or selling its interest to that partner; we may not have the capital to purchase our joint venture parties’ interest under these circumstances even if we believe it would be beneficial to do so.

- Covenant Compliance Risk. Our revolving credit facility prohibits us from making investments in and advances to joint ventures when we are unable to meet certain financial covenants. In addition, the Indenture governing the Notes limits our ability to make investments in joint ventures or give guarantees of joint venture indebtedness when our aggregate investments in joint ventures exceeds 15% of our consolidated tangible assets (before the operation of general baskets and other exceptions). If we become unable to fund our joint venture obligations this could result in, among other things, our default under our joint venture operating agreements, loan agreements, and credit enhancements. And, our failure to satisfy our joint venture obligations could also affect our joint venture's ability to carry out its operations or strategy which could impair the value of our investment in the joint venture.
- Development Risk. Typically, we serve as the administrative member, managing member, or general partner of our joint ventures and one of our subsidiaries acts as the general contractor while our joint venture partner serves as the capital provider. Due to our respective role in these joint ventures, we may become liable for obligations beyond our proportionate equity share. In addition, the projects we build through joint ventures are often larger and have a longer time horizon than the typical project developed by our wholly owned homebuilding operations. Time delays associated with obtaining entitlements, unforeseen development issues, unanticipated labor and material cost increases, higher carrying costs, and general market deterioration and other changes are more likely to impact larger, long-term projects, all of which may negatively impact the profitability and capital needs of these ventures and our proportionate share of income and capital.
- Financing Risk. There are generally a limited number of sources willing to provide acquisition, development and construction financing to land development and homebuilding joint ventures. During difficult market conditions, it may be difficult or impossible to obtain financing for our joint ventures on commercially reasonable terms, or to refinance existing joint venture borrowings as such borrowings mature. In addition, a partner may fail to fund its share of required capital contributions or may become bankrupt, which may cause us and any other remaining partners to fulfill the obligations of the venture in order to preserve our interests and retain any benefits from the joint venture. As a result, we could be required, or elect, to contribute our corporate funds to the joint venture to finance acquisition and development and/or construction costs following termination or step-down of joint venture financing that the joint venture is unable to restructure, extend, or refinance with another third party lender. In addition, our ability to contribute our funds to or for the joint venture may be limited if we do not meet the credit facility conditions discussed above. In addition, we sometimes finance projects in our unconsolidated joint ventures with debt that is secured by the underlying real property. Secured indebtedness increases the risk of the joint venture’s loss of ownership of the property (which would, in turn, impair the value of our ownership interests in the joint venture). See Item 7, "Management’s Discussion and Analysis of Financial Condition and Results of Operations-Liquidity and Capital Resources-Off-Balance Sheet Arrangements and Contractual Obligations"
- Contribution Risk. Under credit enhancements that we typically provide with respect to joint venture borrowings, we and our partners could be required to make additional unanticipated investments in and advances to these joint ventures, either in the form of capital contributions or loan repayments, to reduce such outstanding borrowings. We may have to make additional contributions that exceed our proportional share of capital if our partners fail to contribute any or all of their share. While in most instances we would be able to exercise remedies available under the applicable joint venture documentation if a partner fails to contribute its proportional share of capital, our partner's financial condition may preclude any meaningful cash recovery on the obligation. See Item 7, "Management’s Discussion and Analysis of Financial Condition and Results of Operations-Liquidity and Capital Resources-Off-Balance Sheet Arrangements and Contractual Obligations" and Note 11 to the Consolidated Financial Statements for more information on LTV maintenance agreements and completion guaranties.
- Completion Risk. We often sign a completion agreement in connection with obtaining financing for our joint ventures. Under such agreements, we may be compelled to complete a project, usually with costs within the budget related to the project being funded by the lender with any budget shortfalls being borne by us, even if we no longer

have an economic interest in the joint venture or the joint venture no longer has an interest in the property.

- Illiquid Investment Risk. We lack a controlling interest in our joint ventures and therefore are generally unable to compel our joint ventures to sell assets, return invested capital, require additional capital contributions or take any other action without the vote of at least one or more of our venture partners. This means that, absent partner agreement, we may not be able to liquidate our joint venture investments to generate cash.
- Consolidation Risk. The accounting rules for joint ventures are complex and the decision as to whether it is proper to consolidate a joint venture onto our balance sheet is fact intensive. If the facts concerning an unconsolidated joint

venture were to change and a triggering event under applicable accounting rules were to occur, we might be required to consolidate previously unconsolidated joint ventures onto our balance sheet which could adversely impact our leverage and other financial conditions or covenants.
Any of the above might subject a project to liabilities in excess of those contemplated and adversely affect the value of our current and future joint venture investments.

Our current financing arrangements contain, and our future financing arrangements likely will contain, restrictive covenants relating to our operations.

Our current financing arrangements, including the Indenture governing the Notes, contain covenants (financial and otherwise) affecting our ability to incur additional debt, make certain investments, reduce liquidity below certain levels, make distributions to our stockholders, and otherwise affect our operating policies. These restrictions limit our ability to, among other things:

- incur or guarantee additional indebtedness or issue certain equity interests;
- pay dividends or distributions, repurchase equity or prepay subordinated debt;
- make certain investments;
- sell assets;
- incur liens;
- create certain restrictions on the ability of restricted subsidiaries to transfer assets;
- enter into transactions with affiliates;
- create unrestricted subsidiaries; and
- consolidate, merge or sell all or substantially all of our assets.

In addition, our revolving credit facility provides that our maximum leverage ratio must be less than 65%, which, as defined in our credit agreement, is calculated on a net debt basis after a minimum liquidity threshold. Our leverage ratio as of December 31, 2017, as calculated under our revolving credit facility, was approximately 44%. Our credit facility also contains financial covenants related to our tangible net worth (subject to adjustment if joint ventures exceed 35% of our tangible net worth), liquidity, and interest coverage. Tables measuring our compliance with the financial conditions and covenants under the Notes and credit facility are set forth in "Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources - Senior Unsecured Revolving Credit Facility" included elsewhere in this Report on Form 10-K and incorporated herein by reference. Failure to have sufficient borrowing base availability in the future or to be in compliance with our financial covenants under our revolving credit facility could have a material adverse effect on our operations and financial condition.
A breach of the covenants under the Indenture or any of the other agreements governing our indebtedness could result in an event of default under the Indenture or other such agreements.
A default under the Indenture governing the Notes or our revolving credit facility or other agreements governing our indebtedness may allow our creditors to accelerate the related debt and may result in the acceleration of any other debt to which a cross-acceleration or cross-default provision applies. In addition, an event of default under the credit agreement governing our revolving credit facility would permit the lenders thereunder to terminate all commitments to extend further credit under our revolving credit facility. Furthermore, if we were unable to repay the amounts due and payable under any future secured credit facilities, those lenders could proceed against the collateral granted to them to secure that indebtedness. In the event our lenders or the holders of our Notes accelerate the repayment of our borrowings, we cannot assure you that we and our subsidiaries would have sufficient assets to repay such indebtedness. As a result of these restrictions, we may be:
- limited in how we conduct our business;
- unable to raise additional debt or equity financing to operate during general economic or business downturns; or
-

unable to compete effectively or to take advantage of new business opportunities. These restrictions may affect our ability to grow in accordance with our plans.

Potential future downgrades of our credit ratings could adversely affect our access to capital and could otherwise have a material adverse effect on us.

Rating agencies may elect in the future to downgrade our corporate credit rating or any rating of the Notes due to deterioration in our homebuilding operations, credit metrics or other earnings-based metrics, as well as our leverage or a significant decrease in our tangible net worth. These ratings and our current credit condition affect, among other things, our ability to access new capital, especially debt, and negative changes in these ratings may result in more stringent covenants and higher interest rates under the terms of any new debt. Our credit ratings could be downgraded or rating agencies could issue adverse commentaries in the future, which could have a material adverse effect on our stock price, business, results of operations, financial condition and liquidity. In particular, a weakening of our financial condition, including a significant increase in our leverage or decrease in our profitability or cash flows, could adversely affect our ability to obtain necessary funds, result in a credit rating downgrade or change in outlook, or otherwise increase our cost of borrowing.

Interest expense on debt we incur may limit our cash available to fund our growth strategies.

As of December 31, 2017, we had approximately $318.7 million in aggregate principal amount of debt outstanding, net of the unamortized discount of $2.2 million, unamortized premium of $1.8 million and $5.9 million of debt issuance costs. In addition, we have $200 million in debt commitments under our revolving credit facility, of which no indebtedness is outstanding or utilized to provide letters of credit at December 31, 2017 and $200 million is available for borrowing, subject to satisfaction of the financial covenants and borrowing base requirements in our senior unsecured revolving credit facility. As part of our financing strategy, we may incur a significant amount of additional debt. Our revolving credit facility has, and any additional debt we subsequently incur may have, a floating rate of interest. Our Notes have a fixed rate of interest. We may incur fixed rate debt in the future that may be at a higher interest rate than our floating rate debt. Higher interest rates could increase debt service requirements on our current floating rate debt and on any floating or fixed rate debt we subsequently incur, and could reduce funds available for operations, future business opportunities or other purposes. If we need to repay existing debt during periods of rising interest rates, we could be required to refinance our then-existing debt on unfavorable terms or liquidate one or more of our assets to repay such debt at times that may not permit realization of a favorable return on such assets and could result in a loss or lower profitability. The occurrence of either such event or both could materially and adversely affect our business, prospects, liquidity, financial condition and results of operations.

We may be unable to repurchase the Notes upon a change of control as required by the Indenture.

Upon the occurrence of certain specific kinds of change of control events, we must offer to repurchase the Notes at 101% of their principal amount, plus accrued and unpaid interest thereon. In such circumstances, we cannot assure you that we would have sufficient funds available to repay all of our indebtedness that would become payable upon a change of control and to repurchase all of the Notes. Our failure to purchase the Notes would be a default under the Indenture and would trigger a cross default of the revolving credit facility.

Risks Related to Our Organization and Structure

We are and will continue to be dependent on key personnel and certain members of our management team.

Our success depends to a significant degree upon the contributions of certain key personnel including, but not limited to, our Chief Executive Officer, Chief Operating Officer, Chief Financial Officer and Chief Investment Officer each of whom would be difficult to replace. Although we have entered into employment agreements with our executive officers, there is no guarantee that these executives will remain employed with us. If any of our key personnel were to cease employment with us, our operating results could suffer. Our ability to retain our key personnel or to attract suitable replacements should any members of our management team leave depends on the competitive nature of the employment market. The loss of services from key personnel or a limitation in their availability could materially and adversely impact our business, prospects, liquidity, financial condition and results of operations. Further, such a loss could be negatively perceived in the capital markets. We have not obtained key person life insurance that would provide us with proceeds in the event of death or disability of any of our key personnel.

Our charter and bylaws could prevent a third party from acquiring us or limit the price that investors might be willing to pay for shares of our common stock.

Provisions of the Delaware General Corporation Law, our certificate of incorporation and our bylaws could have the effect of making it more difficult for a third party to acquire, or of discouraging a third party from attempting to acquire, control of us. These provisions could delay or prevent a change in control of and could limit the price that investors might be willing to pay in the future for shares of our common stock.

25

Our Board of Directors is divided into three classes, with the term of one class expiring each year, which could delay a change in our control. Our certificate of incorporation also authorizes our Board of Directors to issue new series of common stock and preferred stock without stockholder approval. Depending on the rights and terms of any new series created, and the reaction of the market to the series, rights of existing stockholders could be negatively affected. For example, subject to applicable law, our Board of Directors could create a series of common stock or preferred stock with preferential rights to dividends or assets upon liquidation, or with superior voting rights to our existing common stock. The ability of our Board of Directors to issue these new series of common stock and preferred stock could also prevent or delay a third party from acquiring us, even if doing so would be beneficial to our stockholders.

We are also subject to the anti-takeover provisions of Section 203 of the Delaware General Corporation Law, which prohibits Delaware corporations from engaging in business combinations specified in the statute with an interested stockholder, as defined in the statute, for a period of three years after the date of the transaction in which the person first becomes an interested stockholder, unless the business combination is approved in advance by a majority of the independent directors or by the holders of at least two-thirds of the outstanding disinterested shares. The application of Section 203 of the Delaware General Corporation Law could also have the effect of delaying or preventing a change of control of us.

The obligations associated with being a public company require significant resources and management attention. Section 404 of the Sarbanes-Oxley Act of 2002, or the Sarbanes Oxley Act, requires annual management assessments of the effectiveness of our internal control over financial reporting and generally requires in the same report a report by our independent registered public accounting firm on the effectiveness of our internal control over financial reporting. However, under the recently enacted JOBS Act, our independent registered public accounting firm will not be required to attest to the effectiveness of our internal control over financial reporting pursuant to Section 404 of the Sarbanes-Oxley Act until we are no longer an "emerging growth company." We could be an "emerging growth company" until the end of our 2019 fiscal year. The rules governing the standards that must be met for our management to assess our internal control over financial reporting are complex and require significant documentation, testing and possible remediation.

We may encounter problems or delays in completing the implementation of any necessary improvements and receiving an unqualified opinion on the effectiveness of the internal controls over financial reporting in connection with the attestation provided by our independent registered public accounting firm. If we cannot favorably assess the effectiveness of our internal control over financial reporting, or if our independent registered public accounting firm is unable to provide an unqualified attestation report on our internal controls, investors could lose confidence in our financial information and the price of our common stock could decline.

As we transition from our status as "an emerging growth company," we may need to upgrade our systems or create new systems, implement additional financial and management controls, reporting systems and procedures, create or outsource an internal audit function, and hire additional accounting and finance staff. If we are unable to accomplish these objectives in a timely and effective fashion, our ability to comply with the financial reporting requirements and other rules that apply to reporting companies could be impaired. Any failure to maintain effective internal control over financial reporting could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

We are an "emerging growth company", and, as a result of the reduced disclosure and governance requirements applicable to emerging growth companies, our common stock may be less attractive to investors.

