PULTE HOMES INC/MI/
Form 10-K
February 23, 2007

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

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

For the fiscal year ended December 31, 2006

OR

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

Commission File Number 1-9804

PULTE HOMES, INC.
(Exact name of registrant as specified in its charter)

MICHIGAN	**38-2766606**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

100 Bloomfield Hills Parkway, Suite 300
Bloomfield Hills, Michigan 48304
(Address of principal executive offices) (Zip Code)
Registrant s telephone number, including area code: (248) 647-2750
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 $.01	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 þ NO o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. YES o NO þ

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 þ NO o

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. o

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

Large accelerated filer þ Accelerated filer o Non-accelerated filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES o NO þ

The aggregate market value of the registrant s voting stock held by nonaffiliates of the registrant as of June 30, 2006, based on the closing sale price per share as reported by the New York Stock Exchange on such date, was $6,057,123,878.

As of February 21, 2007, the registrant had 256,014,973 shares of common stock outstanding.

Documents Incorporated by Reference

Applicable portions of the Proxy Statement for the 2007 Annual Meeting of Shareholders are incorporated by reference in Part III of this Form.

PULTE HOMES, INC.
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Form of Restricted Stock Award Agreement under Pulte Corporation 1995 Stock Incentive Plan
Form of Restricted Stock Award Agreement under Pulte Corporation 2000 Stock Incentive Plan
Form of Restricted Stock Award Agreement under Pulte Homes, Inc. 2004 Stock Incentive Plan
Ratio Earnings to Fixed Charges at December 31, 2006
Subsidiaries of the Registrant
Consent of Independent Registered Public Accounting Firm
Rule 13a-14(a) Certification by Richard J. Dugas Jr., President and Chief Executive Officer
Rule 13a-14(a) Certification by Roger A. Cregg, Executive Vice President and Chief Financial Officer
Certification Pursuant to Section 1350

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PART I

ITEM 1. BUSINESS

Pulte Homes, Inc.

Pulte Homes, Inc. is a publicly held holding company whose subsidiaries engage in the homebuilding and financial services businesses. Pulte Homes, Inc. is a Michigan corporation and was organized in 1956. Our assets consist principally of the capital stock of our subsidiaries and our income primarily consists of dividends from our subsidiaries. Our direct subsidiaries include Pulte Diversified Companies, Inc., Del Webb Corporation (Del Webb) and other subsidiaries engaged in the homebuilding business. Pulte Diversified Companies, Inc. s operating subsidiaries include Pulte Home Corporation, Pulte International Corporation (International) and other subsidiaries engaged in the homebuilding business. Pulte Diversified Companies, Inc. s non-operating thrift subsidiary, First Heights Holding Corp, LLC (First Heights), is classified as a discontinued operation (see Note 3 of our Consolidated Financial Statements). We also have a mortgage banking company, Pulte Mortgage LLC (Pulte Mortgage), which is a subsidiary of Pulte Home Corporation.

In December 2005, we sold substantially all of our Mexico homebuilding operations, realizing cash of $131.5 million, as further described in Note 3 of our Consolidated Financial Statements. For the years ended December 31, 2005 and 2004, the Mexico operations have been presented as discontinued operations.

In January 2005, we sold all of our Argentina operations, as further described in Note 3 of our Consolidated Financial Statements. For the year ended December 31, 2004, the Argentina operations have been presented as discontinued operations.

Homebuilding, our core business, is engaged in the acquisition and development of land principally for residential purposes within the continental United States and Puerto Rico and the construction of housing on such land targeted for the first-time, first and second move-up, and active adult home buyers. We have determined our operating segments to be our Areas, which are aggregated into seven reportable segments based on similarities in the economic and geographic characteristics of our homebuilding operations. Accordingly, our reportable homebuilding segments are as follows:

Northeast:	Northeast and Mid-Atlantic Areas include the following states: *Connecticut, Delaware, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Virginia*
Southeast:	Southeast Area includes the following states: *Georgia, North Carolina, South Carolina, Tennessee*
Florida:	Florida Area includes the following state: *Florida*
Midwest:	Great Lakes Area includes the following states: *Illinois, Indiana, Michigan, Ohio, Minnesota*
Central:	Rocky Mountain and Central Areas include the following states: *Colorado, Kansas, Missouri, Texas*
Southwest:	Southwest and Nevada Areas include the following states: *Arizona, Nevada, New Mexico*
*California:	Northern California and Southern California Areas include the following state: *California*

*

Our homebuilding operations located in Reno, Nevada are reported in the California segment, while our remaining Nevada homebuilding operations are reported in the Southwest segment.

We also have one reportable segment for our financial services operations which consists principally of mortgage banking and title operations conducted through Pulte Mortgage and our other subsidiaries. Our financial services segment operates generally in the same markets as our homebuilding segments.

Pulte Homes, Inc. (continued)

Financial information, including revenues, income (loss) from continuing operations before income taxes, valuation adjustments and write-offs, depreciation and amortization, equity income (loss), total assets and inventory, for each of our business segments is included in Note 2 of our Consolidated Financial Statements.

Available Information

Our internet website address is *www.pulte.com*. Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to section 13(a) or 15(d) of the Exchange Act are available free of charge through our website as soon as reasonably practicable after we electronically file with or furnish them to the Securities and Exchange Commission. Our code of ethics for principal officers, our corporate governance guidelines and the charters of the Audit, Compensation, and Nominating and Governance committees of our Board of Directors is also posted on our website and is available in print, free of charge, upon request.

Homebuilding Operations

	Years Ended December 31, ($000 s omitted)				
	2006	**2005**	**2004**	**2003**	**2002**
Homebuilding settlement revenues	$ 13,975,387	$ 14,370,667	$ 11,094,617	$ 8,482,341	$ 6,991,614
Homebuilding settlement units	41,487	45,630	38,612	32,693	28,903

Through our brands, which include Pulte Homes, Del Webb and DiVosta, we offer a wide variety of home designs including single family detached, townhouses, condominiums and duplexes at different prices and with varying levels of options and amenities to all of our major customer segments: first-time, first and second move-up and active adult. Expanding the number of customer segments served within each of our markets has enabled us to significantly increase our annual unit settlements over the past five years to 41,487 homes closed in 2006. Over our 56-year history, we have delivered nearly 500,000 homes.

As of December 31, 2006, our Homebuilding operations offered homes for sale in 690 communities. Sales prices of homes currently offered for sale in 70% of our communities fall within the range of $100,000 to $400,000 with a 2006 average unit selling price of $337,000, compared with $315,000 in 2005, $287,000 in 2004, $259,000 in 2003, and $242,000 in 2002. Sales of single-family detached homes, as a percentage of total unit sales, were 74% in 2006, compared with 72% in 2005, 80% in 2004, 83% in 2003, and 86% in 2002. The decline in the percentage of single-family detached homes can be attributed to an increase in sales of townhouses, condominiums and duplexes, which are most popular among our first-time and active adult homebuyers. Our Homebuilding operations are geographically diverse and, as a result, better insulate us from demand changes in individual markets. As of December 31, 2006, our Homebuilding business operated in 52 markets spanning 27 states.

Land acquisition and development

We select locations for development of homebuilding communities after completing extensive market research, enabling us to match the location and product offering with our targeted consumer group. We consider factors such as proximity to developed areas, population and job growth patterns and, if applicable, estimated development costs. We historically have managed the risk of controlling our land positions through use of option contracts and outright acquisition. We typically control land with the intent to complete sales of housing units within 24 to 36 months from the date of opening a community, except in the case of certain Del Webb active adult developments and other selected large projects for which the completion of community build out requires a longer time period due to typically larger project sizes. As a result, land is generally purchased after it is properly zoned and developed or is ready for development. In addition, we dispose of owned land not required in the business through sales to appropriate end users. Where we develop land, we engage directly in many phases of the development process, including land and site planning, obtaining environmental and other regulatory approvals, as well as constructing roads, sewers, water and drainage facilities and other amenities. We use our staff and the services of independent engineers and consultants for land development activities. Land development work is performed primarily by independent contractors and local government authorities who construct sewer and water systems in some areas. At December 31, 2006, we controlled approximately 232,200 lots, of which 158,800 were owned and 73,400 were under option agreements.

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Homebuilding Operations (continued)

Sales and marketing

We are dedicated to improving the quality and value of our homes through innovative proprietary architectural and community designs and state-of-the-art customer marketing techniques. Analyzing various qualitative and quantitative data obtained through extensive market research, we segment our potential customers into well-defined buyer profiles. Segmentation analysis provides a method for understanding the business opportunities and risks across the full spectrum of consumer groups in each market. Once the demands of potential buyers are understood, we link our home design and community development efforts to the specific lifestyle of each targeted consumer group.

To meet the demands of our various customers, we have established a solid design expertise for a wide array of product lines. We believe that we are an innovator in the design of our homes and we view design capacity as an integral aspect of our marketing strategy. Our in-house architectural services teams and management, supplemented by outside consultants, are successful in creating distinctive design features, both in exterior facades and interior options and features. In certain markets our strategy is to offer the complete house in which all features shown in the home are included in the sales price. Standard features typically offered include vaulted ceilings, appliances, and a variety of available flooring and carpet.

Typically, our sales teams, together with outside sales brokers, are responsible for guiding the customer through the sales process. We are committed to industry-leading customer service through a variety of quality initiatives, including the customer care program, which ensures that homeowners are comfortable at every stage of the building process. Using a seven-step, interactive process, homeowners are kept informed during their homebuilding and home owning experience. The steps include (1) a pre-construction meeting with the superintendent; (2) pre-dry wall frame walk; (3) quality assurance inspection; (4) first homeowner orientation; (5) 30-day follow-up after the close of the home; (6) three-month follow-up; and (7) an 11-month quality list after the close of the home. Fully furnished and landscaped model homes are used to showcase our homes and their distinctive design features. We have great success with the first-time buyer in the low to moderate price range; in such cases, financing under United States Government-insured and guaranteed programs is often used and is facilitated through our mortgage company. We also enjoy strong sales to the move-up buyer and, in certain markets, offer semi-custom homes in higher price ranges.

Through our Del Webb brand, we are better able to address the needs of active adults, among the fastest growing homebuying segments. We offer both destination communities and in place communities, for those buyers who prefer to remain in their current geographic area. These communities, with highly amenitized products such as golf courses, recreational centers and educational classes, offer the active adult buyer many options to maintain an active lifestyle.

We have received recognition and awards as a result of our achievements as a homebuilder. In September 2006, Pulte was named among the Top 100 on the InformationWeek 100 list, an award honoring the nation s most innovative users of information technology. In April 2006, we were ranked number 147 on the FORTUNE 500 List. Additionally, in July 2006 we were named to the FORTUNE Global 500 list.

In addition, our Maryland, Washington D.C., Orlando, Tampa Bay (DiVosta), Jacksonville, Ft. Myers/Naples (DiVosta), Palm Beach (DiVosta), Dallas/Ft. Worth, Houston, Denver/Colorado Springs, Albuquerque, Las Vegas (Del Webb), Tucson and Central Valley, California divisions were recognized for ranking the highest in their markets in a national customer satisfaction study. Twelve of our divisions ranked second in their respective markets, while ten divisions ranked third. Pulte brands, which include Pulte Homes, Del Webb and DiVosta, were surveyed in 30 of the 34 total markets analyzed. The survey noted customer service, home readiness at the time of closing, and the company s sales staff as the three factors that most heavily influenced the customer s overall level of satisfaction. Developing the Pulte Homes brand and leveraging the strength of the DiVosta and Del Webb brand names helps to distinguish our communities from the competition, and often results in the advantages of additional sales pace, choice community locations, and reduced overall customer acquisition costs.

Our Homeowner for Life™ philosophy has increased our business from those who have previously owned a Pulte home or have been referred by a Pulte homeowner by ensuring a positive home buying and home owning experience. We introduce our homes to prospective buyers through a variety of media advertising, illustrated brochures, Internet listings and link placements, and other advertising displays. In addition, our websites, *www.pulte.com, www.delwebb.com, and www.divosta.com* provide tools to help users find a home that meets their needs, investigate financing alternatives, communicate moving plans, maintain a home, learn more about us and communicate directly with us. Approximately 5.4 million potential customers visited our websites during 2006.

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Homebuilding Operations (continued)

Construction

The construction process for our homes begins with the in-house design of the homes we sell. The building phase is conducted under the supervision of our on-site construction superintendents. The construction work is usually performed by independent contractors under contracts that, in many instances, cover both labor and materials on a fixed-price basis. In certain markets, we provide a unique design and production process that is highly efficient, and results in lower costs, higher overall specification and increased value to our customers. We believe that Pulte Preferred Partnerships (P^3), an extension of our quality assurance program, continues to establish new standards for contractor relations. Using a selective process, we have teamed up with what we believe are premier contractors and suppliers to improve all aspects of the land development and house construction processes.

We maintain efficient construction operations by using standard materials and components from a variety of sources and, when possible, by building on contiguous lots. To minimize the effects of changes in construction costs, the contracting and purchasing of building supplies and materials generally is negotiated at or near the time when related sales contracts are signed. In addition, we leverage our size by actively negotiating our materials needs on a national or regional basis to minimize production component cost. We are also working to establish a more integrated system that can effectively link suppliers, contractors and the production schedule through various strategic business partnerships and e-business initiatives.

We cannot determine the extent to which necessary building materials will be available at reasonable prices in the future and have, on occasion, experienced shortages of skilled labor in certain trades and of building materials in some markets.

Competition and other factors

Our operations are subject to building, environmental and other regulations of various federal, state, and local governing authorities. For our homes to qualify for Federal Housing Administration (FHA) or Veterans Administration (VA) mortgages, we must satisfy valuation standards and site, material and construction requirements of those agencies. Our compliance with federal, state, and local laws relating to protection of the environment has had, to date, no material effect upon capital expenditures, earnings or competitive position. More stringent requirements could be imposed in the future on homebuilders and developers, thereby increasing the cost of compliance.

