TECHNICAL OLYMPIC USA INC
Form 10-Q
November 09, 2005

Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q

(Mark One)

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended September 30, 2005

or

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from to

COMMISSION FILE NUMBER: 001-32322
TECHNICAL OLYMPIC USA, INC.
(Exact name of registrant as specified in its charter)

Delaware	**76-0460831**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*
4000 Hollywood Blvd., Suite 500 N Hollywood, Florida	**33021**
(Address of principal executive offices)	*(ZIP code)*

(954) 364-4000
(Registrant s telephone number, including area code)
(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes þ No o

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date: 59,536,227 shares of common stock as of November 4, 2005.

TECHNICAL OLYMPIC USA, INC.
INDEX

Table of Contents

PART I. Financial Information

ITEM 1. Financial Statements

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
(Dollars in millions, except shares and par value)

	September 30, 2005	December 31, 2004
	(Unaudited)	
ASSETS		
HOMEBUILDING:		
Cash and cash equivalents:		
Unrestricted	$ 43.2	$ 217.6
Restricted	3.1	8.0
Inventory:		
Deposits	199.4	132.8
Homesites and land under development	614.7	341.2
Residences completed and under construction	753.0	671.0
Inventory not owned	79.5	136.2
	1,646.6	1,281.2
Property and equipment, net	24.6	26.7
Investments in unconsolidated joint ventures	188.0	66.6
Receivables from unconsolidated joint ventures	80.3	3.4
Other assets	122.2	67.7
Goodwill	110.7	110.7
	2,218.7	1,781.9
FINANCIAL SERVICES:		
Cash and cash equivalents:		
Unrestricted	7.0	50.9
Restricted	75.7	69.1
Mortgage loans held for sale	64.0	75.8
Other assets	13.3	9.8
	160.0	205.6
Total assets	$ 2,378.7	$ 1,987.5
LIABILITIES AND STOCKHOLDERS EQUITY		
HOMEBUILDING:		
Accounts payable and other liabilities	$ 290.7	$ 188.9
Customer deposits	87.2	69.1
Obligations for inventory not owned	79.5	136.2
Notes payable	811.6	811.4
Bank borrowings	80.0	

		1,349.0		1,205.6
FINANCIAL SERVICES:				
Accounts payable and other liabilities		77.6		70.2
Bank borrowings		54.6		49.0
		132.2		119.2
Total liabilities		1,481.2		1,324.8
Stockholders equity:				
Preferred stock $0.01 par value; 3,000,000 shares authorized; none issued or outstanding				
Common stock $0.01 par value; 97,000,000 shares authorized and 59,536,227 and 56,070,510 shares issued and outstanding at September 30, 2005, and December 31, 2004, respectively		0.6		0.6
Additional paid-in capital		485.6		388.3
Unearned compensation		(11.5)		(9.0)
Retained earnings		422.8		282.8
Total stockholders equity		897.5		662.7
Total liabilities and stockholders equity	$	2,378.7	$	1,987.5

See accompanying notes to consolidated financial statements.

3

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(Dollars in millions, except share and per share amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	**2004**	**2005**	**2004**
		(Unaudited)		
HOMEBUILDING:				
Revenues:				
Home sales	$ 562.8	$ 500.1	$ 1,657.3	$ 1,369.3
Land sales	99.8	7.1	154.7	61.0
	662.6	507.2	1,812.0	1,430.3
Cost of sales:				
Home sales	407.5	398.8	1,256.7	1,104.4
Land sales	69.9	6.6	116.6	47.8
	477.4	405.4	1,373.3	1,152.2
Gross profit	185.2	101.8	438.7	278.1
Selling, general and administrative expenses	90.2	61.2	246.7	176.9
Other income:				
Income from joint ventures, net	(13.3)	(0.7)	(24.0)	(0.7)
Other (income) expense, net	(1.6)	(2.2)	(5.8)	(2.7)
Homebuilding pretax income	109.9	43.5	221.8	104.6
FINANCIAL SERVICES:				
Revenues	13.4	8.2	34.8	26.4
Expenses	10.4	7.6	28.1	20.0
Financial Services pretax income	3.0	0.6	6.7	6.4
Income before provision for income taxes	112.9	44.1	228.5	111.0
Provision for income taxes	42.6	16.0	86.1	40.8
Net income	$ 70.3	$ 28.1	$ 142.4	$ 70.2
EARNINGS PER COMMON SHARE:				
Basic	$ 1.24	$ 0.50	$ 2.53	$ 1.25
Diluted	$ 1.18	$ 0.49	$ 2.43	$ 1.23

WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING:								
Basic		56,753,826		56,064,565		56,304,544		56,056,943
Diluted		59,392,423		57,427,500		58,569,725		57,178,499
CASH DIVIDENDS PER SHARE	$	0.015	$	0.012	$	0.042	$	0.024

See accompanying notes to consolidated financial statements.

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in millions)

	Nine Months Ended September 30,	
	2005	**2004**
	(Unaudited)	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 142.4	$ 70.2
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	9.6	9.5
Non-cash compensation expense	7.6	4.0
Equity in earnings from unconsolidated subsidiaries	(8.9)	
Changes in operating assets and liabilities:		
Restricted cash	(1.7)	5.1
Inventory	(422.0)	(266.6)
Other assets	(113.9)	(13.2)
Accounts payable and other liabilities	105.5	3.5
Customer deposits	18.1	33.7
Mortgage loans held for sale	11.8	5.0
Net cash used in operating activities	(251.5)	(148.8)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net additions to property and equipment	(8.1)	(14.7)
Investments in unconsolidated joint ventures	(112.5)	(20.1)
Earn out consideration paid for acquisitions		(6.6)
Loans to unconsolidated joint ventures	(20.0)	
Net cash used in investing activities	(140.6)	(41.4)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net borrowings from revolving credit facilities	80.0	48.0
Proceeds from notes offerings		125.0
Net proceeds from equity offering	89.3	
Net proceeds from (repayments on) Financial Services bank borrowings	5.6	(5.1)
Payments for deferred financing costs	(0.3)	(2.1)
Dividends paid	(2.4)	(1.3)
Other	1.6	(6.5)
Net cash provided by financing activities	173.8	158.0
Decrease in cash and cash equivalents	(218.3)	(32.2)
Unrestricted cash and cash equivalents at beginning of period	268.5	76.8
Unrestricted cash and cash equivalents at end of period	$ 50.2	$ 44.6
SUPPLEMENTAL DISCLOSURE OF NON-CASH FINANCING ACTIVITY		

Decrease in obligations for inventory not owned and corresponding decrease in inventory	$	(56.7)	$	(44.6)

See accompanying notes to consolidated financial statements.

