

MDC HOLDINGS INC  
Form 10-K  
February 05, 2014

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**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

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**FORM 10-K**

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

**For the fiscal year ended December 31, 2013**

**OR**

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

**For the Transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission file number 1-08951**

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**M.D.C. HOLDINGS, INC.**

**(Exact name of Registrant as specified in its charter)**

Delaware 84-0622967  
(State or other jurisdiction (I.R.S. Employer  
of incorporation or organization) Identification No.)

4350 South Monaco Street, Suite 500 80237  
Denver, Colorado (Zip code)  
(Address of principal executive offices)

(303) 773-1100

(Registrant's telephone number, including area code)

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

| <u>Title of each class</u>         | <u>Name of each exchange<br/>on which registered</u> |
|------------------------------------|------------------------------------------------------|
| Common Stock, \$.01 par value      | New York Stock Exchange                              |
| 5 % Senior Notes due December 2014 | New York Stock Exchange                              |
| 5 % Senior Notes due July 2015     | New York Stock Exchange                              |
| 5 % Senior Notes due January 2020  | New York Stock Exchange                              |
| 6% Senior Notes due January 2043   | New York Stock Exchange                              |

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

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☒ No ☐

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes ☐ No ☒

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. X

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, non-accelerated filer, or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer X

Accelerated Filer     

Non-Accelerated Filer      (Do not check if a smaller reporting company)

Smaller Reporting Company     

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

As of June 30, 2013, the aggregate market value of the Registrants' common stock held by non-affiliates of the Registrants was \$1.3 billion based on the closing sales price of \$32.51 per share as reported on the New York Stock Exchange on June 28, 2013.

As of December 31, 2013, the number of shares outstanding of Registrant's common stock was 48,788,887.

#### DOCUMENTS INCORPORATED BY REFERENCE

Portions of part III of this Form 10-K are incorporated by reference from the Registrant's 2013 definitive proxy statement to be filed with the Securities and Exchange Commission no later than 120 days after the end of the Registrant's fiscal year.

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**M.D.C. HOLDINGS, INC.**

**FORM 10-K**

**For the Year Ended December 31, 2013**

**Table of Contents**

|                                                                                                                      | Page<br>No. |
|----------------------------------------------------------------------------------------------------------------------|-------------|
| <b>PART I</b>                                                                                                        |             |
| ITEM 1. Business                                                                                                     |             |
| (a) General Development of Business                                                                                  | 1           |
| (b) Available Information                                                                                            | 1           |
| (c) Financial Information About Industry Segments                                                                    | 2           |
| (d) Narrative Description of Business                                                                                | 2           |
| ITEM 1A. Risk Factors                                                                                                | 7           |
| ITEM 1B Unresolved Staff Comments                                                                                    | 13          |
| ITEM 2. Properties                                                                                                   | 13          |
| ITEM 3. Legal Proceedings                                                                                            | 13          |
| ITEM 4. Mine Safety Disclosures                                                                                      | 13          |
| <b>PART II</b>                                                                                                       |             |
| ITEM 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities | 14          |
| ITEM 6. Selected Financial Data                                                                                      | 16          |
| ITEM 7. Management's Discussion and Analysis of Financial Condition and Results of Operations                        | 17          |
| ITEM 7A. Quantitative and Qualitative Disclosures About Market Risk                                                  | 43          |
| ITEM 8. Consolidated Financial Statements                                                                            | F-1         |
| ITEM 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure                         | 45          |
| ITEM 9A. Controls and Procedures                                                                                     | 45          |

|                   |                                                                                                |    |
|-------------------|------------------------------------------------------------------------------------------------|----|
| ITEM 9B.          | Other Information                                                                              | 47 |
| <b>PART III</b>   |                                                                                                |    |
| ITEM 10.          | Directors, Executive Officers and Corporate Governance                                         | 47 |
| ITEM 11.          | Executive Compensation                                                                         | 47 |
| ITEM 12.          | Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters | 47 |
| ITEM 13.          | Certain Relationships and Related Transactions, and Director Independence                      | 47 |
| ITEM 14.          | Principal Accountant Fees and Services                                                         | 47 |
| <b>PART IV</b>    |                                                                                                |    |
| ITEM 15.          | Exhibits and Financial Statement Schedules                                                     | 48 |
| <b>SIGNATURES</b> |                                                                                                | 55 |

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**M.D.C. HOLDINGS, INC.**

**FORM 10-K**

**PART I**

**Forward-Looking Statements**

*Certain statements in this Annual Report on Form 10-K, as well as statements made by us in periodic press releases, oral statements made by our officials in the course of presentations about the Company and conference calls in connection with quarterly earnings releases, constitute “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include statements regarding our business, financial condition, results of operation, cash flows, strategies and prospects. These forward-looking statements may be identified by terminology such as “likely,” “may,” “will,” “should,” “expects,” “plans,” “anticipates,” “believes,” “estimates,” “predicts,” “potential” or “continue,” or the negative of such terms and other comparable terminology. Although we believe that the expectations reflected in the forward-looking statements contained in this Report are reasonable, we cannot guarantee future results. These statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company to be materially different from those expressed or implied by the forward-looking statements. We undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future events or otherwise. However, any further disclosures made on related subjects in subsequent reports on Forms 10-K, 10-Q and 8-K should be considered.*

**Item 1. Business**

*(a) General Development of Business*

M.D.C. Holdings, Inc. is a Delaware corporation. We refer to M.D.C. Holdings, Inc. as the “Company,” “MDC,” “we” or “our” in this Annual Report on Form 10-K, and these designations include our subsidiaries unless we state otherwise. We have two primary operations, homebuilding and financial services. Our homebuilding operations consist of wholly-owned subsidiary companies that generally purchase finished lots or develop lots to the extent necessary for the construction and sale primarily of single-family detached homes to first-time and first-time move-up homebuyers under the name “Richmond American Homes.” Our homebuilding operations are comprised of various homebuilding

divisions that we consider to be our operating segments. For financial reporting, we have aggregated our homebuilding operating segments into reportable segments as follows: (1) West (Arizona, California, Nevada and Washington); (2) Mountain (Colorado and Utah); and (3) East (Virginia, Florida, Illinois and Maryland, which includes Pennsylvania, Delaware, and New Jersey).

Our financial services operations primarily consist of HomeAmerican Mortgage Corporation (“HomeAmerican”), which originates mortgage loans primarily for our homebuyers; Allegiant Insurance Company, Inc., A Risk Retention Group (“Allegiant”), which provides insurance coverage primarily to our homebuilding subsidiaries and certain subcontractors for homes sold by our homebuilding subsidiaries and for work performed in completed subdivisions; StarAmerican Insurance Ltd., which is a re-insurer on Allegiant claims; American Home Insurance Agency, Inc., which offers third-party insurance products to our homebuyers; and American Home Title and Escrow Company, which provides title agency services to our homebuilding subsidiaries and our customers in certain states. For financial reporting, we have aggregated our financial services operating segments into reportable segments as follows: (1) Mortgage operations (represents HomeAmerican only) and (2) Other (all remaining operating segments).

*(b) Available Information*

We make our Annual Report 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 Securities Exchange Act of 1934, available free of charge on our website as soon as reasonably practicable after we file or furnish the materials electronically with the Securities and Exchange Commission (“SEC”). To obtain any of this information, go to our website, <http://ir.richmondamerican.com>, and select “SEC Filings.” Our website includes our: (1) Corporate Governance Guidelines; (2) Corporate Code of Conduct; (3) Rules for Senior Financial Officers; (4) Audit Committee Procedures for Handling Confidential Complaints; and (5) charters for the Audit, Compensation and Corporate Governance/Nominating Committees. These materials may also be obtained, free of charge, at <http://ir.richmondamerican.com> (select “Corporate Governance”).

*(c) Financial Information About Industry Segments*

Note 3 to the Consolidated Financial Statements contains information regarding our reportable segments for each of the years ended December 31, 2013, 2012 and 2011.

*(d) Narrative Description of Business*

Our business consists of two primary operations, homebuilding and financial services. Our homebuilding subsidiaries build and sell primarily single-family detached homes that are designed and built to meet local customer preferences. Each homebuilding subsidiary is the general contractor for its projects and retains subcontractors for land development and home construction. Our homebuilding subsidiaries build a variety of home styles in each of their markets, targeting primarily first-time and first-time move-up homebuyers.

For 2013, the percentage of our home deliveries and home sale and land sale revenues by state were as follows:

|            | Percentage<br>of<br>Deliveries |   | Percentage<br>of Home<br>Sale<br>Revenues |   |
|------------|--------------------------------|---|-------------------------------------------|---|
| Arizona    | 13                             | % | 10                                        | % |
| California | 14                             | % | 15                                        | % |
| Nevada     | 13                             | % | 10                                        | % |
| Washington | 7                              | % | 7                                         | % |
| West       | 47                             | % | 42                                        | % |
| Colorado   | 27                             | % | 29                                        | % |
| Utah       | 4                              | % | 4                                         | % |
| Mountain   | 31                             | % | 33                                        | % |
| Maryland   | 8                              | % | 10                                        | % |
| Virginia   | 8                              | % | 11                                        | % |
| Florida    | 6                              | % | 4                                         | % |
| East       | 22                             | % | 25                                        | % |
| Total      | 100                            | % | 100                                       | % |



Our financial services operations include subsidiary companies that provide mortgage financing, place title insurance and homeowner insurance for our homebuyers, and provide general liability insurance for our subsidiaries and most of our subcontractors.

## **Homebuilding Operations**

*Operating Divisions.* The primary functions of our homebuilding segments include land acquisition and development, home construction, sales and marketing, and customer service. Operating decisions are made by our local management teams under the oversight of our Chief Operating Decision Makers (“CODMs”), defined as our Chief Executive Officer and Chief Operating Officer. Our organizational structure (i.e., the grouping and reporting of divisions) changes based upon the current needs of the Company. We had 10 active homebuilding operating divisions at the end of each year ended December 31, 2013, 2012 and 2011.

*Corporate Management.* Our homebuilding business is managed primarily through members of senior management in our Corporate segment and our Asset Management Committees (“AMCs”). Each AMC is comprised of the Chief Operating Officer and three of our corporate officers. All real estate acquisition transactions are reviewed to ensure the transaction achieves the land strategies set forth by CODMs and must be approved by one of the AMCs. Generally, the role of our senior management team and/or AMC includes:

- review and approval of division business plans and budgets;
- oversight of land and home inventory levels;
- review of major personnel decisions; and
- review of capital allocation decisions.

Additionally, our corporate executives and corporate departments generally are responsible for establishing and monitoring compliance with our policies and procedures. Among other things, the corporate office has primary responsibility for:

- asset management and capital allocation;
- treasury;
- insurance and risk management;
- merchandising and marketing;
- national purchasing contracts;
- accounting, tax and internal audit functions;
- legal matters;
- human resources and payroll;
- information technology; and
- training and development.

During 2011 and 2012, we reorganized our finance and accounting operations, focusing on the centralization of certain back office functions. In addition, we reorganized our sales and marketing activities to (1) better communicate the value of our homes to our prospective homebuyers, thereby giving us the opportunity to reduce incentives and increase sales absorptions, (2) better align the compensation structure for our sales organization with Company goals, and (3) simplify our processes to reduce overhead expenses.

*Housing.* Generally, our homebuilding subsidiaries build single-family detached homes in a number of standardized series, designed to provide variety in the size and style of homes for our potential homebuyers. In certain markets our homebuilding subsidiaries build and sell attached townhome product. Within each series for our single-family detached homes, our homebuilding subsidiaries build several different floor plans offering standard and optional features (such as upgraded appliances, cabinetry, flooring, etc.). Differences in sales prices of similar models from market-to-market depend primarily upon homebuyer demand, home prices offered by our competitors, market conditions (such as home inventory supply levels), location, optional features and design specifications. The series of homes offered at a particular location is based on perceived customer preferences, lot size, area demographics and, in

certain cases, the requirements of major land sellers and local municipalities. We monitor levels of inventories of unsold started homes in our markets in order to increase returns based on market demand. Unsold started homes in various stages of completion allow us to meet the immediate and near-term demands of prospective homebuyers.

*Land Acquisition and Development.* Our homebuilding subsidiaries acquire our lots with the intention of constructing and selling homes on the acquired land. Generally, we prefer to purchase finished lots using option contracts, in phases or in bulk for cash. However, under certain circumstances, we may acquire entitled land for development into finished lots when we believe that the risk is justified. In making land purchases, we consider a number of factors, including projected rates of return, estimated gross margins from home sales, sales prices of the homes to be built and mortgage loan limits within the respective county, population and employment growth patterns, proximity to developed areas, estimated cost and complexity of development including environmental and geological factors, quality of schools, estimated levels of competition and demographic trends. Our homebuilding subsidiaries attempt to maintain a supply of finished lots sufficient to enable them to start homes promptly after a contract for a home sale is executed. See “**Forward-Looking Statements**” above.