We are an "emerging growth company," as defined in the JOBS Act, and we are eligible to take advantage of certain exemptions from various reporting requirements applicable to other public companies but not to emerging growth companies, including, but not limited to, an exemption from the auditor attestation requirement of Section 404 of the Sarbanes-Oxley Act, reduced disclosure about executive compensation arrangements pursuant to the rules applicable to smaller reporting companies and no requirement to seek non-binding advisory votes on executive compensation. We have elected to adopt these reduced disclosure requirements. We could be an emerging growth company until the last day of the fiscal year following the fifth anniversary of the completion of our initial public offering, although a variety of circumstances could cause us to lose that status earlier. We cannot predict whether investors will find our common stock less attractive as a result of our taking advantage of these exemptions. If some investors find our common stock less attractive as a result of our choices, there may be a less active trading market for our common stock and our stock price may be more volatile.

Risks Related to Ownership of Our Common Stock

The price of our Common Stock is subject to volatility and our trading volume is relatively low.

The market price of our common stock may be highly volatile and subject to wide fluctuations. Compared to other public homebuilders, we believe we have relatively low trading volume. Because of this limited trading volume, purchases and sales of large numbers of our shares may cause rapid price swings in our stock. In addition, our financial performance, government regulatory action, tax laws, additions or departures of key personnel, interest rates and market conditions in general could have a significant impact on the future market price of our common stock.

If securities or industry analysts do not publish, or cease publishing, research or reports about us, our business or our market, or if they change their recommendations regarding our common stock adversely, our stock price and trading volume could decline.

The trading market for our common stock is influenced by whether industry or securities analysts publish research and reports about us, our business, our market or our competitors and, if any analysts do publish such reports, what they publish in those reports. Any analysts who do cover us may make adverse recommendations regarding our common stock, adversely change their recommendations from time to time or provide more favorable relative recommendations about our competitors. If any analyst who cover us now or may cover us in the future were to cease coverage of our company or fail to regularly publish reports on us, we could lose visibility in the financial markets, which in turn could cause our stock price or trading volume to decline.

We do not intend to pay dividends on our common stock for the foreseeable future.

We currently intend to retain our future earnings to finance the development and expansion of our business and, therefore, do not intend to pay cash dividends on our common stock for the foreseeable future. Any future determination to pay dividends will be at the discretion of our board of directors and will depend on our financial condition, results of operations, capital requirements, restrictions contained in any financing instruments, applicable legal requirements and such other factors as our board of directors deems relevant. Accordingly, stockholders may need to sell their shares of our common stock to realize a return on investment, and may not be able to sell shares at or above the price paid for them.

Certain stockholders have rights to cause our Company to undertake securities offerings. Future sales of our common stock or other securities convertible into our common stock could cause the market value of our common stock to decline and could result in dilution of your shares.

Our board of directors is authorized, without stockholder approval, to cause us to issue additional shares of our common stock or to raise capital through the issuance of preferred stock, securities (including debt securities) convertible into common stock, options, warrants and other rights, on terms and for consideration as our board of directors in its sole discretion may determine. In addition, we entered into a registration rights agreement with the individual founders and certain of our institutional shareholders, IHP Capital Partners VI, LLC, TCN/TNHC LP, and Watt/TNHC LLC (the "Institutional Investors") at the time our Company consummated its initial public offering. If these holders, or any shareholders, sell substantial amounts of their shares, the price of our common stock could decline significantly. In addition, the sale of these shares could impair our ability to raise capital through the sale of additional equity securities. We cannot predict the effect, if any, of future sales of our common stock, or other securities on the value of our common stock. Sales of substantial amounts of our common stock by a large stockholder or otherwise, or the perception that such sales could occur, may adversely affect the market price of our common stock.

Our Notes and Future offerings of debt securities, which rank senior to our common stock upon our bankruptcy or liquidation, and future offerings of equity securities that may be senior to our common stock for the purposes of dividend and liquidating distributions, may adversely affect the market price of our common stock.

We have issued $325 million in aggregate principal amount of Notes. In the future, we may attempt to increase our capital resources by conducting offerings of debt securities or additional offerings of equity securities. Upon bankruptcy or liquidation, holders of our debt securities, including the Senior Notes, and shares of preferred stock and lenders with respect to other borrowings will receive a distribution of our available assets prior to the holders of our common stock. Additional equity offerings may dilute the holdings of our existing stockholders or reduce the market price of our common stock, or both. Our preferred stock, if issued, could have a preference on liquidating distributions or a preference on dividend payments or both that could limit our ability to make a dividend distribution to the holders of our common stock. Our decision to issue securities in any future offering will depend on market conditions and other factors beyond our control. As a result, we cannot predict or estimate the amount, timing or nature of our future offerings, and purchasers of our common stock bear the risk of our future offerings reducing the market price of our common stock and diluting their ownership interest in our company.

Certain large stockholders own a significant percentage of our shares and exert significant influence over us. Their interests may not coincide with ours and may have conflicts of interests with us in the future.

The Institutional Investors, H. Lawrence Webb, Wayne Stelmar, Tom Redwitz and Joseph Davis beneficially own (as such term is defined in Section 13(d)(3) of the Exchange Act), directly or indirectly through their affiliates, approximately 37% of our common stock. Such holders are also party to an investor rights agreement, pursuant to which each such holder agreed to vote, for each of the Institutional Investors, in favor of one individual for nomination and election to the Board chosen by such Institutional Investor for so long as such Institutional Investor owns 4% or more of our then-outstanding stock. Each Institutional Investor has also agreed to vote its shares of common stock in favor of Messrs. Webb, Stelmar or Berchtold (or, if at that time nominated as a director, Messrs. Davis or Redwitz) in any election in which any such individual is a nominee. In addition to the influence such holders have due to their voting arrangement, to the extent they and their affiliates vote their shares together on any matter, their combined stock ownership may effectively give them the power to influence matters reserved for our shareholders, including the election of members of our board of directors and significant corporate or change of control transactions.

Circumstances may occur in which the interest of these shareholders could be in conflict with your interests or our interests. In addition, such persons may have an interest in pursuing transactions that, in their judgment, enhance the value of their equity investment in us, even though such transactions may involve risks to you. For example, our Institutional Investors are also in the real estate and land development business. Such Institutional Investors and their affiliates may have an interest in directly or indirectly pursuing acquisitions, divestitures, financings or other transactions that, in their judgment, could enhance their other equity investments, even though such transactions might involve risks to us. We have entered into various business relationships with some of our Institutional Investors, including real estate development or homebuilding joint ventures. While our audit committee, and in some cases all of our independent or disinterested board members, have reviewed and approved all such transactions, we do not have exclusive control over such joint ventures, which may prevent us from taking actions that are in our best interest but opposed by our partners. If the projects within such joint ventures do not perform well, it is possible that disputes between us and our partners may result in litigation or arbitration which would be further complicated due to the conflict of interest. Any such dispute would increase our expenses and prevent our officers and directors from focusing their time and efforts on our business and could have a material and adverse effect on our business. See the Risk Factor entitled "We currently have significant amounts invested in unconsolidated joint ventures with independent third parties in which we have less than a controlling interest. These investments are highly illiquid and have significant risks due to, in part, a lack of sole decision-making authority and reliance on the financial condition and liquidity of our joint venture partners" for a description of additional risks arising from our investments in joint ventures. Institutional Investors and their affiliates are involved in business that provides equity capital for residential housing, land and development, including for businesses that directly or indirectly compete with our business. In their capacities as principals or executives of those businesses, they may also pursue opportunities that may be complementary to our business, and, as a result, those opportunities may not be available to us.

## Item 1B. Unresolved Staff Comments

Not Applicable.

## Item 2. Properties

We lease our corporate headquarters in Aliso Viejo, California. The lease on this facility consists of approximately 18,700 square feet and expires in November 2020. In addition, we lease divisional offices in Northern California, Southern California and Arizona, including approximately 6,800 square feet through May 2020 in Roseville (of which approximately 5,800 square feet is sublet), approximately 7,700 square feet through September 2021 in Walnut Creek, approximately 1,400 square feet through July 2018 in Agoura Hills and approximately 2,000 square feet through February 2021 in Scottsdale. For information on land owned and controlled by us and our joint ventures for use in our homebuilding activities, please refer to Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Results of Operations - Lots Owned and Controlled", "- Equity in Net Income of Unconsolidated Joint Ventures" and "- Off-Balance Sheet Arrangements and Contractual Obligations - Joint Ventures".

## Item 3. Legal Proceedings

We are involved in various claims and litigation arising in the ordinary course of business. We do not believe that any such claims and litigation will have a material adverse effect upon our results of operations or financial position.

## Item 4. Mine Safety Disclosures

Not Applicable.

PART II

Item 5. Market For Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Our common stock is listed on the New York Stock Exchange under the ticker symbol "NWHM" and began trading on January 31, 2014. The following table sets forth the high and low intra-day sales prices per share of our common stock for the periods indicated, as reported by the NYSE.

| | High | Low |
|---|---|---|
| Fiscal Year 2017 | | |
| First Quarter | $11.93 | $10.07 |
| Second Quarter | $12.23 | $10.24 |
| Third Quarter | $11.96 | $9.75 |
| Fourth Quarter | $13.20 | $10.27 |
| Fiscal Year 2016 | | |
| First Quarter | $12.78 | $7.51 |
| Second Quarter | $12.79 | $8.62 |
| Third Quarter | $11.28 | $8.85 |
| Fourth Quarter | $12.55 | $9.45 |

The following performance graph shows a comparison of the cumulative total returns to stockholders of the Company’s common stock from January 31, 2014 (the date of our initial public offering, using the price of which our shares of common stock were initially sold to the public) to December 31, 2017, as compared with the Standard & Poor’s 500 Composite Stock Index and the Dow Jones Industry Group-U.S. Home Construction Index. The comparison assumes $100 was invested in our common stock on January 31, 2014 and in each of the foregoing indices on January 31, 2014 and assumes the reinvestment of dividends.

The performance graph and related information shall not be deemed to be "soliciting material" or to be "filed" with the Securities and Exchange Commission, nor shall such information be incorporated by reference into any filing under the Securities Act of 1933 or Securities Exchange Act of 1934, each as amended, except to the extent that we specifically incorporate it by reference.

The above graph is based upon common stock and index prices calculated as of the end of each period. The stock price performance of the Company's common stock depicted in the graph above represents past performance only and is not necessarily indicative of future performance.

As of February 12, 2018, we had 12 holders of record of our common stock. The number of holders of record is based upon the actual numbers of holders registered at such date and does not include holders of shares in "street name" or persons, partnerships, associates, corporations or other entities in security position listings maintained by depositories.

Dividends

We currently intend to retain our future earnings to finance the development and expansion of our business and, therefore, do not intend to pay cash dividends on our common stock for the foreseeable future. Any future determination to pay dividends will be at the discretion of our board of directors and will depend on our financial condition, results of operations, capital requirements, compliance with Delaware law, restrictions contained in any financing instruments, including but not limited to, our unsecured credit facility and senior notes indenture, and such other factors as our board of directors deem relevant.

Issuer Share Repurchases

We had no share repurchases during the year ended December 31, 2017.

Recent Sales of Unregistered Securities

We did not sell any unregistered securities during the year ended December 31, 2017.

Item 6. Selected Financial Data

The following sets forth our selected financial data and other operating data on a historical basis. You should read the following selected financial data in conjunction with our consolidated financial statements and the related notes, "Risk Factors" and with "Management's Discussion and Analysis of Financial Condition and Results of Operations," which are included elsewhere in this annual report on Form 10-K. The historical results presented below are not necessarily indicative of the results to be expected for any future period.

| | Year Ended December 31, | | | | |
|---|---|---|---|---|---|
| | 2017 | 2016 | 2015 | 2014 | 2013[1] |
| | (Dollars in thousands, except per share amounts) | | | | |
| Income Statement Data | | | | | |
| Home sales revenue | $560,842 | $ 507,949 | $ 280,209 | $ 56,094 | $ 35,663 |
| Fee building revenue, including management fees | 190,324 | 186,507 | 149,890 | 93,563 | 47,565 |
| Land sales revenue | — | — | — | — | — |
| Total revenues | $751,166 | $ 694,456 | $ 430,099 | $ 149,657 | $ 83,228 |
| | | | | | |
| Pretax income: | | | | | |
| Homebuilding | $27,034 | $ 25,546 | $ 23,698 | $ 497 | $ 1,748 |
| Fee building | 5,497 | 8,404 | 10,213 | 4,506 | 5,248 |
| Pretax income | $32,531 | $ 33,950 | $ 33,911 | $ 5,003 | $ 6,996 |
| | | | | | |
| Net income attributable to the Company | $17,152 | $ 21,022 | $ 21,688 | $ 4,787 | $ 6,706 |
| Basic earnings per share | $0.82 | $ 1.02 | $ 1.29 | $ 0.30 | $ 0.85 |
| Diluted earnings per share | $0.82 | $ 1.01 | $ 1.28 | $ 0.30 | $ 0.85 |
| Weighted Average Common Shares Outstanding: [2] | | | | | |
| Basic | 20,849,736 | 20,685,386 | 16,767,513 | 15,927,917 | 7,905,757 |
| Diluted | 20,995,498 | 20,791,445 | 16,941,088 | 15,969,199 | 7,905,757 |
| | | | | | |
| Balance Sheet Data | | | | | |
| Cash and cash equivalents | $123,546 | $ 30,496 | $ 45,874 | $ 44,058 | $ 9,541 |
| Real estate inventories [3] | $416,143 | $ 286,928 | $ 200,636 | $ 157,629 | $ 44,088 |
| Investment in and advances to unconsolidated joint ventures | $55,824 | $ 50,857 | $ 60,572 | $ 60,564 | $ 32,270 |
| Total assets | $644,512 | $ 419,136 | $ 351,270 | $ 291,958 | $ 98,949 |
| Total debt | $318,656 | $ 118,000 | $ 83,082 | $ 113,751 | $ 17,883 |
| Stockholders' equity[4] | $263,990 | $ 244,523 | $ 220,775 | $ 148,084 | $ 64,356 |
| Stockholders' equity per common share outstanding | $12.64 | $ 11.81 | $ 10.75 | $ 9.00 | $ 7.45 |
| Cash dividends declared per share | $— | $ — | $ — | $ — | $ — |
| | | | | | |
| Operating Data (excluding unconsolidated JVs) | | | | | |
| Net new home orders | 412 | 253 | 174 | 79 | 72 |
| New homes delivered | 341 | 250 | 148 | 53 | 82 |
| Average sales price of homes delivered | $1,645 | $ 2,032 | $ 1,893 | $ 1,058 | $ 435 |
| Selling communities at end of year | 17 | 15 | 10 | 4 | 3 |
| Backlog at end of year, number of homes | 153 | 79 | 67 | 41 | 15 |
| Backlog at end of year, dollar value | $162,250 | $ 187,296 | $ 166,567 | $ 86,711 | $ 11,867 |
| Average sales price of homes in backlog | $1,060 | $ 2,371 | $ 2,486 | $ 2,115 | $ 791 |
| | | | | | |
| Operating Data – Fee Building Projects (excluding unconsolidated JVs) | | | | | |
| Homes started | 533 | 784 | 513 | 550 | 215 |
| Homes delivered | 820 | 644 | 537 | 206 | 194 |

| | | | | | |
|---|---|---|---|---|---|
| Homes under construction at end of period | 299 | 586 | 446 | 470 | 126 |

32

(1) The Company completed its initial public offering ("IPO") on January 30, 2014. Data presented for the years prior to 2014 represent our results operating as TNHC LLC, a private company.