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2005

1. Business and Organization

Business

Technical Olympic USA, Inc. is a homebuilder with a geographically diversified national presence. We operate in 16 metropolitan markets located in four major geographic regions: Florida, the Mid-Atlantic, Texas, and the West. We design, build, and market detached single-family residences, townhomes and condominiums. We also provide title and mortgage brokerage services to our homebuyers and others. Generally, we do not retain or service the mortgages that we originate but, rather, sell the mortgages and related servicing rights to investors.

Organization

Technical Olympic S.A. owns approximately 67% of our outstanding common stock. Technical Olympic S.A. is a publicly-traded Greek company whose shares are traded on the Athens Stock Exchange.

2. Summary of Significant Accounting Policies

Basis of Presentation

The consolidated financial statements include our accounts and those of our subsidiaries. Our accounting and reporting policies conform to accounting principles generally accepted in the United States and general practices within the homebuilding industry. These accounting principles require management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

All significant intercompany balances and transactions have been eliminated in the consolidated financial statements.

Due to our normal operating cycle being in excess of one year, we present unclassified consolidated statements of financial condition.

We have two operating segments which are segregated in the accompanying consolidated financial statements under Homebuilding and Financial Services.

Certain prior period amounts have been reclassified to conform to the current period s presentation.

Interim Presentation

The accompanying unaudited consolidated financial statements reflect all adjustments, consisting primarily of normal recurring items that, in the opinion of management, are considered necessary for a fair presentation of the financial position, results from operations, and cash flows for the periods presented. Results of operations achieved through September 30, 2005 are not necessarily indicative of those that may be achieved for the year ending December 31, 2005. Certain information and footnote disclosures normally included in financial statements presented in accordance with accounting principles generally accepted in the United States have been omitted from the accompanying financial statements. The financial statements included as part of this Form 10-Q should be read in conjunction with the financial statements and notes thereto included in our December 31, 2004 Annual Report on Form 10-K.

For the three months ended September 30, 2005 and 2004, we have eliminated inter-segment Financial Services revenues of $2.7 million and $1.8 million, respectively. For the nine months ended September 30, 2005 and 2004, we have eliminated inter-segment Financial Services revenues of $6.5 million and $5.4 million, respectively.

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Earnings Per Share

Basic earnings per share is computed by dividing income available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share is computed based on the weighted average number of shares of common stock and dilutive securities outstanding during the period. Dilutive securities are options or other common stock equivalents that are freely exercisable into common stock at less than market prices. Dilutive securities are not included in the weighted average number of shares when inclusion would increase the earnings per share or decrease the loss per share.

The following table represents a reconciliation of weighted average shares outstanding:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	**2004**	**2005**	**2004**
Basic weighted average shares outstanding	56,753,826	56,064,565	56,304,544	56,056,943
Net effect of stock options assumed to be exercised	2,638,597	1,362,935	2,265,181	1,121,556
Diluted weighted average shares outstanding	59,392,423	57,427,500	58,569,725	57,178,499

The shares issued and outstanding and the earnings per share amounts in the consolidated financial statements have been adjusted to reflect a five-for-four stock split effected in the form of a 25% stock dividend paid on March 31, 2005.

On September 13, 2005, pursuant to an underwritten public offering, we sold 3,358,000 shares of our common stock at a price of $28.00 per share. The net proceeds of the offering to us were $89.3 million, after deducting offering costs and underwriting fees of $4.8 million. The offering proceeds were used to pay outstanding indebtedness under our revolving credit facility.

Stock-Based Compensation

We account for our stock option plan in accordance with the provisions of Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees,* and related interpretations. As such, compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeds the exercise price. We have adopted the disclosure-only provisions of Statement of Financial Accounting Standards (SFAS) No. 123, *Accounting for Stock-Based Compensation* (SFAS No. 123). Accordingly, no compensation cost has been recognized as all stock options granted under our stock option plan have exercise prices at or greater than the market value of our stock on the grant date. If the methodologies of SFAS No. 123 were applied to determine compensation expense for our stock options based on the fair value of our common stock at the grant dates for awards under our option plan, our net income and earnings per share for the three and nine months ended September 30,

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

2005 and 2004, would have been adjusted to the pro forma amounts indicated below (dollars in millions, except per share amounts):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
Net income as reported	$ 70.3	$ 28.1	$ 142.4	$ 70.2
Add: Stock-based employee compensation included in reported net income, net of tax	1.8	1.5	4.6	2.6
Deduct: Stock-based employee compensation expense determined under the fair value method, net of tax	(1.4)	(0.7)	(3.3)	(1.8)
Pro forma net income	$ 70.7	$ 28.9	$ 143.7	$ 71.0
Reported earnings per common share:				
Basic	$ 1.24	$ 0.50	$ 2.53	$ 1.25
Diluted	$ 1.18	$ 0.49	$ 2.43	$ 1.23
Pro forma earnings per common share:				
Basic	$ 1.24	$ 0.51	$ 2.55	$ 1.27
Diluted	$ 1.19	$ 0.50	$ 2.45	$ 1.24

The fair values of options granted were estimated on the date of their grant using the Black-Scholes option pricing model based on the following assumptions:

Expected life	4	10 years
Risk-free interest rate	1.47%	4.02%
Expected volatility	0.42%	0.48%
Expected dividend yield		0.0%

In December 2004, the FASB issued SFAS No. 123(R), *Share Based Payment*. SFAS No. 123(R) establishes accounting standards for transactions in which a company exchanges its equity instruments for goods or services. In particular, this Statement would require companies to record compensation expense for all share-based payments, such as employee stock options, at fair market value. This Statement is effective as of the beginning of the first annual reporting period that begins after June 15, 2005. As a result, beginning January 1, 2006, we will adopt SFAS 123(R) and begin reflecting the stock option expense determined under fair value based methods in our income statement rather than as pro forma disclosure in the notes to the financial statements. We expect the effect of adopting SFAS 123(R) to be similar to the effect represented in our proforma disclosure related to SFAS 123.