In their option contracts, our homebuilding subsidiaries generally obtain the right to purchase lots in consideration for an option deposit in the form of cash or letters of credit. In the event they elect not to purchase the lots within a specified period of time, they may be required to forfeit the option deposit. Our option contracts generally do not contain provisions requiring our specific performance.

Our homebuilding subsidiaries may own or have the right under option contracts to acquire undeveloped parcels of real estate that they intend to develop into finished lots. They generally develop our land in phases in order to limit our risk in a particular subdivision and to efficiently employ available resources. Generally, building permits and utilities are available and zoning is suitable for the current intended use of substantially all of our undeveloped land. When developed, these lots generally will be used in our homebuilding activities. See “**Forward-Looking Statements**” above.

*Labor and Raw Materials.* For the most part, materials used in our homebuilding operations are standard items carried by major suppliers. We generally contract for our materials and labor at a fixed price for the anticipated construction period of our homes. This allows us to mitigate the risks associated with increases in building materials and labor costs between the time construction begins on a home and the time it is closed. Increases in the cost of building materials and subcontracted labor may reduce gross margins from home sales to the extent that market conditions prevent the recovery of increased costs through higher home sales prices. From time to time and to varying degrees, we may experience shortages in the availability of building materials and/or labor in each of our markets. These shortages and delays may result in delays in the delivery of homes under construction, reduced gross margins from home sales, or both. See “**Forward-Looking Statements**” above.

*Warranty.* Our homebuilding subsidiaries sell their homes with limited third-party warranties that generally provide for ten years of structural coverage, two years of coverage for plumbing, electrical, heating, ventilation and air conditioning systems, and one year of coverage for workmanship and materials. Under our agreement with the issuer of the third-party warranties, our homebuilding subsidiaries are responsible for performing all of the work for the first two years of the warranty coverage, and paying for substantially all of the work required to be performed during years three through ten of the warranties.

*Seasonal Nature of Business.* The homebuilding industry can experience noticeable seasonality and quarter-to-quarter variability in homebuilding activity levels. The seasonal nature of our business is described in more detail in our description of Risk Factors under the heading “Because of the seasonal nature of our business, our quarterly operating results can fluctuate.”

*Backlog.* At December 31, 2013 and 2012, homes under contract but not yet delivered (“backlog”) totaled 1,262 and 1,645, respectively, with an estimated sales value of \$506 million and \$579 million, respectively. We anticipate that homes in backlog at December 31, 2013 generally will close during 2014 under their existing home order contracts or through the replacement of an existing contract with a new home order contract. The estimated backlog sales value at December 31, 2013 may be impacted by, among other things, subsequent home order cancellations and incentives provided, and options and upgrades selected after December 31, 2013. See “**Forward-Looking Statements**” above.

*Customer Service and Quality Control.* Our homebuilding divisions are responsible for pre-closing quality control inspections and responding to customers’ post-closing needs. We have a product service and quality control program, focused on improving and/or maintaining the quality of our customers’ complete home buying and homeownership experience.

*Sales and Marketing.* Our sales and marketing programs are designed to attract homebuyers in a cost effective manner. We have a centralized in-house advertising and marketing department that oversees our efforts to communicate the inherent value of our homes to our prospective homebuyers and distinguish our Richmond American Homes brand from our competitors or other home buying opportunities. The main objective of this team is to generate

homebuyer leads, which are actively pursued by our community sales associates. Our in-house merchandising team furnishes our model homes and sales offices.

Another important part of our marketing presentation takes place in our design centers (also known as Home Galleries). Here, homebuyers are able to personalize their homes with a variety of options and upgrades. These locations also serve as an information center for prospective home buyers and real estate agents who may opt to receive personalized attention from one of our new home specialists, resulting in a more focused and efficient home search across all of our Richmond American communities in a given market place. We believe that the services provided by our Home Galleries represent a key competitive advantage in dealing with prospective homebuyers.

*Competition.* The homebuilding industry is fragmented and highly competitive. The competitive nature of our business is described in more detail in our description of Risk Factors.

*Regulation.* Our homebuilding operations are subject to compliance with applicable laws and regulations, which are described in more detail in our description of Risk Factors.

## Financial Services Operations

### *Mortgage Lending Operations*

*General.* HomeAmerican is a full-service mortgage lender and the principal originator of mortgage loans for our homebuyers. HomeAmerican has a centralized loan processing center where it originates mortgage loans, primarily for our homebuyers.

HomeAmerican is authorized to originate Federal Housing Administration-insured (“FHA”), Veterans Administration-guaranteed (“VA”), Federal National Mortgage Association (“Fannie Mae”), Federal Home Loan Mortgage Corporation (“Freddie Mac”) (together “the government sponsored entities”) and private investor mortgage loans. HomeAmerican also is an authorized loan servicer for Fannie Mae and Freddie Mac and, as such, is subject to the rules and regulations of these entities.

HomeAmerican uses a mortgage repurchase facility, internally generated funds, and temporary financing provided by its parent, to finance the origination of mortgage loans until they are sold. HomeAmerican sells originated mortgage loans to third-party purchasers on either a bulk or flow basis. Mortgage loans sold on a bulk basis include the sale of a package of substantially similar originated mortgage loans, while sales of mortgage loans on a flow basis are completed as HomeAmerican originates each loan. Mortgage loans sold to third-party purchasers include HomeAmerican’s representations and warranties with respect to certain borrower payment defaults, credit quality issues and/or misrepresentations made by us or our homebuyers. Substantially all of the mortgage loans originated by HomeAmerican are sold to third-party purchasers generally within 15 to 40 days of origination.

*Pipeline.* HomeAmerican’s mortgage loans in process for which a rate and price commitment had been made to a borrower that had not closed (the “locked pipeline”) at December 31, 2013 and 2012 had an aggregate principal balance of approximately \$69.8 million and \$50.8 million, respectively, and were under interest rate lock commitments at an average interest rate of 4.13% and 3.26%, respectively.

*Forward Sales Commitments.* HomeAmerican is exposed to market risks related to fluctuations in interest rates. HomeAmerican creates certain derivative instruments in the normal course of business, which primarily include commitments to originate mortgage loans (interest rate lock commitments or locked pipeline). HomeAmerican uses forward sales of mortgage-backed securities and commitments to hedge the interest rate risk inherent with the locked pipeline, as well as its loan inventory held for sale. The market related risks in our business are described in more detail in our description of Risk Factors.

*Competition.* HomeAmerican competes with other mortgage bankers to arrange financing for our homebuyers. The significant decline in demand for re-financings during 2013 has resulted in increased competition from other mortgage bankers for purchased loans.

For loans to be sold, the mortgage industry is de-consolidating with a number of smaller non-bank entities entering the third-party purchaser space. These new entrants offer HomeAmerican better prices and a potentially wider array of product options which has served to mitigate some of the competitive issues that HomeAmerican faced when the mortgage market was less fragmented. The competitive nature of our business is described in more detail in our description of Risk Factors.

*Regulation.* Our mortgage lending operations are subject to compliance with applicable laws and regulations, which are described in more detail in our description of Risk Factors.

#### *Insurance Operations*

*General.* Our insurance operations consist of three business divisions: (1) Allegiant; (2) StarAmerican; and (3) American Home Insurance.

Allegiant and StarAmerican were formed to provide insurance coverage of homebuilding risks for our homebuilding subsidiaries and certain of our homebuilding subcontractors. Allegiant was organized as a risk retention group under the Federal Liability Risk Retention Act of 1981. Allegiant, which began operations in June of 2004, is licensed as a Class 3 Stock Insurance Company by the Division of Insurance of the State of Hawaii and is subject primarily to the regulations of its state of incorporation. StarAmerican is a single parent captive insurance company licensed by the Division of Insurance of the State of Hawaii and is a wholly-owned subsidiary of MDC. Pursuant to agreements beginning in June 2004, StarAmerican re-insures Allegiant for all claims in excess of \$50,000 per occurrence up to \$3.0 million per occurrence, subject to various aggregate limits.

Allegiant generates premium revenue generally by providing to its customers, comprised of the Company's homebuilding subsidiaries and certain subcontractors of the Company's homebuilding subsidiaries, general liability insurance on homes sold by our homebuilding subsidiaries and for work performed in completed subdivisions. Allegiant seeks to provide to its customers coverage and insurance rates that are competitive with other insurers. StarAmerican generates premium revenue by providing re-insurance coverage to Allegiant. Allegiant and StarAmerican incur expenses for actual losses and loss adjustment expenses and for reserves established based on actuarial studies including known facts, such as our experience with similar insurance cases and historical trends involving insurance claim payment patterns, pending levels of unpaid insurance claims, claim severity, claim frequency patterns and interpretations of circumstances including changing regulatory and legal environments.

*Regulation.* Allegiant and StarAmerican are licensed in the State of Hawaii and, therefore, are subject to regulation by the Hawaii Insurance Division. This regulation includes restrictions and oversight regarding: types of insurance provided; investment options; required capital and surplus; financial and information reporting; use of auditors, actuaries and other service providers; periodic examinations; and other operational items. Additionally, as a risk retention group, Allegiant also is registered in other states where certain MDC homebuilding subsidiaries do business.

American Home Insurance is an insurance agency that sells primarily personal property and casualty insurance products in the same markets as our homebuilding subsidiaries and primarily to our homebuyers.

#### *Title Operations*

American Home Title provides title agency services to the Company and its homebuyers in Colorado, Florida, Maryland, Nevada and Virginia.

#### **Employees.**

The table below summarizes the approximate number of employees for our combined Homebuilding, combined Financial Services and Corporate segments at December 31, 2013 and 2012.

|                    | December<br>31, |      |
|--------------------|-----------------|------|
|                    | 2013            | 2012 |
| Homebuilding       | 800             | 665  |
| Financial Services | 99              | 84   |



|           |       |     |
|-----------|-------|-----|
| Corporate | 212   | 171 |
| Total     | 1,111 | 920 |

**Item 1A. Risk Factors.**

*The homebuilding industry is cyclical and affected by changes in general economic, real estate and other business conditions that could adversely affect our business or financial results.*

The homebuilding industry is cyclical and is significantly affected by changes in industry conditions, as well as in general and local economic conditions, such as:

- employment levels;
- availability of financing for homebuyers;
- interest rates;
- consumer confidence;
- levels of new and existing homes for sale;
- demographic trends; and
- housing demand.

These conditions may exist on a national level, like the recent downturn, or may affect some of the regions or markets in which we operate more than others. When adverse conditions affect any of our larger markets, they could have a proportionately greater impact on us than on some other homebuilding companies.

An oversupply of alternatives to new homes, including foreclosed homes, homes held for sale by investors and speculators, other existing homes, and rental properties, can also reduce our ability to sell new homes, depress new home prices and reduce our margins on the sale of new homes. High levels of foreclosures and short-sales not only contribute to additional inventory available for sale, but also can reduce appraisal valuations for new homes, potentially resulting in lower sales prices.

Continued military deployments, terrorist attacks, other acts of violence or threats to national security, and any corresponding response by the United States or others, or related domestic or international instability, may adversely affect general economic conditions or cause a slowdown of the economy.

The impact of the Affordable Care Act could adversely affect individuals and businesses, which could negatively impact homebuyer discretionary spending and demand for new homes.

As a result of the foregoing matters, potential customers may be less willing or able to buy our homes. In the future, our pricing strategies may continue to be limited by market conditions. We may be unable to change the mix of our home offerings, reduce the costs of the homes we build or offer more affordable homes to maintain our gross margins or satisfactorily address changing market conditions in other ways. In addition, cancellations of home sales contracts in backlog may increase as homebuyers choose to not honor their contracts.

Our financial services business is closely related to our homebuilding business, as it originates mortgage loans principally to purchasers of the homes we build. A decrease in the demand for our homes because of the foregoing matters may also adversely affect the financial results of this segment of our business. An increase in the default rate on the mortgages we originate may adversely affect our ability to sell the mortgages or the pricing we receive upon the sale of mortgages or may increase our potential exposure regarding those mortgage loan sales.

***A deterioration in homebuilding industry conditions or in the broader economic conditions, including government shutdowns and debt ceiling debates, could have adverse effects on our business and financial results.***

The recovery in the housing market has been negatively impacted by the continuing effects of the recent recession, including high unemployment rates, high levels of foreclosures and homeowners in default or with negative equity under their current mortgages, more stringent mortgage loan underwriting standards and difficulty in customers' ability to qualify for mortgage loans.