(2) The Company completed a follow-on offering on December 9, 2015 issuing and selling 4,025,000 shares of common stock at a price of $12.50 per share.

(3) Effective July 1, 2016, certain capitalizable selling and marketing costs were reclassified to other assets from real estate inventories. Prior year periods have been reclassified to conform to current year presentation. $9.3 million, $5.9 million, and $1.3 million, was reclassified from real estate inventories to other assets for the years ended December 31, 2015, 2014, and 2013, respectively.

(4) For the year ended December 31, 2013 (prior to the Company's IPO), amount represents members' equity in TNHC LLC.

Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations
You should read the following in conjunction with the sections of this annual report on Form 10-K entitled "Risk Factors," "Cautionary Note Concerning Forward-Looking Statements," "Selected Financial Data" and "Business" and our historical financial statements and related notes thereto included elsewhere in this annual report on Form 10-K. This discussion contains forward-looking statements reflecting current expectations that involve risks and uncertainties. Actual results and the timing of events may differ materially from those contained in these forward-looking statements due to a number of factors, including those discussed in the section entitled "Risk Factors" and elsewhere in this annual report on Form 10-K.

Non-GAAP Measures

This annual report on Form 10-K includes certain non-GAAP measures, including homebuilding gross margin before impairments, homebuilding gross margin percentage before impairments, Adjusted EBITDA, Adjusted EBITDA margin percentage, the ratio of Adjusted EBITDA to total interest incurred, net income attributable to the Company before noncash deferred tax asset charge, earnings per share and diluted earnings per share attributable to the Company before noncash deferred tax asset charge, net debt, the ratio of net debt-to-capital, adjusted homebuilding gross margin, adjusted homebuilding gross margin percentage, and the effective tax rate before noncash deferred tax asset charge. For a reconciliation of homebuilding gross margin before impairments, homebuilding gross margin percentage before impairments, Adjusted EBITDA, Adjusted EBITDA margin percentage, and the ratio of Adjusted EBITDA to total interest incurred to the comparable GAAP measures please see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Consolidated Financial Data." For a reconciliation of net income attributable to the Company before noncash deferred tax asset charge, earnings per share and diluted earnings per share attributable to the Company before noncash deferred tax asset charge, and the effective tax rate before noncash deferred tax asset charge to the comparable GAAP measures, please see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Overview." For a reconciliation of adjusted homebuilding gross margin and adjusted homebuilding gross margin percentage to the comparable GAAP measures, please see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Results of Operations - Homebuilding Gross Margin." For a reconciliation of net debt and net debt-to-capital to the comparable GAAP measures, please see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources - Debt-to-Capital Ratios."

Consolidated Financial Data

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2017 | 2016 | 2015 |
| | (Dollars in thousands) | | |
| Revenues: | | | |
| Home sales | $560,842 | $507,949 | $280,209 |
| Fee building, including management fees from unconsolidated joint ventures of $4,945, $8,202 and $12,426, respectively | 190,324 | 186,507 | 149,890 |
| | 751,166 | 694,456 | 430,099 |
| Cost of Sales: | | | |
| Home sales | 473,213 | 433,559 | 235,232 |
| Home sales impairments | 2,200 | 2,350 | — |
| Land sales impairment | — | 1,150 | — |
| Fee building | 184,827 | 178,103 | 139,677 |
| | 660,240 | 615,162 | 374,909 |
| Gross Margin: | | | |
| Home sales | 85,429 | 72,040 | 44,977 |
| Land sales | — | (1,150) | — |
| Fee building | 5,497 | 8,404 | 10,213 |
| | 90,926 | 79,294 | 55,190 |
| | | | |
| Home sales gross margin | 15.2% | 14.2% | 16.1% |
| Home sales gross margin before impairments[1] | 15.6% | 14.6% | 16.1% |
| Fee building gross margin | 2.9% | 4.5% | 6.8% |
| | | | |
| Selling and marketing expenses | (32,702) | (26,744) | (13,741) |
| General and administrative expenses | (26,330) | (25,882) | (20,278) |
| Equity in net income of unconsolidated joint ventures | 866 | 7,691 | 13,767 |
| Other income (expense), net | (229) | (409) | (1,027) |
| Pretax income | 32,531 | 33,950 | 33,911 |
| Provision for income taxes | (15,390) | (13,024) | (12,533) |
| Net income | 17,141 | 20,926 | 21,378 |
| Net loss attributable to noncontrolling interest | 11 | 96 | 310 |
| Net income attributable to The New Home Company Inc. | $17,152 | $21,022 | $21,688 |
| | | | |
| Interest incurred | $21,978 | $7,484 | $4,722 |
| Adjusted EBITDA[2] | $50,145 | $43,144 | $46,209 |
| Adjusted EBITDA margin percentage [2] | 6.7% | 6.2% | 10.7% |
| Ratio of Adjusted EBITDA to total interest incurred [2] | 2.3x | 5.8x | 9.8x |

35

(1) Home sales gross margin before impairments (also referred to as homebuilding gross margin before impairments) is a non-GAAP measure. The table below reconciles this non-GAAP financial measure to homebuilding gross margin, the nearest GAAP equivalent.

| | Year Ended December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2017 | % | 2016 | % | 2015 | % |
| | (Dollars in thousands) | | | | | |
| Home sales revenue | $560,842 | 100.0% | $507,949 | 100.0% | $280,209 | 100.0% |
| Cost of home sales | 475,413 | 84.8 % | 435,909 | 85.8 % | 235,232 | 83.9 % |
| Homebuilding gross margin | 85,429 | 15.2 % | 72,040 | 14.2 % | 44,977 | 16.1 % |
| Add: Home sales impairments | 2,200 | 0.4 % | 2,350 | 0.4 % | — | — % |
| Homebuilding gross margin before impairments | 87,629 | 15.6 % | 74,390 | 14.6 % | 44,977 | 16.1 % |

(2) Adjusted EBITDA, Adjusted EBITDA margin percentage and ratio of Adjusted EBITDA to total interest incurred are non-GAAP measures. Adjusted EBITDA margin percentage is calculated as a percentage of total revenue. Management believes that Adjusted EBITDA, which is a non-GAAP measure, assists investors in understanding and comparing the operating characteristics of homebuilding activities by eliminating many of the differences in companies' respective capitalization, interest costs, tax position and inventory impairments. Due to the significance of the GAAP components excluded, Adjusted EBITDA should not be considered in isolation or as an alternative to net income, cash flows from operations or any other performance measure prescribed by GAAP. The table below reconciles net income, calculated and presented in accordance with GAAP, to Adjusted EBITDA, Adjusted EBITDA margin percentage and ratio of Adjusted EBITDA to total interest incurred.

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2017 | 2016 | 2015 |
| | (Dollars in thousands) | | |
| Net income | $17,141 | $20,926 | $21,378 |
| Add: | | | |
| Interest amortized to cost of sales and other expense | 11,057 | 5,331 | 2,596 |
| Provision for income taxes | 15,390 | 13,024 | 12,533 |
| Depreciation and amortization | 449 | 511 | 473 |
| Amortization of equity-based compensation | 2,803 | 3,471 | 3,884 |
| Cash distributions of income from unconsolidated joint ventures | 1,588 | 3,742 | 18,477 |
| Noncash impairments and abandonments | 2,583 | 4,080 | 635 |
| Less: | | | |
| Gain from notes payable principal reduction | — | (250) | — |
| Equity in income of unconsolidated joint ventures | (866) | (7,691) | (13,767) |
| Adjusted EBITDA | $50,145 | $43,144 | $46,209 |
| Total Revenue | $751,166 | $694,456 | $430,099 |
| Adjusted EBITDA margin percentage | 6.7 % | 6.2 % | 10.7 % |
| Interest incurred | 21,978 | 7,484 | 4,722 |
| Ratio of Adjusted EBITDA to total interest incurred | 2.3x | 5.8x | 9.8x |

Overview

Solid buyer demand continued in California during 2017 as the Company continued to make progress with its strategy to grow its wholly owned business by increasing its wholly owned deliveries by 36%, community count at period end by 13% and net new orders by 63%. Total revenues for 2017 totaled $751.2 million as compared to $694.5 million in 2016, with home sales revenue up 10% to $560.8 million even after a 19% lower average selling price to $1.6 million as compared to $2.0 million a year ago. The decrease in average selling price was the result of expanding our total community count as well as our strategy to broaden our product price points to more affordably-priced product. At the same time our gross margins from home sales improved 100 basis points during 2017 to 15.2%.
Net income attributable to the Company for 2017 was $17.2 million, or $0.82 per diluted share, and included a noncash deferred tax asset charge of $3.2 million (or $0.15 per diluted share) attributable to the revaluation of the Company's deferred tax asset related to the reduction in the federal corporate tax rate in connection with the Tax Cuts and Jobs Act enacted in December 2017. Excluding the noncash deferred tax asset charge, net income for 2017 was $20.3 million*, or $0.97* per diluted share, compared to $21.0 million, or $1.01 per diluted share, for 2016. Net income excluding the noncash deferred tax asset charge is a non-GAAP measure. See the table below reconciling this non-GAAP financial measure to net income. The slight decrease in net income before the adjustment to our deferred tax asset was primarily due to a $6.8 million reduction in joint venture income, a $3.3 million decrease in joint venture management fees and a $2.9 million decline in fee building gross margin, which was largely offset by a 10% increase in the Company's wholly owned home sales revenues and a 100 basis point improvement in homes sales gross margin.
During 2017, the Company executed on its strategic initiative to broaden its product portfolio by including more affordably-priced product to attract a deeper, more diverse customer base. The strategic shift in product offerings included the opening of seven new communities with initial base pricing below $750,000. Overall, the Company ended 2017 with 17 active selling communities compared to 15 at the end of 2016. Net new orders for 2017 were up 63% compared to 2016 due to a 59% higher monthly sales absorption rate driven by healthy buyer demand and lower price points offered in 2017. The increase in orders drove a 94% increase in backlog units at December 31, 2017 as compared to a year ago.
The Company also made significant progress during the year in improving its financial position and liquidity by issuing $325 million of senior unsecured notes due 2022. The Company ended the year with $123.5 million in cash and cash equivalents, no debt outstanding under its $200 million unsecured revolving credit facility, a debt-to-capital ratio of 54.7% and a net debt-to-capital ratio of 42.4%*. The Company also grew the number of lots owned and controlled by its wholly owned operations by 75% to approximately 2,750 lots, including the first acquisition of wholly owned lots in Arizona. Of the wholly owned lots owned and controlled, approximately 66% were controlled through option contracts.

We expect the product transition experienced in 2017 to continue into 2018 with the anticipated opening of six new communities at price points of $750,000 or below. With the continued product mix shift, we expect increased deliveries for 2018 at a lower average selling price. The foundation we have established during 2017 positions us well in our markets and has set us up to deliver solid returns for our shareholders.

* Net income attributable to the Company before noncash deferred tax asset charge, diluted earnings per share attributable to the Company before noncash deferred tax asset charge, and net debt-to-capital ratio are non-GAAP measures. For a reconciliation of net income attributable to the Company before noncash deferred tax asset charge and diluted earnings per share attributable to the Company before noncash deferred tax asset to the comparable GAAP measures, please see the table below. For a reconciliation of the net debt-to-capital ratio to the appropriate GAAP measure, please see "Liquidity and Capital Resources - Debt-to-Capital Ratios." We believe removing the impact of the noncash deferred tax asset charge is relevant to provide investors with an understanding of the impact the charge had to earnings and our effective tax rate and to allow a more direct comparison of earnings to the prior year period. We believe that the ratio of net debt-to-capital is a relevant financial measure for management and investors to understand the leverage employed in our operations and as an indicator of the Company’s ability to obtain financing.