Our dedication to customer satisfaction is evidenced by our consumer and value-based brand approach to product development, and is something that we believe distinguishes us in the homebuilding industry and contributes to our long-term competitive advantage. The housing industry in the United States, however, is highly competitive. In each of our market areas, there are numerous homebuilders with which we compete. We also compete with the resales of existing house inventory. Any provider of housing units, for-sale or to rent, including apartment builders, may be considered a competitor. Conversion of apartments to condominiums further provides certain segments of the population an alternative to traditional housing, as does manufactured housing. We compete primarily on the basis of price, reputation, design, location and quality of our homes. The housing industry is affected by a number of economic and other factors including: (1) significant national and world events, which impact consumer confidence; (2) changes in the costs of building materials and labor; (3) changes in interest rates; (4) changes in other costs associated with home ownership, such as property taxes and energy costs; (5) various demographic factors; (6) changes in federal income tax laws; (7) changes in government mortgage financing programs, and (8) availability of sufficient mortgage capacity. In addition to these factors, our business and operations could be affected by shifts in demand for new homes.

Financial Services Operations

We conduct our financial services business, which includes mortgage and title operations, through Pulte Mortgage and other subsidiaries. Our mortgage bank arranges financing through the origination of mortgage loans primarily for the benefit of our homebuyers. We also engage in the sale of such loans and the related servicing rights. We are a lender approved by the FHA and VA and are a seller/servicer approved by Government National Mortgage Association (GNMA), Federal National Mortgage Association (FNMA), Federal Home Loan Mortgage Corporation (FHLMC) and other investors. In our conventional mortgage lending activities we follow underwriting guidelines established by FNMA, FHLMC, and private investors.

Our mortgage underwriting, processing and closing functions are centralized in Denver, Colorado and Charlotte, North Carolina using a mortgage operations center (MOC) concept. We also use a centralized telephone loan officer concept where loan officers are centrally located at mortgage application centers (MAC) in Denver and Charlotte. In addition, during 2006, we initiated a web application program in certain markets. Once the loan applications are received, our sales representatives, who are the mortgage customers main contact, forward them to a MAC loan counselor who calls the customer to complete the loan application and then forwards it to the MOC for processing. We believe both the MOC and the MAC improve the speed and efficiency of our mortgage operations, thereby improving our profitability and allowing us to focus on creating attractive mortgage financing opportunities for our customers.

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Financial Services Operations (continued)

In originating mortgage loans, we initially use our own funds and borrowings made available to us through various credit arrangements. Subsequently, we sell such mortgage loans and mortgage-backed securities to outside investors.

Our capture rate for the years ended December 31, 2006, 2005, and 2004 was approximately 91%, 89%, and 88%, respectively. Our capture rate represents loan originations from our homebuilding business as a percent of total loan opportunities, excluding cash settlements, from our homebuilding business. During the years ended December 31, 2006, 2005, and 2004, we originated mortgage loans for approximately 77%, 75%, and 72%, respectively, of the homes we sold. Such originations represented nearly 100%, 98%, and 92%, respectively, of our total originations. During 2006, 21% of total origination dollars were from brokered loans, which are less profitable to us, compared with 26% and 36% in 2005 and 2004, respectively. The decrease in brokered loans can be attributed to a shift in product mix towards funded production.

We sell our servicing rights monthly on a flow basis through fixed price servicing sales contracts to reduce the risks inherent in servicing loans. This strategy results in owning the servicing rights for only a short period of time, which substantially reduces the risk of impairment with respect to the fair value of these reported assets. The servicing sales contracts provide for the reimbursement of payments made when loans prepay within specified periods of time, usually 90 days after sale or securitization.

The mortgage industry in the United States is highly competitive. We compete with other mortgage companies and financial institutions to provide attractive mortgage financing to both our homebuyers and to the general public. The Internet is also an important resource for homebuyers in obtaining financing as a number of companies provide online approval for their customers. These Internet-based mortgage companies may also be considered competitors.

In originating and servicing mortgage loans, we are subject to rules and regulations of the FHA, VA, GNMA, FNMA and FHLMC. In addition to being affected by changes in these programs, our mortgage banking business is also affected by several of the same factors that impact our homebuilding business.

Our subsidiary title insurance companies serve as title insurance agents in selected markets by providing title insurance policies, examination and closing services to buyers of homes we sell.

Financial Information About Geographic Areas

We currently operate primarily within the United States. However, we have some non-operating foreign entities, which are insignificant to our consolidated financial results.

Discontinued Operations

Mexico Homebuilding Operations

In January 2005, the minority shareholders of Pulte Mexico S. de R.L. de C.V. (Pulte Mexico) exercised a put option under the terms of a reorganization agreement dated as of December 31, 2001, to sell their shares to us, the consummation of which resulted in our owning 100% of Pulte Mexico. In March 2005, we purchased 60% of the minority interest of Pulte Mexico for approximately $18.7 million in cash. In June 2005, we purchased the remaining 40% of the minority interest of Pulte Mexico for approximately $12.5 million in cash.

In December 2005, we sold substantially all of our Mexico homebuilding operations to a consortium of purchasers involved in residential and commercial real estate development. The disposition of the Mexico homebuilding operations will enable us to invest additional resources in the U.S. housing market. We realized cash of $131.5 million related to the sale. The sale of these operations did not include our investment in the capital stock of a mortgage company in Mexico as well as various non-operating entities. For the year ended December 31, 2005, we recognized a pre-tax loss of $6.6 million (after-tax loss of $13.1 million) related to the sale of our Mexico homebuilding operations. For the years ended December 31, 2005 and 2004, the Mexico homebuilding operations have been presented as discontinued operations in our Consolidated Financial Statements.

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Discontinued Operations (continued)

Argentina

In January 2005, we sold all of our Argentina operations to an Argentine company involved in residential and commercial real estate development. For the year ended December 31, 2004, the Argentina operations are presented as discontinued operations in our Consolidated Financial Statements.

First Heights

During the first quarter of 1994, we adopted a plan of disposal for First Heights and announced our strategy to exit the thrift industry and increase our focus on housing and related mortgage banking. First Heights sold all but one of its 32 bank branches and related deposits to two unrelated purchasers. The sale was substantially completed during the fourth quarter of 1994. Although we expected to complete the plan of disposal within a reasonable period of time, contractual disputes precluded us from completing the disposal in accordance with our original plan.

In August 2005, the United States Court of Appeals affirmed the United States Court of Federal Claims final judgment that we had been damaged by approximately $48.7 million as a result of the United States government s breach of contract in connection with the enactment of Section 13224 of the Omnibus Budget Reconciliation Act of 1993. In December 2005, we received payment of the judgment in the amount of $48.7 million, which was recorded as income from discontinued operations.

In September 2005, First Heights received notice confirming the voluntary dissolution of the First Heights Bank. The Office of Thrift Supervision also canceled First Heights charter. Accordingly, the day-to-day activities of First Heights, which had been principally devoted to supporting residual regulatory compliance matters and the litigation with the United States government, have now ceased.

Other non-operating

Other non-operating is comprised primarily of Pulte Homes, Inc. and Pulte Diversified Companies, Inc., both of which are holding companies. The primary purpose of these entities is to support the operations of our subsidiaries by acting as the internal source of financing, developing and implementing strategic initiatives centered around new business development and operating efficiencies. Business development activities include the pursuit of additional opportunities as well as the development of innovative building components and processes. Other non-operating also includes the activities associated with supporting a publicly traded entity listed on the New York Stock Exchange.

Other non-operating assets include equity investments in subsidiaries, short-term financial instruments and affiliate advances. Liabilities include senior debt and income taxes. Other non-operating revenues consist primarily of investment earnings of excess funds, while expenses include costs associated with supporting a publicly traded company and its subsidiaries operations, and investigating strategic initiatives.

Organization/Employees

All subsidiaries and operating units operate independently with respect to daily operations. Homebuilding real estate purchases and other significant homebuilding, mortgage banking, financing activities and similar operating decisions must be approved by the business unit and/or corporate senior management.

At December 31, 2006, we employed approximately 12,400 people. Our employees are not represented by any union. Contracted work, however, may be performed by union contractors. Homebuilding and mortgage banking management personnel are paid performance bonuses and incentive compensation. Performance bonuses are based on individual performance while incentive compensation is based on the performance of the applicable business unit, subsidiary or the Company. Our corporate management personnel are paid incentive compensation based on our overall performance. Each subsidiary is given autonomy regarding employment of personnel, although our senior corporate management acts in an advisory capacity in the employment of subsidiary officers. We consider our employee and contractor relations to be satisfactory.

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ITEM 1A. RISK FACTORS

Discussion of our business and operations included in this annual report on Form 10-K should be read together with the risk factors set forth below. They describe various risks and uncertainties to which we are, or may become subject. These risks and uncertainties, together with other factors described elsewhere in this report, have the potential to affect our business, financial condition, results of operations, cash flows, strategies or prospects in a material and adverse manner.

Downward changes in general economic, real estate construction or other business conditions could adversely affect our business or our financial results.

The residential homebuilding industry is sensitive to changes in economic conditions and other factors, such as the level of employment, consumer confidence, consumer income, availability of financing and interest rate levels. Adverse changes in any of these conditions generally, or in the markets where we operate, could decrease demand and pricing for new homes in these areas or result in customer cancellations of pending contracts, which could adversely affect the number of home deliveries we make or reduce the prices we can charge for homes, either of which could result in a decrease in our revenues and earnings and would adversely affect our financial condition.

The homebuilding industry is currently experiencing an economic down cycle, which has resulted in the overvaluation of land and new homes in certain markets.

In recent years, land and home prices rose significantly in many of our markets. However, during the year ended December 31, 2006, the homebuilding industry was impacted by lack of consumer confidence, decreased housing affordability and large supplies of resale and new home inventories which resulted in an industry-wide softening of demand for new homes. As a result of these factors, we are experiencing slower sales and higher cancellations which have impacted most of our markets and therefore, we are making greater use of sales incentives. We cannot predict the duration or the severity of the current market conditions, nor provide any assurances that the adjustments we have made in our operating strategy to address these conditions will be successful.

If the market value of our land and homes drops significantly, our profits could decrease.

The market value of land, building lots and housing inventories can fluctuate significantly as a result of changing market conditions and the measures we employ to manage inventory risk may not be adequate to insulate our operations from a severe drop in inventory values. We acquire land for expansion into new markets and for replacement of land inventory and expansion within our current markets. If housing demand decreases below what we anticipated when we acquired our inventory, we may not be able to make profits similar to what we have made in the past, we may experience less than anticipated profits and/or we may not be able to recover our costs when we sell and build homes. When market conditions are such that land values are not appreciating, option arrangements previously entered into may become less desirable, at which time we may elect to forego deposits and pre-acquisition costs and terminate the agreement. In the face of adverse market conditions, we may have substantial inventory carrying costs, we may have to write-down our inventory to its fair value, and/or we may have to sell land or homes at a loss.

As a result of the changing market conditions in the real estate industry which occurred during the year ended December 31, 2006, our land inventories and communities under development demonstrated impairment indicators which were evaluated for potential impairment. Consequently, we recorded land and community valuation adjustments of $203.8 million to reduce the carrying value of the impaired projects to their estimated fair values and we also recorded $95.4 million of land and community valuation adjustments related to our unconsolidated joint ventures. In addition, we recorded $54.6 million of net realizable value adjustments to land held for sale and $151.2 million for the write-off of deposits and pre-acquisition costs for land option contracts we no longer plan to pursue. It is possible that the estimated cash flows from these projects may change and could result in a future need to record additional valuation or net realizable adjustments. Additionally, if conditions in the homebuilding industry worsen in the future, we may be required to evaluate additional projects for potential impairment which may result in additional valuation and net realizable value adjustments which could be significant.

Our success depends on our ability to acquire land suitable for residential homebuilding at reasonable prices, in accordance with our land investment criteria.

The homebuilding industry is highly competitive for suitable land. The availability of finished and partially finished developed lots and undeveloped land for purchase that meet our internal criteria depends on a number of factors outside our control, including land availability in general, competition with other homebuilders and land buyers for desirable property, inflation in land prices, and zoning, allowable housing density and other regulatory requirements. Should suitable lots or land become less available, the number of homes we may be able to build and sell could be reduced, and the cost of land could be increased, perhaps substantially, which could adversely impact our results of operations.

Our long-term ability to build homes depends on our acquiring land suitable for residential building at reasonable prices in locations where we want to build. Over the past few years, we have experienced an increase in competition for suitable land as a result of land constraints in many of our markets. As competition for suitable land increases, and as available land is developed, the cost of acquiring suitable remaining land could rise, and the availability of suitable land at acceptable prices may decline. Any land shortages or any decrease in the supply of suitable land at reasonable prices could limit our ability to develop new communities or result in increased land costs. We may not be able to pass through to our customers any increased land costs, which could adversely impact our revenues, earnings, and margins.

Future increases in interest rates, reductions in mortgage availability or increases in the effective costs of owning a home could prevent potential customers from buying our homes and adversely affect our business or our financial results.

Most of our customers finance their home purchases through our mortgage bank. Interest rates have been at historical lows for several years. Many homebuyers have also chosen adjustable rate, interest only or mortgages that involve initial lower monthly payments. As a result, new homes have been more affordable. Increases in interest rates or decreases in availability of mortgage financing, however, could reduce the market for new homes. Potential homebuyers may be less willing or able to pay the increased monthly costs or to obtain mortgage financing that exposes them to interest rate changes. Lenders may increase the qualifications needed for mortgages or adjust their terms to address any increased credit risk. Even if potential customers do not need financing, changes in interest rates and mortgage availability could make it harder for them to sell their current homes to potential buyers who need financing. These factors could adversely affect the sales or pricing of our homes and could also reduce the volume or margins in our financial services business. Our financial services business could be impacted to the extent we are unable to match interest rates and amounts on loans we have committed to originate through the various hedging strategies we employ.