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

3. Inventory

A summary of Homebuilding interest capitalized in inventory is (dollars in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
Interest capitalized, beginning of period	$ 43.1	$ 35.7	$ 36.8	$ 29.7
Interest incurred	21.1	16.7	59.8	48.4
Less interest included in:				
Cost of sales	(16.5)	(12.6)	(48.9)	(36.1)
Other*	(4.3)	(1.4)	(4.3)	(3.6)
Interest capitalized, end of period	$ 43.4	$ 38.4	$ 43.4	$ 38.4

* Included in Other for the three and nine months ended September 30, 2005 is interest which was capitalized to inventory that was subsequently contributed to an unconsolidated joint venture.

In the ordinary course of business, we enter into contracts to purchase homesites and land held for development. At September 30, 2005 and December 31, 2004, we had refundable and nonrefundable deposits aggregating $199.4 million and $132.8 million, respectively, included in inventory in the accompanying consolidated statements of financial condition. Our liability for nonperformance under such contracts is generally limited to forfeiture of the related deposits.

In January 2003, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 46, *Consolidation of Variable Interest Entities* (Interpretation No. 46). Interpretation No. 46 addresses consolidation by business enterprises of variable interest entities (VIEs) in which an entity absorbs a majority of the expected losses, receives a majority of the entity s expected residual returns, or both, as a result of ownership, contractual or other financial interests in the entity.

Generally, homebuilders will enter into option contracts for the purchase of land or homesites with land sellers and third-party financial entities, some of which may qualify as VIEs. In applying Interpretation No. 46 to our homesite option contracts and other transactions with VIEs, we make estimates regarding cash flows and other assumptions. We believe that our critical assumptions underlying these estimates are reasonable based on historical evidence and industry practice. Based on our analysis of transactions entered into with VIEs, we determined that we are the primary beneficiary of certain of these homesite option contracts. Consequently, Interpretation No. 46 requires us to consolidate the assets (homesites) at their fair value, although (1) we have no legal title to the assets, (2) our maximum exposure to loss is generally limited to the deposits or letters of credits placed with these entities, and (3) creditors, if any, of these entities have no recourse against us. The effect of Interpretation No. 46 at September 30, 2005 was to increase inventory by $42.4 million, excluding deposits of $10.0 million, which had been previously recorded, with a corresponding increase to obligations for inventory not owned in the accompanying consolidated statement of financial condition. We have also entered into arrangements with VIEs to acquire homesites in which our variable interest is insignificant and, therefore, we have determined that we are not the primary beneficiary and are not required to consolidate the assets of such VIEs.

From time to time we transfer title to certain parcels of land to unrelated third parties and enter into options with the purchasers to acquire fully developed homesites. In accordance with SFAS No. 66, *Accounting for the Sales of*

Real Estate, we have accounted for these transactions as financing arrangements because we have retained a continuing involvement in these properties. As of September 30,

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

2005, $37.1 million of inventory not owned and obligations for inventory not owned related to sales with continuing involvement.

4. Investments in Unconsolidated Joint Ventures

Summarized condensed combined financial information of unconsolidated entities in which we have investments that are accounted for by the equity method is (dollars in millions):

	September 30, 2005		
	Land Development	Home Construction	Total
Assets:			
Cash	$ 13.4	$ 122.0	$ 135.4
Inventories	203.9	941.2	1,145.1
Other assets	3.6	230.4	234.0
Total assets	$ 220.9	$ 1,293.6	$ 1,514.5
Liabilities and equity:			
Accounts payable and other liabilities	$ 11.5	$ 194.1	$ 205.6
Notes payable	143.6	782.7	926.3
Equity of:			
Technical Olympic USA, Inc.	32.0	153.7	185.7
Others	33.8	163.1	196.9
Total equity	65.8	316.8	382.6
Total liabilities and equity	$ 220.9	$ 1,293.6	$ 1,514.5

	December 31, 2004		
	Land Development	Home Construction	Total
Assets:			
Cash	$ 1.4	$ 14.8	$ 16.2
Inventories	74.0	196.8	270.8
Other assets	1.4	8.4	9.8
Total assets	$ 76.8	$ 220.0	$ 296.8
Liabilities and equity:			

Accounts payable and other liabilities	$ 11.0	$ 10.0	$ 21.0
Notes payable	32.0	81.8	113.8
Equity of:			
Technical Olympic USA, Inc.	15.6	51.0	66.6
Others	18.2	77.2	95.4
Total equity	33.8	128.2	162.0
Total liabilities and equity	$ 76.8	$ 220.0	$ 296.8

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Three Months Ended September 30, 2005			Three Months Ended September 30, 2004		
	Land Development	Home Construction	Total	Land Development	Home Construction	Total
Revenues	$ 10.6	$ 169.1	$ 179.7	$ 8.9	$ 7.6	$ 16.5
Cost and expenses	11.4	158.4	169.8	7.8	7.1	14.9
Net earnings (losses) of unconsolidated entities	$ (0.8)	$ 10.7	$ 9.9	$ 1.1	$ 0.5	$ 1.6
Our share of net earnings (losses)	$ (0.6)	$ 5.7	$ 5.1	$ 0.0	$ 0.0	$ 0.0
Management fees earned	0.8	7.4	8.2	0.0	0.7	0.7
Income from joint ventures	$ 0.2	$ 13.1	$ 13.3	$ 0.0	$ 0.7	$ 0.7

	Nine Months Ended September 30, 2005			Nine Months Ended September 30, 2004		
	Land Development	Home Construction	Total	Land Development	Home Construction	Total
Revenues	$ 20.8	$ 272.5	$ 293.3	$ 11.9	$ 8.2	$ 20.1
Cost and expenses	23.2	251.3	274.5	10.9	7.8	18.7
Net earnings (losses) of unconsolidated entities	$ (2.4)	$ 21.2	$ 18.8	$ 1.0	$ 0.4	$ 1.4
Our share of net earnings (losses)	$ (1.4)	$ 10.3	$ 8.9	$ 0.0	$ 0.0	$ 0.0
Management fees earned	2.3	12.8	15.1	0.0	0.7	0.7
Income from joint ventures	$ 0.9	$ 23.1	$ 24.0	$ 0.0	$ 0.7	$ 0.7

We enter into strategic joint ventures to acquire, to develop and to sell land and/or homesites, as well as to construct and sell homes, in which we have a voting ownership interest of 50% or less and do not have a controlling interest. Our partners generally are unrelated homebuilders, land sellers, financial partners or other real estate entities. At September 30, 2005, we had receivables of $80.3 million from these joint ventures, of which $45.5 million represent notes receivable.