37

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2017 | 2016 | 2015 |
| | (Dollars in thousands, except per share amounts) | | |
| Net income attributable to The New Home Company Inc. | $17,152 | $21,022 | $21,688 |
| Noncash deferred tax asset charge | 3,190 | — | — |
| Net income attributable to The New Home Company before noncash deferred tax asset charge | $20,342 | $21,022 | $21,688 |
| | | | |
| Earnings per share attributable to The New Home Company Inc.: | | | |
| Basic | $0.82 | $1.02 | $1.29 |
| Diluted | $0.82 | $1.01 | $1.28 |
| | | | |
| Earnings per share attributable to The New Home Company Inc. before noncash deferred tax asset charge: | | | |
| Basic | $0.98 | $1.02 | $1.29 |
| Diluted | $0.97 | $1.01 | $1.28 |
| | | | |
| Weighted average shares outstanding: | | | |
| Basic | 20,849,736 | 20,685,386 | 16,767,513 |
| Diluted | 20,995,498 | 20,791,445 | 16,941,088 |
| | | | |
| Effective tax rate for The New Home Company Inc.: | | | |
| Pretax Income | $32,531 | $33,950 | $33,911 |
| Provision for income taxes | $15,390 | $13,024 | $12,533 |
| Effective tax rate[1] | 47.3 % | 38.4 % | 37.0 % |
| | | | |
| Effective tax rate for The New Home Company Inc. before noncash deferred tax asset charge: | | | |
| Provision for income taxes | $15,390 | $13,024 | $12,533 |
| Less: noncash deferred tax asset charge | (3,190) | — | — |
| Provision for income taxes before noncash deferred tax asset charge | $12,200 | $13,024 | $12,533 |
| Effective tax rate for The New Home Company Inc. before noncash deferred tax asset charge[1] | 37.5 % | 38.4 % | 37.0 % |

[1] Effective tax rate is computed by dividing provision for income taxes by pretax income.

## Results of Operations

### Net New Home Orders

| | Year Ended December 31, | | | | | | |
|---|---|---|---|---|---|---|---|
| | | Change | | | Change | | |
| | 2017 | Amount | % | 2016 | Amount | % | 2015 |
| Net new home orders | | | | | | | |
| Southern California | 197 | 56 | 40 % | 141 | 55 | 64 % | 86 |
| Northern California | 215 | 103 | 92 % | 112 | 24 | 27 % | 88 |
| Total net new home orders | 412 | 159 | 63 % | 253 | 79 | 45 % | 174 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Selling communities at end of period | | | | | | | |
| Southern California | 10 | 2 | 25 % | 8 | 4 | 100 % | 4 |
| Northern California | 7 | — | — % | 7 | 1 | 17 % | 6 |
| Total selling communities | 17 | 2 | 13 % | 15 | 5 | 50 % | 10 |
| | | | | | | | |
| Average selling communities | 13 | 1 | 8 % | 12 | 5 | 71 % | 7 |
| Monthly sales absorption rate per community (1) | 2.7 | 1.0 | 59 % | 1.7 | (0.2) | (11 )% | 1.9 |
| Cancellation rate | 9 % | (3 )% | NA | 12 % | 2 % | NA | 10 % |

(1) Monthly sales absorption represents the number of net new home orders divided by the number of average selling communities for the period.

38

Net new home orders for the year ended December 31, 2017 increased 63% compared to the same period in 2016. The increase was primarily driven by a 59% increase in the monthly sales absorption rate per community and to a lesser extent, an 8% increase in average selling communities. The improvement in absorption rate was driven by solid order activity in both Southern and Northern California resulting from the addition of more affordably-priced product, which generally sells at a faster pace than move-up or luxury product. Southern California experienced monthly absorption of 2.3 sales per community in 2017, compared to 1.8 in the prior year, while high buyer demand resulted in an 82% increase in monthly sales absorption to 3.1 sales per community for Northern California in 2017 compared to 2016.

Net new home orders for the year ended December 31, 2016 increased 45% compared to 2015 primarily due to an increase in the number of selling communities, which was partially offset by a slightly slower monthly sales absorption rate.

The Company continued to experience a fairly modest cancellation rate in 2017 that was relatively consistent with the prior two years. We believe our cancellation rate is one of the lower rates in the industry due to many factors, including loan prequalifying buyers before writing sales contracts, the high level of personalized options that our homebuyers select, which creates emotional attachment, and a higher proportion of affluent buyers with strong credit profiles.

Backlog

| | Year Ended December 31, | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2017 | | | 2016 | | | % Change | | |
| | Homes | Dollar Value | Average Price | Homes | Dollar Value | Average Price | Homes | Dollar Value | Average Price |
| | (Dollars in thousands) | | | | | | | | |
| Southern California | 71 | $93,955 | $1,323 | 48 | $162,599 | $3,387 | 48 % | (42 )% | (61 )% |
| Northern California | 82 | 68,295 | 833 | 31 | 24,697 | 797 | 165% | 177 % | 5 % |
| Total | 153 | $162,250 | $1,060 | 79 | $187,296 | $2,371 | 94 % | (13 )% | (55 )% |

| | Year Ended December 31, | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2016 | | | 2015 | | | % Change | | |
| | Homes | Dollar Value | Average Price | Homes | Dollar Value | Average Price | Homes | Dollar Value | Average Price |
| | (Dollars in thousands) | | | | | | | | |
| Southern California | 48 | $162,599 | $3,387 | 45 | $149,405 | $3,320 | 7 % | 9 % | 2 % |
| Northern California | 31 | 24,697 | 797 | 22 | 17,162 | 780 | 41% | 44 % | 2 % |
| Total | 79 | $187,296 | $2,371 | 67 | $166,567 | $2,486 | 18% | 12 % | (5 )% |

Backlog reflects the number of homes, net of cancellations, for which we have entered into a sales contract with a customer, but for which we have not yet delivered the home. Backlog dollar value at December 31, 2017 declined 13% compared to the prior year end due to a 55% decrease in average selling price to $1.1 million as compared to $2.4 million, which was partially offset by a 94% increase in backlog units. The decline in the average selling price of homes in backlog was primarily related to the delivery of the final homes from two higher-priced luxury communities in Newport Coast, CA in 2017. Additionally, ending 2017 backlog included increased contributions from more affordably-priced communities consistent with the Company's strategic shift to diversify its product offerings and access a deeper buyer pool as compared to ending backlog at December 31, 2016. The increase in the number of homes in backlog as of December 31, 2017 compared to the prior year period was largely the result of higher monthly sales absorption rates.

The dollar value of backlog at December 31, 2016 was up 12% to $187.3 million over the prior year period due to an 18% increase in the number of homes in backlog, partially offset by a 5% reduction in the average selling price of homes in backlog. The higher backlog dollar value in Southern California as compared to Northern California was due to higher community counts in Southern California combined with higher-priced communities, particularly in Newport Coast, CA, where we had two coastal luxury communities where average home prices in backlog exceeded $5 million. The increase in the number of homes in backlog as of December 31, 2016 compared to the prior year period was the result of increased net new home orders.

Lots Owned and Controlled

| | December 31, | | | | | | |
|---|---|---|---|---|---|---|---|
| | | Change | | | Change | | |
| | 2017 | Amount | % | 2016 | Amount | % | 2015 |
| Lots Owned | | | | | | | |
| Southern California | 563 | 273 | 94 % | 290 | 167 | 136 % | 123 |
| Northern California | 318 | 18 | 6 % | 300 | 11 | 4 % | 289 |
| Arizona | 65 | 65 | NA | — | — | NA | — |
| Total | 946 | 356 | 60 % | 590 | 178 | 43 % | 412 |
| Lots Controlled[1] | | | | | | | |
| Southern California | 278 | (443 ) | (61 )% | 721 | (33 ) | (4 )% | 754 |
| Northern California | 1,031 | 766 | 289 % | 265 | 113 | 74 % | 152 |
| Arizona | 497 | 497 | NA | — | — | — % | — |
| Total | 1,806 | 820 | 83 % | 986 | 80 | 9 % | 906 |
| Lots Owned and Controlled - Wholly Owned | 2,752 | 1,176 | 75 % | 1,576 | 258 | 20 % | 1,318 |
| Fee Building[2] | 920 | (15 ) | (2 )% | 935 | (487) | (34 )% | 1,422 |
| Total Lots Owned and Controlled | 3,672 | 1,161 | 46 % | 2,511 | (229) | (8 )% | 2,740 |

(1) Includes lots that we control under purchase and sale agreements, option agreements or non-binding letters of intent that are subject to customary conditions and have not yet closed. There can be no assurance that such acquisitions will occur.
(2) Lots owned by third party property owners for which we perform general contracting services.

Consistent with our focus to grow our wholly owned business, the Company increased the number of wholly owned lots owned and controlled by 75% and 20% year-over-year for the years ending December 31, 2017 and 2016, respectively. Of the lots owned and controlled at December 31, 2017, 66% were controlled through option contracts. The increase in wholly owned lots owned and controlled was due to our planned expansion in Arizona where we entered into contracts on four land parcels totaling 562 aggregate lots, and an increase in lots controlled in Northern California primarily due to two new developments with multiple planning areas, one for 418 lots in Vacaville, CA and a second for 394 lots in a masterplan development in Folsom, CA. The increase in wholly owned lots owned and controlled was partially offset by a 36% increase in new home deliveries in 2017.

The slight decrease in fee building lots at December 31, 2017 as compared to 2016 was attributable to delivering 820 homes during 2017, offset partially by contracts from the Company's largest customer awarded in 2017 for seven new fee building communities totaling 804 lots.

Home Sales Revenue and New Homes Delivered

| | Year Ended December 31, | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2017 | | | 2016 | | | % Change | | |
| | Homes | Dollar Value | Average Price | Homes | Dollar Value | Average Price | Homes | Dollar Value | Average Price |
| | (Dollars in thousands) | | | | | | | | |
| Southern California | 174 | $433,651 | $2,492 | 147 | $422,041 | $2,871 | 18% | 3 % | (13 )% |
| Northern California | 167 | 127,191 | 762 | 103 | 85,908 | 834 | 62% | 48 % | (9 )% |
| Total | 341 | $560,842 | $1,645 | 250 | $507,949 | $2,032 | 36% | 10 % | (19 )% |

| | Year Ended December 31, | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2016 | | | 2015 | | | % Change | | |
| | Homes | Dollar Value | Average Price | Homes | Dollar Value | Average Price | Homes | Dollar Value | Average Price |
| | (Dollars in thousands) | | | | | | | | |
| Southern California | 147 | $422,041 | $2,871 | 74 | $205,815 | $2,781 | 99% | 105 % | 3 % |
| Northern California | 103 | 85,908 | 834 | 74 | 74,394 | 1,005 | 39% | 15 % | (17 )% |
| Total | 250 | $507,949 | $2,032 | 148 | $280,209 | $1,893 | 69% | 81 % | 7 % |

New home deliveries increased 36% for the year ended December 31, 2017 compared to the prior year period. The increase in deliveries was the result of a higher number of homes in backlog at December 31, 2016 and an increase in new home orders during the year. Home sales revenue for 2017 increased 10% compared to 2016 primarily due to an increase in new home deliveries, which was offset by a 19% lower average sales price per delivery. The year-over-year decrease in average sales price was driven by increased deliveries from our Northern California operations, which has lower-priced communities than Southern California, coupled with a product mix shift for both Southern California and Northern California as deliveries from more affordably-priced communities increased.

Home sales revenue for the year ended December 31, 2016 increased 81% to $507.9 million compared to $280.2 million in 2015. The increase in home sales revenue in 2016 as compared to 2015 was driven primarily by a 69% increase in deliveries and to a lesser extent, a 7% increase in the average selling price of homes to $2.0 million. The increase in deliveries was the result of a higher number of homes in beginning backlog to start 2016 and a 45% increase in net new home orders during 2016. The increase in our average selling price was due to a 99% increase in deliveries from our Southern California operations, which had a significantly higher average selling price than our Northern California operations due to a higher concentration of luxury homes in coastal locations.

Homebuilding Gross Margin

Homebuilding gross margin percentage for 2017 improved 100 basis points to 15.2% as compared to 14.2% in the prior year. 2017 included $2.2 million in noncash inventory impairments related to one homebuilding community in Southern California while 2016 included $2.4 million in noncash inventory impairment charges related to two homebuilding communities, one in each of Southern and Northern California. The impairments in both years were due to project specific issues, including slower monthly sales absorption rates that required additional sales incentives. In addition, the 2017 and 2016 homebuilding gross margins included a benefit related to warranty adjustments of $0.8 million and $1.1 million, respectively. The homebuilding gross margin before impairments for 2017 was 15.6% versus 14.6% in 2016. Homebuilding gross margin before impairments is a non-GAAP measure. See the table below reconciling this non-GAAP financial measure to homebuilding gross margin, the nearest GAAP equivalent. The 100 basis point improvement in homebuilding gross margin before impairments as compared to the prior year was due primarily to a change in product mix, including the favorable impact of higher-margin, coastal communities located in Newport Coast, CA.

Homebuilding gross margin percentage for the year ended December 31, 2016 was 14.2%, compared to 16.1% for 2015. Homebuilding gross margin before impairments for 2016 was 14.6% versus 16.1% in the prior year period. The 150 basis point decline in homebuilding gross margin before impairments as compared to the prior year was due primarily to a change in mix, including lower margins in masterplan communities located in Irvine and lower margins in the Bay Area. These decreases were partially offset by higher margins from the initial deliveries in our Crystal Cove communities in Newport Coast, CA, and to a

lesser extent, a 20 basis point benefit from a warranty accrual adjustment made during the 2016 third quarter that increased homebuilding gross margin by $1.1 million.
Excluding home sales impairments and interest in cost of home sales, adjusted homebuilding gross margin percentage for the years ended December 31, 2017, 2016 and 2015 were 17.6%, 15.7% and 16.9%, respectively. See the table below reconciling this non-GAAP financial measure to homebuilding gross margin, the nearest GAAP equivalent.

| | Year Ended December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2017 | % | 2016 | % | 2015 | % |
| | (Dollars in thousands) | | | | | |
| Home sales revenue | $560,842 | 100.0% | $507,949 | 100.0% | $280,209 | 100.0% |
| Cost of home sales | 475,413 | 84.8 % | 435,909 | 85.8 % | 235,232 | 83.9 % |
| Homebuilding gross margin | 85,429 | 15.2 % | 72,040 | 14.2 % | 44,977 | 16.1 % |
| Add: Home sales impairments | 2,200 | 0.4 % | 2,350 | 0.4 % | — | — % |
| Homebuilding gross margin before impairments [1] | 87,629 | 15.6 % | 74,390 | 14.6 % | 44,977 | 16.1 % |
| Add: Interest in cost of home sales | 11,021 | 2.0 % | 5,331 | 1.1 % | 2,511 | 0.8 % |
| Adjusted homebuilding gross margin[1] | $98,650 | 17.6 % | $79,721 | 15.7 % | $47,488 | 16.9 % |

(1) Homebuilding gross margin before impairments and adjusted homebuilding gross margin are non-GAAP financial measures. We believe this information is meaningful as it isolates the impact that home sales impairments and leverage have on homebuilding gross margin and permits investors to make better comparisons with our competitors who also break out and adjust gross margins in a similar fashion.