In addition, we believe that the availability of FHA and VA mortgage financing is an important factor in marketing some of our homes. We also believe that the liquidity provided by Fannie Mae and Freddie Mac to the mortgage industry is important to the housing market. However, the federal government has recently sought to reduce the size of the home-loan portfolios and operations of these two government-sponsored enterprises. Any limitations or restrictions on the availability of the financing or on the liquidity by them could adversely affect interest rates, mortgage financing and our sales of new homes and mortgage loans.

Our future growth may require additional capital, which may not be available.

Our operations require significant amounts of cash. We may be required to seek additional capital, whether from sales of equity or debt or additional bank borrowings, for the future growth and development of our business. We can give no assurance as to the availability of such additional capital or, if available, whether it would be on terms acceptable to us. Moreover, the indentures for most of our outstanding public debt and the covenants of our revolving credit facility contain provisions that may restrict the debt we may incur in the future. If we are not successful in obtaining sufficient capital, it could reduce our sales and may adversely affect our future growth and financial results.

Competition for homebuyers could reduce our deliveries or decrease our profitability.

The housing industry in the United States is highly competitive. We compete primarily on the basis of price, reputation, design, location and quality of our homes. We compete in each of our markets with numerous national, regional and local homebuilders. This competition with other homebuilders could reduce the number of homes we deliver, or cause us to accept reduced margins in order to maintain sales volume.

We also compete with resales of existing used or foreclosed homes, housing speculators and available rental housing. Increased competitive conditions in the residential resale or rental market in the regions where we operate could decrease demand for new homes and increase cancellations of sales contracts in backlog.

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Supply shortages and other risks related to the demand for skilled labor and building materials could increase costs and delay deliveries.

The homebuilding industry is highly competitive for skilled labor and materials. Increased costs or shortages of skilled labor and/or lumber, framing, concrete, steel and other building materials could cause increases in construction costs and construction delays. The current national debate related to immigration reform could impact the related laws and regulations in the markets in which we operate, and result in shortages of skilled labor and higher labor and compliance costs, potentially affecting our ability to complete construction and land development. We generally are unable to pass on increases in construction costs to those customers who have already entered into sale contracts, as those sales contracts generally fix the price of the home at the time the contract is signed, which may be well in advance of the construction of the home. Sustained increases in construction costs may, over time, erode our margins, and pricing competition for materials and labor may restrict our ability to pass on any additional costs, thereby decreasing our margins.

Government regulations could increase the cost and limit the availability of our development and homebuilding projects or affect our related financial services operations and adversely affect our business or financial results.

Our operations are subject to building, environmental and other regulations of various federal, state, and local governing authorities. For our homes to qualify for FHA or VA mortgages, we must satisfy valuation standards and site, material and construction requirements of those agencies. Our compliance with federal, state, and local laws relating to protection of the environment has had, to date, no material effect upon capital expenditures, earnings or competitive position. More stringent requirements could be imposed in the future on homebuilders and developers, thereby increasing the cost of compliance.

New housing developments may be subject to various assessments for schools, parks, streets and other public improvements. These can cause an increase in the effective prices for our homes. In addition, increases in property tax rates by local governmental authorities, as recently experienced in response to reduced federal and state funding, can adversely affect the ability of potential customers to obtain financing or their desire to purchase new homes.

We also are subject to a variety of local, state and federal laws and regulations concerning protection of health, safety and the environment. The impact of environmental laws varies depending upon the prior uses of the building site or adjoining properties and may be greater in areas with less supply where undeveloped land or desirable alternatives are less available. These matters may result in delays, may cause us to incur substantial compliance, remediation and other costs, and can prohibit or severely restrict development and homebuilding activity in environmentally sensitive regions or areas.

Our financial services operations are also subject to numerous federal, state and local laws and regulations. These include eligibility requirements for participation in federal loan programs and compliance with consumer lending and similar requirements such as disclosure requirements, prohibitions against discrimination and real estate settlement procedures. They may also subject our operations to examination by applicable agencies. These may limit our ability to provide mortgage financing or title services to potential purchasers of our homes.

Homebuilding is subject to warranty and liability claims in the ordinary course of business that can be significant.

As a homebuilder, we are subject to home warranty and construction defect claims arising in the ordinary course of business. We record warranty and other reserves for the homes we sell based on historical experience in our markets and our judgment of the qualitative risks associated with the types of homes built. We have, and require the majority of our subcontractors to have, general liability, property, errors and omissions, workers compensations and other business insurance. These insurance policies protect us against a portion of our risk of loss from claims, subject to certain self-insured retentions, deductibles, and other coverage limits. Through our captive insurance subsidiaries, we reserve for costs to cover our self-insured and deductible amounts under these policies and for any costs of claims and lawsuits, based on an analysis of our historical claims, which includes an estimate of claims incurred but not yet reported. Because of the uncertainties inherent to these matters, we cannot provide assurance that our insurance coverage, our subcontractor arrangements and our reserves will be adequate to address all our warranty and construction defect claims in the future. Contractual indemnities can be difficult to enforce, we may be responsible for applicable self-insured retentions and some types of claims may not be covered by insurance or may exceed applicable coverage limits. Additionally, the coverage offered by and the availability of general liability insurance for construction defects are currently limited and costly. We have responded to the recent increases in insurance costs and coverage limitations by increasing our self-insured retentions and claim reserves. There can be no assurance that coverage will not be further restricted and become more costly.

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Natural disasters and severe weather conditions could delay deliveries, increase costs and decrease demand for new homes in affected areas.

Our homebuilding operations are located in many areas that are subject to natural disasters and severe weather. The occurrence of natural disasters or severe weather conditions can delay new home deliveries, increase costs by damaging inventories, reduce the availability of materials and negatively impact the demand for new homes in affected areas. Furthermore, if our insurance does not fully cover business interruptions or losses resulting from these events, our earnings, liquidity or capital resources could be adversely affected.

Inflation may result in increased costs that we may not be able to recoup if demand declines.

Inflation can have a long-term impact on us because increasing costs of land, materials and labor may require us to increase the sales prices of homes in order to maintain satisfactory margins. However, inflation is often accompanied by higher interest rates, which have a negative impact on housing demand, in which case we may not be able to raise home prices sufficiently to keep up with the rate of inflation and our margins could decrease.

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

A future terrorist attack against the United States could cause a sharp decrease in the number of new contracts signed for homes and an increase in the cancellation of existing contracts. Accordingly, adverse developments in the war on terrorism, future terrorist attacks against the United States, or increased domestic and international instability could adversely affect our business.

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ITEM 1B. UNRESOLVED STAFF COMMENTS

This Item is not applicable.

ITEM 2. PROPERTIES

Our homebuilding and corporate headquarters are located at 100 Bloomfield Hills Parkway, Bloomfield Hills, Michigan 48304, where we lease 155,392 square feet of office space. We lease 54,380 square feet of office space at 1230 West Washington Street, Tempe, Arizona 85281 for certain corporate and business services. Pulte Mortgage s offices are located at 7475 South Joliet Street, Englewood, Colorado 80112, 99 Inverness Drive East, Englewood, Colorado 80112, and 12300 East Arapahoe Road, Centennial, Colorado 80112. We lease approximately 61,436 square feet, 24,400 square feet and 43,050 square feet, respectively, of office space at these locations. Pulte Mortgage also leases 31,803 square feet of office space at 3700 Arco Corporate Drive, Charlotte, North Carolina 28273. Our homebuilding markets and mortgage branch operations generally lease office space for their day-to-day operations.

Because of the nature of our homebuilding operations, significant amounts of property are held as inventory in the ordinary course of our homebuilding business. Such properties are not included in response to this Item.

ITEM 3. LEGAL PROCEEDINGS

We are involved in various legal and governmental proceedings incidental to our continuing business operations, many involving claims related to certain construction defects. The consequences of these matters are not presently determinable but, in our opinion after consulting with legal counsel and taking into account insurance and reserves, the ultimate liability is not expected to have a material adverse impact on our results of operations, financial position or cash flows.

Storm Water Discharge Practices

In July 2006, one of our 50%-owned, unconsolidated joint ventures located in Northern California received a civil liability complaint from the Central Valley Regional Water Quality Control Board pursuant to the Clean Water Act and Sections 13376 and 13385 of the California Water Code. The complaint sought information about storm water discharge practices in connection with homebuilding projects completed or underway by our joint venture. Our joint venture entered into settlement negotiations with the Regional Board to resolve this matter. The final settlement imposes an administrative civil liability of $200,000 and requires the completion of a Supplemental Environmental Project (SEP) at a cost of not less than $500,000. As of December 31, 2006 our joint venture has accrued for costs associated with the resolution of this matter. Accordingly, we have recorded our 50% proportionate share of the joint venture loss at December 31, 2006.

In April 2004, we received a request for information from the United States Environmental Protection Agency (EPA) pursuant to Section 308 of the Clean Water Act. The request seeks information about storm water discharge practices in connection with homebuilding projects completed or underway by us. We have provided the EPA with this information. Although the matter has since been referred to the United States Department of Justice (DOJ) for enforcement, the EPA has asked that we engage in pre-filing negotiations to resolve the matter short of litigation. We are actively engaged in these negotiations. If the negotiations fail and the DOJ alleges that we have violated regulatory requirements applicable to storm water discharges, the government may seek injunctive relief and penalties. We believe that we have defenses to any such allegations. At this time, however, we can neither predict the outcome of this inquiry, nor can we currently estimate the costs that may be associated with its eventual resolution.

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ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

This Item is not applicable.

ITEM 4A. EXECUTIVE OFFICERS OF THE REGISTRANT

Set forth below is certain information with respect to our executive officers.

Name	Age	Position	Year Became An Officer
William J. Pulte	74	Chairman of the Board	1956
Richard J. Dugas, Jr.	41	President and Chief Executive Officer	2002
Steven C. Petruska	48	Executive Vice President and Chief Operating Officer	2004
Roger A. Cregg	50	Executive Vice President and Chief Financial Officer	1997
James R. Ellinghausen	48	Executive Vice President, Human Resources	2005
Peter J. Keane	41	Senior Vice President, Operations	2006
Steven M. Cook	48	Vice President, General Counsel and Secretary	2006
Vincent J. Frees	56	Vice President and Controller	1995
Gregory M. Nelson	51	Vice President and Assistant Secretary	1993
Bruce E. Robinson	45	Vice President and Treasurer	1998

The following is a brief account of the business experience of each officer during the past five years:

Mr. Pulte was appointed Chairman of the Board in December 2001. He has also served as Chairman of the Executive Committee of the Board of Directors since January 1999.

Mr. Dugas was appointed President and Chief Executive Officer in July 2003. Prior to that date, he served as Executive Vice President and Chief Operating Officer. He was appointed Chief Operating Officer in May 2002 and Executive Vice President in December 2002. Since 1994, he has served in a variety of management positions. Most recently, he was Coastal Region President with responsibility for our Georgia, North Carolina, South Carolina, and Tennessee operations.

Mr. Petruska was appointed Executive Vice President and Chief Operating Officer in January 2004. Since joining our company in 1984, he has held a number of management positions. Most recently, he was the President for both the Arizona Area and Nevada Area operations.

Mr. Cregg was appointed Executive Vice President in May 2003 and was named Chief Financial Officer effective January 1998.

Mr. Ellinghausen was appointed Executive Vice President, Human Resources in December 2006 and previously held the position of Senior Vice President, Human Resources since April 2005. Prior to joining our Company, Mr. Ellinghausen held the position of Head of Human Resources for Bristol-Meyers Squibb Company Worldwide Businesses and was employed by Bristol-Meyers Squibb Company since 1997.

Mr. Keane was appointed Senior Vice President, Operations, in January 2006. He joined Pulte in 1993 and has served in a variety of management positions, mostly in the Midwest region. Most recently, he was the President of the Great Lakes Area.

Mr. Cook was appointed Vice President, General Counsel and Secretary in February 2006. Prior to joining our Company, Mr. Cook most recently held the position of Vice President and Deputy General Counsel, Corporate, at Sears Holdings Corporation and was employed by Sears, Roebuck and Co. since 1996.

Mr. Frees has been Vice President and Controller since May 1995.

Mr. Nelson has been Vice President and Assistant Secretary since August 1993.

Mr. Robinson has been Vice President and Treasurer since July 1998.

There is no family relationship between any of the officers. Each officer serves at the pleasure of the Board of Directors.

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PART II

ITEM 5. MARKET FOR THE REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common shares are listed on the New York Stock Exchange (Symbol: PHM).

Related Stockholder Matters

The table below sets forth, for the quarterly periods indicated, the range of high and low closing prices and cash dividends declared per share.

	2006			2005		
	High	**Low**	**Declared Dividends**	**High**	**Low**	**Declared Dividends**
1st Quarter	$40.72	$36.04	$.04	$39.69	$30.07	$.025
2nd Quarter	37.05	26.56	.04	42.89	33.74	.025
3rd Quarter	33.23	27.53	.04	47.83	41.36	.040
4th Quarter	34.80	28.29	.04	43.16	35.15	.040

At December 31, 2006, there were 1,868 shareholders of record.