In many instances, we are appointed as the day-to-day manager of the unconsolidated entities and receive management fees for performing this function. We received management fees from the unconsolidated entities of

$8.2 million and $15.1 million for the three and nine months ended September 30, 2005, respectively. These fees are included in income from joint ventures in the accompanying consolidated statements of income. Management fees were $0.7 million during the three and nine months ended September 30, 2004 as our unconsolidated joint venture operations during these periods were insignificant. In the aggregate, these joint ventures delivered 528 and 872 homes for the three and nine months ended September 30, 2005, respectively.

On August 1, 2005, through a joint venture (the Transeastern JV), we completed the acquisition of the homebuilding assets and operations of Transeastern Properties, Inc. (Transeastern) headquartered in Coral Springs, Florida. Our joint venture partner is an entity controlled by the former majority owners of Transeastern. The Transeastern JV acquired Transeastern s homebuilding assets, including work in process, finished lots and certain land option rights, for approximately $826.2 million (which includes the assumption of $112.0 million of liabilities, net of $30.8 million of cash). Additional consideration of up to $75.0 million will be paid to the sellers pursuant to an earn out agreement if certain conditions are met, such as achieving predetermined quarterly EBITDA targets and delivery of entitlement on certain tracts of land currently held under lot option contracts. In addition to the net assets acquired in the transaction, the

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Transeastern JV will have a right of first offer on land developed by a related entity of our joint venture partner for a period of five years. We are the managing member of the Transeastern JV and hold a 50% voting interest. The Transeastern JV was funded with $675.0 million of third party debt capacity (of which $560.0 million was drawn upon acquisition), a $20.0 million subordinated bridge loan from us and $165.0 million of equity, of which $90.0 million was contributed by us. The third party debt is secured by the Transeastern JV s assets and ownership interests and is non-recourse to us.

5. Goodwill

The change in goodwill for the nine months ended September 30, 2005 and 2004 is as follows (dollars in millions):

	Nine Months Ended September 30,	
	2005	**2004**
Balance at January 1	$ 110.7	$ 100.1
Earn out consideration paid or accrued on acquisitions		6.6
Balance at September 30	$ 110.7	$ 106.7

6. Borrowings

Our revolving credit facility permits us to borrow to the lesser of (i) $600.0 million or (ii) our borrowing base (calculated in accordance with the revolving credit facility agreement) minus our outstanding senior debt. The facility has a letter of credit subfacility of $300.0 million. In addition, we have the right to increase the size of the facility to provide up to an additional $150.0 million of revolving loans, provided we satisfy certain conditions. Loans outstanding under the facility may be base rate loans or Eurodollar loans, at our election. Our obligations under the revolving credit facility are guaranteed by our material direct and indirect subsidiaries, other than our mortgage and title subsidiaries (unrestricted subsidiaries). The revolving credit facility expires on October 26, 2008. As of September 30, 2005, we had $80.0 million outstanding under the revolving credit facility, and had issued letters of credit totaling $177.1 million. Therefore as of September 30, 2005, we had $342.9 million remaining in availability, all of which we could have borrowed without violating any of our debt covenants.

Our mortgage subsidiary has the ability to borrow up to $120.0 million under two revolving warehouse lines of credit to fund the origination of residential mortgage loans. One of these warehouse lines can be increased to provide up to an additional $50.0 million of availability, subject to meeting certain requirements. One of the lines of credit bears interest at the 30 day LIBOR rate plus a margin of 1.25% to 3.0%, based upon the type of mortgage loans being financed, and the other bears interest at the 30 day Eurodollar rate plus a margin of 1.125%. Both warehouse lines of credit are secured by funded mortgages, which are pledged as collateral, and require our mortgage subsidiary to maintain certain financial ratios and minimums. Our primary warehouse line of credit was to expire on October 22, 2005 and has been extended until November 21, 2005. Our other warehouse line of credit expires December 15, 2005. As of September 30, 2005, we had $54.6 million in borrowings under our warehouse lines of credit.

7. Commitments and Contingencies

We are involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on our consolidated financial condition or results of operations.

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

We provide homebuyers with a one-year or two-year limited warranty of workmanship and materials, and an eight-year or ten-year limited warranty covering major structural defects. We generally have recourse against our subcontractors for claims relating to workmanship and materials. We also have a homebuilder protective policy which covers warranty claims for structure and design defects related to homes sold by us during the policy period, subject to a significant self-insured retention per occurrence. Estimated warranty costs are recorded at the time of sale based on historical experience and current factors.

During the nine months ended September 30, 2005 and 2004, changes in our warranty accrual consisted of (dollars in millions):

	Nine Months Ended September 30,	
	2005	2004
Accrued warranty costs at January 1	$ 6.4	$ 5.2
Liability recorded for warranties issued during the period	8.2	10.4
Warranty work performed	(6.1)	(5.7)
Adjustments	(1.5)	(3.6)
Accrued warranty costs at September 30	$ 7.0	$ 6.3

8. Stockholders Equity and Stock-Based Compensation

During 2001, we adopted the Technical Olympic USA, Inc. Annual and Long-Term Incentive Plan (the Plan) pursuant to which our employees, consultants and directors, and those of our subsidiaries and affiliated entities, are eligible to receive shares of restricted common stock and/or options to purchase shares of common stock. Under the Plan, subject to adjustment as defined, the maximum number of shares with respect to which awards may be granted is 7,500,000. At September 30, 2005, 6,644,110 options and 35,428 shares of restricted stock were outstanding. Of the stock options outstanding at September 30, 2005, 1,567,072 contain accelerated vesting criteria or other features that are being accounted for under the variable accounting method as provided by APB Opinion No. 25. Additionally, certain stock purchase rights have been granted to our chief executive officer that are subject to the variable accounting method. During the three and nine months ended September 30, 2005, we recognized expense of $2.9 million and $7.4 million, respectively, related to these accelerated vesting options and stock purchase rights, as compared to expense of $2.4 million and $4.0 million, respectively, during the three and nine months ended September 30, 2004.