Land Sales

During the fourth quarter of 2016, the Company recorded a noncash land sale impairment charge of $1.2 million related to land under development in Northern California that the Company initially intended to sell. The land sale was ultimately not consummated and the Company made the determination to develop and build homes on this land.
Fee Building

| | Year Ended December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2017 | % | 2016 | % | 2015 | % |
| | (Dollars in thousands) | | | | | |
| Fee building revenue | $190,324 | 100.0% | $186,507 | 100.0% | $149,890 | 100.0% |
| Cost of fee building | 184,827 | 97.1 % | 178,103 | 95.5 % | 139,677 | 93.2 % |
| Fee building gross margin | $5,497 | 2.9 % | $8,404 | 4.5 % | $10,213 | 6.8 % |

Our fee building revenues include (i) billings to third-party land owners for general contracting services, and (ii) management fees from our unconsolidated joint ventures for construction management services. Cost of fee building includes (i) labor, subcontractor, and other indirect construction and development costs that are reimbursable by the land owner, and (ii) general and administrative, or G&A, expenses that are attributable to fee building activities and joint venture management overhead. Besides allocable G&A expenses, there are no other material costs associated with management fees from our unconsolidated joint ventures.
Billings to land owners are a function of construction activity and reimbursable costs are incurred as homes are started. The total billings and reimbursable costs are driven by the pace at which the land owner has us execute its development plan. Management fees from our unconsolidated joint ventures are collected over the project's life and as homes and lots are delivered.
For the year ended December 31, 2017, fee building revenues increased 2% from the prior year period primarily due to an increase in fee building costs incurred related to a higher fee building delivery volume. Included in fee building revenues for the years ended December 31, 2017 and December 31, 2016 were (i) $185.4 million and $178.3 million of billings to land owners for general contracting services for 2017 and 2016, respectively, and (ii) $4.9 million and

$8.2 million of management fees from our unconsolidated joint ventures for 2017 and 2016, respectively. The decrease in management fees from JVs was primarily the result of fewer deliveries and lower land sales revenue from JV communities.

For the year ended December 31, 2017, cost of fee building increased due to the increase in fee building activity, compared to the same period during 2016. The amount of G&A expenses included in cost of fee building was $8.3 million and $8.8

million for the years ended December 31, 2017 and 2016, respectively. Fee building gross margin percentage decreased to 2.9% for the year ended December 31, 2017 from 4.5% in the prior year period. The decrease in fee building gross margin was due to a change in the fee building business arrangements on certain projects combined with a decrease in management fees received from joint ventures.

For the year ended December 31, 2016, fee building revenues were up 24% from the prior year period due to an increase in fee building activity resulting from a higher number of homes under construction during the year. The increase in number of homes under construction was due to an increased number of homes started during the year, at the direction of the land owner, offset partially by an increase in the number of homes completed and delivered. Included in fee building revenues for the years ended December 31, 2016 and December 31, 2015 were (i) $178.3 million and $137.5 million of billings to land owners for general contracting services for 2016 and 2015, respectively, and (ii) $8.2 million and $12.4 million of management fees from our unconsolidated joint ventures for 2016 and 2015, respectively. The decrease in management fees from JVs was primarily the result of fewer deliveries and lower home and land sales revenue from JV communities, which was consistent with the Company’s strategic shift to emphasize wholly owned operations.

For the year ended December 31, 2016, cost of fee building increased due to the increase in fee building revenues, compared to the same period during 2015. The amount of G&A expenses included in cost of fee building was $8.8 million in both 2016 and 2015. Fee building gross margin percentage decreased to from 6.8% to 4.5% for the year ended December 31, 2016 compared to the prior year period. The reduction in fee building gross margin percentage was largely due to a decrease in management fees received from joint ventures, partially offset by a slightly higher fee rate with our largest customer on certain fee building communities.

Our fee building revenue has historically been concentrated with a small number of customers. For the years ended December 31, 2017, 2016 and 2015, one customer comprised 97%, 96% and 92% of fee building revenue, respectively.

Selling, General and Administrative Expenses

| | Year Ended December 31, | | | As a Percentage of Home Sales Revenue | | |
|---|---|---|---|---|---|---|
| | 2017 | 2016 | 2015 | 2017 | 2016 | 2015 |
| | (Dollars in thousands) | | | | | |
| Selling and marketing expenses | $32,702 | $26,744 | $13,741 | 5.8 % | 5.3 % | 4.9 % |
| General and administrative expenses ("G&A") | 26,330 | 25,882 | 20,278 | 4.7 % | 5.1 % | 7.2 % |
| Total selling, marketing and G&A expenses ("SG&A") | $59,032 | $52,626 | $34,019 | 10.5% | 10.4% | 12.1% |

The Company's SG&A expense ratio for the year ended December 31, 2017 increased 10 basis points over 2016 to 10.5%. The slight increase was primarily attributable to higher selling and marketing costs, driven by greater amortization of capitalized selling and marketing costs from our two luxury communities located in Newport Coast, CA and an increase in marketing spend and model operating costs related to new community openings.

SG&A expenses for the year ended December 31, 2016 were up year-over-year, consistent with the 81% increase in our homebuilding revenues and 50% increase in wholly owned community count at December 31, 2015. However, our SG&A operating leverage improved significantly resulting in a 170 basis point reduction in our SG&A expense ratio for the year ended December 31, 2016 from 12.1% to 10.4%. The improvement was largely attributable to the increase in home sales revenue, which was driven by a significant increase in new home deliveries and higher average selling prices due to a heavier Southern California mix. Selling and marketing expenses as a percentage of home sales revenue for 2016 was up 40 basis points year-over-year to 5.3% due to higher amortization of capitalizable marketing costs and increased model operating costs associated with higher-priced, luxury homes in Southern California.

Equity in Net Income of Unconsolidated Joint Ventures

As of December 31, 2017 and 2016, we had ownership interests in 10 and 13, respectively, unconsolidated joint ventures. We own interests in our unconsolidated joint ventures that generally range from 5% to 35% and these interests vary by entity.

The Company's share of joint venture income was $0.9 million for the year ended December 31, 2017 as compared to $7.7 million for the year ended December 31, 2016. A 37% reduction in joint venture revenues from decreased home and lot deliveries and lower gross margins from joint venture home sales contributed to the year-over-year decrease in the Company's share of joint venture income. The decline in home sales revenue is attributable to a 24% decrease in joint venture home deliveries partially offset by a 6% increase in average selling price. The year-over-year reduction in land sales revenues was due to the close-out of one masterplan community located in Foster City, CA as well as fewer lot sales from a masterplan community in Davis, CA where substantially all lots were delivered at December 31, 2016. The 2017 joint venture home sales gross margin decrease was primarily due to a mix shift in deliveries including increased deliveries in 2017 from five Sacramento communities with lower margins as well as the close out of our higher-margin Orchard Park project in the Bay Area, which delivered its last home in the 2017 first quarter. Additionally, in 2017, the Company purchased the equity interest of its joint venture partner in the joint venture known as Larkspur. Prior to the close out, the Company received a $0.1 million income allocation from the joint venture. Upon close out, the Company recognized a gain of $0.3 million due to the purchase of its joint venture partner's interest for less than its carrying value. In 2016, the Company purchased the equity interest of its joint venture partner in the joint venture known as Lambert Ranch. Prior to the close out, the Company received a $0.5 million income allocation from the joint venture. Upon closeout, the Company recognized a gain of $1.1 million due to the purchase of its joint venture partner's interest for less than its carrying value. The joint venture close outs mentioned are discussed in further detail within Note 11, "Related Party Transactions," in our accompanying Consolidated Financial Statements.

The Company's share of joint venture income for the year ended December 31, 2016 was $7.7 million as compared to $13.8 million for the year ended December 31, 2015. The reduction in joint venture income was driven by a 47% decrease in total JV home sales revenues resulting from a 29% decrease in our JV average selling price and a 26% decrease in JV home deliveries. This decline was partially offset by a one-time gain related to the close-out of Lambert Ranch, described above.

The following sets forth supplemental operational and financial information about our unconsolidated joint ventures. Such information is not included in our financial data for GAAP purposes, but is reflected in our results as a component of equity in net income of unconsolidated joint ventures. This data is included for informational purposes only.

| | Year Ended December 31, | | | | | | |
|---|---|---|---|---|---|---|---|
| | | Change | | | Change | | |
| | 2017 | Amount | % | 2016 | Amount | % | 2015 |
| | (Dollars in thousands) | | | | | | |
| Unconsolidated Joint Ventures—Homebuilding Operational Data | | | | | | | |
| Net new home orders | 170 | 11 | 7 % | 159 | (140) | (47)% | 299 |
| New homes delivered | 149 | (48) | (24)% | 197 | (68) | (26)% | 265 |
| Average sales price of homes delivered | $958 | $57 | 6 % | $901 | $(365) | (29)% | $1,266 |
| | | | | | | | |
| Home sales revenue | $142,697 | $(34,847) | (20)% | $177,544 | $(157,971) | (47)% | $335,515 |
| Land sales revenue | 4,750 | (50,925) | (91)% | 55,675 | (18,691) | (25)% | 74,366 |
| Total Revenue | $147,447 | $(85,772) | (37)% | $233,219 | $(176,662) | (43)% | $409,881 |
| Net income | $(529) | $(26,720) | (102)% | $26,191 | $(39,003) | (60)% | $65,194 |
| | | | | | | | |
| Selling communities at end of period | 7 | (2) | (22)% | 9 | 1 | 13 % | 8 |
| Backlog (dollar value) | $66,636 | $11,222 | 20 % | $55,414 | $(62,522) | (53)% | $117,936 |
| Backlog (homes) | 80 | 18 | 29 % | 62 | (47) | (43)% | 109 |
| Average sales price of homes in backlog | $833 | $(61) | (7)% | $894 | $(188) | (17)% | $1,082 |
| | | | | | | | |
| Homebuilding lots owned and controlled | 341 | (244) | (42)% | 585 | (164) | (22)% | 749 |
| Land development lots owned and controlled | 2,323 | (92) | (4)% | 2,415 | (160) | (6)% | 2,575 |
| Total lots owned and controlled | 2,664 | (336) | (11)% | 3,000 | (324) | (10)% | 3,324 |

Provision for Income Taxes

For the year ended December 31, 2017, the Company recorded a provision for income taxes of $15.4 million. The effective tax rate for 2017 differs from the 35% federal statutory tax rate, primarily due to a $3.2 million noncash, provisional charge related to the revaluation of the Company's deferred tax asset to reflect a reduction in the federal corporate tax rate from 35% to 21%, effective for fiscal year 2018 that was enacted in 2017, and state income taxes, offset partially by the benefit from production activities.

On December 22, 2017, the President of the United States signed into law the Tax Cuts and Jobs Act (the "Tax Act"). The Tax Act amends the Internal Revenue Code to reduce tax rates and modify policies, credits, and deductions for individuals and businesses. For businesses, the Tax Act reduces the corporate federal tax rate from a maximum of 35% to a flat 21% rate. The rate reduction took effect on January 1, 2018. In accordance with ASC 740, Income Taxes ("ASC 740"), the consolidated provision for income taxes is calculated using the asset and liability method, under which deferred tax assets and liabilities are recorded based on the difference between the financial statement and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. As a result of the reduction in the corporate income tax rate from 35% to 21% under the Tax Act, the Company revalued its net deferred tax asset at December 31, 2017 and recorded a noncash, provisional charge of $3.2 million, which is included in the tax provision for 2017. The Company is currently analyzing the effects of the Tax Act and will update this provisional rate as it completes its analysis. Excluding the $3.2 million deferred tax asset charge, the Company's effective tax rate would have been 37.5% for 2017 as compared to 38.4% in 2016. Effective tax rate before noncash deferred tax charge is a non-GAAP measure. Please refer to "Management's Discussion and Analysis of Financial Condition and Results of Operations - Overview" for a reconciliation to effective tax rate, the nearest GAAP equivalent.

As part of the Tax Act, the Company will no longer be able to take certain tax deductions for production activities that currently reduce our effective tax rate. Additionally, the Company will be subject to increased deduction limitations on certain executive compensation. For 2018, we believe the Company's deduction for certain executive compensation will not be limited due to transition rules included in the Tax Act. However, the deduction limitation could increase our effective tax rate for 2019 and beyond. Based on our current operations and geographic footprint coupled with current state income tax laws, our preliminary estimate for the full year 2018 effective tax rate is approximately 28% to 29%, excluding the impact of any potential discrete items; however actual results could differ.

For the year ended December 31, 2016, the Company recorded a provision for income taxes of $13.0 million and its effective tax rate was 38.4%. Included in this provision is an allocation of income of $0.5 million from LR8 and a $1.1 million gain from the closeout of our LR8 joint venture, which resulted in a provision for income taxes of $0.6 million for the year December 31, 2016 and did not impact our effective tax rate. The effective tax rate for 2016 differs from the 35% federal statutory tax rate, primarily due to state income taxes, offset partially by the benefit from production activities and energy efficient credits.

For the year ended December 31, 2015, we recorded a provision for income taxes of $12.5 million and its effective tax rate was 37.0%. The effective tax rate for the year ended December 31, 2015 differs from the 35% statutory tax rate due to state income taxes, offset partially by the benefit from production activities and energy efficient credits.