Issuer Purchases of Equity Securities (1)

	(a) Total Number of shares purchased (2)	(b) Average price paid per share (2)	(c) Total number of shares purchased as part of publicly announced plans or programs	(d) Approximate dollar value of shares that may yet be purchased under the plans or programs ($000 s omitted)
October 1, 2006 to October 31, 2006				$ 102,342(1)
November 1, 2006 to November 30, 2006				$ 102,342(1)
December 1, 2006 to December 31, 2006	83,944	$ 33.33		$ 102,342(1)
Total	83,944	$ 33.33		$ 102,342(1)

(1) Pursuant to the two $100 million stock repurchase programs authorized and announced by our Board of

Directors in October 2002 and 2005 and the $200 million stock repurchase authorized and announced in February 2006 (for a total stock repurchase authorization of $400 million), the Company has repurchased a total of 9,688,900 shares for a total of $297.7 million. There are no expiration dates for the programs.

(2) During December 2006, 83,944 shares were surrendered by employees for payment of minimum tax obligations upon the vesting of restricted stock, and were not repurchased as part of our publicly announced stock repurchase programs.

Performance Graph

The following line graph compares for the fiscal years ended December 31, 2002, 2003, 2004, 2005 and 2006 (a) the yearly cumulative total shareholder return (i.e. , the change in share price plus the cumulative amount of dividends, assuming dividend reinvestment, divided by the initial share price, expressed as a percentage) on Pulte s common shares, with (b) the cumulative total return of the Standard & Poor s 500 Stock Index, and with (c) the cumulative total return on the common stock of publicly-traded peer issuers we deem to be our principal competitors in the homebuilding line of business (assuming dividend reinvestment and weighted based on market capitalization at the beginning of each year):

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Performance Graph (continued)

COMPARISON OF FIVE YEAR CUMULATIVE TOTAL RETURN*
AMONG PULTE HOMES, INC., S&P 500 INDEX AND PEER INDEX
Fiscal Year Ended December 31, 2006
Assumes Initial Investment of $100

	2001	2002	2003	2004	2005	2006
PULTE HOMES INC	100.00	107.52	210.71	288.24	356.80	301.69
S&P500 Index - Total Return	100.00	77.89	100.23	111.13	116.57	134.98
PEER Only**	100.00	99.15	212.78	276.06	324.53	254.49

* Assumes $100 invested on December 31, 2001, and the reinvestment of dividends.

** Includes Centex Corporation, D.R. Horton Inc., Hovnanian Enterprises, Inc., KB Home, Lennar Corporation, The Ryland Group, Inc., Standard Pacific Corporation and Toll Brothers, Inc.

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ITEM 6. SELECTED FINANCIAL DATA

Set forth below is selected consolidated financial data for each of the past five fiscal years. The selected financial data should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and our Consolidated Financial Statements and Notes thereto included elsewhere in this report.

	Years Ended December 31, ($000 s omitted)				
	2006	**2005**	**2004**	**2003**	**2002**
OPERATING DATA:					
Homebuilding:					
Revenues	$ 14,075,248	$ 14,528,236	$ 11,400,008	$ 8,701,661	$ 7,167,915
Income before income taxes	$ 1,010,368	$ 2,298,822	$ 1,635,580	$ 1,000,513	$ 717,931
Financial Services:					
Revenues	$ 194,596	$ 161,414	$ 112,719	$ 115,847	$ 106,628
Income before income taxes	$ 115,460	$ 70,586	$ 47,429	$ 68,846	$ 66,723
Other non-operating:					
Revenues	$ 4,564	$ 4,885	$ 1,749	$ 3,281	$ 1,202
Loss before income taxes	$ (43,100)	$ (92,394)	$ (90,685)	$ (75,351)	$ (61,968)
Consolidated results:					
Revenues	$ 14,274,408	$ 14,694,535	$ 11,514,476	$ 8,820,789	$ 7,275,745
Income from continuing operations before income taxes	$ 1,082,728	$ 2,277,014	$ 1,592,324	$ 994,008	$ 722,686
Income taxes	393,082	840,126	598,751	376,460	280,587
Income from continuing operations	689,646	1,436,888	993,573	617,548	442,099
Income (loss) from discontinued operations *(a)*	(2,175)	55,025	(7,032)	7,086	11,546
Net income	$ 687,471	$ 1,491,913	$ 986,541	$ 624,634	$ 453,645
PER SHARE DATA:					
Earnings per share basic:					
Income from continuing operations	$ 2.73	$ 5.62	$ 3.93	$ 2.53	$ 1.83
Income (loss) from discontinued operations *(a)*	(.01)	.22	(.03)	.03	.05

Net income	$ 2.73	$ 5.84	$ 3.91	$ 2.56	$ 1.88
Weighted-average common shares outstanding (000 s omitted)	252,200	255,492	252,590	244,323	241,812
Earnings per share assuming dilution:					
Income from continuing operations	$ 2.67	$ 5.47	$ 3.82	$ 2.46	$ 1.79
Income (loss) from discontinued operations *(a)*	(.01)	.21	(.03)	.03	.05
Net income	$ 2.66	$ 5.68	$ 3.79	$ 2.48	$ 1.84
Weighted-average common shares outstanding and effect of dilutive securities (000 s omitted)	258,621	262,801	260,234	251,460	246,985
Shareholders equity	$ 25.76	$ 23.18	$ 17.68	$ 13.78	$ 11.29
Cash dividends declared	$ .16	$ .13	$ .10	$ .05	$ .04

(a) Income (loss) from discontinued operations is comprised of our former thrift operation and Argentina and Mexico homebuilding operations which have been presented as discontinued operations for all periods presented.

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ITEM 6. SELECTED FINANCIAL DATA (continued)

	December 31, ($000 s omitted)				
	2006	2005	2004	2003	2002
BALANCE SHEET DATA:					
House and land inventories	$ 9,374,335	$ 8,756,093	$ 7,241,350	$5,378,125	$4,175,170
Total assets	13,176,874	13,060,860	10,406,897	8,072,151	6,872,087
Senior notes	3,537,947	3,386,527	2,861,550	2,150,972	1,913,268
Shareholders equity	6,577,361	5,957,342	4,522,274	3,448,123	2,760,426

	Years Ended December 31,				
	2006	2005	2004	2003	2002
OTHER DATA:					
Homebuilding:					
Total markets, at year-end	52	54	45	44	44
Total active communities	690	662	626	535	460
Total settlements units	41,487	45,630	38,612	32,693	28,903
Total net new orders units *(a)*	33,925	47,531	40,576	34,989	30,830
Backlog units, at year-end	10,255	17,817	15,916	13,952	10,605
Average unit selling price	$337,000	$315,000	$287,000	$259,000	$242,000
Gross profit margin from home sales *(b)*	17.4%	23.4%	22.6%	20.6%	19.4%

(a) *Total net new orders-units for the year ended December 31, 2003 does not include 1,051 units of acquired backlog.*

(b) *Homebuilding interest expense, which represents the amortization of capitalized interest, is included in homebuilding cost of sales.*

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ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

During the year ended December 31, 2006, the U.S. housing market was impacted by a lack of consumer confidence, decreased housing affordability, and large supplies of resale and new home inventories and related pricing pressures. These factors contributed to weakened demand for new homes, slower sales, higher cancellation rates, and increased price discounts and selling incentives to attract homebuyers, compared with the years ended December 31, 2005 and 2004, when we had experienced record growth in our homebuilding operations. As a result, gross margins recorded during the year ended December 31, 2006 decreased from the same periods in the prior years. From time to time, we write-off deposit and pre-acquisiton costs related to land and lot option contracts which we no longer plan to pursue. As a result of changing market conditions during the year ended December 31, 2006, we wrote-off deposit and pre-acquisition costs of $151.2 million related to land transactions we no longer plan to pursue. Additionally, during the year ended December 31, 2006, we recorded land valuation and net realizable value adjustments of $353.8 million, including our investment in unconsolidated joint ventures, to reduce the carrying value of these assets to fair value. Our evaluation for these adjustments assumed our best estimate of cash flows for the communities tested. If conditions in the homebuilding industry worsen in the future, we may be required to evaluate for additional impairment, resulting in additional impairment charges that could be significant.

We continue to operate our business with the expectation that these difficult market conditions will continue to impact us for at least the near term. We have adjusted our approach to land acquisition and construction practices, continuing to shorten our land pipeline, reduce production volumes, and balance home price and profitability with sales pace. We are slowing down planned land purchases and reducing our total number of controlled lots owned and under option. Additionally, we are reducing the number of spec homes put into production. However, we continue to purchase select land positions where it makes economic and strategic sense to do so. We believe that these measures will help to strengthen our market position and allow us to take advantage of opportunities that will develop in the future.

The following is a summary of our operating results for the years ended December 31, 2006, 2005 and 2004 ($000 s omitted):

	Years Ended December 31,		
	2006	2005	2004
Pre-tax income (loss):			
Homebuilding	$ 1,010,368	$ 2,298,822	$ 1,635,580
Financial Services	115,460	70,586	47,429
Other non-operating	(43,100)	(92,394)	(90,685)
Income from continuing operations before income taxes	1,082,728	2,277,014	1,592,324
Income taxes	393,082	840,126	598,751
Income from continuing operations	689,646	1,436,888	993,573
Income (loss) from discontinued operations	(2,175)	55,025	(7,032)
Net income	$ 687,471	$ 1,491,913	$ 986,541
Per share data assuming dilution:			
Income from continuing operations	$ 2.67	$ 5.47	$ 3.82

Income (loss) from discontinued operations		(.01)		.21		(.03)
Net income	$	2.66	$	5.68	$	3.79

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Overview (continued)

The following is a comparison of pre-tax income for the years ended December 31, 2006, 2005 and 2004:

During 2006, demand for new homes weakened in many of our markets as a result of increases in the supply of existing homes for sale, increases in incentives offered by homebuilders and sellers of existing homes and increases in cancellation rates. These factors negatively impacted the homebuilding industry and contributed to a 56% decrease in the pre-tax income of our homebuilding operations for the year ended December 31, 2006, compared with the prior year period. During 2005, strong demand for new homes in many of our markets as well as geographic and product mix shifts contributed to a 41% increase in the pre-tax income of our homebui1ding operations for the year ended December 31, 2005, compared with the prior year period. For the year ended December 31, 2006, pre-tax income was negatively impacted by $505 million of valuation adjustments recorded to land inventory ($203.8 million) and land held for sale ($54.6 million), our investment in unconsolidated joint ventures ($95.4 million) and the write-off of deposits and pre-acquisition costs ($151.2 million) related to land option contracts we no longer plan to pursue due to declining market conditions in the homebuilding industry.

Pre-tax income from our financial services business segment increased 64% for the year ended December 31, 2006, compared with the prior year period due to increased origination volume, favorable product mix and a one-time gain of $31.6 million related to the sale of our investment in Su Casita, a Mexican mortgage banking company. Pre-tax income increased 49% for the year ended December 31, 2005 compared with the prior year period. Capture rates were 91%, 89% and 88% for the years ended December 31, 2006, 2005 and 2004, respectively.

The decrease in non-operating expenses for the year ended December 31, 2006, compared with the same period in the prior year, was due primarily to an increase in the amount of interest capitalized into homebuilding inventory.

Loss from discontinued operations included a provision of $2.3 million, net of taxes for the year ended December 31, 2006, resulting from a contractual adjustment related to the December 2005 disposition of our Mexico homebuilding operations. Income from discontinued operations for the year ended December 31, 2005 includes a $48.7 million payment received due to final judgment in litigation related to our former thrift operation. Income (loss) from discontinued operations also includes non-cash, after-tax gains of $7.8 million and $10.8 million realized during the years ended December 31, 2005 and 2004, respectively, from the favorable resolution of certain tax matters related to our former thrift operation. For the year ended December 31, 2004, the sale of our Argentina homebuilding operations is included in discontinued operations.

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Homebuilding Operations

The following table presents a summary of pre-tax income for our Homebuilding operations ($000 s omitted):

	Year Ended December 31,		
	2006	**2005**	**2004**
Home sale revenue (settlements)	$ 13,975,387	$ 14,370,667	$ 11,094,617
Land sale revenue	99,861	157,569	305,391
Home cost of sales *(a)*	(11,544,905)	(11,005,591)	(8,583,551)
Land cost of sales *(b)*	(138,528)	(139,377)	(205,589)
Selling, general and administrative expenses	(1,136,027)	(1,107,816)	(973,629)
Equity income (loss) *(c)*	(95,244)	72,604	53,908
Other income (expense), net *(d)*	(150,176)	(49,234)	(55,567)
Pre-tax income	$ 1,010,368	$ 2,298,822	$ 1,635,580
Unit settlements	41,487	45,630	38,612
Average selling price	$ 337	$ 315	$ 287
Net new orders:			
Units	33,925	47,531	40,576
Dollars	$ 11,253,000	$ 15,518,000	$ 12,101,000
Backlog at December 31:			
Units	10,255	17,817	15,916
Dollars	$ 3,580,000	$ 6,301,000	$ 5,154,000

(a) *Includes homebuilding interest expense which represents the amortization of capitalized interest; land and community valuation adjustments of $203.8 million, $7.7 million and $0 for the years ended December 31, 2006, 2005 and 2004, respectively.*

(b)

Includes net realizable value adjustments for land held for sale of $54.6 million, $3.1 million and $265,000 for the years ended December 31, 2006, 2005 and 2004, respectively.

(c) *Includes land and community valuation adjustments for two of our unconsolidated joint ventures, which totaled $95.4 million for the year ended December 31, 2006.*

(d) *Includes the write-off of deposits and pre-acquisition costs for land option contracts we no longer plan to pursue of $151.2 million, $19.2 million and $27 million for the years ended December 31, 2006, 2005 and 2004, respectively. For the year ended December 31, 2006, other income* *(expense) also includes $18.5 million related to the closure of our production facility in Virginia.*

Home sale revenues for the year ended December 31, 2006 were lower than those for the prior year by approximately $395 million, or 3%. The decrease in homebuilding revenues was attributable to a 9% decrease in the number of homes closed to 41,487, partially offset by a 7% increase in the average selling price of homes delivered to $337,000. The increase in average selling price reflects a combination of changes in product mix and geographic mix of homes closed during the year ended December 31, 2006. Home sale revenues set a record for the year ended December 31, 2005 at 45,630 units, an increase of 18% over the same period in 2004, while the 2005 average selling price for our homes increased 10% to $315,000, compared with 2004.