9. Summarized Financial Information

Our outstanding senior notes and senior subordinated notes are fully and unconditionally guaranteed, on a joint and several basis, by the Guarantor Subsidiaries, which are all of our material direct and indirect subsidiaries, other than our mortgage and title operations subsidiaries (the Non-guarantor Subsidiaries). Each of the Guarantor Subsidiaries is directly or indirectly 100% owned by us. In lieu of providing separate financial statements for the Guarantor Subsidiaries, consolidated condensed financial statements are presented below. Separate financial statements and other disclosures concerning the Guarantor Subsidiaries are not presented because management has determined that they are not material to investors.

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
Consolidating Statement of Financial Condition
September 30, 2005

	Technical Olympic USA, Inc.	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Intercompany Eliminations	Total
			(Dollars in millions)		
ASSETS					
HOMEBUILDING:					
Cash and cash equivalents	$ 10.8	$ 35.5	$	$	$ 46.3
Inventory		1,646.6			1,646.6
Property and equipment, net	6.8	17.8			24.6
Investments in unconsolidated joint ventures		188.0			188.0
Receivables from unconsolidated joint ventures		80.3			80.3
Investments in/ Advances to consolidated subsidiaries	1,843.7	(402.8)	(6.0)	(1,434.9)	
Other assets	19.8	102.4			122.2
Goodwill		110.7			110.7
	1,881.1	1,778.5	(6.0)	(1,434.9)	2,218.7
FINANCIAL SERVICES:					
Cash and cash equivalents			82.7		82.7
Mortgage loans held for sale			64.0		64.0
Other assets			13.3		13.3
			160.0		160.0
Total Assets	$ 1,881.1	$ 1,778.5	$ 154.0	$ (1,434.9)	$ 2,378.7
LIABILITIES AND STOCKHOLDERS EQUITY					
HOMEBUILDING:					
Accounts payable and other liabilities	$ 92.0	$ 198.7	$	$	$ 290.7
Customer deposits		87.2			87.2
Obligations for inventory not owned		79.5			79.5
Notes payable	811.6				811.6
Bank borrowings	80.0				80.0
	983.6	365.4			1,349.0
FINANCIAL SERVICES:					
Accounts payable and other liabilities			77.6		77.6

Bank borrowings			54.6		54.6
			132.2		132.2
Total liabilities	983.6	365.4	132.2		1,481.2
Total stockholders equity	897.5	1,413.1	21.8	(1,434.9)	897.5
Total liabilities and stockholders equity	$ 1,881.1	$ 1,778.5	$ 154.0	$ (1,434.9)	$ 2,378.7

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
Consolidating Statement of Financial Condition
December 31, 2004

	Technical Olympic USA, Inc.	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Intercompany Eliminations	Total
			(Dollars in millions)		
ASSETS					
HOMEBUILDING:					
Cash and cash equivalents	$ 159.3	$ 66.3	$	$	$ 225.6
Inventory		1,281.2			1,281.2
Property and equipment, net	6.8	19.9			26.7
Investments in unconsolidated joint ventures		66.6			66.6
Receivables from unconsolidated joint ventures		3.4			3.4
Investments in/ Advances to consolidated subsidiaries	1,349.9	24.0	(62.8)	(1,311.1)	
Other assets	22.4	45.3			67.7
Goodwill		110.7			110.7
	1,538.4	1,617.4	(62.8)	(1,311.1)	1,781.9
FINANCIAL SERVICES:					
Cash and cash equivalents			120.0		120.0
Mortgage loans held for sale			75.8		75.8
Other assets			9.8		9.8
			205.6		205.6
Total assets	$ 1,538.4	$ 1,617.4	$ 142.8	$ (1,311.1)	$ 1,987.5
LIABILITIES AND STOCKHOLDERS EQUITY					
HOMEBUILDING:					
Accounts payable and other liabilities	$ 64.3	$ 124.6	$	$	$ 188.9
Customer deposits		69.1			69.1
Obligations for inventory not owned		136.2			136.2
Notes payable	811.4				811.4
	875.7	329.9			1,205.6
FINANCIAL SERVICES:					
Accounts payable and other liabilities			70.2		70.2
Bank borrowings			49.0		49.0

						119.2				119.2
Total liabilities		875.7		329.9		119.2				1,324.8
Total stockholders equity		662.7		1,287.5		23.6		(1,311.1)		662.7
Total liabilities and stockholders equity	$	1,538.4	$	1,617.4	$	142.8	$	(1,311.1)	$	1,987.5

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
Consolidating Statement of Income
Three Months Ended September 30, 2005

	Technical Olympic USA, Inc.	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Intercompany Eliminations	Total
			(Dollars in millions)		
HOMEBUILDING:					
Revenues	$	$ 662.6	$	$	$ 662.6
Cost of sales		477.4			477.4
Gross profit		185.2			185.2
Selling, general and administrative expenses	23.5	69.4		(2.7)	90.2
Other income:					
Income from joint ventures, net		(13.3)			(13.3)
Other (income) expense, net	(92.1)	15.4		75.1	(1.6)
Homebuilding pretax income	68.6	113.7		(72.4)	109.9
FINANCIAL SERVICES:					
Revenues			16.1	(2.7)	13.4
Expenses			12.4	(2.0)	10.4
Financial Services pretax income			3.7	(0.7)	3.0
Income before provision (benefit) for income taxes	68.6	113.7	3.7	(73.1)	112.9
Provision (benefit) for income taxes	(1.7)	42.9	1.4		42.6
Net income	$ 70.3	$ 70.8	$ 2.3	$ (73.1)	$ 70.3

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
Consolidating Statement of Income
Three Months Ended September 30, 2004