In the event of another downturn in the homebuilding and mortgage lending industries, or if the national economy weakens as a result of a decline in consumer confidence, government shutdowns, debt ceiling debates or other causes, we could experience declines in the market value of our inventory and demand for our homes, which could have a significant negative impact on our gross margin from home sales and financial and operating results.

Monetary policy tightening and tapering of bond purchases by the Federal Reserve could have an adverse effect on interest rates, including mortgage interest rates, equity markets and consumer confidence, which could have a material adverse effect on the homebuilding industry and our results of operations.

Additionally, as a result of recent economic circumstances, we may be subject to increased counterparty risks, which may include, among others, banks under our credit facilities and mortgage purchasers who may not be willing or able to perform on obligations to us. To the extent a third-party is unable to meet its obligations to us, our financial position, results of operations and/or cash flows could be negatively impacted.

These challenging conditions are complex and interrelated. We cannot predict their occurrence or severity, nor can we provide assurance that our responses would be successful.

***Increased competition levels in the homebuilding and mortgage lending industries could result in lower net home orders, deliveries and decreases in the average selling prices of sold and delivered homes, which would have a negative impact on our home sale revenues and results of operations.***

The homebuilding industry is fragmented and highly competitive. Our homebuilding subsidiaries compete with numerous public and private homebuilders, including a number that are substantially larger than us and may have greater financial resources than we do. Our homebuilding subsidiaries also compete with subdivision developers and land development companies, some of which are themselves homebuilders or affiliates of homebuilders. Homebuilders compete for customers, land, building materials, subcontractor labor and desirable financing. Competition for home orders primarily is based upon home sales price, location of property, home style, financing available to prospective homebuyers, quality of homes built, customer service and general reputation in the community, and may vary market-by-market and/or submarket-by-submarket. Additionally, competition within the homebuilding industry can be impacted by an excess supply of new and existing homes available for sale resulting from a number of factors, including, among other things, increases in the number of new home communities, increases in unsold started homes available for sale and increases in home foreclosures. Increased competition can result in a decrease in our new home orders, a decrease in our home sales prices and/or an increase in our home sales incentives in an effort to generate new home sales and maintain homes in backlog until they close. These competitive pressures may negatively impact our future financial and operating results.

Through our mortgage lending subsidiary, HomeAmerican, we also compete with numerous banks and other mortgage bankers and brokers, many of which are larger than us and may have greater financial resources than we do. Competitive factors include pricing, mortgage loan terms, underwriting criteria and customer service. To the extent that we are unable to adequately compete with other companies that originate mortgage loans, total revenue and the results of operations from our Mortgage operations may be negatively impacted.

***If land is not available at reasonable prices or terms, our homes sales revenue and results of operations could be negatively impacted and/or we could be required to scale back our operations in a given market.***

Our operations depend on our homebuilding subsidiaries' ability to obtain land for the development of our residential communities at reasonable prices and with terms that meet our underwriting criteria. Our ability to obtain land for new residential communities may be adversely affected by changes in the general availability of land, the willingness of land sellers to sell land at reasonable prices, competition for available land, availability of financing to acquire land, zoning, regulations that limit housing density, and other market conditions. If the supply of land, and especially finished lots, appropriate for development of residential communities continues to be limited because of these factors, or for any other reason, the number of homes that our homebuilding subsidiaries build and sell may decline. To the extent that we are unable to timely purchase land or enter into new contracts for the purchase of land at reasonable prices, due to the lag time between the time we acquire land and the time we begin selling homes, our home sale revenues and results of operations could be negatively impacted and/or we could be required to scale back our operations in a given market.

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

The residential construction industry experiences labor and material shortages from time to time, including: work stoppages; labor disputes; shortages in qualified trades people; lack of availability of adequate utility infrastructure and services; our need to rely on local subcontractors who may not be adequately capitalized or insured; and delays in availability, or fluctuations in prices, of building materials. These labor and material shortages can be more severe during periods of strong demand for housing or during periods in which the markets where we operate experience natural disasters that have a significant impact on existing residential and commercial structures. Additionally, we could experience labor shortages as a result of subcontractors going out of business or leaving the residential construction market due to low levels of housing production and volumes. Any of these circumstances could give rise to delays in the start or completion of our residential communities, increase the cost of developing one or more of our residential communities and/or increase the construction cost of our homes. To the extent that market conditions prevent the recovery of increased costs, including, among other things, subcontracted labor, finished lots, building materials, and other resources, through higher selling prices, our gross margin from home sales and results of operations could be adversely affected.

Increased costs of lumber, framing, concrete, steel and other building materials could cause increases in construction costs. We generally are unable to pass on increases in construction costs to customers who have already entered into sales contracts, as those sales contracts fix the price of the homes at the time the contracts are signed, which may be in advance of the construction of the home. Sustained increases in construction costs may, over time, erode our gross margin from home sales, particularly if pricing competition restricts our ability to pass on any additional costs of materials or labor, thereby decreasing our gross margin from home sales.

***If mortgage interest rates rise, if down payment requirements are increased, if loan limits are decreased, or if mortgage financing otherwise becomes less available, it could adversely affect our business, and the duration and ultimate severity of the effects are uncertain.***

The mortgage lending industry continues to experience significant instability. Beginning in 2014, new regulations will take effect that may, among other things, cap the fees and place additional restrictions on what our mortgage company and its affiliates may collect, limit the types of loans our mortgage company may originate and place additional restrictions on loans that are sold to entities such as Fannie Mae and Freddie Mac, insured by the FHA or guaranteed by VA. The ultimate impact of these changes is uncertain and may have a negative impact on our financial position, results of operations and/or cash flows.

We believe that the liquidity provided by Fannie Mae and Freddie Mac to the mortgage industry has been very important to the housing market. The future of these entities is in question. Any reduction in the availability of the liquidity provided by these institutions could adversely affect interest rates, mortgage availability and our sales of new

homes and mortgage loans.

Mortgage liquidity provided by government sponsored enterprises (GSEs) like the FHA, VA, Fannie Mae and Freddie Mac continues to be an important factor in marketing our homes. Financial losses or other factors may limit, restrict or otherwise curtail their ability or willingness to insure mortgage loans, offer insurance at rates and on terms that are not prohibitive, or purchase mortgage loans. Should this occur, it may negatively impact the availability of mortgage financing and our sales of new homes.

Loans sold to or insured by the GSEs are subject to various loan limits. Decreases in these loan limits may require homebuyers to make larger down payments or obtain more restrictive non-conforming or “jumbo” mortgages, which could adversely impact on our financial position, results of operations and/or cash flows.

Even if potential customers do not need financing, changes in the availability of mortgage products may make it harder for them to sell their current homes to potential buyers who need financing.

If interest rates increase, the costs of owning a home may be affected and could result in further reductions in the demand for our homes. Similarly, potential changes to the tax code with respect to deduction of home mortgage interest payments or other changes may decrease affordability of and demand for homeownership.

***Expirations, amendments or changes to tax laws, incentives or credits currently available to our customers may negatively impact our business.***

Many homeowners receive substantial tax benefits in the form of tax deductions against their personal taxable income for mortgage interest and property tax payments and the loss or reduction of these deductions could affect homeowners' net cost of owning a home. Significant changes to existing tax laws that currently benefit homebuyers, such as the ability to deduct mortgage interest and real property taxes, may result in an increase in the total cost of home ownership and may make the purchase of a home less attractive to buyers. This could adversely impact demand for and/or sales prices of new homes, which would have a negative impact on our business. Also, federal or state governments have in the past provided for substantial benefits in the form of tax credits for buyers of new or used homes.

***Increases in our cancellations could have a negative impact on our gross margin from home sales and home sale revenues.***

Home order cancellations can result from a number of factors, including declines in the market value of homes, increases in the supply of homes available to be purchased, increased competition, higher mortgage interest rates, homebuyers' inability to sell their existing homes, homebuyers' inability to obtain suitable financing, including providing sufficient down payments, and adverse changes in economic conditions.

Increased levels of home order cancellations could have a negative impact on our home sale revenues and financial and operating results in future reporting periods.

***A decline in the market value of our homes or carrying value of our land would have a negative impact on our results of operations and financial position.***

Our homebuilding subsidiaries acquire land for the replacement of land inventory and/or expansion within our current markets and may, from time to time, purchase land for expansion into new markets. The fair value of our land and land under development and housing completed or under construction inventory depends on market conditions. Factors that can impact our determination of the fair value of our inventory primarily include home sales prices, levels of home sales incentives and home construction and land costs. Our home sales prices and/or levels of home sales incentives can be impacted by, among other things, uncertainty in the homebuilding and mortgage industries or the United States economy overall, decreased demand for new homes, decreased home prices offered by our competitors, home foreclosure and short-sale levels, decreased ability of our homebuyers to obtain suitable mortgage loan financing and high levels of home order cancellations. Under such circumstances, we may be required to record impairments of our inventory. Any such inventory impairments would have a negative impact on our financial



position and results of operations in the future reporting period in which they were recorded.

***Natural disasters could cause an increase in home construction costs, as well as delays, and could negatively impact our results of operations.***

The climates and geology of many of the markets in which we operate present increased risks of natural disasters. To the extent that hurricanes, severe storms, earthquakes, droughts, floods, heavy or prolonged precipitation, wildfires or other natural disasters or similar events occur, the financial and operating results of our business may be negatively impacted.

***We have financial needs that we meet through the capital markets, including the debt and secondary mortgage markets, and disruptions in these markets could have an adverse impact on our results of operations, financial position and/or cash flows.***

We have financial needs that we meet through the capital markets, including the debt and secondary mortgage markets. Our requirements for additional capital, whether to finance operations or to service or refinance our existing indebtedness, fluctuate as market conditions and our financial performance and operations change. We cannot provide assurance that we will maintain cash reserves and generate sufficient cash flow from operations in an amount to enable us to service our debt or to fund other liquidity needs.

The availability of additional capital, whether from private capital sources or the public capital markets, fluctuates as our financial condition and market conditions in general change. There may be times when the private capital markets and the public debt or equity markets lack sufficient liquidity or when our securities cannot be sold at attractive prices, in which case we would not be able to access capital from these sources. In addition, a weakening of our financial condition or deterioration in our credit ratings could adversely affect our ability to obtain necessary funds. Even if financing is available, it could be costly or have other adverse consequences.

In addition, the sources and terms and conditions of warehouse financing and mortgage repurchase arrangements and other lending arrangements for the mortgage lending industry are changing. These changes can impact, among other things, availability of capital, terms and structures for debt and line of credit agreements, collateral requirements and collateral advance rates.

***Our business is subject to numerous federal, local and state laws and regulations concerning land development, construction of homes, sales, mortgage lending, environmental and other aspects of our business. These laws and regulations could give rise to additional liabilities or expenditures, or restrictions on our business.***

Our operations are subject to continuing compliance requirements mandated by applicable federal, state and local statutes, ordinances, rules and regulations, including zoning and land use ordinances, building, plumbing and electrical codes, contractors' licensing laws, state insurance laws, federal and state human resources laws and regulations and health and safety laws and regulations. Various localities in which we operate have imposed (or may impose in the future) fees on developers to fund schools, road improvements and low and moderate-income housing.

From time to time, various municipalities in which our homebuilding subsidiaries operate restrict or place moratoria on the availability of utilities, including water and sewer taps. Additionally, certain jurisdictions in which our homebuilding subsidiaries operate have proposed or enacted "slow growth" or "no growth" initiatives and other measures that may restrict the number of building permits available in any given year. These initiatives or other slow or no growth measures could reduce our ability to open new subdivisions and build and sell homes in the affected markets and may create additional costs and administration requirements, which in turn could negatively impact our future home sales and results of operations.

Our homebuilding operations also are affected by environmental laws and regulations pertaining to availability of water, municipal sewage treatment capacity, stormwater discharges, land use, hazardous waste disposal, dust controls, building materials, population density and preservation of endangered species, natural terrain and vegetation.

The particular environmental laws and regulations that apply to any given homebuilding project vary greatly according to a particular site's location, the site's environmental conditions and the present and former uses. These environmental laws may result in project delays, cause us to incur substantial compliance and other costs and/or prohibit or severely restrict homebuilding activity in certain environmentally sensitive locations.