Homebuilding gross profit margins from home sales in 2006 decreased 600 basis points from 2005 to 17.4%, and in 2005 increased 80 basis points to 23.4% compared with 2004. The increase in homebuilding gross profit margins in 2005 is due to strong consumer demand, positive home pricing, favorable shifts in product and geographic mix, the benefits of leverage-buy purchasing activities and effective production and inventory management. During the fourth quarter of 2006, homebuilding gross profit margins were 11.0% compared with 22.3% and 22.7% in the same periods of 2005 and 2004, respectively. The significant decrease in gross profit margins during 2006 is attributable to the difficult market conditions and challenging sales environment where we have realized increased sales incentives and increased material and labor costs related to homes closed during the year. Additionally, during 2006, we identified communities under development that demonstrated potential impairment indicators which were evaluated for potential impairment in accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* (SFAS 144). Consequently, during the fourth quarter and year ended December 31, 2006, we recorded respective land valuation adjustments of $146 million and $203.8 million, which included capitalized interest of $16 million, to reduce the carrying value of the impaired projects to their estimated fair value. There were no significant land valuation adjustments recorded during the years ended December 31, 2005 and 2004.

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Homebuilding Operations (continued)

We consider land acquisition and development to be one of our core competencies. We acquire land primarily for the construction of our homes for sale to homebuyers. We select locations for development of homebuilding communities after completing extensive market research, enabling us to match the location and product offering with our targeted consumer group. Where we develop land, we engage directly in many phases of the development process, including land and site planning, obtaining environmental and other regulatory approvals, as well as constructing roads, sewers, water and drainage facilities and other amenities. We will often sell select parcels of land within or adjacent to our communities to retail and commercial establishments. We also will, on occasion, sell lots within our communities to other homebuilders. Gross profit (loss) from land sales was ($38.7) million, $18.2 million and $99.8 million for the years ended December 31, 2006, 2005 and 2004, respectively. Revenues and their related gains/losses may vary significantly between periods, depending on the timing of land sales. We continue to evaluate our existing land positions to ensure the most effective use of capital. Land held for disposition was approximately $465.8 million as of December 31, 2006, compared with $257.7 million and $230.1 million at December 31, 2005 and 2004, respectively. During the fourth quarter and year ended December 31, 2006, we recorded net realizable value adjustments for land held for sale of $25.8 million and $54.6 million, respectively. There were no significant net realizable value adjustments for land held for sale during the years ended December 31, 2005 and 2004.

For the year ended December 31, 2006, selling, general and administrative expenses, as a percentage of home settlement revenues, increased 40 basis points to 8.1% compared with 2005, after decreasing 110 basis points to 7.7% in 2005 compared with 2004. The decreased conversion in 2006 compared with the prior year was the result of lower home sale revenues, offset by our internal initiatives focused on controlling costs in the current business environment. The conversion improvement in 2005, compared with 2004, can be attributed to an increase in average selling prices, our internal initiatives focused on controlling costs and better overhead leverage as a result of volume increases.

The decrease in equity income of $167.8 million for the year ended December 31, 2006, compared with the prior year period, is primarily the result of a $95.4 million land valuation adjustment for two of our unconsolidated joint ventures, to reduce the carrying values of these investments to their estimated fair values. Additionally, the decrease in 2006 equity income, compared with the prior year, is also the result of our January 2006 acquisition of the remaining 50% interest in an entity that supplies and installs basic building components and operating systems. As a result of this acquisition, we own 100% of this entity, which is consolidated in our financial statements. For the year ended December 31, 2005 and 2004, earnings for this investment were recorded in equity income. In addition, earnings from our 50% investment in a Nevada-based joint venture, related to the sale of commercial and residential properties, decreased in 2006 as the venture substantially completed its operations in 2005.

Other income (expense), net includes the write-off of deposits and pre-acquisition costs resulting from decisions not to pursue certain land acquisitions and options, insurance-related expenses and settlements and other non-operating expenses. The changes in other income (expense), net are due primarily to write-offs of deposit and pre-acquisition costs during the fourth quarter of 2006, 2005 and 2004 of $82.7 million, $6.2 million and $13.8 million, respectively, and for the years ended December 31, 2006, 2005 and 2004 of $151.2 million, $19.2 million and $27 million, respectively. These write-offs vary in amount from year to year as we continue to evaluate potential land acquisitions for the most effective use of capital. During the fourth quarter and year ended December 31, 2006 we recorded an $18.5 million charge related to the closure of a production facility located in Virginia.

Unit settlements decreased 9% for the year ended December 31, 2006 to 41,487 units, compared with the same period in 2005 and increased 18% for the year ended December 31, 2005 to 45,630 units, compared with the same period in 2004. The average selling price for homes closed for the years ended December 31, 2006, 2005 and 2004 was $337,000, $315,000 and $287,000, respectively. Changes in average selling price reflect a number of factors, including changes in market selling prices and the mix of product closed during each period.

For the year ended December 31, 2006, unit net new orders decreased 29% to 33,925 units, compared with the same period in 2005. For the year ended December 31, 2005, unit net new orders increased 17% to 47,531 units, compared with the same period in 2004. During 2006, net new orders were impacted by the closeout of several large, established communities, where the replacement communities are still in the early phases of development. In addition, rising home prices, higher interest rates, and increased resale home inventories have negatively affected demand for new homes. Cancellation rates for the fourth quarter of 2006 were approximately 34.7%, compared with 22.7% and 25.7% for the same periods in 2005 and 2004, respectively. Year to date cancellation rates were 29.4% for the year ended December 31, 2006, compared with 17.3% and 17.6% for the same periods in 2005 and 2004, respectively. Most markets have experienced a substantial increase in resale home inventory, and this, combined with declining consumer confidence, has resulted in higher cancellation rates and reduced net new orders during 2006.

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Homebuilding Operations (continued)

The dollar value of net new orders decreased 28% for the year ended December 31, 2006 compared with the prior year period and increased 28% for the year ended December 31, 2005 compared with the same period in 2004. However, while net new order dollars decreased during 2006, average selling prices increased or remained stable in many of our markets, primarily as a result of favorable shifts in product and geographic mix. For the year ended December 31, 2006, we had 690 active selling communities, an increase of 4% from the same period in 2005. For the year ended December 31, 2005, we had 662 active selling communities, an increase of 6% from the same period in 2004. Ending backlog, which represents orders for homes that have not yet closed, was 10,255 units at December 31, 2006 with a dollar value of $3.6 billion. Ending backlog was 17,817 units at December 31, 2005 with a dollar value of $6.3 billion.

At December 31, 2006 and 2005, our Homebuilding operations controlled approximately 232,200 and 362,600 lots, respectively. Approximately 158,800 and 173,800 lots were owned, and approximately 63,700 and 133,400 lots were under option agreements approved for purchase at December 31, 2006 and 2005, respectively. In addition, there were approximately 9,700 and 55,400 lots under option agreements, pending approval, at December 31, 2006 and 2005, respectively. For the fourth quarter and year ended December 31, 2006, we withdrew from land contracts representing approximately 37,500 lots and 95,200 lots, respectively, valued at $1.2 billion and $3.8 billion, respectively. We believe that the depth of our existing land supply, coupled with our entitlement expertise, will enable us to continue opening new communities during the course of 2007 and beyond.

The total purchase price related to approved land under option for use by our Homebuilding operations at future dates approximated $3.9 billion at December 31, 2006. In addition, total purchase price related to land under option pending approval was valued at approximately $450.3 million at December 31, 2006. Land option agreements, which may be cancelled at our discretion, may extend over several years and are secured by deposits and advanced costs totaling $369.5 million, of which $5.4 million is refundable and $12.9 million is related to deposits that our Homebuilding operations have made in regards to lots optioned from an unconsolidated joint venture in which we have an equity interest. This balance excludes $98.7 million of contingent payment obligations which may or may not become actual obligations of the Company.

The following table presents markets that represent 10% or more of unit new orders, unit settlements, and settlement revenues for the years ended December 31, 2006, 2005 and 2004:

	Year Ended December 31,		
	2006	**2005**	**2004**
Unit net new orders:			
Phoenix	12%	10%	16%
Unit settlements:			
Phoenix	11%	12%	14%
Las Vegas	11%	*	*
Settlement revenues:			
Phoenix	12%	11%	12%
Las Vegas	12%	*	12%

* *Represents less than 10%.*

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Homebuilding Segment Operations

The Homebuilding operations represent our core business. Homebuilding offers a broad product line to meet the needs of first-time, first and second move-up, and active adult homebuyers. We have determined our operating segments to be our Areas, which are aggregated into seven reportable segments based on similarities in the economic and geographic characteristics of our homebuilding operations. We conduct our operations in 52 markets, located throughout 27 states, and have presented our reportable homebuilding segments as follows:

Northeast:	Northeast and Mid-Atlantic Areas include the following states: *Connecticut, Delaware, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Virginia*
Southeast:	Southeast Area includes the following states: *Georgia, North Carolina, South Carolina, Tennessee*
Florida:	Florida Area includes the following state: *Florida*
Midwest:	Great Lakes Area includes the following states: *Illinois, Indiana, Michigan, Ohio, Minnesota*
Central:	Rocky Mountain and Central Areas include the following states: *Colorado, Kansas, Missouri, Texas*
Southwest:	Southwest and Nevada Areas include the following states: *Arizona, Nevada, New Mexico*
*California:	Northern California and Southern California Areas include the following state: *California*

* *Our homebuilding operations located in Reno, Nevada are reported in the California segment, while our remaining Nevada homebuilding operations are reported in the Southwest segment.*

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Homebuilding Segment Operations (continued)
The following table presents selected financial information for our homebuilding reporting segments:

	Year Ended December 31,		
	2006	2005	2004
Home sale revenue (settlements) ($000 s omitted):			
Northeast	$ 1,650,129	$ 1,856,906	$ 1,435,532
Southeast	1,254,337	950,792	758,994
Florida	2,209,864	2,247,513	1,270,797
Midwest	1,270,072	1,757,842	1,592,804
Central	1,264,318	1,090,914	938,966
Southwest	3,694,571	3,259,913	2,945,918
California	2,632,096	3,206,787	2,151,606
	$ 13,975,387	$ 14,370,667	$ 11,094,617
Income (loss) before income taxes ($000 s omitted):			
Northeast	$ 127,376	$ 326,399	$ 267,494
Southeast	88,162	86,683	53,502
Florida	381,924	475,939	198,975
Midwest	(37,327)	149,063	175,845
Central	(37,330)	1,729	45,736
Southwest	714,185	745,163	647,179
California	107,368	654,940	379,765
Unallocated *(a)*	(333,990)	(141,094)	(132,916)
	$ 1,010,368	$ 2,298,822	$ 1,635,580
Unit settlements:			
Northeast	3,489	3,909	3,249
Southeast	4,504	4,127	3,719
Florida	7,374	8,784	5,643
Midwest	4,171	5,879	5,315
Central	6,192	6,424	5,576
Southwest	10,548	10,237	10,179
California	5,209	6,270	4,931
	41,487	45,630	38,612
Net new orders units:			
Northeast	2,813	4,019	3,197
Southeast	4,632	4,888	3,896
Florida	4,501	8,383	7,045

Midwest	4,087	5,928	5,219
Central	5,437	7,549	5,568
Southwest	8,365	10,723	10,353
California	4,090	6,041	5,298
	33,925	47,531	40,576
Unit backlog:			
Northeast	917	1,593	1,483
Southeast	1,708	1,580	819
Florida	1,212	4,085	4,486
Midwest	1,199	1,283	1,234
Central	1,320	2,075	950
Southwest	2,719	4,902	4,416
California	1,180	2,299	2,528
	10,255	17,817	15,916

(a) Unallocated primarily includes amortization of capitalized interest of $255.7 million, $179.6 million and $133 million for the years ended December 31, 2006, 2005 and 2004, respectively, and other costs which are not allocated to the operating segments reported above.

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Homebuilding Segment Operations (continued)

	Year Ended December 31,		
	2006	**2005**	**2004**
Controlled Lots:			
Northeast	27,524	44,088	41,405
Southeast	23,332	31,863	22,926
Florida	48,640	70,434	73,799
Midwest	18,436	36,334	38,578
Central	22,966	39,331	42,572
Southwest	66,034	97,290	82,630
California	25,291	43,275	41,508
	232,223	362,615	343,418
Land and community valuation adjustments ($000 s omitted):			
Northeast	$ 22,206	$	$
Southeast	1,083		
Florida	22,715		
Midwest	52,555	4,000	
Central	23,866	3,718	
Southwest	9,774		
California	55,569		
Total segment land and community valuation adjustments	187,768	7,718	
Corporate and unallocated *(a)*	16,000		
Total valuation adjustments	$ 203,768	$ 7,718	$
Net realizable value adjustments (NRV) land held for sale ($000 s omitted):			
Northeast	$ 3,204	$	$
Southeast		14	
Florida	5,596		
Midwest	10,789	314	
Central	27,674	2,756	265
Southwest	7,014		
California	293		
Total NRV adjustments land held for sale	$ 54,570	$ 3,084	$ 265
Write-off of deposits and pre-acquisition costs ($000 s omitted):			
Northeast	$ 33,798	$ 2,931	$ 2,811
Southeast	4,514	2,194	1,617
Florida	25,108	1,119	1,573
Midwest	24,892	4,065	5,263

Central	10,739	5,292	3,248
Southwest	21,013	2,283	2,444
California	33,102	2,548	10,047
Total segment write-off of deposits and pre-acquisition costs	153,166	20,432	27,003
Corporate and unallocated	(1,981)	(1,237)	
Total write-off of deposits and pre-acquisition costs	$ 151,185	$ 19,195	$ 27,003

(a) Corporate and unallocated includes a $16 million write-off of capitalized interest related to land and community valuation adjustments recorded during 2006.