	Technical Olympic USA, Inc.	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Intercompany Eliminations	Total
			(Dollars in millions)		
HOMEBUILDING:					
Revenues	$	$ 507.2	$	$	$ 507.2
Cost of sales		405.4			405.4
Gross profit		101.8			101.8
Selling, general and administrative expenses	12.1	50.4		(1.3)	61.2
Other income:					
Income from joint ventures, net		(0.7)			(0.7)
Other (income) expense, net	(35.3)	(3.3)		36.4	(2.2)
Homebuilding pretax income	23.2	55.4		(35.1)	43.5
FINANCIAL SERVICES:					
Revenues			10.0	(1.8)	8.2
Expenses			8.8	(1.2)	7.6
Financial Services pretax income			1.2	(0.6)	0.6
Income before provision (benefit) for income taxes	23.2	55.4	1.2	(35.7)	44.1
Provision (benefit) for income taxes	(4.9)	20.2	0.7		16.0
Net income	$ 28.1	$ 35.2	$ 0.5	$ (35.7)	$ 28.1

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
Consolidating Statement of Income
Nine Months Ended September 30, 2005

	Technical Olympic USA, Inc.	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Intercompany Eliminations	Total
			(Dollars in millions)		
HOMEBUILDING:					
Revenues	$	$ 1,812.0	$	$	$ 1,812.0
Cost of sales		1,373.3			1,373.3
Gross profit		438.7			438.7
Selling, general and administrative expenses	60.0	193.2		(6.5)	246.7
Other income:					
Income from joint ventures, net		(24.0)			(24.0)
Other (income) expense, net	(199.5)	32.6		161.1	(5.8)
Homebuilding pretax income	139.5	236.9		(154.6)	221.8
FINANCIAL SERVICES:					
Revenues			41.3	(6.5)	34.8
Expenses			32.5	(4.4)	28.1
Financial Services pretax income			8.8	(2.1)	6.7
Income before provision (benefit) for income taxes	139.5	236.9	8.8	(156.7)	228.5
Provision (benefit) for income taxes	(2.9)	86.2	2.8		86.1
Net income	$ 142.4	$ 150.7	$ 6.0	$ (156.7)	$ 142.4

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
Consolidating Statement of Income
Nine Months Ended September 30, 2004

	Technical Olympic USA, Inc.	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Intercompany Eliminations	Total
			(Dollars in millions)		
HOMEBUILDING:					
Revenues	$	$ 1,430.3	$	$	$ 1,430.3
Cost of sales		1,152.2			1,152.2
Gross profit		278.1			278.1
Selling, general and administrative expenses	33.5	148.7		(5.3)	176.9
Other income:					
Income from joint ventures, net		(0.7)			(0.7)
Other (income) expense, net	(90.1)	(5.9)		93.3	(2.7)
Homebuilding pretax income	56.6	136.0		(88.0)	104.6
FINANCIAL SERVICES:					
Revenues			31.8	(5.4)	26.4
Expenses			24.0	(4.0)	20.0
Financial Services pretax income			7.8	(1.4)	6.4
Income before provision (benefit) for income taxes	56.6	136.0	7.8	(89.4)	111.0
Provision (benefit) for income taxes	(13.6)	49.9	4.5		40.8
Net income	$ 70.2	$ 86.1	$ 3.3	$ (89.4)	$ 70.2

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
Consolidating Statement of Cash Flows
Nine Months Ended September 30, 2005

	Technical Olympic USA, Inc.	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Intercompany Eliminations	Total
			(Dollars in millions)		
CASH FLOWS FROM OPERATING ACTIVITIES:					
Net income	$ 142.4	$ 150.7	$ 6.0	$ (156.7)	$ 142.4
Adjustments to reconcile net income to net cash (used in) provided by operating activities:					
Depreciation and amortization	2.9	5.9	0.8		9.6
Non-cash compensation expense	7.6				7.6
Equity in earnings from unconsolidated subsidiaries		(8.9)			(8.9)
Changes in operating assets and liabilities:					
Restricted cash	(1.5)	6.3	(6.5)		(1.7)
Inventory		(422.0)			(422.0)
Other assets	2.9	(114.0)	(2.8)		(113.9)
Accounts payable and other liabilities	24.0	74.1	7.4		105.5
Customer deposits		18.1			18.1
Mortgage loans held for sale			11.8		11.8
Net cash (used in) provided by operating activities	178.3	(289.8)	16.7	(156.7)	(251.5)
CASH FLOWS FROM INVESTING ACTIVITIES:					
Net additions to property and equipment	(2.9)	(3.8)	(1.4)		(8.1)
Investments in unconsolidated joint ventures		(112.5)			(112.5)
Loans to unconsolidated joint ventures		(20.0)			(20.0)
Net cash used in investing activities	(2.9)	(136.3)	(1.4)		(140.6)
CASH FLOWS FROM FINANCING ACTIVITIES:					
Net borrowings on revolving credit facilities	80.0				80.0
Proceeds from equity offering	89.3				89.3
Net proceeds from Financial Services bank borrowings			5.6		5.6

Payments for deferred financing costs	(0.3)				(0.3)
Dividends paid	(2.4)		(8.0)	8.0	(2.4)
Increase (decrease) in intercompany transactions	(493.6)	401.7	(56.8)	148.7	
Other	1.6				1.6
Net cash provided by (used in) financing activities	(325.4)	401.7	(59.2)	156.7	173.8
Decrease in cash and cash equivalents	(150.0)	(24.4)	(43.9)		(218.3)
Unrestricted cash and cash equivalents at beginning of period	159.3	58.3	50.9		268.5
Unrestricted cash and cash equivalents at end of period	$ 9.3	$ 33.9	$ 7.0	$	$ 50.2

Table of Contents

TECHNICAL OLYMPIC USA, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
Consolidating Statement of Cash Flows
Nine Months Ended September 30, 2004