We also are subject to rules and regulations with respect to originating, processing, selling and servicing mortgage loans, which, among other things: prohibit discrimination and establish underwriting guidelines; provide for audits and inspections; require appraisals and/or credit reports on prospective borrowers and disclosure of certain information concerning credit and settlement costs; establish maximum loan amounts; prohibit predatory lending

practices; and regulate the referral of business to affiliated entities. The turmoil caused by the increased number of defaults in subprime and other mortgages during the last industry downturn has encouraged ongoing consumer lawsuits and the investigation of financial services industry practices by governmental authorities. These investigations have included the examination of consumer lending practices, sales of mortgages to financial institutions and other investors and the practices in the financial services segments of homebuilding companies. New rules and regulations or revised interpretations of existing rules and regulations applicable to our mortgage lending operations could result in more stringent compliance standards, which may substantially increase costs of compliance.

***In the ordinary course of business, we are required to obtain surety bonds, the unavailability of which could adversely affect our results of operations and/or cash flows.***

As is customary in the homebuilding industry, we often are required to provide surety bonds to secure our performance under construction contracts, development agreements and other arrangements. Our ability to obtain surety bonds primarily depends upon our credit rating, capitalization, working capital, past performance, management expertise and certain external factors, including the overall capacity of the surety market and the underwriting practices of surety bond issuers. The ability to obtain surety bonds also can be impacted by the willingness of insurance companies to issue surety bonds. If we were unable to obtain surety bonds when required, our results of operations and/or cash flows could be adversely impacted.

***Decreases in the market value of our investments in marketable securities could have an adverse impact on our results of operations.***

We have a material amount of investments in marketable securities, the market value of which is subject to changes from period to period. Decreases in the market value of our marketable securities could have an adverse impact on our statements of financial position, results of operations and cash flow.

***Product liability litigation and warranty claims that arise in the ordinary course of business may be costly.***

As a homebuilder, we are subject to construction defect and home warranty claims, as well as claims associated with the sale and financing of our homes arising in the ordinary course of business. These types of claims can be costly. The costs of insuring against construction defect and product liability claims can be high and the amount of coverage offered by insurance companies may be limited. If we are not able to obtain adequate insurance against these claims, we may incur additional expenses that would have a negative impact on our results of operations in future reporting periods. Additionally, changes in the facts and circumstances of our pending litigation matters could have a material impact on our results of operations and cash flows in future reporting periods.

***Further uncertainty in the mortgage lending industry, including repurchase requirements associated with HomeAmerican's sale of mortgage loans, could negatively impact our results of operations.***

We are subject to risks associated with mortgage loans, including conventional mortgage loans, FHA and VA mortgage loans, previously originated and sold Alt-A and sub-prime mortgage loans, second mortgage loans, high loan-to-value mortgage loans and jumbo mortgage loans (mortgage loans with principal balances that exceed various thresholds in our markets). These risks may include, among other things, compliance with mortgage loan underwriting criteria and the associated homebuyers' performance, which could require HomeAmerican to repurchase certain of those mortgage loans or provide indemnification. Repurchased mortgage loans and/or the settlement of claims associated with such loans could have in the future a substantial impact on HomeAmerican's results of operations, liquidity and cash flow.

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

We may experience noticeable seasonality and quarter-to-quarter variability in homebuilding activity levels. In general, the number of homes delivered and the associated home sale revenues increase during the third and fourth quarters, compared with the first and second quarters. We believe that this type of seasonality reflects the historical

tendency of homebuyers to purchase new homes in the spring and summer with deliveries scheduled in the fall or winter, as well as the scheduling of construction to accommodate seasonal weather conditions in certain markets.

***We are dependent on the services of key employees, and the loss of their services could hurt our business.***

Although we believe that we have made provision for adequately staffing current operations, because of our efforts to “right-size” our organization at times during the past seven years, retaining our skilled people has become a critical area of focus. Our future success depends, in part, on our ability to attract, train and retain skilled personnel. If we are unable to retain our key employees or attract, train and retain other skilled personnel in the future, it could have an adverse impact on our financial and operating results.

***The interests of certain controlling shareholders may be adverse to investors***

Larry A. Mizel, David D. Mandarich and other of our affiliates beneficially own, directly or indirectly, in the aggregate, approximately 26% of our common stock. To the extent they and their affiliates vote their shares in the same manner, their combined stock ownership may effectively give them the power to influence the election of members of our board of directors and other matters reserved for our shareholders. Circumstances may occur in which the interest of these shareholders could be in conflict with your interests. In addition, such persons may have an interest in pursuing transactions that, in their judgment, enhance the value of their equity investment in us, even though such transactions may involve risks to you.

***Information technology failures and data security breaches could harm our business.***

We and our financial services operations use information technology and other computer resources to carry out important operational activities and to maintain our business records. These information technology systems are dependent upon electronic systems and other aspects of the internet infrastructure. A material breach in the security of our information technology systems or other data security controls could result in third parties obtaining customer, employee or company data. Such occurrences could have a material and adverse effect on our consolidated results of operations or financial position.

**Item 1B. Unresolved Staff Comments.**

None

**Item 2. Properties.**

Our corporate office is located at 4350 South Monaco Street, Denver, Colorado 80237, where we lease office space in a 144,000 square foot office building. In some markets, our homebuilding divisions and other MDC subsidiaries lease additional office space. The table below outlines the number of office facilities that are leased and the approximate square footage leased in each market at December 31, 2013. While currently we are satisfied with the suitability and capacity of our office locations, we continue to evaluate them in view of market conditions and the size of our operations.

|            | Number<br>of<br>Leased<br>Facilities | Total<br>Square<br>Footage<br>Leased |
|------------|--------------------------------------|--------------------------------------|
| Arizona    | 2                                    | 18,000                               |
| California | 2                                    | 19,000                               |
| Colorado   | 5                                    | 145,000                              |
| Florida    | 2                                    | 11,000                               |
| Maryland   | 2                                    | 18,000                               |
| Nevada     | 1                                    | 10,000                               |
| Utah       | 1                                    | 6,000                                |
| Virginia   | 3                                    | 13,000                               |
| Washington | 2                                    | 22,000                               |
| Total      | 20                                   | 262,000                              |

**Item 3. Legal Proceedings.**

Because of the nature of the homebuilding business, we and certain of our subsidiaries and affiliates have been named as defendants in various claims, complaints and other legal actions arising in the ordinary course of business, including product liability claims and claims associated with the sale and financing of our homes. In the opinion of management, the outcome of these ordinary course matters will not have a material adverse effect upon our financial

condition, results of operations or cash flows.

**Item 4. Mine Safety Disclosures.**

Not applicable.

**PART II****Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.**

At December 31, 2013, we had 603 shareholders of record. The shares of our common stock are traded on the New York Stock Exchange. The following table sets forth, for the periods indicated, the closing price ranges of our common stock.

|             | Three Months Ended |            |                 |                |
|-------------|--------------------|------------|-----------------|----------------|
|             | March<br>31        | June<br>30 | September<br>30 | December<br>31 |
| <b>2013</b> |                    |            |                 |                |
| High        | \$41.76            | \$39.71    | \$ 34.00        | \$ 32.24       |
| Low         | 35.90              | 31.56      | 27.12           | 27.81          |
| <b>2012</b> |                    |            |                 |                |
| High        | \$27.20            | \$32.67    | \$ 40.15        | \$ 40.62       |
| Low         | 17.77              | 23.76      | 30.81           | 33.11          |

During the year ended December 31, 2013 we did not declare or pay any dividends. We paid dividends of \$2.00 per share during the year ended December 31, 2012. Of the \$2.00 per share in dividends, \$1.00 was in lieu of declaring and paying regular quarterly dividends in calendar year 2013. The following table sets forth the cash dividends declared and paid in 2012.

|                                       | Date of<br>Declaration | Date of<br>Payment | Dividend<br>per Share | Total<br>Dividends<br>Paid |
|---------------------------------------|------------------------|--------------------|-----------------------|----------------------------|
| <b>2012</b>                           |                        |                    |                       |                            |
| First Quarter                         | 01/23/12               | 02/22/12           | \$ 0.25               | \$ 11,994                  |
| Second Quarter                        | 04/23/12               | 05/23/12           | 0.25                  | 11,996                     |
| Third Quarter                         | 07/24/12               | 08/22/12           | 0.25                  | 12,056                     |
| Fourth Quarter                        | 10/22/12               | 11/21/12           | 0.25                  | 12,172                     |
| Accelerated payment of 2013 dividends | 12/13/12               | 12/28/12           | 1.00                  | 48,697                     |
|                                       |                        |                    | \$ 2.00               | \$ 96,915                  |



There were no shares of MDC common stock repurchased during the years ended December 31, 2013, 2012 or 2011. At December 31, 2013, we were authorized to repurchase up to 4,000,000 shares of our common stock.

## Performance Graph

Set forth below is a graph comparing the yearly change in the cumulative total return of MDC's common stock with the cumulative total return of the Standard & Poor's 500 Stock Index and with that of a peer group of other homebuilders over the five-year period ending on December 31, 2013, weighted as of the beginning of that period.

It is assumed in the graph that \$100 was invested (1) in our common stock; (2) in the stocks of the companies in the Standard & Poor's 500 Stock Index; and (3) in the stocks of the peer group companies, just prior to the commencement of the period and that all dividends received within a quarter were reinvested in that quarter. The peer group index is composed of the following companies: Beazer Homes USA, Inc., D.R. Horton, Inc., Hovnanian Enterprises, Inc., KB Home, Lennar Corporation, M/I Homes, Inc., Meritage Homes Corporation, NVR, Inc., Pulte Homes, Inc., The Ryland Group, Inc., Standard Pacific Corp. and Toll Brothers, Inc.

The stock price performance shown on the following graph is not indicative of future price performance.

**COMPARISON OF CUMULATIVE TOTAL RETURN  
OF MDC COMMON STOCK, THE S&P 500 STOCK INDEX  
AND A SELECTED PEER GROUP**



**Item 6. Selected Financial Data**

The data in these tables and related footnotes should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our Consolidated Financial Statements.

|                                                     | Year Ended December 31,                          |             |             |             |             |
|-----------------------------------------------------|--------------------------------------------------|-------------|-------------|-------------|-------------|
|                                                     | 2013                                             | 2012        | 2011        | 2010        | 2009        |
|                                                     | (Dollars in thousands, except per share amounts) |             |             |             |             |
| <b>Income Statement Data</b>                        |                                                  |             |             |             |             |
| Home sale and land sale revenues                    | \$1,629,175                                      | \$1,156,142 | \$817,023   | \$926,905   | \$867,784   |
| Financial services revenues                         | 51,259                                           | 46,881      | 26,086      | 30,473      | 28,318      |
| Total revenues                                      | \$1,680,434                                      | \$1,203,023 | \$843,109   | \$957,378   | \$896,102   |
| Homebuilding pretax income (loss)                   | \$100,323                                        | \$32,617    | \$(110,628) | \$(80,896)  | \$(113,289) |
| Financial services pretax income                    | 29,502                                           | 28,498      | 3,156       | 10,295      | 5,954       |
| Total income (loss) before income taxes             | \$129,825                                        | \$61,115    | \$(107,472) | \$(70,601)  | \$(107,335) |
| Net income (loss) <sup>(1)(2)(3)</sup>              | \$314,385                                        | \$62,699    | \$(98,390)  | \$(64,770)  | \$24,679    |
| Basic earnings (loss) per share                     | \$6.39                                           | \$1.29      | \$(2.12)    | \$(1.40)    | \$0.52      |
| Diluted earnings (loss) per share                   | \$6.34                                           | \$1.29      | \$(2.12)    | \$(1.40)    | \$0.52      |
| Weighted Average Common Shares Outstanding:         |                                                  |             |             |             |             |
| Basic                                               | 48,453,119                                       | 47,660,629  | 46,796,334  | 46,627,815  | 46,537,092  |
| Diluted                                             | 48,831,785                                       | 47,834,156  | 46,796,334  | 46,627,815  | 46,919,362  |
| <b>Balance Sheet Data</b>                           |                                                  |             |             |             |             |
| Cash and cash equivalents                           | \$199,338                                        | \$160,095   | \$343,361   | \$572,225   | \$1,234,252 |
| Marketable securities                               | \$588,067                                        | \$551,938   | \$519,943   | \$968,729   | \$327,944   |
| Total inventories                                   | \$1,411,661                                      | \$1,002,521 | \$806,052   | \$787,659   | \$523,184   |
| Total assets                                        | \$2,595,449                                      | \$1,945,441 | \$1,858,725 | \$2,547,769 | \$2,429,308 |
| Senior notes, net <sup>(3)</sup>                    | \$1,095,620                                      | \$744,842   | \$744,108   | \$1,242,815 | \$997,991   |
| Mortgage repurchase facility                        | \$63,074                                         | \$76,327    | \$48,702    | \$25,434    | \$29,115    |
| Stockholders' equity                                | \$1,213,249                                      | \$880,897   | \$868,636   | \$983,683   | \$1,073,146 |
| Stockholders' equity per common share               | \$24.87                                          | \$18.09     | \$18.11     | \$20.87     | \$22.82     |
| Cash dividends declared per share <sup>(4)</sup>    | \$-                                              | \$2.00      | \$1.00      | \$1.00      | \$1.00      |
| <b>Operational Data</b>                             |                                                  |             |             |             |             |
| Homes delivered (units)                             | 4,710                                            | 3,740       | 2,762       | 3,245       | 3,013       |
| Average selling price                               | \$345                                            | \$308       | \$292       | \$284       | \$278       |
| Net new orders (units)                              | 4,327                                            | 4,342       | 2,887       | 3,261       | 3,306       |
| Homes in backlog at period end (units)              | 1,262                                            | 1,645       | 1,043       | 842         | 826         |
| Estimated backlog sales value at period end         | \$506,000                                        | \$579,000   | \$330,000   | \$269,000   | \$265,000   |
| Estimated average selling price of homes in backlog | \$401                                            | \$352       | \$316       | \$320       | \$321       |

|                                   |     |     |     |     |     |
|-----------------------------------|-----|-----|-----|-----|-----|
| Active subdivisions at period-end | 146 | 148 | 187 | 148 | 133 |
|-----------------------------------|-----|-----|-----|-----|-----|

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Net income for the year ended December 31, 2009 includes the income tax benefit of being able to carry back (1) \$142.6 million of net operating losses due to the expanded NOL carryback provisions contained in the Worker, Homeownership, and Business Assistance Act of 2009, signed into law on November 6, 2009.