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Homebuilding Segment Operations (continued)

Northeast:

For the year ended December 31, 2006, our Northeast operations experienced weakened demand for new homes primarily as a result of increases in existing home inventories. Net new orders for the fourth quarter of 2006 decreased 11% to 623 units, and for the year ended December 31, 2006 decreased 30% to 2,813 units, compared with the same periods in 2005. During 2006, increased cancellation rates were attributable to lower new order sign-up activity and increased cancellations in all markets. For the fourth quarter of 2006 cancellation rates were approximately 25% compared with 19% for the same period in 2005. Cancellation rates for fiscal year 2006 were 22%, compared with 14% for the same period in 2005. For the fourth quarter and year ended December 31, 2006, operating results were negatively impacted by $12.2 million and $22.2 million of respective land valuation adjustments taken in our New England markets as well as higher sales incentives offered to homebuyers. During 2006, we also recorded $3.2 million of net realizable value adjustments for land held for sale. During the fourth quarter and year ended December 31, 2006, we wrote-off $17.7 million and $33.8 million, respectively, of deposits and pre-acquisition costs associated with transactions we no longer plan to pursue, resulting in a reduction of lots controlled of approximately 6,800 and 12,900, respectively. There were no significant land valuation adjustments or write-offs taken during the same periods in 2005 and 2004.

For the year ended December 31, 2005, our Northeast operations contributed positively to our Homebuilding operating results with increased revenues and higher average selling prices and profits compared with 2004. During 2005, most of the markets in the Northeast experienced strong demand conditions, particularly in Lehigh Valley and Baltimore, which were offset by increased resale inventories and pricing pressures in Washington D.C. Net new orders increased 26% to 4,019 units for the year ended December 31, 2005 compared with the same period in 2004. However, during the fourth quarter of 2005, net new orders decreased 10% to 697 units compared with the fourth quarter of 2004. For the year ended December 31, 2005, cancellation rates were approximately 14% compared with 11% for the same period in 2004. Cancellation rates for the fourth quarter of 2005 increased to 19% compared with 14% for the same period in 2004. As of December 31, 2005, we had 99 active selling communities, compared with 78 as of December 31, 2004. In addition, the year-over-year comparability of our Northeast operations was affected by a significant land sale ($19.4 million of income before income taxes) in our Washington D.C. market during the year ended December 31, 2004.

Southeast:

During the fourth quarter and year ended December 31, 2006, our Southeast operations contributed positively to our Homebuilding operating results, evidenced by increased revenues and unit settlements as well as higher average selling prices and profits compared with prior year periods. The increases in the Southeast s profitability are attributable to a continued shift in product mix associated with the active adult homebuyer. Additionally, we opened a new large active adult community in Charlotte during 2006. Net new orders for the fourth quarter of 2006 decreased 27% to 715 units, and for the year ended December 31, 2006 decreased 5% to 4,632 units, compared with the same periods in 2005. The reduction in new orders during the fourth quarter and year ended December 31, 2006 contributed to the increase in cancellation rates. Cancellation rates for the fourth quarter of 2006 were approximately 35%, compared with 23% for the same periods in 2005, while cancellation rates were 24% for the year ended December 31, 2006, compared with 18% for the same period in 2005. During 2006, selling, general and administrative expenses decreased as we continue to align our operations to meet current market conditions. There were no significant land related valuation adjustments or write-offs taken during 2006, 2005 or 2004 in our Southeast markets.

Most of the markets in the Southeast experienced strong demand conditions during 2005. Additionally, during 2005 we opened several new communities, including two new active adult communities in Atlanta and Raleigh. As of December 31, 2005, we had 64 active selling communities, compared with 74 as of December 31, 2004. For the year ended December 31, 2005, net new orders increased 26% to 4,888 units compared with the same period in 2004. Net new orders for the fourth quarter of 2005 increased 7% to 976 units, compared with the same periods in 2004. Cancellation rates for the year ended December 31, 2005 were approximately 18%, which was comparable with the same period in 2004. For the fourth quarter and year ended 2005, our Carolina operating results were negatively impacted by $7 million of lot cost adjustments recorded primarily in Hilton Head.

Homebuilding Segment Operations (continued)

Florida:

During 2006, our Florida operations experienced weakened demand, largely attributable to increased existing home inventories, especially in Orlando and Naples/Ft. Myers. During the fourth quarter and year ended December 31, 2006, Florida experienced high cancellation rates and pricing pressures associated with excess inventories and aggressive sales incentives offered by competitors. Net new orders for the fourth quarter of 2006 decreased 51% to 769 units, and for the year ended December 31, 2006 decreased 46% to 4,501 units, compared with the same periods in 2005. For the fourth quarter and year ended December 31, 2006, increased cancellation rates were attributable to lower new order sign-up activity and increased cancellations in all Florida markets. For the fourth quarter of 2006, cancellation rates were approximately 40% compared with 17% for the same period in 2005, while cancellation rates for the year ended December 31, 2006 were approximately 31% compared with 12% for the same period in 2005. Selling, general and administrative expenses decreased during 2006, as we continue to align our operations to meet current market conditions. During the fourth quarter and year ended December 31, 2006, we recorded valuation adjustments of $21.7 million and $22.7 million, respectively, related to land inventory. During the fourth quarter and year ended December 31, 2006, we also recorded charges of $17.6 million and $25.1 million, respectively, for the write-off of deposits and pre-acquisition costs associated with transactions we no longer plan to pursue in Jacksonville and Southeast Florida. During the fourth quarter and year ended December 31, 2006, these charges resulted in a reduction of lots controlled of approximately 3,800 and 10,500, respectively. There were no significant land valuation adjustments or write-offs taken during the same periods in 2005 and 2004.

During the year ended December 31, 2005, our Florida operations had increased revenues and higher average selling prices and profits compared with the same period in 2004. As of December 31, 2005, we had 73 active selling communities, compared with 65 as of December 31, 2004. For the year ended December 31, 2005, net new orders increased 19% to 8,383 units compared with 2004. During the fourth quarter of 2005, net new orders decreased 20% to 1,577 units compared with the prior year quarter, due primarily to a decreased community count of approximately 20% in Tampa and the fact that we were transitioning out of a recently completed active adult community in Ocala. Additionally, some of our Florida operations began to experience weakened demand for new homes due to excess resale inventories and pricing pressures in Orlando and Naples/Ft. Myers. At December 31, 2005 unit backlog decreased 9% to 4,085 units compared with the same period in 2004. Cancellation rates for the year ended December 31, 2005 were approximately 12%, which was comparable with 2004. In addition, for the year ended December 31, 2004, our Florida operations were affected by land sales (totaling $14.4 million of income before income taxes), which occurred primarily in our Tampa and Jacksonville markets.

Midwest:

The Midwest operations have been one of the most challenged areas in the country as Cleveland and Michigan continue to experience weakened demand due to difficult local economic conditions. Net new orders for the fourth quarter of 2006 decreased 40% to 749 units, and for the year ended December 31, 2006 decreased 31% to 4,087 units, compared with the same periods in 2005. During 2006, reduced new order sign-up activity resulted in higher cancellation rates. For the fourth quarter of 2006 cancellation rates were approximately 22% compared with 18% for the same period in 2005, while cancellation rates for the year ended December 31, 2006 were approximately 17% compared with 13% for the same periods in 2005. For the fourth quarter and year ended December 31, 2006, Midwest operating results were negatively impacted by land and community valuation adjustments of $32.6 million and $52.6 million, respectively. During the fourth quarter and year ended December 31, 2006 we recorded net realizable value adjustments for land held for sale of $5.1 million and $10.8 million, respectively. During the fourth quarter and year ended December 31, 2006, we recorded charges of $9 million and $24.9 million, respectively, for the write-off of deposits and pre-acquisition costs associated with transactions we no longer plan to pursue in the Michigan, Minnesota and Indianapolis markets, resulting in a reduction of lots controlled of 3,600 and 11,800, respectively. There were no significant land valuation and net realizable adjustments or write-offs taken during the same periods in 2005 and 2004.

For the year ended December 31, 2005, our Midwest operations realized increased revenues compared with the same period in 2004, primarily due to higher unit settlements. During the year ended December 31, 2005 average selling prices and profits decreased compared with the same period in 2004. During 2005, some of our Midwest operations were impacted by weakened demand for new homes due to increased resale home inventories and challenging local economic conditions, especially in Michigan. However, other Midwest operations, such as Illinois, Indianapolis and Ohio experienced solid demand, as evidenced by increased net new orders. For the year ended December 31, 2005, net new orders increased 14% to 5,928 units compared with 2004. During the fourth quarter of 2005, net new orders increased 11% to 1,240 units compared with the prior year period. In 2005, we opened large active adult communities in Detroit and Cleveland which contributed to the 2005 increase in net new orders. Cancellation rates for the year ended December 31, 2005 were approximately 13%, compared with 16% for the same periods in 2004.

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Homebuilding Segment Operations (continued)

Central:

For the year ended December 31, 2006, revenue from home settlements increased compared with the same period in 2005. Higher average selling prices realized during 2006 were the result of unit settlements in new communities in both Texas and Colorado. However, the Central reporting segment recorded losses for both the fourth quarter and year ended December 31, 2006, compared with profits during the same period in 2005, which was largely attributable to decreased home settlements. Net new orders for the fourth quarter of 2006 decreased 50% to 895 units, and for the year ended December 31, 2006 decreased 28% to 5,437 units, compared with the same periods in 2005. For the fourth quarter of 2006 cancellation rates were approximately 38% compared with 31% for the same period in 2005, while cancellation rates for the year ended December 31, 2006 were approximately 30% compared with 23% for the same period in 2005. During 2006 and 2005, Central operating results were negatively impacted by valuation adjustments to land inventory, net realizable value adjustments and write-offs of deposits and pre-acquisition costs associated with transactions we no longer plan to pursue. We recorded valuation adjustments to land inventory of $15.1 million and $3.1 million during the fourth quarter of 2006 and 2005, respectively, and $23.9 million and $3.7 million during the years ended December 31, 2006 and 2005, respectively. We also recorded net realizable value adjustments on land held for sale of $8.1 million and $2.5 million during the fourth quarter of 2006 and 2005, respectively, and $27.7 million and $2.8 million during the years ended December 31, 2006 and 2005, respectively. There were no significant land valuation and net realizable adjustments or write-offs taken during the same periods in 2004.

For the year ended December 31, 2005, our Central operations realized increased revenues primarily due to higher unit settlements, compared with the same period in 2004. During the year ended December 31, 2005 average selling prices increased compared with the same period in 2004, and net new orders increased 36% to 7,549 units compared with the same period in 2004. During the fourth quarter of 2005, net new orders increased 53% to 1,801 units compared with the prior year period. During 2005, we realized increases in net new orders in Houston and San Antonio as well as Denver, which experienced significant increases from the successful grand opening of a large traditional/active adult community in November 2005. For the year ended December 31, 2005, our Central operations were negatively impacted by a shift in product mix as well as delays in the opening of certain new communities, compared with the prior year period for 2004. Cancellation rates for the year ended December 31, 2005 were approximately 23%, compared with 29% for the same period in 2004. For the fourth quarter of 2005, the cancellation rate was 31%, compared with 38% for the same period in 2004.

Southwest:

The Southwest operations continued to contribute positively to our Homebuilding operating results, evidenced by increased revenues, unit settlements and higher average selling prices compared with 2005. Net new orders for the fourth quarter of 2006 decreased 28% to 1,755 units, and for the year ended December 31, 2006 decreased 22% to 8,365 units, compared with the same periods in 2005. During 2006, reduced new order sign-up activity resulted in higher cancellation rates. For the fourth quarter of 2006 cancellation rates were approximately 37%, compared with 19% for the same period in 2005, while cancellation rates for the year ended December 31, 2006 were approximately 35%, compared with 16% for the same period in 2005. Operating results for the Southwest segment were positively impacted by our January 2006 acquisition of the remaining 50% interest in an entity that supplies and installs basic building components and operating systems in both Arizona and Nevada. During 2005 and 2004, income from this entity was recorded as equity income and had no impact on segment pre-tax income. However, during the fourth quarter and year ended December 31, 2006, operating results were negatively impacted by land valuation and net realizable adjustments and the write-off of deposits and pre-acquisition costs. For the fourth quarter and year ended December 31, 2006, we recorded land and community valuation adjustments for both periods of $9.8 million, as well as net realizable value adjustments for land held for sale of $6.9 million and $7 million, respectively. During the fourth quarter and year ended December 31, 2006, we also recorded charges of $11.9 million and $21 million, respectively, for the write-off of deposits and pre-acquisition costs associated with transactions we no longer plan to pursue, primarily in the Phoenix and Tucson markets, which resulted in a reduction of lots controlled of 7,600 and 21,200, respectively. There were no significant land valuation and net realizable adjustments or write-offs taken during the same periods in 2005 and 2004.