	Technical Olympic USA, Inc.	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Intercompany Eliminations	Total
			(Dollars in millions)		
CASH FLOWS FROM OPERATING ACTIVITIES:					
Net income	$ 70.2	$ 86.1	$ 3.3	$ (89.4)	$ 70.2
Adjustments to reconcile net income to net cash (used in) provided by operating activities:					
Depreciation and amortization	2.2	7.3			9.5
Non-cash compensation expense	4.0				4.0
Changes in operating assets and liabilities:					
Restricted cash	1.5	17.5	(13.9)		5.1
Inventory	0.6	(267.2)			(266.6)
Other assets	46.8	(5.0)	(2.5)	(52.5)	(13.2)
Accounts payable and other liabilities	(2.8)	(58.4)	12.2	52.5	3.5
Customer deposits		33.7			33.7
Mortgage loans held for sale			5.0		5.0
Net cash (used in) provided by operating activities	122.5	(186.0)	4.1	(89.4)	(148.8)
CASH FLOWS FROM INVESTING ACTIVITIES:					
Net additions to property and equipment	(1.5)	(13.2)			(14.7)
Investments in unconsolidated joint ventures		(20.1)			(20.1)
Earn out consideration paid for acquisitions		(6.6)			(6.6)
Net cash used in investing activities	(1.5)	(39.9)			(41.4)
CASH FLOWS FROM FINANCING ACTIVITIES:					
Net borrowings on revolving credit facilities	48.0				48.0
Proceeds from notes offering	125.0				125.0
Net repayments on Financial Services bank borrowings			(5.1)		(5.1)
Payments for deferred financing costs	(2.1)				(2.1)
Dividends paid	(1.3)				(1.3)

Increase (decrease) in intercompany transactions	(340.3)	253.0	(2.1)	89.4	
Other	0.3	(6.8)			(6.5)
Net cash provided by (used in) financing activities	(170.4)	246.2	(7.2)	89.4	158.0
Increase (decrease) in cash and cash equivalents	(49.4)	20.3	(3.1)		(32.2)
Unresticted cash and cash equivalents at beginning of period	46.0	27.7	3.1		76.8
Unresticted cash and cash equivalents at end of period	$ (3.4)	$ 48.0	$	$	$ 44.6

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

Executive Summary

We generate revenues from our homebuilding operations (Homebuilding) and financial services operations (Financial Services), which comprise our operating segments. Through our Homebuilding operations we design, build and market high-quality detached single-family residences, town homes and condominiums in 16 metropolitan markets located in four major geographic regions: Florida, the Mid-Atlantic, Texas and the West.

Florida	Mid-Atlantic	Texas	West
Jacksonville	Baltimore/Southern Pennsylvania	Austin	Central Colorado
Orlando	Delaware	Dallas/Ft. Worth	Las Vegas
Southeast Florida	Nashville	Houston	Phoenix
Southwest Florida	Northern Virginia	San Antonio	
Tampa/St. Petersburg			

We build homes for inventory and on a pre-sold basis. At September 30, 2005, we had 7,541 homes completed or under construction (including unconsolidated joint ventures), of which approximately 13% were unsold. At September 30, 2005, we had 114 completed unsold homes in our inventory (including unconsolidated joint ventures), of which approximately 38% had been completed for more than 90 days. Our completed unsold homes at September 30, 2005 have decreased by 44% from 203 at December 31, 2004 and by 11% from 128 at June 30, 2005. At September 30, 2005, our completed unsold homes in inventory represented under 2% of the total homes completed or under construction (and averaged less than one per active community) as compared to 5% at December 31, 2004. We are actively working to control our finished speculative home inventory to reduce carrying costs, increase our available capital and improve our gross margins.

Once a sales contract with a buyer has been approved, we classify the transaction as a new sales order and include the home in backlog. Such sales orders are usually subject to certain contingencies such as the buyer s ability to qualify for financing. At closing, title passes to the buyer and a home is considered to be delivered and is removed from backlog. Revenue and cost of sales are recognized upon the delivery of the home, land or homesite when title is transferred to the buyer. We estimate that the average period between the execution of a sales contract for a home and closing is approximately six to twelve months for presold homes; however, this varies by market. The principal expenses of our Homebuilding operations are (i) cost of sales and (ii) selling, general and administrative (SG&A) expenses. Costs of home sales include land and land development costs, home construction costs, previously capitalized indirect costs, capitalized interest and estimated warranty costs. SG&A expenses for our Homebuilding operations include administrative costs, advertising expenses, on-site marketing expenses, sales commission costs, and closing costs. Sales commissions are included in selling, general and administrative costs when the related revenue is recognized. As used herein, Homebuilding includes results of home and land sales. Home sales includes results related only to the sale of homes.

To provide homebuyers with a seamless home purchasing experience, we have a complementary financial services business where we provide mortgage financing and closing services and offer title, homeowners and other insurance products to our homebuyers and others. Our mortgage financing operation derives most of its revenues from buyers of our homes, although it also offers its services to existing homeowners refinancing their mortgages. Our closing services and our insurance agency operations are used by our homebuyers and a broad range of other clients purchasing or refinancing residential or commercial real estate. Our mortgage financing operations revenues consist primarily of origination and premium fee income, interest income, and the gain on the sale of the mortgages. Our title operations revenues consist primarily of fees and premiums from title insurance and closing services. The principal expenses of our Financial Services operations are SG&A expenses, which consist primarily of compensation and interest expense on our warehouse lines of credit.

We were actively selling homes in 246 communities (including 52 through our unconsolidated joint ventures at September 30, 2005) at both September 30, 2005 and 2004. Excluding the 25 active

22

Table of Contents

communities acquired through our Transeastern joint venture, our active communities actually decreased as compared to September 30, 2004. This decrease is due to delays associated with bringing new communities on line and our intentional efforts to limit our early sales activities and manage community openings in an effort to decrease the time from contract to delivery to improve our gross margins. For the three months ended September 30, 2005, total revenues increased 31%, net income increased 150%, net sales orders (including unconsolidated joint ventures) increased 12% and home deliveries (including unconsolidated joint ventures) increased 33% as compared to the same period in the prior year. For the nine months ended September 30, 2005, total revenues increased 27%, net income increased 103%, net sales orders (including unconsolidated joint ventures) increased 8% and home deliveries (including unconsolidated joint ventures) increased 32% as compared to the same period in the prior year. Sales value in backlog at September 30, 2005 as compared to September 30, 2004 increased by 7% to $1.8 billion. Our joint ventures had an additional $1.7 billion in sales backlog at September 30, 2005. Our home cancellation rate was approximately 18% for the quarter ended September 30, 2005, and 15% for the nine months ended September 30, 2005. Our cancellation rate for the quarter was generally consistent with the first two quarters of 2005. Our percentage of converting backlog units at the beginning of the quarter to deliveries during the quarter was 32%, which is generally consistent with the first two quarters of 2005.