Liquidity and Capital Resources

Overview

Our principal uses of capital for the year ended December 31, 2017 were land purchases, land development, home construction, repayments on our revolving credit facility, contributions and advances to our unconsolidated joint ventures, and payment of operating expenses and routine liabilities. Our principal sources of capital for the year ended December 31, 2017 were proceeds from the sale of our senior notes due 2022, cash generated from home sales activities, advances from our unsecured revolving credit facility, distributions from our unconsolidated joint ventures and fees from our fee building agreements.

Cash flows for each of our communities depend on their stage in the development cycle, and can differ substantially from reported earnings. Early stages of development or expansion require significant cash outlays for land acquisitions, entitlements and other approvals, and construction of model homes, roads, utilities, general landscaping and other amenities. Because these costs are a component of our real estate inventories and not recognized in our consolidated statement of operations until a home is delivered, we incur significant cash outlays prior to our recognition of earnings. In the later stages of community development, cash inflows may significantly exceed earnings reported for financial statement purposes, as the cash outflow associated with home and land construction was previously incurred. From a liquidity standpoint, we are actively acquiring and developing lots to increase our lot supply and community count. As we continue to expand our business, we expect cash outlays for land purchases, land

development and home construction to exceed our cash generated by operations.
We ended 2017 with $123.5 million of cash and cash equivalents, a $93.1 million increase from December 31, 2016, primarily as a result of the issuance of our senior notes due 2022 and home closing revenues offset by land acquisition expenditures and development activity. We expect to generate cash from the sale of our inventory, but intend to redeploy the net cash generated from the sale of inventory to acquire and develop strategic, well-positioned lots that represent opportunities to generate future income and cash flows.
As of December 31, 2017 and 2016, we had $11.3 million and $22.8 million, respectively, in accounts payable that related to costs incurred under our fee building agreements. Funding to pay these amounts is the obligation of the third-party land

owner, which is generally funded on a monthly basis. Similarly, contracts and accounts receivable and due from affiliates as of the same dates included $11.6 million and $24.3 million, respectively, related to the payment of the above payables.
We intend to utilize both debt and equity as part of our ongoing financing strategy, coupled with redeployment of cash flows from continuing operations, to provide us with the financial flexibility to operate our business. In that regard, we expect to employ prudent levels of leverage to finance the acquisition and development of our lots and construction of our homes. As of December 31, 2017, we had outstanding borrowings of $325 million in aggregate principal related to our senior notes. We will consider a number of factors when evaluating our level of indebtedness and when making decisions regarding the incurrence of new indebtedness, including the purchase price of assets to be acquired with debt financing, the estimated market value of our assets and the ability of particular assets, and our company as a whole, to generate cash flow to cover the expected debt service. In addition, our debt contains certain financial covenants that limits the amount of leverage we can maintain.
We intend to finance future acquisitions and developments with what we believe to be the most advantageous source of capital available to us at the time of the transaction, which may include unsecured corporate level debt, property-level debt, and other public, private or bank debt, or common and preferred equity.
Senior Notes Due 2022
On March 17, 2017, the Company completed the sale of $250 million in aggregate principal amount of 7.25% Senior Unsecured Notes due 2022 (the "Existing Notes"), in a private placement. The Notes were issued at an offering price of 98.961% of their face amount, which represents a yield to maturity of 7.50%. On May 4, 2017, the Company completed a tack-on private placement offering through the sale of an additional $75 million in aggregate principal amount of the 7.25% Senior Notes due 2022 ("Additional Notes"). The Additional Notes were issued at an offering price of 102.75% of their face amount plus accrued interest since March 17, 2017, which represented a yield to maturity of 6.438%. Net proceeds from the Existing Notes were used to repay all borrowings outstanding under the Company's senior unsecured revolving credit facility with the remainder to be used for general corporate purposes. Net proceeds from the Additional Notes will be used for working capital, land acquisition and general corporate purposes. Interest on the Existing Notes and the Additional Notes (the "Original Notes") will be paid semiannually in arrears on April 1 and October 1, which commenced on October 1, 2017. In accordance with its obligations under two registration rights agreements executed in connection with the private placements of the Original Notes, on September 8, 2017, the Company completed an exchange offer of the Original Notes for an equal principal amount of 7.25% Senior Notes due 2022 (the "Notes") which terms are identical in all material respects to the Original Notes except that the Notes are registered under the Securities Act of 1933, as amended (the "Securities Act") and are freely tradeable in accordance with applicable law. The Notes will mature on April 1, 2022.

The Notes contain certain restrictive covenants, including a limitation on additional indebtedness and a limitation on restricted payments. Restricted payments include, among other things, dividends, investments in unconsolidated entities, and stock repurchases. Under the limitation on additional indebtedness, we are permitted to incur specified categories of indebtedness but are prohibited, aside from those exceptions, from incurring further indebtedness if we do not satisfy either a leverage condition or an interest coverage condition. The leverage and interest coverage conditions are summarized in the table below, as described and defined further in the indenture for the Notes. Exceptions to the additional indebtedness limitation include, among other things, borrowings of up to $260 million under existing or future bank credit facilities, non-recourse indebtedness, and indebtedness incurred for the purpose of refinancing or repaying certain existing indebtedness. Under the limitation on restricted payments, we are also prohibited from making restricted payments, aside from certain exceptions, if we do not satisfy either condition. In addition, the amount of restricted payments that we can make is subject to an overall basket limitation, which builds based on, among other things, 50% of consolidated net income from January 1, 2017 and 100% of the net cash proceeds from qualified equity offerings. Exceptions to the foregoing limitations on our ability to make restricted payments include, among other things, investments in joint ventures and other investments up to 15% of our consolidated tangible net assets and a general basket of $15 million. The Notes are guaranteed by all of the Company's 100% owned subsidiaries, for more information about these guarantees, please see Note 17 of the notes to our consolidated financial statements.

| Financial Conditions | December 31, 2017 Actual | Requirement |
|---|---|---|
| Fixed Charge Coverage Ratio: EBITDA to Consolidated Interest Incurred | 2.2 | > 2.0 : 1.0 |
| Leverage Ratio: Indebtedness to Tangible Net Worth | 1.22 | < 2.25 : 1.0 |

As of December 31, 2017, we were able to satisfy both the leverage condition and the interest coverage condition. The foregoing conditions are further defined and described in the indenture for the Notes.

Senior Unsecured Revolving Credit Facility

The Company's unsecured revolving credit facility ("Credit Facility") is with a bank group. On September 27, 2017, the Company entered into a Modification Agreement (the "Modification") to its Credit Facility. The Modification, among other things, (i) extends the maturity date of the revolving credit facility to September 1, 2020, (ii) decreases (A) the total commitments under the facility to $200 million from $260 million and (B) the accordion feature to $300 million from $350 million, (iii) revises certain financial covenants, including the tangible net worth, minimum liquidity, and interest coverage tests, in addition to providing relief on compliance with the interest coverage test so long as the Company maintains cash equal to not less than the trailing twelve month consolidated interest incurred, and (iv) adds certain wholly owned subsidiaries as guarantors.

A portion of the net proceeds from the sale of our senior notes due 2022 was used to repay the outstanding balance of the Credit Facility. As of December 31, 2017, there was no outstanding balance on the Credit Facility. Interest is payable monthly and is charged at a rate of 1-month LIBOR plus a margin ranging from 2.25% to 3.00% depending on the Company's leverage ratio as calculated at the end of each fiscal quarter. As of December 31, 2017, the interest rate under the facility was 4.56%. Pursuant to the Credit Facility, the Company is required to maintain certain financial covenants as defined in the Credit Facility, including, but not limited to, those listed in the following table. The table below reflects any updates to covenant requirements that resulted from the modification agreement.

| | December 31, 2017 | | |
|---|---|---|---|
| Financial Covenants | Actual | Covenant Requirement | |
| | (Dollars in thousands) | | |
| Unencumbered Liquid Assets (Minimum Liquidity Covenant) | $123,546 | $ 10,000 | (1) |
| EBITDA to Interest Incurred (2) | 2.23 | > 1.75 : 1.0 | |
| Tangible Net Worth | $263,990 | $ 187,349 | |
| Leverage Ratio | 44 % | < 65% | |
| Adjusted Leverage Ratio (3) | NA | < 50% | |

(1) So long as the Company is in compliance with the interest coverage test, the minimum unencumbered liquid assets that the Company must maintain as of the quarter end measurement date is $10 million. If the Company is not in compliance with the interest coverage test, the minimum liquidity requirement as of each quarter end measurement date is not less than the trailing 12 month consolidated interest incurred, which was $22.0 million as of December 31, 2017.

(2) The modification of the Credit Facility executed September 27, 2017, provides relief on compliance with the interest coverage test. If the test is not met, it will not be considered an event of default so long as the Company maintains cash equal to not less than the trailing 12 month consolidated interest incurred.

(3) Adjusted Leverage Ratio is computed as total joint venture debt divided by total joint venture equity. The Adjusted Leverage Ratio requirement ceases to apply as of and after the fiscal quarter in which consolidated tangible net worth is at least $250 million. During any period when the Adjusted Leverage Ratio ceases to apply, consolidated tangible net worth shall be reduced by an adjustment equal to the aggregate amount of investments in and advance to unconsolidated joint ventures that exceed 35% of consolidated tangible net worth as calculated without giving effect to this adjustment (the "Adjustment Amount"). At December 31, 2017, the Company's consolidated tangible net worth exceeded $250 million and the Adjusted Leverage Ratio ceased to apply and, accordingly, the Adjustment Amount was considered in the calculation of consolidated tangible net worth.

As of December 31, 2017 and 2016, we were in compliance with all financial covenants.

Debt-to-Capital Ratios

We believe that debt-to-capital ratios provide useful information to the users of our financial statements regarding our financial position and leverage. Net debt-to-capital ratio is a non-GAAP financial measure. See the table below reconciling this non-GAAP measure to debt-to-capital ratio, the nearest GAAP equivalent.

| | December 31, | |
|---|---|---|
| | 2017 | 2016 |
| | (Dollars in thousands) | |
| Total debt, net | $318,656 | $118,000 |
| Equity, exclusive of noncontrolling interest | 263,990 | 244,523 |
| Total capital | $582,646 | $362,523 |
| Ratio of debt-to-capital [(1)] | 54.7 % | 32.5 % |
| | | |
| Total debt, net | $318,656 | $118,000 |
| Less: cash, cash equivalents and restricted cash | 123,970 | 31,081 |
| Net debt | 194,686 | 86,919 |
| Equity, exclusive of noncontrolling interest | 263,990 | 244,523 |
| Total capital | $458,676 | $331,442 |
| Ratio of net debt-to-capital [(2)] | 42.4 % | 26.2 % |

(1) The ratio of debt-to-capital is computed as the quotient obtained by dividing total debt, net by the sum of total debt, net plus equity, exclusive of noncontrolling interest.

(2) The ratio of net debt-to-capital is computed as the quotient obtained by dividing net debt (which is total debt, net less cash to the extent necessary to reduce the debt balance to zero) by total capital, exclusive of noncontrolling interest. The most directly comparable GAAP financial measure is the ratio of debt-to-capital. We believe the ratio of net debt-to-capital is a relevant financial measure for investors to understand the leverage employed in our operations and as an indicator of our ability to obtain financing. We believe that by deducting our cash from our debt, we provide a measure of our indebtedness that takes into account our cash liquidity. We believe this provides useful information as the ratio of debt-to-capital does not take into account our liquidity and we believe that the ratio net of cash provides supplemental information by which our financial position may be considered. Investors may also find this to be helpful when comparing our leverage to the leverage of our competitors that present similar information. See the table above reconciling this non-GAAP financial measure to the ratio of debt-to-capital.

Cash Flows

For the year ended December 31, 2017 as compared to the year ended December 31, 2016, the comparison of cash flows is as follows:

- Net cash used in operating activities was $90.7 million in 2017 versus $42.4 million in 2016. The change was primarily the result of a net increase in cash outflows for real estate inventories to $114.9 million in 2017 compared to $71.4 million in 2016 due to greater land acquisition spend and increased construction in progress.
- Net cash used in investing activities was $10.6 million in 2017 compared $1.8 million provided by investing activities in 2016. For the year ended December 31, 2017, our contributions and advances to joint ventures were $27.5 million compared to $15.1 million during the year ended December 31, 2016 and was the primary reason net cash used in investing activities increased. The increase in contributions to joint ventures primarily related to a large contribution to a land development joint venture in Folsom, CA.
- Net cash provided by financing activities was $194.3 million in 2017 compared to $25.2 million in 2016. The increase was primarily due to an increase in net borrowings, in particular the issuance of our senior notes due 2022, offset partially by increased repayments of the unsecured credit facility.

For the year ended December 31, 2016 as compared to the year ended December 31, 2015, the comparison of cash flows is as follows:

- Net cash used in operating activities was $42.4 million in 2016 versus $32.3 million in 2015. The change was primarily the result of a reduction of distributions of earnings from unconsolidated joint ventures to $3.7 million in 2016 from $18.5 million and an increase in cash outflows for real estate inventories to $71.4 million in 2016 compared to $65.9 million in 2015. Cash inflows for distributions of earnings from unconsolidated joint ventures decreased due to the reduction of total revenues of the unconsolidated joint ventures during the same periods. Despite a 43% increase in net wholly owned lots year-over-year, we were able to continue utilizing favorable lot option takedown structures that defrayed a portion of the upfront capital required to acquire land. In addition, we delivered more homes in 2016 as compared to the prior year, which partially offset increased land acquisition and construction costs capitalized to inventory as compared to 2015.

- Net cash provided by investing activities was $1.8 million in 2016 compared $16.6 million in 2015. For the year ended December 31, 2016, our net distributions of capital from unconsolidated joint ventures was $0.2 million compared to net distributions of $17.0 million during the year ended December 31, 2015 and was the primary reason net cash provided by investing activities decreased. The decrease in distributions related to the decrease in total revenues of the unconsolidated joint ventures. The decrease in distributions was partially offset by the assumption of $2.0 million in cash as a result in the change in control in our LR8 Investors LLC unconsolidated joint venture during 2016. The Company assumed the joint venture's cash, accounts receivable. accounts payable, and accrued liabilities upon the exit of its joint venture partner.
- Net cash provided by financing activities was $25.2 million in 2016 versus $17.5 million in 2015. The increase primarily related to an increase in net borrowings, offset partially by the issuance of common stock in the 2015 period. Cash inflows for net borrowings from the unsecured credit facility and other notes payable was $27.8 million for the year ending December 31, 2016 compared to net paydowns on the unsecured credit facility and other notes payable of $27.2 million for the year ended December 31, 2015. Additionally, 2015 included the follow-on issuance of common stock, which generated $47.3 million in net cash proceeds while 2016 did not include any net proceeds from the issuance of common stock.