Homebuilding Segment Operations (continued)

Southwest (continued):

During the year ended December 31, 2005, our Southwest operations contributed positively to our Homebuilding operating results, evidenced by increased revenues and higher average selling prices and profits compared with 2004. For the year ended December 31, 2005, net new orders increased 4% to 10,723 units compared with the same period in 2004. During the fourth quarter of 2005, net new orders increased 33% to 2,447 units compared with the prior year period. As of December 31, 2005, the decrease in Arizona s active community count, compared with the prior year, is attributable to the close-out of several communities, including a large, established active adult community located in Phoenix. We opened two large active adult communities, also located in Phoenix, during the first quarter of 2006 as replacement communities. In the fourth quarter of 2004, we lowered pricing in Las Vegas to better align pricing in our communities with pricing in the market. This action was in response to a period of slow sign-ups and increased cancellation rates, which we attributed to our then above-market pricing. After the price reductions took effect in the fourth quarter of 2004, our communities in Las Vegas experienced improved traffic and new order activity during 2005. Cancellation rates in the Southwest for the year ended December 31, 2005 were approximately 16%, which was comparable with the same period in 2004. During the fourth quarter of 2005, cancellation rates were 19% compared with 34% during the same period in 2004.

California:

The California operations were impacted by weakened demand for new homes, evidenced by increased resale inventories and pricing pressures, especially in Sacramento. During 2006, these factors contributed to a decrease in net new orders, unit settlements and average selling prices in California. Net new orders for the fourth quarter of 2006 decreased 13% to 940 units, and for the year ended December 31, 2006 decreased 32% to 4,090 units, compared with the same periods in 2005. During 2006, reduced new order sign-up activity resulted in higher cancellation rates. For the fourth quarter of 2006 cancellation rates were approximately 35% compared with 31% for the same period in 2005 while cancellation rates for the year ended December 31, 2006 were approximately 36% compared with 24% for the same period in 2005. California operating results were impacted during the fourth quarter and year ended December 31, 2006 by valuation adjustments to land inventory of $37.5 million and $55.6 million, respectively, in addition to a $95.4 million land valuation adjustment recorded during the fourth quarter of 2006 for two of our unconsolidated joint ventures located in Sacramento. During the fourth quarter and year ended December 31, 2006, we also recorded charges of $18.8 million and $33.1 million, respectively, for the write-off of deposits and pre-acquisition costs associated with transactions we no longer plan to pursue primarily in the Sacramento and the San Francisco Bay Area markets, which resulted in a reduction of lots controlled of 9,200 and 19,300, respectively. There were no significant land valuation and net realizable adjustments or write-offs taken during the same periods in 2005 and 2004.

During the year ended December 31, 2005, our California operations contributed positively to our Homebuilding operating results, evidenced by increased revenues and higher average selling prices and profits compared with 2004. For the year ended December 31, 2005, net new orders increased 14% to 6,041 units compared with the same period in 2004. For the fourth quarter of 2005, net new orders decreased 6% to 1,083 units compared with the prior year period. At December 31, 2005, unit backlog decreased 9% to 2,299 units compared with December 31, 2004. During the fourth quarter of 2005, our California operations were impacted by weakened demand for new homes evidenced by increased resale inventories and pricing pressures, especially in Sacramento. In addition, the closeout of a large, successful active adult community which contributed significantly to our operations impacted the California reporting segment during the fourth quarter of 2005 and contributed to the decrease in net new orders, unit settlements and average selling price during this period. Cancellation rates for the year ended December 31, 2005 were approximately 24%, compared with 15% for the year ended December 31, 2004.

Financial Services Operations

We conduct our financial services business, which includes mortgage and title operations, through Pulte Mortgage and other subsidiaries.

We originate mortgage loans using our own funds or borrowings made available through various credit arrangements, and then sell such mortgage loans monthly to outside investors. Also, we sell our servicing rights on a flow basis through fixed price servicing sales contracts. Due to the short period of time the servicing rights are held, we do not amortize the servicing asset. Since the servicing rights are recorded based on the value in the servicing sales contracts, there are no impairment issues related to these assets.

The following table presents mortgage origination data for our Financial Services operations:

	Years Ended December 31,		
	2006	**2005**	**2004**
Total originations:			
Loans	40,269	42,994	35,232
Principal ($000 s omitted)	$ 8,683,500	$ 8,528,600	$ 6,739,200
Originations for Pulte customers:			
Loans	40,117	42,302	32,290
Principal ($000 s omitted)	$ 8,642,900	$ 8,397,600	$ 6,268,100

Pre-tax income of our financial services operations was $115.5 million, $70.6 million, and $47.4 million for the years ended December 31, 2006, 2005 and 2004, respectively.

Mortgage origination unit volume decreased 6%, while mortgage origination principal volume increased 2% for the year ended December 31, 2006. The decrease in unit volume is attributable to lower home settlements in 2006 compared with 2005, offset by a higher capture rate in 2006 compared with 2005, while the increase in origination principal volume is attributable to a higher average loan size. For the year ended December 31, 2005, mortgage origination unit and principal volume increased 22% and 27%, respectively, over 2004. This growth can be attributed to increases in the capture rate of 140 basis points to 89.2% in 2005 combined with the volume increases experienced in our homebuilding business and an increase in average loan size. Our capture rate represents loan originations from our homebuilding business as a percent of total loan opportunities, excluding cash settlements, from our homebuilding business. Our homebuilding customers continue to account for the majority of total loan production, representing nearly 100% of Pulte Mortgage unit production for 2006, compared with 98% in 2005 and 92% in 2004.

Adjustable rate mortgages (ARMs) represented 28% of total funded origination dollars and 22% of total funded origination units for the year ended December 31, 2006, compared with 45% and 39%, respectively, in 2005 and 43% and 42%, respectively, in 2004. Interest only mortgages, a component of ARMs, represented 79% of ARMs origination dollars and 81% of ARMs origination units for the year ended December 31, 2006, compared with 65% and 56% in 2005, and 42% and 30%, respectively, in 2004. Interest only mortgages represented 22%, 29%, and 18%, respectively, of total funded origination dollars for the years ended December 31, 2006, 2005, and 2004.

Refinancings represented 1% of total loan production in 2006 and 2005, compared with 3% in 2004. Our customers average FICO scores for the years ended December 31, 2006, 2005, and 2004 were 743, 741, and 737, respectively. Combined Loan-to-Value was 82% for the year ended December 31, 2006, and 81% for the years ended December 31, 2005 and 2004, respectively. At December 31, 2006, loan application backlog was $2.1 billion, compared with $4.2 billion and $3.5 billion at December 31, 2005 and 2004, respectively.

Pre-tax income increased 64% for the year ended December 31, 2006, compared with 2005, primarily due to the sale of our investment in Su Casita, a Mexico-based mortgage banking company. As a result of this transaction, we recognized a pre-tax gain of approximately $31.6 million ($20.1 million after-tax). Excluding this gain, pre-tax income increased 19% in 2006 compared with 2005, due to the combination of increased origination principal volume and a shift in product mix to more profitable loans. In 2006, 21% of total origination dollars were from brokered loans, which are less profitable to us, compared with 26% in 2005. Mortgage origination fees of $15.5 million in 2006 were $5.2 million, or 25%, lower than the $20.7 million recorded for the same period in 2005. The 25% decrease over the same period in 2005 is due to a shift in product mix towards funded production.

Pre-tax income increased 49% for the year ended December 31, 2005, compared with 2004, due to increased volume and a favorable product mix shift to funded, from non-funded originations. In 2005, 26% of total origination dollars were from brokered loans, which are less profitable to us, compared with 36% in 2004. Mortgage origination fees of $20.7 million in 2005 were $0.2 million, or 1%, higher than the $20.5 million recorded for the same period in 2004. The 1% increase over the same period in 2004 is due to higher revenues per loan as brokered origination volume decreased 7% in 2005 when compared with 2004.

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Financial Services Operations (continued)

The net gain from sale of mortgages of $110.8 million in 2006 was $29.7 million, or 37%, higher than the $81.1 million recorded for the same period in 2005. This favorable variance was due primarily to an increase in loans available for sale combined with a favorable shift in product mix in 2006 when compared to 2005. Net interest income in 2006 was $9.8 million, or 2%, lower than the $10 million for the same period in 2005. The decrease was primarily due to a lower net interest margin partially offset by higher funded origination volume. Income from our title operations was $20 million in 2006, a decrease of 10% over 2005, due primarily to a decrease in the number of homes closed in 2006 compared to 2005. Selling, general and administrative expense increased $10.2 million, or 13%, from 2005, due primarily to higher operating expenses.

Our minority interest in Su Casita, a Mexican mortgage banking company, contributed income from operations of approximately $350 thousand for the year ended December 31, 2005. During February 2005, 25% of our investment in the capital stock of Su Casita was redeemed for a gain of approximately $620 thousand. Our remaining interest of 16.66% was accounted for under the cost method of accounting and therefore no income was recorded for periods subsequent to the sale. Income from Su Casita for the year ended December 31, 2004 was $4 million. In February 2006, we completed the sale of our remaining investment in Su Casita for approximately $50 million, and realized a pre-tax gain of approximately $31.6 million related to the transaction.

We hedge portions of our forecasted cash flow from sales of closed mortgage loans with derivative financial instruments. For the year ended December 31, 2006, we did not recognize any material net gains or losses related to an ineffective portion of the hedging instrument. We also did not recognize any material net gains or losses during 2005 for cash flow hedges that were discontinued because it is probable that the original forecasted transaction will not occur. At December 31, 2006, we expect to reclassify $978 thousand, net of taxes, of net gains on derivative instruments from accumulated other comprehensive income to earnings during the next twelve months as sales of mortgage backed securities occur.

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Other non-operating

Other non-operating expenses, net consists of income and expenses related to corporate services provided to our subsidiaries. These expenses are incurred for financing, developing and implementing strategic initiatives centered on new business development and operating efficiencies, and providing the necessary administrative support associated with being a publicly traded entity listed on the New York Stock Exchange. Accordingly, these results will vary from year to year as these strategic initiatives evolve.

The following table presents results of operations ($000 s omitted):

	Years Ended December 31,		
	2006	2005	2004
Net interest expense	$ 531	$ 43,344	$ 47,372
Other expenses, net	42,569	49,050	43,313
Loss before income taxes	$ 43,100	$ 92,394	$ 90,685

Net interest expense was $531 thousand for the year ended December 31, 2006, compared with approximately $43.3 million and $47.4 million for the years ended December 31, 2005 and 2004, respectively. These variances are the result of an increase in the amount of interest capitalized into homebuilding inventory.

Changes in other expenses, net for the years ended December 31, 2006 and 2005, compared with prior years were primarily due to changes in compensation-related costs. Additionally, during 2004 we recognized income from the sale and adjustment to fair value of various non-operating parcels of commercial land held for sale.

Interest capitalized into homebuilding inventory is charged to home cost of sales based on the cyclical timing of our unit settlements over a period that approximates the average life cycle of our communities. During 2006 and 2005, interest in homebuilding inventory increased compared with the prior years due to increased amounts of interest capitalized based on our homebuilding inventory and debt levels. In addition, during the fourth quarter of 2006, $16 million of capitalized interest related to inventory impairment write-offs was expensed. Information related to corporate interest capitalized into homebuilding inventory is as follows ($000 s omitted):

	Years Ended December 31,		
	2006	2005	2004
Interest in homebuilding inventory at beginning of year	$ 229,798	$ 223,591	$ 200,584
Interest capitalized into homebuilding inventory	261,486	185,792	156,056
Interest expensed to homebuilding cost of sales	(255,688)	(179,585)	(133,049)
Interest in homebuilding inventory at end of year	$ 235,596	$ 229,798	$ 223,591
Interest incurred *	$ 266,561	$ 234,024	$ 205,176

* *Interest incurred includes interest on our senior debt, short-term borrowings, and other financing arrangements and excludes*

interest incurred by our financial services operations.

Discontinued Operations

First Heights In September 2003, the United States Court of Federal Claims issued final judgment that Pulte Homes, Inc., Pulte Diversified Companies, Inc. and First Heights (collectively, the Pulte Parties) had been damaged by approximately $48.7 million as a result of the United States government s breach of contract with them. The final judgment follows the Court s August 17, 2001 ruling that the United States breached the contract related to the Pulte Parties 1988 acquisition of five savings and loan associations by enacting Section 13224 of the Omnibus Budget Reconciliation Act of 1993. The United States government and the Pulte Parties filed Notices of Appeal with the United States Court of Appeals for the Federal Circuit in October 2003.

In August 2005, the United States Court of Appeals affirmed the United States Court of Federal Claims judgment, in its entirety, that we had been damaged by approximately $48.7 million as a result of the United States government s breach of contract in connection with the enactment of Section 13224 of the Omnibus Budget Reconciliation Act of 1993. In December 2005, we received payment of the judgment in the amount of $48.7 million, which was recorded as income from discontinued operations.

In September 2005, First Heights received notice confirming the voluntary dissolution of the First Heights Bank. The Office of Thrift Supervision also canceled First Heights charter. Accordingly, the day-to-day activities of First Heights, which had been principally devoted to supporting residual regulatory compliance matters and the litigation with the United States government, have now ceased.

W e also recorded non-cash, after-tax gains of $7.8 million and $10.8 million, during the third quarter of 2005 and 2004, respectively, related to the favorable resolution of certain tax matters relating to our former thrift operation, which was discontinued in 1994.

Mexico In January 2005, the minority shareholders of Pulte Mexico S. de R.L. de C.V. (Pulte Mexico) exercised a put option under the terms of a reorganization agreement dated as of December 31, 2001, to sell their shares to us, the consummation of which resulted in our owning 100% of Pulte Mexico. In March 2005, we purchased 60% of the minority interest of Pulte Mexico for approximately $18.7 million in cash. In June 2005, we purchased the remaining 40% of the minority interest of Pulte Mexico for approximately $12.5 million in cash. We assigned approximately $17.6 million of the purchase price premium to house and land inventory, which was amortized through cost of sales as homes were sold. The excess of the purchase price over the estimated fair values of the underlying assets acquired and liabilities assumed, of $5.3 million, was recorded as goodwill.