We continue to be impacted by labor and supply shortages and increases in the cost of materials caused by the hurricanes in 2004 and 2005 and the rising costs of petroleum. We have been notified by certain vendors and subcontractors to expect near term increases in the costs of materials and labor. We are proactively responding to these situations by (1) actively working to reduce the amount of time from sale to delivery; (2) increasing cost contingencies in our home budgets; and (3) increasing home sales prices as quickly as the competitive market will allow. In addition, while the initial direct costs to us from Hurricane Wilma are minimal, we believe sales, home deliveries and community openings in the Florida region will be negatively impacted by the hurricane, but we cannot currently determine the extent or duration of any such impact.

We have entered into, and expect to expand our use of, joint ventures that acquire and develop land for our Homebuilding operations and/or joint ventures that additionally build and market homes. The majority of these joint ventures are not consolidated. At September 30, 2005, our investment in these unconsolidated joint ventures was $188.0 million, and we had receivables of $80.3 million from these joint ventures. In addition, we seek to use option contracts to acquire land whenever feasible. Option contracts allow us to control significant homesite positions with minimal capital investment and substantially reduce the risks associated with land ownership and development. At September 30, 2005, we controlled approximately 96,000 homesites (including through unconsolidated joint ventures) of which 72% were controlled through various option arrangements.

Critical Accounting Policies

There have been no significant changes to our critical accounting policies during the nine months ended September 30, 2005, as compared to those we disclosed in Management s Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2004.

Recent Developments

On August 1, 2005, through a joint venture (the Transeastern JV), we completed the acquisition of the homebuilding assets and operations of Transeastern Properties, Inc. (Transeastern) headquartered in Coral Springs, Florida. Our joint venture partner is an entity controlled by the former majority owners of Transeastern. The Transeastern JV acquired Transeastern s homebuilding assets, including work in process, finished lots and certain land option rights, for approximately $826.2 million (which includes the assumption of $112.0 million of liabilities, net of $30.8 million of cash). Additional consideration of up to $75.0 million will be paid to the sellers pursuant to an earn out agreement if certain conditions are met, such as achieving predetermined quarterly EBITDA targets and delivery of entitlement on certain tracts of land currently held under lot option contracts. In addition to the net assets acquired in the transaction, the

Table of Contents

Transeastern JV will have a right of first offer on land developed by a related entity of our joint venture partner for a period of five years. We are the managing member of the Transeastern JV and hold a 50% voting interest. The Transeastern JV was funded with $675.0 million of third party debt capacity (of which $560.0 million was drawn upon acquisition), a $20.0 million subordinated bridge loan from us and $165.0 million of equity, of which $90.0 million was contributed by us. The third party debt is secured by the Transeastern JV s assets and ownership interests and is non-recourse to us. We are accounting for the Transeastern JV under the equity method of accounting.

Results of Operations Consolidated

Three Months Ended September 30, 2005 Compared to Three Months Ended September 30, 2004

Total revenues increased 31% to $676.0 million for the three months ended September 30, 2005, from $515.4 million for the three months ended September 30, 2004. This increase is attributable to an increase in Homebuilding revenues of 31%, and an increase in Financial Services revenues of 63%.

Income before provision for income taxes increased by 156% to $112.9 million for the three months ended September 30, 2005, from $44.1 million for the comparable period in 2004. This increase is mainly attributable to an increase in Homebuilding pretax income to $109.9 million for the three months ended September 30, 2005, from $43.5 million for the three months ended September 30, 2004.

Our effective tax rate was 37.8% and 36.4% for the three months ended September 30, 2005 and 2004, respectively. This increase was due to increases in income in states with higher tax rates.

As a result of the above, net income increased to $70.3 million (or $1.18 per diluted share) for the three months ended September 30, 2005 from $28.1 million (or $0.49 per diluted share) for the three months ended September 30, 2004.

Nine Months Ended September 30, 2005 Compared to Nine Months Ended September 30, 2004

Total revenues increased 27% to $1,846.8 million for the nine months ended September 30, 2005, from $1,456.7 million for the nine months ended September 30, 2004. This increase is attributable to an increase in Homebuilding revenues of 27%, and an increase in Financial Services revenues of 32%.

Income before provision for income taxes increased by 106% to $228.5 million for the nine months ended September 30, 2005, from $111.0 million for the comparable period in 2004. This increase is attributable to an increase in Homebuilding pretax income to $221.8 million for the nine months ended September 30, 2005, from $104.6 million for the nine months ended September 30, 2004.

Our effective tax rate was 37.7% and 36.7% for the nine months ended September 30, 2005 and 2004, respectively. This increase was due to increases in income in states with higher tax rates.

As a result of the above, net income increased to $142.4 million (or $2.43 per diluted share) for the nine months ended September 30, 2005 from $70.2 million (or $1.23 per diluted share) for the nine months ended September 30, 2004.

Table of Contents

Results of Operations

The following tables set forth certain operating and financial data for our homebuilding operations in our four major geographic regions, Florida, the Mid-Atlantic, Texas and the West (dollars in millions, except average price in thousands):

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2005		2004		2005		2004	
Deliveries:	**Homes**	**$**	**Homes**	**$**	**Homes**	**$**	**Homes**	**$**
Florida	627	$ 190.8	541	$ 149.9	2,144	$ 627.0	1,641	$ 438.6
Mid-Atlantic	171	75.1	143	62.9	448	186.3	378	151.5
Texas	555	134.3	489	127.2	1,402	338.6	1,378	348.5
West	528	162.6	611	160.1	1,766	505.4	1,586	430.7
Consolidated total	1,881	$ 562.8	1,784	$ 500.1	5,760	$ 1,657.3	4,983	$ 1,369.3
From unconsolidated joint ventures	528	169.1	25	7.6	872	272.5	27	8.2
Total	2,409	$ 731.9	1,809	$ 507.7	6,632	$ 1,929.8	5,010	$ 1,377.5

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2005		2004		2005		2004	
Net Sales Orders(1):	**Homes**	**$**	**Homes**	**$**	**Homes**	**$**	**Homes**	**$**
Florida	714	$ 239.0	952	$ 301.2	2,196	$ 753.9	3,008	$ 890.3
Mid-Atlantic	95	35.7	83	31.7	491	209.1	595	252.7
Texas	709	175.8						