(2) Net income for the year ended December 31, 2013 includes the impact of a \$187.6 million reversal of the valuation allowance against our deferred tax assets in the 2013 second quarter.

During 2011, we completed a debt tender offer and redemptions of our 7% Senior Notes due 2012 and 5½% (3) Senior Notes due 2013. As a result of these transactions, we paid \$537.7 million to extinguish \$500 million in debt principal and recorded a \$38.8 million expense for loss on extinguishment of debt.

(4) Total dividends declared per share for the year ended December 31, 2012 include \$1.00 per share representing the accelerated payment of dividends for 2013.

**Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

The following discussion should be read in conjunction with, and is qualified in its entirety by, the Consolidated Financial Statements and Notes thereto included elsewhere in this Annual Report on Form 10-K. This item contains forward-looking statements that involve risks and uncertainties. Actual results may differ materially from those indicated in such forward-looking statements. Factors that may cause such a difference include, but are not limited to, those discussed in "Item 1A, Risk Factors Relating to our Business."

|                                                    | Year Ended December 31,                          |              |              |
|----------------------------------------------------|--------------------------------------------------|--------------|--------------|
|                                                    | 2013                                             | 2012         | 2011         |
|                                                    | (Dollars in thousands, except per share amounts) |              |              |
| <b>Homebuilding:</b>                               |                                                  |              |              |
| Home sale revenues                                 | \$ 1,626,707                                     | \$ 1,150,998 | \$ 805,164   |
| Land sale revenues                                 | 2,468                                            | 5,144        | 11,859       |
| Total home and land sale revenues                  | 1,629,175                                        | 1,156,142    | 817,023      |
| Home cost of sales                                 | (1,336,978 )                                     | (973,120 )   | (686,661 )   |
| Land cost of sales                                 | (1,961 )                                         | (4,823 )     | (10,796 )    |
| Inventory impairments                              | (919 )                                           | (1,105 )     | (12,965 )    |
| Total cost of sales                                | (1,339,858 )                                     | (979,048 )   | (710,422 )   |
| Gross margin                                       | 289,317                                          | 177,094      | 106,601      |
| Gross margin %                                     | 17.8 %                                           | 15.3 %       | 13.0 %       |
| Selling, general and administrative expenses       | (213,283 )                                       | (167,295 )   | (179,105 )   |
| Interest income                                    | 26,938                                           | 23,398       | 26,068       |
| Interest expense                                   | (1,726 )                                         | (808 )       | (20,842 )    |
| Other income (expense)                             | (923 )                                           | 228          | (43,350 )    |
| Homebuilding pretax income (loss)                  | 100,323                                          | 32,617       | (110,628 )   |
| <b>Financial Services:</b>                         |                                                  |              |              |
| Revenues                                           | 51,259                                           | 46,881       | 26,086       |
| Expenses                                           | (25,271 )                                        | (21,645 )    | (26,306 )    |
| Interest and other income                          | 3,514                                            | 3,262        | 3,376        |
| Financial services pretax income                   | 29,502                                           | 28,498       | 3,156        |
| Income before income taxes                         | 129,825                                          | 61,115       | (107,472 )   |
| Benefit from income taxes                          | 184,560                                          | 1,584        | 9,082        |
| Net income (loss)                                  | \$ 314,385                                       | \$ 62,699    | \$ (98,390 ) |
| <b>Earnings (loss) per share:</b>                  |                                                  |              |              |
| Basic                                              | \$ 6.39                                          | \$ 1.29      | \$ (2.12 )   |
| Diluted                                            | \$ 6.34                                          | \$ 1.29      | \$ (2.12 )   |
| <b>Weighted average common shares outstanding:</b> |                                                  |              |              |
| Basic                                              | 48,453,119                                       | 47,660,629   | 46,796,334   |

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|                              |              |              |              |
|------------------------------|--------------|--------------|--------------|
| Diluted                      | 48,831,785   | 47,834,156   | 46,796,334   |
| Dividends declared per share | \$-          | \$2.00       | \$1.00       |
| Cash provided by (used in):  |              |              |              |
| Operating Activities         | \$(269,549 ) | \$(108,819 ) | \$(80,284 )  |
| Investing Activities         | \$(30,402 )  | \$(21,781 )  | \$404,264    |
| Financing Activities         | \$339,194    | \$(52,666 )  | \$(552,844 ) |

## EXECUTIVE SUMMARY

### *Overview*

For the year ended December 31, 2013, we improved in most operating metrics. Significant increases in volume and average selling prices of homes delivered, in addition to notable improvements in our homebuilding selling, general and administrative (“SG&A”) expenses as a percentage of home sale revenues (“SG&A rate”), drove top and bottom line growth for our Homebuilding operations. However, the temporary spike in mortgage interest rates from historically low levels, significant year-over-year home price increases, and the economic uncertainty created by the government shutdown, debt ceiling debates, and the discussion surrounding tapering of federal stimulus, slowed housing demand during the second half of 2013. These factors, combined with a lower average active community count, resulted in a slight year-over-year decline in our net new orders and a year-over-year decrease in ending backlog despite a year-over-year increase in our monthly absorption pace per community. We continue to believe that a solid housing recovery is ongoing, supported by attractive affordability levels, a historically low inventory of available-for-sale housing, and improving economic conditions.

For the year ended December 31, 2013, we reported net income of \$314.4 million, or \$6.34 per diluted share, compared to net income of \$62.7 million, or \$1.29 per diluted share for the year earlier period. The improvement in our performance was driven primarily by a 41% increase in home sale revenues, a 240 basis point improvement in our gross margin from home sales and a 140 basis point reduction in our SG&A rate. The combination of these factors led to a 260 basis point year-over-year improvement in our total pretax operating margin to 7.7%. Our favorable results for the full year were significantly impacted by a \$187.6 million tax benefit related to the reversal of a portion of our deferred tax asset valuation allowance in the second quarter.

Our net new home orders decreased negligibly year-over-year to 4,327 homes, driven largely by an 18% decrease in our average active communities, which was partially offset by a 21% improvement in our monthly absorption pace per active community. Our monthly absorption pace increased despite our implementation of routine price increases in most active subdivisions during the year, which were designed to create an appropriate balance between gross margins and absorption pace.

Our active community count as of December 31, 2013 was 146, down slightly from 148 a year ago. However, our investment in new homebuilding projects over the past year totaling approximately 7,900 lots purchased in 168 communities during the year ended December 31, 2013, 128 of which were new communities, resulted in a 38% year-over-year increase in our total supply of lots owned and under option to approximately 15,800 at December 31, 2013. We believe that this increase in acquisition activity will help drive sequential and year-over-year growth in our active community count in future periods. See “**Forward-Looking Statements**” above.



Our financial services continued to improve with pretax income of \$29.5 million for the year ended December 31, 2013. The slight improvement in our financial services pretax income was attributable to our Other financial services segment, which benefited primarily from an increase in the volume of new home deliveries. The improvement in our Other financial services segment was partially offset by reduced pretax income from our Mortgage operations due to more competitive market conditions that adversely impacted our capture rate and margins on loans locked and originated.

Our financial position remained strong at the end of 2013, as evidenced by our total cash and marketable securities of \$787.4 million, compared to our total senior note debt of \$1,095.6 million. During the first half of 2013, we issued \$350 million of 30-year 6% senior unsecured notes. Additionally, to further strengthen our liquidity, we entered into a 5-year, \$450 million unsecured revolving credit agreement in December 2013. More recently, in January of 2014, we issued \$250 million of 10-year 5.5% senior unsecured notes. We believe that our strong financial position gives us a competitive advantage as we pursue attractive land acquisition opportunities as the housing market improves, which can help us further grow our operations.

**Homebuilding****Pretax Income**

|                                          | Year Ended December 31, |          |       |          |           |        |             |
|------------------------------------------|-------------------------|----------|-------|----------|-----------|--------|-------------|
|                                          | Change                  |          |       | Change   |           |        |             |
|                                          | 2013                    | Amount   | %     | 2012     | Amount    | %      | 2011        |
|                                          | (Dollars in thousands)  |          |       |          |           |        |             |
| <b>Homebuilding pretax income (loss)</b> |                         |          |       |          |           |        |             |
| West                                     | \$65,672                | \$38,596 | 143 % | \$27,076 | \$43,965  | 260 %  | \$(16,889 ) |
| Mountain                                 | 52,392                  | 28,090   | 116 % | 24,302   | 22,905    | 1640 % | 1,397       |
| East                                     | 19,590                  | 8,579    | 78 %  | 11,011   | 18,206    | 253 %  | (7,195 )    |
| Corporate                                | (37,331 )               | (7,559 ) | -25 % | (29,772) | 58,169    | 66 %   | (87,941 )   |
| Total homebuilding pretax income (loss): | \$100,323               | \$67,706 | 208 % | \$32,617 | \$143,245 | 129 %  | \$(110,628) |

The \$67.7 million improvement in our homebuilding financial performance for the year ended December 31, 2013 was driven primarily by a 41% increase in home sale revenues, a 240 basis point improvement in our gross margin from home sales and a 140 basis point reduction in our SG&A rate.

Each of our homebuilding reportable segments, most notably our West and Mountain segments, showed substantial improvements in pretax income for the twelve months ended December 31, 2013 as compared with the same period in 2012, benefiting from significant increases in home sale revenues and gross margins from home sales. Also, excluding a \$2.5 million legal recovery in 2012 for our East segment, our SG&A rates for all homebuilding segments showed improvements. Our pretax loss for our non-operating Corporate reportable segment increased by \$7.6 million primarily due to increases in our general and administrative expenses related to our accrual for higher incentive-based compensation and higher legal expenses, which were partially offset by reduced stock-based compensation expense. While the SG&A expenses increased during 2013 in the Corporate segment, the SG&A rate decreased due to increased homebuilding revenues.

For the year ended December 31, 2012, we reported homebuilding pretax income of \$32.6 million, compared to a pretax loss of \$110.6 million for the year ended December 31, 2011. The \$143.2 million improvement in our homebuilding financial performance was driven primarily by a 43% increase in home sale revenues, a 230 basis point improvement in our gross margin from home sales, a 770 basis point reduction in our SG&A rate and a \$20.0 million decrease in our interest expense. In addition, the 2011 results were adversely impacted by a \$38.8 million charge related to the early extinguishment of \$500 million of debt.

Our West, Mountain and East segments all showed improvements in pretax results for the year ended December 31, 2012 compared to 2011. The improvements in each of these segments were driven by reductions in SG&A expenses and improvements in our gross margins in many markets. The improvements in pretax results were also aided by increases in our homebuilding revenues in our West, Mountain and East segments due to increases in homebuilding deliveries and average price per home delivered. Our pretax results for our non-operating Corporate segment improved \$58.2 million for the year ended December 31, 2012 due primarily to reductions in both interest and SG&A expenses, which included a various significant legal recoveries totaling \$9.8 million during 2012, and a \$38.8 million reduction in loss on extinguishment of senior debt that was recorded in 2011.