Off-Balance Sheet Arrangements and Contractual Obligations

Option Contracts

In the ordinary course of business, we enter into land option contracts in order to procure lots for the construction of our homes. We are subject to customary obligations associated with entering into contracts for the purchase of land and improved lots. These purchase contracts typically require a cash deposit and the purchase of properties under these contracts is generally contingent upon satisfaction of certain requirements by the sellers, including obtaining applicable property and development entitlements. We also utilize option contracts with land sellers as a method of acquiring land in staged takedowns, to help us manage the financial and market risk associated with land holdings, to reduce the use of funds from our corporate financing sources, and to enhance our return on capital. Option contracts generally require a nonrefundable deposit for the right to acquire lots over a specified period of time at pre-determined prices. We generally have the right, at our discretion, to terminate our obligations under both purchase contracts and option contracts by forfeiting our cash deposit with no further financial responsibility to the land seller. In some instances, we may also expend funds for due diligence and development activities with respect to our option contracts prior to purchase which we would have to write off should we not purchase the land. As of December 31, 2017, we had $34.2 million of nonrefundable and $0.8 million of refundable cash deposits pertaining to land option contracts and purchase contracts with an estimated aggregate remaining purchase price of $330.9 million, net of deposits ("Aggregate Remaining Purchase Price"). These cash deposits are included as a component of our real estate inventories in our consolidated balance sheets. In addition, the Company has agreed to liquidated damages of $9.1 million should the Company not fulfill its obligations under a contract to control $53.1 million which is included in the Aggregate Remaining Purchase Price noted above.

Our utilization of land option contracts is dependent on, among other things, the availability of land sellers willing to enter into option arrangements, the availability of capital to financial intermediaries to finance the development of optioned lots, general housing market conditions, and local market dynamics. Options may be more difficult to procure from land sellers in strong housing markets and are more prevalent in certain geographic regions.

Joint Ventures

We enter into land development and homebuilding joint ventures from time to time as means of:

- leveraging our capital base
- accessing larger or desirable lot positions
- expanding our market opportunities
- managing financial and market risk associated with land holdings
- establishing strategic alliances

These joint ventures have historically obtained secured acquisition, development and/or construction financing which reduces the use of funds from our corporate financing sources.

The Company has provided credit enhancements in connection with joint venture borrowings in the form of loan-to-value ("LTV") maintenance agreements in order to secure the joint venture's performance under the loans and maintenance of certain LTV ratios. The Company has also entered into agreements with its partners in each of the unconsolidated joint ventures whereby the Company and its partners are apportioned liability under the LTV maintenance agreements according to their respective capital interest. In addition, the agreements provide the Company, to the extent its partner has an unpaid liability under such credit enhancements, the right to receive distributions from the unconsolidated joint venture that would otherwise be made to the partner. However, there is no guarantee that such distributions will be made or will be sufficient to cover the Company's liability under such LTV maintenance agreements. The loans underlying the LTV maintenance agreements comprise acquisition and development loans, construction revolvers and model home loans, and the agreements remain in force until the loans are satisfied. Due to the nature of the loans, the outstanding balance at any given time is subject to a number of factors including the status of site improvements, the mix of horizontal and vertical development underway, the timing of phase build outs, and the period necessary to complete the escrow process for homebuyers. As of December 31, 2017 and 2016, $38.6 million and $56.0 million, respectively, was outstanding under the loans and credit enhanced by the

Company through LTV maintenance agreements. Under the terms of the joint venture agreements, the Company's proportionate share of LTV maintenance agreement liabilities was $6.7 million and $8.6 million, respectively, as of December 31, 2017 and December 31, 2016. In addition, the Company has provided completion agreements regarding specific performance for certain projects whereby the Company is required to complete the given project with funds provided by the beneficiary of the agreement. If there are not adequate funds available under the specific project loans, the Company would then be subject to financial liability under such completion guaranties. Typically, under such terms of the joint venture agreements, the Company has the right to apportion the respective share of any costs funded under such completion guaranties to its partners. However, there is no guarantee that we will be able to recover against our partners for such amounts owed to us under the terms of such joint venture agreements. In connection with joint venture borrowings, the Company also selectively provides (a) an environmental indemnity provided to the lender that holds the lender harmless from and against losses arising from the discharge of hazardous materials from the property and non-compliance with applicable environmental laws; and (b) indemnification of the lender from "bad boy acts" of the unconsolidated entity such as fraud, misrepresentation, misapplication or non-payment of rents, profits, insurance, and condemnation proceeds, waste and mechanic liens, and bankruptcy.

For more information about our off-balance sheet arrangements, please see Note 10 to our consolidated financial statements.

As of December 31, 2017, we held membership interests in 10 unconsolidated joint ventures, six of which related to homebuilding activities and four related to land development as noted below. We were a party to three loan-to-value maintenance agreements related to unconsolidated joint ventures as of December 31, 2017. The following table reflects certain financial and other information related to our unconsolidated joint ventures as of December 31, 2017:

| | | | | December 31, 2017 | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | Total Joint Venture | | | | | | | |
| Joint Venture (Project Name) | Year Formed | Location | Ownership % | Assets | Debt[1] | Equity | NWHM Equity (2) | Debt-to-Total Capital-ization | Loan-to-Value Maintenance Agreement | Future Capital Commitment [3] | Lots Owned and Controlled |
| | | | | (Dollars in 000's) | | | | | | | |
| TNHC-HW San Jose LLC (Orchard Park) | 2012 | San Jose, CA | 15% | 2,656 | — | 556 | 167 | — % | N/A | — | — |
| TNHC-TCN Santa Clarita LP (Villa Metro)[4] | 2012 | Santa Clarita, CA | 10% | 1,373 | — | 784 | 196 | — % | N/A | — | — |
| TNHC Newport LLC (Meridian)[4] | 2013 | Newport Beach, CA | 12% | 3,091 | — | 1,643 | 300 | — % | N/A | — | — |
| Encore McKinley Village LLC (McKinley Village) | 2013 | Sacramento, CA | 10% | 87,264 | 23,884 | 56,265 | 5,632 | 30 % | Yes | — | 255 |
| TNHC Russell Ranch LLC (Russell Ranch)[4] [5] | 2013 | Folsom, CA | 35% | 85,897 | 22,513 | 54,152 | 20,739 | 29 % | N/A | 20,817 | 870 |
| TNHC-HW Foster City LLC (Foster Square)[5] | 2013 | Foster City, CA | 35% | 2,861 | — | 1,368 | 635 | — % | N/A | — | — |
| Calabasas Village LP (Avanti)[4] | 2013 | Calabasas, CA | 10% | 43,958 | 1,564 | 40,582 | 5,172 | 4 % | Yes | — | 27 |
| TNHC-HW Cannery LLC (Cannery Park)(5) | 2013 | Davis, CA | 35% | 10,693 | — | 7,028 | 2,459 | — % | N/A | — | 18 |

| | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Arantine Hills Holdings LP (Bedford Ranch) (4) (5) | 2014 | Corona, CA | 5% | 142,172 | — | 139,028 | 6,949 | — % | N/A | 2,120 | 1,435 |
| TNHC Mountain Shadows LLC (Mountain Shadows) | 2015 | Paradise Valley, AZ | 25% | 65,885 | 30,380 | 31,144 | 8,274 | 49 % | Yes | — | 59 |
| Total Unconsolidated Joint Ventures | | | | $445,850 | $78,341 | $332,550 | 50,523 | 19 % | | $22,937 | 2,664 |

(1) The carrying value of the debt is presented net of $0.5 million in unamortized debt issuance costs. Scheduled maturities of the unconsolidated joint venture debt as of December 31, 2017 are as follows: $41.8 million matures in 2018 and $37.0 million matures in 2019. Projects at McKinley Village and Mountain Shadows have multiple debt instruments, some of which do not have LTV maintenance agreements.

(2) Represents the Company's equity in unconsolidated joint ventures. Equity does not include $3.8 million in advances to unconsolidated joint ventures and $1.5 million of interest capitalized to certain investments in unconsolidated joint ventures which along with equity, are included in investments in and advances to unconsolidated joint ventures in the accompanying consolidated balance sheets.

(3) Estimated future capital commitment represents our proportionate share of estimated future contributions to the respective unconsolidated joint ventures as of December 31, 2017. Actual contributions may differ materially.

(4) Certain members of the Company's board of directors are affiliated with entities that have an investment in these joint ventures. See Note 11 to the consolidated financial statements of the Company included in this Annual Report.

(5) Land development joint venture.

As of December 31, 2017, the unconsolidated joint ventures were in compliance with their respective loan covenants, where applicable, and we were not required to make any loan-to-value maintenance related payments during the year ended December 31, 2017.

Contractual Obligations Table

The following table summarizes our future payment obligations under existing contractual obligations as of December 31, 2017 including payment obligations due by period. Our purchase obligations primarily represent commitments for land purchases under purchase and land option contracts with nonrefundable deposits and commitments for subcontractor labor and material to be utilized in the normal course of business.

| | Payments Due By Period | | | | |
|---|---|---|---|---|---|
| Contractual Obligations | Total | Less than 1 Year | 1-3 Years | 4-5 Years | More than 5 Years |
| | (Dollars in thousands) | | | | |
| Long-term debt principal payments [1] | $325,000 | $— | $— | $325,000 | $ — |
| Long-term interest payments [2] | 100,141 | 23,563 | 47,125 | 29,453 | — |
| Operating leases | 3,831 | 1,202 | 2,344 | 285 | — |
| Purchase obligations [3] | 365,831 | 320,905 | 44,926 | — | — |
| Total | $794,803 | $345,670 | $94,395 | $354,738 | $ — |

(1) For a more detailed description of our long-term debt, please see Note 8 of the notes to our consolidated financial statements.

(2) Future interest payments for our senior notes due 2022.

(3) Includes $266.3 million (net of deposits) of the remaining purchase price for land option and land purchase contracts where deposits are nonrefundable and $99.0 million of subcontractor labor and material commitments as of December 31, 2017 for which we are responsible if the subcontractor completes the work as specified in their respective commitments. Excluded from this number is $63.7 million in purchase obligations made on behalf of the owner(s) of fee build projects for which we are reimbursed per our fee building agreements.

Inflation

Our homebuilding and fee building segments can be adversely impacted by inflation, primarily from higher land, financing, labor, material and construction costs. In addition, inflation can lead to higher mortgage rates, which can significantly affect the affordability of mortgage financing to homebuyers. While we attempt to pass on cost increases to customers through increased prices, when weak housing market conditions exist, we may be unable to offset cost increases with higher selling prices.

Seasonality

Historically, the homebuilding industry experiences seasonal fluctuations in quarterly operating results and capital requirements. We typically experience the highest new home order activity in spring and summer, although this activity is also highly dependent on the number of active selling communities, timing of new community openings and other market factors. Since it typically takes five to nine months to construct a new home, we typically deliver more homes in the second half of the year as spring and summer home orders convert to home deliveries. Because of this seasonality, home starts, construction costs and related cash outflows have historically been highest in the second and third quarters, and a higher level of cash receipts from home deliveries occurs during the second half of the year. We expect this seasonal pattern to continue over the long-term, although it may be affected by volatility in the homebuilding industry.

Critical Accounting Policies

The preparation of financial statements in conformity with accounting policies generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Management bases its estimates and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Management evaluates such estimates and judgments on an on-going basis and makes adjustments as deemed necessary. Actual results could differ from these estimates if conditions are significantly different in the future.

Real Estate Inventories

We capitalize pre-acquisition, land, development and other allocated costs, including interest, property taxes and indirect construction costs to real estate inventories. Land, development and other common costs are typically allocated to real estate inventories using a methodology that approximates the relative-sales-value method. Home construction costs per production phase are recorded using the specific identification method. In accordance with Accounting Standards Codification ("ASC") 360, Property, Plan and Equipment ("ASC 360") inventory is stated at cost, unless the carrying amount is determined not to be recoverable, in which case inventory is written down to its fair value.

We review each real estate asset at each project (including unconsolidated joint venture real estate projects) on a periodic basis or whenever indicators of impairment exist. Real estate assets include projects actively selling and projects under development or held for future development. Indicators of impairment include, but are not limited to, significant decreases in local housing market values and selling prices of comparable homes, significant decreases in gross margins or sales absorption rates, costs significantly in excess of budget, and actual or projected cash flow losses.

If there are indicators of impairment, we perform a detailed budget and cash flow review of the applicable real estate inventories to determine whether the estimated remaining undiscounted future cash flows of the project are more or less than the asset's carrying value. If the estimated undiscounted cash flows are more than the asset's carrying value, no impairment adjustment is required. However, if the estimated undiscounted cash flows are less than the asset's carrying value, the asset is reviewed for impairment and if deemed impaired, is written down to fair value.

When estimating undiscounted future cash flows of a project, we make various assumptions, including: (i) expected sales prices and sales incentives to be offered, including the number of homes available, pricing and incentives being offered by us or other builders in other projects, and future sales price adjustments based on market and economic trends; (ii) expected sales pace and cancellation rates based on local housing market conditions, competition and historical trends; (iii) costs expended to date and expected to be incurred including, but not limited to, land and land development costs, home construction costs, interest costs, indirect construction and overhead costs, and selling and marketing costs; (iv) alternative product offerings that may be offered that could have an impact on sales pace, sales price and/or building costs; and (v) alternative uses for the property.