In December 2005, we sold substantially all of our Mexico homebuilding operations to a consortium of purchasers involved in residential and commercial real estate development. The disposition of the Mexico homebuilding operations will allow us to invest additional resources in the U.S. housing market. We realized cash of $131.5 million related to the sale. The sale of these operations did not include our investment in the capital stock of a mortgage company in Mexico as well as various non-operating entities, which are not considered to be material to our results of operations or our financial position.

Revenues of these discontinued operations were $201 million and $185.8 million for the years ended December 31, 2005 and 2004, respectively. For the years ended December 31, 2005 and 2004, discontinued Mexico homebuilding operations reported total after-tax income (losses) of ($1.5) million and $4.4 million, respectively. Results of Mexico homebuilding operations, for the years ended December 31, 2005 and 2004, resulted in pre-tax operating income of $4.6 million and $8.2 million, respectively.

For the year ended December 31, 2005, we recognized a pre-tax loss of $6.6 million (after-tax loss of $13.1 million) related to the sale of our Mexico homebuilding operations. The pre-tax loss on sale includes the accounting recognition of the economic losses related to accumulated foreign currency translation adjustments of $7.6 million, which had previously been reported in other comprehensive income, as well as the write-off of $5.3 million of goodwill related to the 2005 acquisition of the minority shareholder interests. At December 31, 2005, the Mexico homebuilding operations have been presented as discontinued operations in our Consolidated Financial Statements, while previously they were included in our Homebuilding operations. Certain amounts previously reported in the 2004 financial statements and notes thereto were reclassified to conform to the 2005 presentation.

Concurrent with the sale of the Mexico homebuilding operations, we elected to repatriate all of our earnings from our Mexico operations in accordance with the American Jobs Creation Act of 2004 (Internal Revenue Code

Section 965, Temporary Dividends Received Deduction) and recorded $4.8 million of related income taxes, which have been included in the Mexico loss on sale from discontinued operations.

For the year ended December 31, 2006, loss from discontinued operations included a provision of $2.3 million, net of taxes, which resulted from a contractual adjustment related to the December 2005 disposition of the our Mexico homebuilding operations.

Discontinued Operations (continued)

Argentina In January 2005, we sold all of our Argentina operations to an Argentine company involved in residential and commercial real estate development. The disposition of these operations was intended to improve our overall returns. At December 31, 2004, the Argentina operations were classified as held for sale and presented as discontinued operations in our Consolidated Financial Statements, while previously they were included in our Homebuilding operations.

Revenues of these discontinued Argentine operations were $24.6 million for the year ended December 31, 2004. For the year ended December 31, 2004 discontinued Argentine operations reported total after-tax losses of $22 million. For the year ended December 31, 2004, the Argentina operations reported after-tax operating losses of $1.4 million. In addition, we recognized a pre-tax loss of $33.2 million ($20.6 million after-tax) on the write-down of the Argentina operations to fair value less costs to sell. The pre-tax loss includes the accounting recognition of the economic losses related to accumulated foreign currency translation adjustments of $25.1 million ($15.6 million after-tax), which had previously been reported in other comprehensive income.

For the year ended December 31, 2006, loss from discontinued operations included a provision of $111 thousand, net of taxes, which resulted from a contractual adjustment related to the January 2005 disposition of our Argentine operations.

Liquidity and Capital Resources

We finance our homebuilding land acquisition, development and construction activities by using internally generated funds and existing credit arrangements. We routinely monitor current operational requirements and financial market conditions to evaluate the use of available financing sources, including securities offerings.

At December 31, 2006, we had cash and equivalents of $551.3 million and $3.5 billion of senior notes outstanding. Other financing included non-recourse collateralized financing totaling $26.9 million. Sources of our working capital include our cash and equivalents, our $2.01 billion committed unsecured revolving credit facility and Pulte Mortgage s $955 million committed credit arrangements and other uncommitted borrowing arrangements.

Our ratio of debt-to-total capitalization, excluding our collateralized debt related to financial services, was approximately 35% at December 31, 2006, and approximately 31.2% net of cash and equivalents.

Pulte Mortgage provides mortgage financing for many of our home sales and uses its own funds and borrowings made available pursuant to various committed and uncommitted credit arrangements. At December 31, 2006, Pulte Mortgage had committed credit arrangements of $955 million, comprised of a $405 million bank revolving credit facility and a $550 million asset-backed commercial paper program. In May 2006, Pulte Mortgage amended its revolving credit facility, which included amendments to its restrictive covenants. In August 2006, Pulte Mortgage amended the bank credit agreement related to its asset-backed commercial paper program, which also included amendments to its restrictive covenants. Both amended credit agreements now require Pulte Mortgage to maintain a consolidated tangible net worth of at least $50 million or eighty-five percent of the average month-end tangible net worth for the last twelve months of the preceding calendar year and funded debt cannot exceed 15 times tangible net worth.

Our income tax liability and related effective tax rate are affected by a number of factors. In 2006, our effective tax rate was 36.3% compared with 36.9% in 2005 and 37.6% in 2004. The reduction in the effective tax rate for 2006 was primarily due to an adjustment for the Section 199 manufacturing deduction, a change in the overall state tax rate associated with the geographical mix in income and certain other tax matters. The reduction in the effective tax rate for 2005 was principally due to the Section 199 manufacturing deduction established by the American Jobs Creation Act of 2004. We anticipate that our effective tax rate for 2007 will be approximately 37%.

Our net cash used in operating activities for the year ended December 31, 2006 amounted to $267.5 million, while net cash provided by operating activities was $18.7 million for the year ended December 31, 2005. For the year ended December 31, 2004, net cash used in operating activities was $692.2 million. In 2006, decreased net income and an increase in deferred income taxes were offset by the write-down of land and deposits and pre-acquisition costs of $409.5 million. In 2005 and 2004, increased net income was offset primarily by significant investments in land inventory.

Liquidity and Capital Resources (continued)

Cash used in investing activities was $86.9 million for the year ended December 31, 2006, compared with $25.3 million and $198.6 million for the years ended December 31, 2005 and 2004, respectively. We invested approximately $65.8 million, net of cash acquired, to purchase the remaining 50% of an entity that installs basic building components and operating systems. In addition, we received cash of $49.2 million for the sale of our investment in Su Casita, a Mexico-based mortgage banking company. Also, we made $58.2 million of capital contributions to and received $67.4 million in capital distributions from our unconsolidated joint ventures for the year ended December 31, 2006. Further we incurred approximately $98.6 million in capital expenditures to support the growth of our business.

The change in net cash used in investing activities from 2004 to 2005 primarily relates to proceeds from the sale of subsidiaries during 2005 of $142.9 million, increases in distributions from unconsolidated entities of $41.9 million, offset by increases in capital expenditures of $13.7 million. During 2005, we invested approximately $37.3 million in three new joint ventures that develop and/or sell land within the United States. Also, we contributed $124.6 million of additional capital contributions to and received $108 million in capital distributions from our unconsolidated joint ventures for the year ended December 31, 2005. Further, we incurred approximately $88.9 million in capital expenditures to support the growth of our business. During January 2004, we invested $35 million for a 50% ownership in an entity that supplies and installs basic building components and operating systems. During 2004, we invested approximately $117.8 million in new joint ventures that develop and/or sell land in the United States. Also, we contributed $44.2 million of additional capital contributions to and received $66.1 million in capital distributions from our unconsolidated joint ventures for the year ended December 31, 2004.

Net cash used in financing activities totaled $96.2 million for the year ended December 31, 2006. Cash inflows from financing activities are primarily attributed to the issuance of $150 million, 7.375% senior notes and $8.4 million from the issuance of common stock. Cash outflows from financing activities are primarily attributed to $78.3 million repayment of Pulte Mortgage s collateralized short term debt, $19.8 million payment of non-recourse collateralized financing, $122.3 million used to repurchase our common stock, and $40.9 million of cash dividends paid to shareholders.

Net cash provided by financing activities was $700.4 million for the year ended December 31, 2005. Cash inflows from financing activities are primarily attributed to proceeds from our $350 million, 5.2% senior notes and $300 million, 6% senior notes issued in February 2005, proceeds from Pulte Mortgage s line of credit of approximately $275.6 million, proceeds from non-recourse collateralized financing arrangements of approximately $46.8 million, and proceeds from the exercise of stock options of $31.2 million. Cash outflows from financing activities for the year ended December 31, 2005 primarily relate to the repayment of our $125 million, 7.3% senior notes in October 2005, approximately $33.6 million of cash dividends paid to our shareholders, and $143.2 million used to repurchase our common stock.

Net cash provided by financing activities totaled $809.6 million for the year ended December 31, 2004. Cash inflows from financing activities for the year ended December 31, 2004 are primarily attributed to proceeds received from our $500 million, 5.25% senior notes issued in January 2004 and our $400 million, 4.875% senior notes issued in July 2004 and $44 million of cash received from the exercise of stock options. Cash outflows from financing activities for the year ended December 31, 2004 primarily relate to the repayment of our $112 million, 8.375% senior notes in August 2004, redemption of the remaining $77 million of Del Webb 10.25% senior subordinated notes in February 2004, approximately $25.4 million of cash dividends paid to our shareholders, $44.9 million used to repay borrowings, and $14.7 million used to repurchase our common stock.

In May 2006, we sold $150 million of 7.375% senior notes, which mature on June 1, 2046, which are guaranteed by us and certain of our 100%-owned subsidiaries. These notes are unsecured and rank equally with all of our other unsecured and unsubordinated indebtedness. The notes are redeemable at any time on or after June 1, 2011, at a redemption price equal to 100% of the principal amount to be redeemed, plus accrued and unpaid interest thereon to the redemption date. Proceeds from the sale were used to repay the indebtedness of our revolving credit facility and for general corporate purposes, including continued investment in our business.

In August 2006, we increased the borrowing availability under our 4-year unsecured revolving credit facility from $1.66 billion to $2.01 billion. The credit facility includes an uncommitted accordion feature, under which the credit facility may be increased to $2.25 billion. We have the capacity to issue letters of credit up to $1.125 billion. Borrowing availability is reduced by the amount of letters of credit outstanding. The credit facility contains restrictive covenants, the most restrictive of which requires us not to exceed a debt-to-total capitalization ratio of 60% and also requires us to maintain a minimum interest coverage ratio of 2:1 (EBITDA to interest incurred), as defined in the agreement. As of December 31, 2006, we had no borrowings outstanding and $1.45 billion available for borrowing under this facility.

Pursuant to the two $100 million stock repurchase programs authorized by our Board of Directors in October 2002 and 2005, and the $200 million stock repurchase authorization in February 2006 (for a total stock repurchase authorization of $400 million), we have repurchased a total of 9,688,900 shares for a total of $297.7 million. At December 31, 2006, we had remaining authorization to purchase $102.3 million of common stock.

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Liquidity and Capital Resources (continued)

Inflation

We, and the homebuilding industry in general, may be adversely affected during periods of high inflation because of higher land and construction costs. Inflation also increases our financing, labor and material costs. In addition, higher mortgage interest rates significantly affect the affordability of permanent mortgage financing to prospective homebuyers. We attempt to pass to our customers any increases in our costs through increased sales prices.

Contractual Obligations and Commercial Commitments

The following table summarizes our payments under contractual obligations as of December 31, 2006:

	Payments Due by Period ($000 s omitted)				
	Total	**2007**	**2008-2009**	**2010-2011**	**After 2011**
Contractual obligations:					
Long-term debt *(a)*	$ 6,703,950	$ 227,839	$ 855,678	$ 1,107,116	$ 4,513,317
Operating lease obligations	287,360	58,575	96,598	57,581	74,606
Other long-term liabilities *(b)*	27,295	19,945	7,350		
Total contractual obligations *(c)*	$ 7,018,605	$ 306,359	$ 959,626	$ 1,164,697	$ 4,587,923

(a) *Represents our senior notes and related interest payments*

(b) *Represents our non-recourse collateralized financing arrangements and related interest payments*

(c) *We do not have any payments due in connection with capital lease or purchase obligations*

We are subject to the usual obligations associated with entering into contracts (including option contracts) for the purchase, development and sale of real estate in the routine conduct of our business. Option contracts for the purchase of land enable us to defer acquiring portions of properties owned by third parties and unconsolidated entities until we are ready to build homes on them. This reduces our financial risks associated with long-term land holdings. At December 31, 2006, we had agreements to acquire approximately 71,800 homesites through option contracts and unconsolidated entities in which we have investments. At December 31, 2006, we had $369.5 million of non-refundable option deposits and advanced costs related to certain of these agreements.

The following table summarizes our other commercial commitments as of December 31, 2006:

	Amount of Commitment Expiration by Period ($000 s omitted)				
	Total	2007	2008-2009	2010-2011	After 2011
Other commercial commitments:					
Guarantor revolving credit facilities *(a)*	$ 2,010,000	$	$	$ 2,010,000	$
Non-guarantor revolving credit facilities *(b)*	955,000	550,000	405,000		
Standby letters of credit *(c)*	32,184	32,184			
Total commercial commitments *(d)*	$ 2,997,184	$ 582,184	$ 405,000	$ 2,010,000	$

(a) *Includes capacity to issue up to $1.125 billion in standby letters of credit, of which $559 million was outstanding at December 31, 2006.*

(b) *Includes credit facility of $405 million and $550 million asset-backed commercial paper program.*

(c) *Excludes standby letters of credit issued under the Guarantor revolving credit facilities.*

(d) *Excludes performance and surety bonds of approximately*

$1.8 billion, which typically do not have stated expiration dates.

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Off-Balance Sheet Arrangements

We use standby letters of credit and performance bonds to guarantee our performance under various contracts, principally in connection with the development of our projects. The expiration dates of the letter of credit contracts coincide with the expected completion date of the related homebuilding projects. If the obligations related to a project are ongoing, annual extensions of the letters of credit are typically granted on a year-to-year basis. At December