*Assets*

|                            | December 31,<br>2013<br>(Dollars in thousands) | 2012         | Change<br>Amount | %  |   |
|----------------------------|------------------------------------------------|--------------|------------------|----|---|
| <b>Homebuilding assets</b> |                                                |              |                  |    |   |
| West                       | \$ 760,450                                     | \$ 459,807   | \$ 300,643       | 65 | % |
| Mountain                   | 418,796                                        | 332,939      | 85,857           | 26 | % |
| East                       | 297,627                                        | 274,199      | 23,428           | 9  | % |
| Corporate                  | 951,809                                        | 692,500      | 259,309          | 37 | % |
| Total homebuilding assets  | \$ 2,428,682                                   | \$ 1,759,445 | \$ 669,237       | 38 | % |

Homebuilding assets in all of our reportable segments, most notably our West segment, increased considerably from December 31, 2012 to December 31, 2013, as higher construction and land acquisition activity drove an increase in our inventory balances. Homebuilding assets in our Corporate segment increased \$259.3 million from December 31, 2012 to December 31, 2013, primarily due to an increase in our deferred tax asset after the \$187.6 million reversal of our deferred tax asset valuation allowance in the 2013 second quarter. The remainder of the increase in our Corporate segment was primarily related to the net proceeds generated from the issuance of \$350 million of 30-year 6% senior unsecured notes, much of which was used for investments in homebuilding inventories.

*Revenues*

|                                    | Year Ended December 31,<br>2013 |           |     | 2012             |           |     | 2011      |
|------------------------------------|---------------------------------|-----------|-----|------------------|-----------|-----|-----------|
|                                    | Change<br>Amount                | %         |     | Change<br>Amount | %         |     |           |
|                                    | (Dollars in thousands)          |           |     |                  |           |     |           |
| <b>Home and land sale revenues</b> |                                 |           |     |                  |           |     |           |
| West                               | \$671,278                       | 155,199   | 30% | \$516,079        | \$243,279 | 89% | \$272,800 |
| Mountain                           | 546,801                         | 191,433   | 54% | 355,368          | 39,179    | 12% | 316,189   |
| East                               | 411,096                         | 126,401   | 44% | 284,695          | 56,661    | 25% | 228,034   |
| Total home and land sale revenues  | \$1,629,175                     | \$473,033 | 41% | \$1,156,142      | \$339,119 | 42% | \$817,023 |

The increases in home and land sale revenues for the years ended December 31, 2013 and 2012 were driven primarily by 26% and 35% increases in new home deliveries, respectively, and 12% and 6% increases in average selling price, respectively.



*New Home Deliveries:*

|            | Year Ended December 31,<br>2013 |              |          | 2012  | % Change     |          |         |        |       |         |  |
|------------|---------------------------------|--------------|----------|-------|--------------|----------|---------|--------|-------|---------|--|
|            | Dollar                          |              | Average  |       | Dollar       |          | Average | Dollar |       | Average |  |
|            | Homes                           |              |          |       | Homes        |          |         | Homes  |       |         |  |
|            | Value                           | Price        |          |       | Value        | Price    |         | Value  | Price |         |  |
|            | (Dollars in thousands)          |              |          |       |              |          |         |        |       |         |  |
| Arizona    | 635                             | \$ 156,308   | \$ 246.2 | 603   | \$ 131,278   | \$ 217.7 | 5 %     | 19 %   | 13 %  |         |  |
| California | 643                             | 243,804      | 379.2    | 543   | 184,490      | 339.8    | 18 %    | 32 %   | 12 %  |         |  |
| Nevada     | 593                             | 163,127      | 275.1    | 604   | 125,725      | 208.2    | -2 %    | 30 %   | 32 %  |         |  |
| Washington | 333                             | 108,038      | 324.4    | 247   | 73,074       | 295.8    | 35 %    | 48 %   | 10 %  |         |  |
| West       | 2,204                           | 671,277      | 304.6    | 1,997 | 514,567      | 257.7    | 10 %    | 30 %   | 18 %  |         |  |
| Colorado   | 1,287                           | 479,619      | 372.7    | 807   | 289,416      | 358.6    | 59 %    | 66 %   | 4 %   |         |  |
| Utah       | 208                             | 65,292       | 313.9    | 226   | 64,006       | 283.2    | -8 %    | 2 %    | 11 %  |         |  |
| Mountain   | 1,495                           | 544,911      | 364.5    | 1,033 | 353,422      | 342.1    | 45 %    | 54 %   | 7 %   |         |  |
| Maryland   | 368                             | 159,169      | 432.5    | 233   | 99,476       | 426.9    | 58 %    | 60 %   | 1 %   |         |  |
| Virginia   | 355                             | 177,142      | 499.0    | 280   | 135,067      | 482.4    | 27 %    | 31 %   | 3 %   |         |  |
| Florida    | 288                             | 74,208       | 257.7    | 195   | 47,915       | 245.7    | 48 %    | 55 %   | 5 %   |         |  |
| Illinois   | -                               | -            | -        | 2     | 551          | 275.5    | N/M     | N/M    | N/M   |         |  |
| East       | 1,011                           | 410,519      | 406.1    | 710   | 283,009      | 398.6    | 42 %    | 45 %   | 2 %   |         |  |
| Total      | 4,710                           | \$ 1,626,707 | \$ 345.4 | 3,740 | \$ 1,150,998 | \$ 307.8 | 26 %    | 41 %   | 12 %  |         |  |

N/M - Not meaningful

|            | Year Ended December 31,<br>2012 |            |          | 2011  | % Change  |          |         |        |      |         |  |  |
|------------|---------------------------------|------------|----------|-------|-----------|----------|---------|--------|------|---------|--|--|
|            | Dollar                          |            | Average  |       | Dollar    |          | Average | Dollar |      | Average |  |  |
|            | Homes                           |            |          |       | Homes     |          |         | Homes  |      | Homes   |  |  |
|            | Value                           | Price      | Value    |       | Price     | Value    | Price   |        |      |         |  |  |
|            | (Dollars in thousands)          |            |          |       |           |          |         |        |      |         |  |  |
| Arizona    | 603                             | \$ 131,278 | \$ 217.7 | 423   | \$ 80,133 | \$ 189.4 | 43 %    | 64 %   | 15 % |         |  |  |
| California | 543                             | 184,490    | 339.8    | 272   | 83,488    | 306.9    | 100 %   | 121 %  | 11 % |         |  |  |
| Nevada     | 604                             | 125,725    | 208.2    | 331   | 61,833    | 186.8    | 82 %    | 103 %  | 11 % |         |  |  |
| Washington | 247                             | 73,074     | 295.8    | 146   | 38,710    | 265.1    | 69 %    | 89 %   | 12 % |         |  |  |
| West       | 1,997                           | 514,567    | 257.7    | 1,172 | 264,164   | 225.4    | 70 %    | 95 %   | 14 % |         |  |  |
| Colorado   | 807                             | 289,416    | 358.6    | 748   | 251,935   | 336.8    | 8 %     | 15 %   | 6 %  |         |  |  |
| Utah       | 226                             | 64,006     | 283.2    | 225   | 61,761    | 274.5    | 0 %     | 4 %    | 3 %  |         |  |  |
| Mountain   | 1,033                           | 353,422    | 342.1    | 973   | 313,696   | 322.4    | 6 %     | 13 %   | 6 %  |         |  |  |
| Maryland   | 233                             | 99,476     | 426.9    | 207   | 90,312    | 436.3    | 13 %    | 10 %   | -2 % |         |  |  |
| Virginia   | 280                             | 135,067    | 482.4    | 211   | 90,844    | 430.5    | 33 %    | 49 %   | 12 % |         |  |  |
| Florida    | 195                             | 47,915     | 245.7    | 190   | 43,450    | 228.7    | 3 %     | 10 %   | 7 %  |         |  |  |
| Illinois   | 2                               | 551        | 275.5    | 9     | 2,698     | 299.8    | N/M     | N/M    | N/M  |         |  |  |

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|       |       |             |          |       |           |          |    |   |    |   |   |   |
|-------|-------|-------------|----------|-------|-----------|----------|----|---|----|---|---|---|
| East  | 710   | 283,009     | 398.6    | 617   | 227,304   | 368.4    | 15 | % | 25 | % | 8 | % |
| Total | 3,740 | \$1,150,998 | \$ 307.8 | 2,762 | \$805,164 | \$ 291.5 | 35 | % | 43 | % | 6 | % |

N/M - Not meaningful

The dollar value of new home deliveries for the year ended December 31, 2013 increased significantly for all of our homebuilding operating segments and was primarily attributable to an increase of 76% in the dollar value of homes in backlog to start 2013 as compared to the beginning of 2012 coupled with significant price increases implemented throughout the year at many of our communities and more speculative home deliveries. Our West and Mountain segments had the strongest increases in beginning backlog due to improved market conditions, especially within each state within the West, and in Colorado in the Mountain segment.

The increase in new home deliveries for the year ended December 31, 2012 was primarily attributable to a 24% increase in the number of homes in backlog to start 2012 as compared to the start of 2011. The West segment was the primary driver of the increase, as the 2012 beginning backlog rose 91% year-over-year due to increased demand, particularly in our Arizona, California and Nevada markets. Resale listings and the level of distressed properties in many of our markets shrank, particularly in the West, which provided a boost in demand for new home sales.

The year-over-year increases in our average selling price for both 2013 and 2012 were primarily driven by price increases instituted at most of our communities in combination with decreased incentives as we took advantage of the improved housing market demand, as well as a shift in the mix of closings to more desirable communities within individual markets.

### *Gross Margin*

Gross margin from home sales for the year ended December 31, 2013 was 17.8%, up 240 basis points from 15.4% for 2012. The increase in our gross margin percentage was primarily due to increased prices and reduced incentives as a percentage of home sales in all of our markets, as lower new and resale inventory supply levels, historically low lending rates and general improvements in the state of the U.S. economy improved homebuyer demand.

Gross margin from home sales for the year ended December 31, 2012 was 15.4%, up 230 basis points from 13.1% for the year earlier period. The increase in gross margins was primarily due to reduced incentives as a percentage of home sales and increased prices in many of our markets, particularly in Arizona and Nevada. In addition, the gross margins were impacted in part by a reduction in impairment charges from \$13.0 million in the year ended December 31, 2011 to \$1.1 million in the year ended December 31, 2012, which was largely offset by a \$6.4 million benefit recorded in 2011 from the settlement of a construction defect claim, the impact of project close-out adjustments and a \$5.5 million warranty accrual reduction in 2011, while 2012 did not include any of these significant adjustments.

Excluding inventory impairments, warranty accrual adjustments and interest in cost of sales, our adjusted gross margin percentage from home sales for the years ended December 31, 2013, 2012 and 2011 was 21.1%, 18.2% and 16.7%, respectively. The table set forth below is a reconciliation of our gross margin and gross margin percentage, as reported, to gross margin from home sales and gross margins from home sales excluding inventory impairments, warranty adjustments and interest in home cost of sales, which is a non-GAAP measure.

| Year Ended December 31, |                               |      |                               |      |                               |
|-------------------------|-------------------------------|------|-------------------------------|------|-------------------------------|
| 2013                    | <i>Gross<br/>Margin<br/>%</i> | 2012 | <i>Gross<br/>Margin<br/>%</i> | 2011 | <i>Gross<br/>Margin<br/>%</i> |



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|                                                      | (Dollars in thousands) |      |   |           |      |   |           |      |   |
|------------------------------------------------------|------------------------|------|---|-----------|------|---|-----------|------|---|
| Gross Margin                                         | \$289,317              | 17.8 | % | \$177,094 | 15.3 | % | \$106,601 | 13.0 | % |
| Less: Land Sale Revenues                             | (2,468 )               |      |   | (5,144 )  |      |   | (11,859 ) |      |   |
| Add: Land Cost of Sales                              | 1,961                  |      |   | 4,823     |      |   | 10,796    |      |   |
| Gross Margin from Home Sales                         | 288,810                | 17.8 | % | 176,773   | 15.4 | % | 105,538   | 13.1 | % |
| Add: Inventory Impairments                           | 919                    |      |   | 1,105     |      |   | 12,965    |      |   |
| Add: Interest in Cost of Sales                       | 54,261                 |      |   | 31,106    |      |   | 21,152    |      |   |
| Add: Warranty Adjustments                            | -                      |      |   | -         |      |   | (5,478 )  |      |   |
| Adjusted Gross Margin from Home Sales <sup>(1)</sup> | \$343,990              | 21.1 | % | \$208,984 | 18.2 | % | \$134,177 | 16.7 | % |

Adjusted gross margin from home sales is a non-GAAP financial measure. We believe this information is meaningful as it isolates the impact that inventory impairments, warranty adjustments and interest have on our

(1) Gross Margin from Home Sales and permits investors to make better comparisons with our competitors, who also break out and adjust gross margins in a similar fashion. Furthermore, this measure was used by us in 2012 as one financial metric criteria for performance-based stock options awarded to certain executive officers.