Many assumptions are interdependent and a change in one may require a corresponding change to other assumptions. For example, increasing or decreasing sales absorption rates has a direct impact on the estimated per unit sales price of a home and the level of time sensitive costs (such as indirect construction, overhead and carrying costs). Depending on the underlying objective of the project, assumptions could have a significant impact on the projected cash flow analysis. For example, if our objective is to preserve operating margins, our cash flow analysis will be different than if the objective is to increase the velocity of sales. These objectives may vary significantly from project to project and over time. If real estate assets are considered impaired, the impairment adjustments are calculated by determining the amount the asset's carrying value exceeds its fair value. Fair value is determined based on either a land residual value analysis or a discounted cash flow analysis. Under the land residual value analysis, we estimate what a willing buyer would pay and what a willing seller would sell a parcel of land for (other than in a forced liquidation) in order to generate a market rate operating margin and return. Under the discounted cash flow method, the fair value is determined by calculating the present value of future cash flows using a risk adjusted discount rate. Critical assumptions that are included as part of these analyses include estimating future housing revenues, sales absorption rates, land development, construction and related carrying costs (including future capitalized interest), and all direct selling and marketing costs. This evaluation and the assumptions used by management to determine future estimated cash flows and fair value require a substantial degree of judgment, especially with respect to real estate projects that have a substantial amount of development to be completed, have not started selling or are in the early stages of sales, or are longer in duration. Actual revenues, costs and time to complete and sell a community could vary from these estimates which could impact the calculation of fair value of the asset and the corresponding amount of impairment that is recorded in our results of operations.

Home Sales Revenue and Cost of Home Sales

Homebuilding revenue and cost of sales are recognized after construction is completed, a sufficient down payment has been received, title has transferred to the homebuyer, collection of the purchase price is reasonably assured and we have no continuing involvement. Cost of sales is recorded based upon total estimated costs to be allocated to each home within a community. Any changes to the estimated costs are allocated to the remaining undelivered lots and homes within their respective community. The estimation and allocation of these costs requires a substantial degree of judgment by management.

The estimation process involved in determining relative sales or fair values is inherently uncertain because it involves estimating future sales values of homes before sale and delivery. Additionally, in determining the allocation of costs to a particular land parcel or individual home, we rely on project budgets that are based on a variety of assumptions, including assumptions about construction schedules and future costs to be incurred. It is common that actual results differ from budgeted amounts for various reasons, including construction delays, increases in costs that have not been committed or unforeseen issues encountered during construction that fall outside the scope of existing contracts, or costs that come in less than originally anticipated. While the actual results for a particular construction project are accurately reported over time, a variance between the budget and actual costs could result in the understatement or overstatement of costs and have a related impact on gross margins between reporting periods. To reduce the potential for such variances, we have procedures that have been applied on a consistent basis, including assessing and revising project budgets on a periodic basis, obtaining commitments from subcontractors and vendors for future costs to be incurred, and utilizing the most recent information available to estimate costs. We believe that these policies and procedures provide for reasonably dependable estimates for purposes of calculating amounts to be relieved from inventories and expensed to cost of sales in connection with the delivery of homes.

Fee Building

The Company enters into fee building agreements to provide services whereby it builds homes on behalf of third-party property owners. The third-party property owner funds all project costs incurred by the Company to build and sell the homes. The Company primarily enters into cost plus fee contracts where it charges independent third-party property owners for all direct and indirect costs, plus a negotiated management fee. For these types of contracts, the Company recognizes revenue based on the actual total costs it has expended plus the applicable management fee. The management fee is typically a per unit fixed fee or based on a percentage of the cost or home sales revenue of the project depending on the terms of the agreement with the third-party property owner. In accordance with ASC 605, Revenue Recognition ("ASC 605"), revenues from fee building services are recognized using a cost-to-cost approach in applying the percentage-of-completion method. Under this approach, revenue is earned in proportion to total costs incurred, divided by total costs expected to be incurred. The total estimated cost plus the management fee represents the total contract value. The Company recognizes revenue based on the actual labor and other direct costs incurred, plus the portion of the management fee it has earned to date. In the course of providing its services, the Company routinely subcontracts for services and incurs other direct costs on behalf of the property owners. These costs are passed through to the property owners and, in accordance with GAAP, are included in the Company’s revenue and cost of sales.

The Company also enters into fee building and management contracts with third parties and its unconsolidated joint ventures where it provides construction supervision services, as well as sales and marketing services, and does not bear financial risks for any services provided. In accordance with ASC 605, revenues from these services are recognized over a proportional performance method or completed performance method. Under ASC 605, revenue is earned as services are provided in proportion to total services expected to be provided to the customer or on a straight line basis if the pattern of performance cannot be determined. Costs are recognized as incurred. Revenue recognition for any portion of the fees earned from these services that are contingent upon a financial threshold or specific event is deferred until the threshold is achieved or the event occurs.

Variable Interest Entities

The Company accounts for variable interest entities in accordance with ASC 810, Consolidation ("ASC 810"). Under ASC 810, a variable interest entity ("VIE") is created when: (a) the equity investment at risk in the entity is not sufficient to permit the entity to finance its activities without additional subordinated financial support provided by other parties, including the equity holders; (b) the entity’s equity holders as a group either (i) lack the direct or indirect ability to make decisions about the entity, (ii) are not obligated to absorb expected losses of the entity or (iii) do not have the right to receive expected residual returns of the entity; or (c) the entity’s equity holders have voting rights that are not proportionate to their economic interests, and the activities of the entity involve or are conducted on behalf of the equity holder with disproportionately few voting rights.

Once we consider the sufficiency of equity and voting rights of each legal entity, we then evaluate the characteristics of the equity holders' interests, as a group, to see if they qualify as controlling financial interests. Our real estate joint ventures consist of limited partnerships and limited liability companies. For entities structured as limited partnerships or limited liability companies, our evaluation of whether the equity holders (equity partners other than us in each our joint ventures) lack the characteristics of a controlling financial interest includes the evaluation of whether the limited partners or non-managing members (the noncontrolling equity holders) lack both substantive participating rights and substantive kick-out rights, defined as follows:

- Participating rights - provide the noncontrolling equity holders the ability to direct significant financial and operational decision made in the ordinary course of business that most significantly influence the entity's economic performance.
- Kick-out rights - allow the noncontrolling equity holders to remove the general partner or managing member without cause.

If we conclude that any of the three characteristics of a VIE are met, including if equity holders lack the characteristics of a controlling financial interest because they lack both substantive participating rights and substantive kick-out rights, we conclude that the entity is a VIE and evaluate it for consolidation under the variable interest model.

If an entity is deemed to be a VIE pursuant to ASC 810, the enterprise that has both (i) the power to direct the activities of a VIE that most significantly impact the entity's economic performance and (ii) the obligation to absorb the expected losses of the entity or right to receive benefits from the entity that could be potentially significant to the VIE is considered the primary beneficiary and must consolidate the VIE. In accordance with ASC 810, we perform ongoing reassessments of whether an enterprise is the primary beneficiary of a VIE.

Investments in and Advances to Unconsolidated Joint Ventures

We use the equity method to account for investments in homebuilding and land development joint ventures that qualify as VIEs where we are not the primary beneficiary and other entities that we do not control but have the ability to exercise significant influence over the operating and financial policies of the investee. The Company also uses the equity method when we function as the managing member or general partner and our venture partner has substantive participating rights or where we can be replaced by our venture partner as managing member without cause.

Under the equity method, we recognize our proportionate share of earnings and losses generated by the joint venture upon the delivery of lots or homes to third parties. If applicable, our proportionate share of intra-entity profits and losses are eliminated until the related asset has been sold by the unconsolidated joint venture to third parties. Our ownership interests in our unconsolidated joint ventures vary, but are generally less than or equal to 35%. The accounting policies of our joint ventures are consistent with those of the Company.

We review real estate inventory held by our unconsolidated joint ventures for impairment, consistent with our real estate inventories. We also review our investments in and advances to unconsolidated joint ventures for evidence of other-than-temporary declines in value. To the extent we deem any portion of our investment in and advances to unconsolidated joint ventures as not recoverable, we impair our investment accordingly.

Warranty Accrual

We offer warranties on our homes that generally cover various defects in workmanship or materials, or structural construction defects for one year. In addition, we generally provide a more limited warranty, which generally ranges from a minimum of two years up to the period covered by the applicable statute of repose, that covers certain defined construction defects. Estimated future direct warranty costs are accrued and charged to cost of sales in the period when the related homebuilding revenues are recognized. Amounts are accrued based upon the Company's historical rates. In addition, the Company has received warranty payments from third party property owners for certain of its fee building projects that have since closed out where the Company has the contractual risk of construction. These payments are recorded as warranty accruals. We assess the adequacy of our warranty accrual on a quarterly basis and adjust the amounts recorded if necessary. Although we consider the warranty accruals reflected in our consolidated balance sheet to be adequate, actual future costs could differ significantly from our currently estimated amounts.

Income Taxes

Income taxes are accounted for in accordance with ASC 740, Income Taxes ("ASC 740"). The consolidated provision for, or benefit from, income taxes is calculated using the asset and liability method under which deferred tax assets and liabilities are recorded based on the difference between the financial statement and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse.

Deferred tax assets are evaluated on a quarterly basis to determine if adjustments to the valuation allowance are required. In accordance with ASC 740, we assess whether a valuation allowance should be established based on the consideration of all available evidence using a "more likely than not" standard with respect to whether deferred tax assets will be realized. The ultimate realization of deferred tax assets depends primarily on the generation of future taxable income during the periods in which the differences become deductible. The value of our deferred tax assets will depend on applicable income tax rates. Judgment is required in determining the future tax consequences of events that have been recognized in our consolidated financial statements and/or tax returns. Differences between anticipated and actual outcomes of these future tax consequences could have a material impact on our consolidated financial statements. Changes in existing tax laws and tax rates also affect actual tax results and the valuation of deferred tax assets over time.

ASC 740 defines the methodology for recognizing the benefits of uncertain tax return positions as well as guidance regarding the measurement of the resulting tax benefits. These provisions require an enterprise to recognize the financial statement effects of a tax position when it is more likely than not (defined as a likelihood of more than 50%), based on the technical merits, that the position will be sustained upon examination. In addition, these provisions provide guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. The evaluation of whether a tax position meets the more-likely-than-not recognition threshold requires a substantial degree of judgment by management based on the individual facts and circumstances. Changes in the recognition or measurement of uncertain tax positions could result in material increases or decreases in our income tax expense in the period in which we make the change.

Stock-Based Compensation

We account for share-based awards in accordance with ASC 718, Compensation – Stock Compensation ("ASC 718") and ASC 505-50, Equity – Equity Based Payments to Non-Employees ("ASC 505-50").

ASC 718 requires that the cost resulting from all share-based payment transactions be recognized in a company's financial statements. ASC 718 requires all entities to apply a fair-value-based measurement method in accounting for share-based payment transactions with employees except for equity instruments held by employee share ownership plans.

ASC 505-50 requires that if an employee becomes a non-employee and continues to vest in a share-based award pursuant to the award's original terms, the award be treated as an award to a non-employee prospectively, provided the individual is required to continue providing services to the employer (such as consulting services). These awards are to be accounted for prospectively, such that the fair value of the award will be re-measured at each reporting date until the earlier of (a) the performance commitment date or (b) the date the services required under the agreement have been completed. ASC 505-50 requires that compensation cost ultimately recognized in the Company's financial statements be the sum of (a) the compensation cost recognized during the period of time the individual was an employee (based on the grant-date fair value) plus (b) the fair value of the award determined on the measurement date determined in accordance with ASC 505-50 for the pro-rata portion of the vesting period in which the individual was a non-employee.

The determination of the fair value of share-based awards at the grant date, or subsequent remeasurement dates under ASC 505-50, requires judgment in developing assumptions and involves a number of variables. These variables include, but are not limited to: expected stock-price volatility over the term of the awards and expected stock option exercise behavior. Additionally, judgment is required in the case of performance share awards in estimating the level of performance that will be achieved and the number of shares that will be earned. If actual results differ significantly from these estimates, stock-based compensation expense and our consolidated results of operations could be significantly impacted.

Recently Issued Accounting Standards

See Note 1 to the accompanying notes to consolidated financial statements included in this annual report on Form 10-K.

JOBS Act

We qualify as an "emerging growth company" pursuant to the provisions of the JOBS Act. For as long as we are an "emerging growth company," we may take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not "emerging growth companies," including, but not limited to, not being required to comply with the auditor attestation requirements of Section 404(b) of the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, exemptions from the requirements of holding advisory "say-on-pay" votes on executive compensation and shareholder advisory votes on golden parachute compensation.

In addition, Section 107 of the JOBS Act also provides that an "emerging growth company" can take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act for complying with new or revised accounting standards. An "emerging growth company" can therefore delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. However, we have chosen to "opt out" of such extended transition period and, as a result, we will comply with new or revised accounting standards on the relevant dates on which adoption of such standards is required for nonemerging growth companies. Section 107 of the JOBS Act provides that our decision to opt out of the extended transition period for complying with new or revised accounting standards is irrevocable.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to market risks related to fluctuations in interest rates on our outstanding variable rate debt. We did not utilize swaps, forward or option contracts on interest rates or commodities, or other types of derivative financial instruments as of or during the year ended December 31, 2017. We have not entered into and currently do not hold derivatives for trading or speculative purposes.

The table below details the principal amount and the average interest rates for the outstanding debt for each category based upon the expected maturity or disposition dates. The fair value of our senior unsecured notes is derived from quoted market prices. The fair value of our variable rate debt consists of the balance of our senior unsecured revolving credit facility (the "Credit Facility"). Based on the short-term duration of LIBOR rates, the fair value of debt under the Credit Facility approximates the carrying value.

| | Expected Maturity Date | | | | |
|---|---|---|---|---|---|
| | 2018 | 2019 - 2022 | Thereafter | Total | Estimated Fair Value |
| | (Dollars in thousands) | | | | |
| Senior Unsecured Notes | | | | | |
| Fixed Rate | $ — | $ 325,000 | $ — | $ | |