*Inventory Impairments*

Impairments recognized for the years ended December 31, 2013, 2012 and 2011 are shown in the table below:

|                       | Year Ended December<br>31,<br>2013 2012 2011<br>(Dollars in thousands) |         |          |
|-----------------------|------------------------------------------------------------------------|---------|----------|
| Inventory Impairments |                                                                        |         |          |
| West                  | \$-                                                                    | \$-     | \$8,769  |
| Mountains             | -                                                                      | -       | 2,299    |
| East                  | 919                                                                    | 1,105   | 1,897    |
| Total                 | \$919                                                                  | \$1,105 | \$12,965 |

During the year ended December 31, 2013, we recorded \$0.9 million of inventory impairments related to three projects in our Maryland division in our East segment. In the same division, we recorded \$1.1 million of inventory impairments related to two projects during the year ended December 31, 2012. Based on the slow sales absorption rates experienced during both periods and the estimated sales price reductions required to sell the remaining lots and houses in these communities, it was determined that the fair values were less than the carrying values.

During the year ended December 31, 2011, we recorded \$13.0 million of inventory impairments. These impairments primarily were incurred during the 2011 second and third quarters in select subdivisions, primarily in California and Nevada in our West segment, and Utah in our Mountain segment. The impairment of these specific subdivisions, most of which were purchased during 2010, primarily resulted from lowering anticipated home sales prices from those that were expected at the time we purchased the land, based on our experience with homes sold or closed in these subdivisions. As a result of declining home sales prices at that time, we determined based upon our impairment evaluation, that the fair market values of the land and homes in these subdivisions were less than their carrying values.

The table below shows the number of subdivisions and carrying value of the inventory we tested for impairment during each quarter in the years ended December 31, 2013, 2012 and 2011. The table also includes impairments that we recorded during such periods, as well as the quarter-end fair value, number of lots and number of subdivisions for the impaired inventories. For the years ended December 31, 2013, 2012 and 2011, we used discount rates ranging from 10% to 18% for the subdivisions that were impaired.

| Three Months Ended     | Total Subdivisions Tested for Impairment During Quarter | Carrying Value of Inventory Tested for Impairment During Quarter | Carrying Value of Impaired Inventory Before Impairment at Quarter End | Inventory Impairments | Fair Value of Inventory After Impairments | Number of Subdivisions Impaired During the Quarter | Number of Lots Impaired During the Quarter |
|------------------------|---------------------------------------------------------|------------------------------------------------------------------|-----------------------------------------------------------------------|-----------------------|-------------------------------------------|----------------------------------------------------|--------------------------------------------|
| (Dollars in thousands) |                                                         |                                                                  |                                                                       |                       |                                           |                                                    |                                            |
| March 31, 2013         | 17                                                      | \$ 42,919                                                        | \$ -                                                                  | \$ -                  | \$ -                                      | -                                                  | -                                          |
| June 30, 2013          | 23                                                      | 48,329                                                           | -                                                                     | -                     | -                                         | -                                                  | -                                          |
| September 30, 2013     | 8                                                       | 14,731                                                           | 2,326                                                                 | 350                   | 1,976                                     | 1                                                  | 9                                          |
| December 31, 2013      | 17                                                      | 51,043                                                           | 3,446                                                                 | 569                   | 2,877                                     | 2                                                  | 18                                         |
| Total                  | 65                                                      | \$ 157,022                                                       | \$ 5,772                                                              | \$ 919                | \$ 4,853                                  | 3                                                  | 27                                         |
| March 31, 2012         | 33                                                      | \$ 81,492                                                        | \$ -                                                                  | \$ -                  | \$ -                                      | -                                                  | -                                          |
| June 30, 2012          | 27                                                      | 63,616                                                           | -                                                                     | -                     | -                                         | -                                                  | -                                          |
| September 30, 2012     | 22                                                      | 62,681                                                           | -                                                                     | -                     | -                                         | -                                                  | -                                          |
| December 31, 2012      | 17                                                      | 62,808                                                           | 3,840                                                                 | 1,105                 | 2,735                                     | 2                                                  | 25                                         |
| Total                  | 99                                                      | \$ 270,597                                                       | \$ 3,840                                                              | \$ 1,105              | \$ 2,735                                  | 2                                                  | 25                                         |
| March 31, 2011         | 10                                                      | \$ 80,915                                                        | \$ -                                                                  | \$ -                  | \$ -                                      | -                                                  | -                                          |
| June 30, 2011          | 49                                                      | 95,407                                                           | 29,205                                                                | 8,633                 | 20,572                                    | 9                                                  | 392                                        |
| September 30, 2011     | 50                                                      | 109,247                                                          | 22,613                                                                | 4,049                 | 18,564                                    | 11                                                 | 313                                        |
| December 31, 2011      | 40                                                      | 89,031                                                           | 2,765                                                                 | 283                   | 2,482                                     | 2                                                  | 12                                         |
| Total                  | 149                                                     | \$ 374,600                                                       | \$ 54,583                                                             | \$ 12,965             | \$ 41,618                                 | 22                                                 | 717                                        |

### *Selling, General and Administrative Expenses*

Our SG&A rate decreased 140 basis points from 14.5% in 2012 to 13.1% in 2013. The decrease was primarily driven by improved operating leverage that resulted from higher revenues. The impact of the improved operating leverage on our SG&A rate was partially offset by various legal recoveries generated during the year ended December 31, 2012 (discussed below), that did not recur for the same period in 2013, and certain additional 2013 legal expense accruals discussed below.

For the year ended December 31, 2013, our SG&A expenses were \$213.3 million, compared to \$167.3 million for the year ended December 31, 2012. The increase in SG&A expense was largely attributable to higher incentive-based compensation expense, due to increased profitability, higher commissions expense resulting from increased sales volume, and increased headcount due to our recent growth. In addition, the year ended December 31, 2012 benefited from significant legal recoveries totaling \$9.8 million, whereas 2013 did not benefit from any significant legal recoveries and included additional legal expense accruals for certain matters encountered in the normal course of

business that totaled \$5.9 million. These increases to our 2013 SG&A expense were slightly offset by lower stock-based compensation expense.

Our SG&A rate decreased 770 basis points from 22.2% in 2011 to 14.5% in 2012. The decrease was primarily driven by improved operating leverage that resulted from higher revenues as well as the \$9.8 million in various significant legal recoveries received during 2012 discussed above.

Our SG&A expenses for the year ended December 31, 2012 decreased \$11.8 million to \$167.3 million, compared to \$179.1 million for same period in 2011. The decrease in SG&A was attributable to reductions in salaries and other overhead costs and the \$9.8 million in significant legal recoveries discussed above. These items were partially offset by higher commissions expense resulting from increased sales volume.

*Interest Income*

Our interest income for the years ended December 31, 2013, 2012 and 2011 was \$26.9 million, \$23.4 million and \$26.1 million, respectively. The changes in interest income over each period were attributable to the year-over-year changes in our cash and cash equivalents and marketable securities balances, as well as changing yields.

*Interest Expense*

For the years ended December 31, 2013, 2012 and 2011, we expensed \$1.7 million, \$0.8 million and \$20.8 million of interest, respectively, related to the portion of our homebuilding debt that exceeded our qualified assets. The year-over-year decrease from 2011 to 2012 was the result of a significant reduction in the amount by which our homebuilding debt exceeded our qualified assets, resulting primarily from the repayment of \$500 million of senior debt during the latter half of 2011 in addition to an increase in total inventories from 2011 to 2012.

*Other Income (Expense)*

For the years ended December 31, 2013, 2012 and 2011, our other income (expense) was \$(0.9) million, \$0.2 million and \$(43.4) million, respectively. Other expense for the year ended December 31, 2011 was largely related to a \$38.8 million charge for the early extinguishment of \$500 million of debt.

**Other Homebuilding Operating Data***Net New Orders:*

| Year Ended December 31,<br>2013 |        |         | 2012       |       |        | % Change |            |          |
|---------------------------------|--------|---------|------------|-------|--------|----------|------------|----------|
| Homes                           | Dollar | Average | Monthly    | Homes | Dollar | Average  | Monthly    | % Change |
|                                 | Value  | Price   | Absorption |       | Value  | Price    | Absorption |          |
|                                 |        |         | Rate *     |       |        |          | Rate *     |          |
| (Dollars in thousands)          |        |         |            |       |        |          |            |          |

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|            |       |              |          |      |       |              |          |      |      |       |      |
|------------|-------|--------------|----------|------|-------|--------------|----------|------|------|-------|------|
| Arizona    | 645   | \$ 165,101   | \$ 256.0 | 2.91 | 625   | \$ 137,159   | \$ 219.5 | 2.93 | 3 %  | 20 %  | 17 % |
| California | 561   | 237,694      | 423.7    | 3.90 | 654   | 225,174      | 344.3    | 3.11 | -14% | 6 %   | 23 % |
| Nevada     | 529   | 162,270      | 306.7    | 3.47 | 652   | 146,094      | 224.1    | 3.10 | -19% | 11 %  | 37 % |
| Washington | 300   | 98,156       | 327.2    | 2.19 | 272   | 82,325       | 302.7    | 2.14 | 10 % | 19 %  | 8 %  |
| West       | 2,035 | 663,221      | 325.9    | 3.11 | 2,203 | 590,752      | 268.2    | 2.90 | -8 % | 12 %  | 22 % |
| Colorado   | 1,234 | 466,285      | 377.9    | 2.67 | 1,044 | 364,056      | 348.7    | 1.90 | 18 % | 28 %  | 8 %  |
| Utah       | 153   | 48,893       | 319.6    | 1.80 | 239   | 71,080       | 297.4    | 1.19 | -36% | -31 % | 7 %  |
| Mountain   | 1,387 | 515,178      | 371.4    | 2.53 | 1,283 | 435,136      | 339.2    | 1.71 | 8 %  | 18 %  | 9 %  |
| Maryland   | 314   | 145,310      | 462.8    | 1.45 | 303   | 129,891      | 428.7    | 1.39 | 4 %  | 12 %  | 8 %  |
| Virginia   | 273   | 136,054      | 498.4    | 2.07 | 362   | 179,744      | 496.5    | 2.20 | -25% | -24 % | 0 %  |
| Florida    | 318   | 84,897       | 267.0    | 2.09 | 189   | 46,493       | 246.0    | 1.06 | 68 % | 83 %  | 9 %  |
| Illinois   | -     | -            | -        | -    | 2     | 550          | 275.0    | N/M  | N/M  | N/M   | N/M  |
| East       | 905   | 366,261      | 404.7    | 1.81 | 856   | 356,678      | 416.7    | 1.52 | 6 %  | 3 %   | -3 % |
| Total      | 4,327 | \$ 1,544,660 | \$ 357.0 | 2.54 | 4,342 | \$ 1,382,566 | \$ 318.4 | 2.10 | 0 %  | 12 %  | 12 % |

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|                        | Year Ended December 31,<br>2012 |                 |                  |                                 | 2011  |                 |                  |                                 | % Change |                 |                  |  |
|------------------------|---------------------------------|-----------------|------------------|---------------------------------|-------|-----------------|------------------|---------------------------------|----------|-----------------|------------------|--|
|                        | Homes                           | Dollar<br>Value | Average<br>Price | Monthly<br>Absorption<br>Rate * | Homes | Dollar<br>Value | Average<br>Price | Monthly<br>Absorption<br>Rate * | Homes    | Dollar<br>Value | Average<br>Price |  |
| (Dollars in thousands) |                                 |                 |                  |                                 |       |                 |                  |                                 |          |                 |                  |  |
| Arizona                | 625                             | \$137,159       | \$219.5          | 2.93                            | 467   | \$87,223        | \$186.8          | 6.71                            | 34 %     | 57 %            | 18 %             |  |
| California             | 654                             | 225,174         | 344.3            | 3.11                            | 311   | 92,760          | 298.3            | 1.73                            | 110 %    | 143 %           | 15 %             |  |
| Nevada                 | 652                             | 146,094         | 224.1            | 3.10                            | 411   | 75,011          | 182.5            | 1.96                            | 59 %     | 95 %            | 23 %             |  |
| Washington             | 272                             | 82,325          | 302.7            | 2.14                            | 124   | 32,577          | 262.7            | 1.85                            | 119 %    | 153 %           | 15 %             |  |
| West                   | 2,203                           | 590,752         | 268.2            | 2.90                            | 1,313 | 287,571         | 219.0            | 2.50                            | 68 %     | 105 %           | 22 %             |  |
| Colorado               | 1,044                           | 364,056         | 348.7            | 1.90                            | 708   | 240,671         | 339.9            | 1.47                            | 47 %     | 51 %            | 3 %              |  |
| Utah                   | 239                             | 71,080          | 297.4            | 1.19                            | 224   | 61,760          | 275.7            | 1.00                            | 7 %      | 15 %            | 8 %              |  |
| Mountain               | 1,283                           | 435,136         | 339.2            | 1.71                            | 932   | 302,431         | 324.5            | 1.32                            | 38 %     | 44 %            | 5 %              |  |
| Maryland               | 303                             | 129,891         | 428.7            | 1.39                            | 194   | 87,279          | 449.9            | 1.30                            | 56 %     | 49 %            | -5 %             |  |
| Virginia               | 362                             | 179,744         | 496.5            | 2.20                            | 244   | 109,103         | 447.1            | 1.88                            | 48 %     | 65 %            | 11 %             |  |
| Florida                | 189                             | 46,493          | 246.0            | 1.06                            | 196   | 45,592          | 232.6            | 1.15                            | -4 %     | 2 %             | 6 %              |  |
| Illinois               | 2                               | 550             | 275.0            | N/M                             | 8     | 2,279           | 284.9            | N/M                             | N/M      | N/M             | -3 %             |  |
| East                   | 856                             | 356,678         | 416.7            | 1.52                            | 642   | 244,253         | 380.5            | 1.43                            | 33 %     | 46 %            | 10 %             |  |
| Total                  | 4,342                           | \$1,382,566     | \$318.4          | 2.10                            | 2,887 | \$834,255       | \$289.0          | 1.72                            | 50 %     | 66 %            | 10 %             |  |

\* Calculated as total net new orders in period ÷ average active communities during period ÷ number of months in period

N/M - Not meaningful

Net new orders for the year ended December 31, 2013 decreased slightly to 4,327 homes, compared with 4,342 homes for the year ended December 31, 2012, as a 21% increase in our monthly absorption rate to 2.54 per community was offset by an 18% decline in our average community count. The declines in our California, Nevada and Utah markets were driven by a decline in average active subdivisions during the year as monthly absorption rates were up in each of these markets. Virginia also saw a decline in net new orders resulting from a decline in average active subdivisions as well as monthly absorption rate. Substantial improvements in the monthly absorption rate for our Colorado and Florida markets sufficiently offset year-over-year declines in average active subdivisions driving increases in net new orders. The increase in the dollar value of new orders was due to higher average price per home, which was driven by price increases instituted at most of our communities and a shift in product mix to more move-up homes.

Net new orders for the year ended December 31, 2012 increased 50% to 4,342 homes, compared with 2,887 homes for the year ended December 31, 2011. Our monthly sales absorption rate for the year ended December 31, 2012 was 2.10 per community compared to 1.72 per community for the year ended December 31, 2011. We experienced substantial order growth in most of our homebuilding segments due to a combination of a change in our sales processes and procedures, and the overall improvement in housing market conditions. Our West segment experienced the most

significant increase due to particularly strong demand.



*Active Subdivisions:*

|                        | At December 31, |             |   |      |             |       |
|------------------------|-----------------|-------------|---|------|-------------|-------|
|                        | 2013            | %<br>Change |   | 2012 | %<br>Change | 2011  |
| Arizona                | 25              | 108         | % | 12   | -52         | % 25  |
| California             | 11              | -15         | % | 13   | -24         | % 17  |
| Nevada                 | 15              | 25          | % | 12   | -40         | % 20  |
| Washington             | 13              | 30          | % | 10   | 11          | % 9   |
| West                   | 64              | 36          | % | 47   | -34         | % 71  |
| Colorado               | 38              | -10         | % | 42   | -11         | % 47  |
| Utah                   | 5               | -64         | % | 14   | -33         | % 21  |
| Mountain               | 43              | -23         | % | 56   | -18         | % 68  |
| Maryland               | 17              | -6          | % | 18   | 13          | % 16  |
| Virginia               | 10              | -17         | % | 12   | -20         | % 15  |
| Florida                | 12              | -20         | % | 15   | -12         | % 17  |
| East                   | 39              | -13         | % | 45   | -6          | % 48  |
| Total                  | 146             | -1          | % | 148  | -21         | % 187 |
| Average for Year Ended | 142             | -18         | % | 173  | 1           | % 171 |

The year-over-year slight decrease in active subdivisions for 2013 and larger decrease for 2012 were primarily caused by higher than expected sales in each year resulting in certain subdivisions selling out more quickly than anticipated. Furthermore, active subdivisions for both periods were negatively impacted by our decision to slow the pace of new community acquisitions from the second half of 2011 through the first half of 2012 in light of uncertainties regarding future economic conditions at that time. Delays encountered with various municipalities also adversely impacted our ability to open new communities during 2013.

However, based on our significant land acquisition activity over the past year and our efforts to open communities, we have increased our active subdivisions count by 9% from 134 active subdivisions as of September 30, 2013, marking the largest sequential active subdivision increase since the fourth quarter of 2011.

*Cancellation Rate:*

|            | Year Ended December 31, |        |   |      |        |        |
|------------|-------------------------|--------|---|------|--------|--------|
|            | 2013                    | Change |   | 2012 | Change | 2011   |
| Arizona    | 17 %                    | -4     | % | 21 % | -13    | % 34 % |
| California | 24 %                    | 1      | % | 23 % | -15    | % 38 % |
| Nevada     | 21 %                    | 4      | % | 17 % | -20    | % 37 % |
| Washington | 18 %                    | -2     | % | 20 % | 1      | % 19 % |

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|          |      |    |   |    |   |     |   |    |   |
|----------|------|----|---|----|---|-----|---|----|---|
| West     | 20 % | 0  | % | 20 | % | -15 | % | 35 | % |
| Colorado | 22 % | -1 | % | 23 | % | -13 | % | 36 | % |
| Utah     | 22 % | -1 | % | 23 | % | -19 | % | 42 | % |
| Mountain | 22 % | -1 | % | 23 | % | -14 | % | 37 | % |
| Maryland | 25 % | -9 | % | 34 | % | -10 | % | 44 | % |
| Virginia | 26 % | 1  | % | 25 | % | -6  | % | 31 | % |
| Florida  | 22 % | -2 | % | 24 | % | -14 | % | 38 | % |
| East     | 25 % | -3 | % | 28 | % | -10 | % | 38 | % |
| Total    | 22 % | -1 | % | 23 | % | -13 | % | 36 | % |

For the year ended December 31, 2013, our cancellation rate of 22% was slightly better than the prior year. Our cancellation rates were most improved in our Maryland and Arizona markets, primarily driven by various efforts to enhance the quality of our backlog, including reduced acceptance of contingencies and enhanced review of buyer creditworthiness before the ratification of sales contracts. The increase in cancellation rate for our Nevada market was due to a decline in gross orders from lower average active community counts and the inability of certain buyers to qualify for mortgage financing.

Our cancellation rate for the year ended December 31, 2012 was 23% compared to 36% for the year ended December 31, 2011. The improvement in our cancellation rate reflected the overall improvement in housing market conditions and the implementation of more strict underwriting standards for recognizing new home orders as a part of our efforts to improve our sales processes. We experienced our highest cancellation rate in the East segment, due to more cancellations in our Maryland market resulting from efforts to reduce contingent buyers in backlog, and we experienced our lowest cancellation rate in the West segment, where we experienced strong demand in each market within this segment during 2012.

#### Backlog:

|                        | At December 31,<br>2013 |                 | % Change |                 | 2012  |                 | % Change |                 | 2011  |                 |
|------------------------|-------------------------|-----------------|----------|-----------------|-------|-----------------|----------|-----------------|-------|-----------------|
|                        | Homes                   | Dollar<br>Value | Homes    | Dollar<br>Value | Homes | Dollar<br>Value | Homes    | Dollar<br>Value | Homes | Dollar<br>Value |
| (Dollars in thousands) |                         |                 |          |                 |       |                 |          |                 |       |                 |
| Arizona                | 160                     | \$43,184        | 7 %      | 23 %            | 150   | \$35,064        | 17 %     | 30 %            | 128   | \$26,875        |
| California             | 147                     | 71,855          | -36 %    | -8 %            | 229   | 78,400          | 94 %     | 110 %           | 118   | 37,341          |
| Nevada                 | 140                     | 49,350          | -31 %    | -2 %            | 204   | 50,533          | 31 %     | 69 %            | 156   | 29,969          |
| Washington             | 46                      | 16,430          | -42 %    | -39 %           | 79    | 26,761          | 46 %     | 79 %            | 54    | 14,958          |
| West                   | 493                     | 180,819         | -26 %    | -5 %            | 662   | 190,758         | 45 %     | 75 %            | 456   | 109,143         |
| Colorado               | 417                     | 171,688         | -11 %    | -1 %            | 470   | 174,280         | 102 %    | 106 %           | 233   | 84,519          |
| Utah                   | 26                      | 8,422           | -68 %    | -66 %           | 81    | 25,058          | 19 %     | 30 %            | 68    | 19,253          |
| Mountain               | 443                     | 180,110         | -20 %    | -10 %           | 551   | 199,338         | 83 %     | 92 %            | 301   | 103,772         |
| Maryland               | 129                     | 65,435          | -30 %    | -17 %           | 183   | 79,162          | 62 %     | 62 %            | 113   | 48,987          |
| Virginia               | 103                     | 51,594          | -44 %    | -44 %           | 185   | 92,303          | 80 %     | 85 %            | 103   | 49,953          |
| Florida                | 94                      | 28,037          | 47 %     | 61 %            | 64    | 17,452          | -9 %     | -3 %            | 70    | 18,020          |
| East                   | 326                     | 145,066         | -25 %    | -23 %           | 432   | 188,917         | 51 %     | 62 %            | 286   | 116,960         |
| Total                  | 1,262                   | \$505,995       | -23 %    | -13 %           | 1,645 | \$579,013       | 58 %     | 76 %            | 1,043 | \$329,875       |

#### Average Prices of Homes in Backlog:

|            | At December 31,<br>2013 |    | % Change |         | 2012 |   | % Change |  | 2011 |  |
|------------|-------------------------|----|----------|---------|------|---|----------|--|------|--|
| Arizona    | \$269.9                 | 15 | %        | \$233.8 | 11   | % | \$210.0  |  |      |  |
| California | 488.8                   | 43 | %        | 342.4   | 8    | % | 316.4    |  |      |  |
| Nevada     | 352.5                   | 42 | %        | 247.7   | 29   | % | 192.1    |  |      |  |
| Washington | 357.2                   | 5  | %        | 338.7   | 22   | % | 277.0    |  |      |  |
| West       | 366.8                   | 27 | %        | 288.2   | 20   | % | 239.3    |  |      |  |
| Colorado   | 411.7                   | 11 | %        | 370.8   | 2    | % | 362.7    |  |      |  |

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|          |         |    |   |         |    |   |         |
|----------|---------|----|---|---------|----|---|---------|
| Utah     | 323.9   | 5  | % | 309.4   | 9  | % | 283.1   |
| Mountain | 406.6   | 12 | % | 361.8   | 5  | % | 344.8   |
| Maryland | 507.2   | 17 | % | 432.6   | 0  | % | 433.5   |
| Virginia | 500.9   | 0  | % | 498.9   | 3  | % | 485.0   |
| Florida  | 298.3   | 9  | % | 272.7   | 6  | % | 257.4   |
| East     | 445.0   | 2  | % | 437.3   | 7  | % | 409.0   |
| Total    | \$400.9 | 14 | % | \$352.0 | 11 | % | \$316.3 |

The dollar value of backlog at December 31, 2013 decreased in all segments and in total by 13% year-over-year. The decrease was driven by a 23% decrease in homes in the backlog, which was partially offset by a 14% increase in the average price of homes in backlog. Florida and Arizona were the only markets that showed increases. The increase in Florida was due to higher sales absorption rates generated in 2013 as compared to 2012 as well as our expansion into Orlando and South Florida in 2013. The increase in Arizona was due primarily to higher active subdivision counts during 2013. The decreases in all other markets were driven by lower sales activity, which was due to lower average active communities in the latter half of 2013 when compared to the same period in 2012.

The 58% increase in the number of homes in our backlog from December 31, 2011 to December 31, 2012 was primarily the result of the increase in net orders during the year ended December 31, 2012. Our West and Mountain segments experienced the strongest growth in backlog due to improved market conditions, especially within each state within the West, and in Colorado in the Mountain segment.

*Homes Completed or Under Constructions (WIP lots):*

|                                             | December 31, 2013 |        | December 31, 2012 |        | December 31, 2011 |   |
|---------------------------------------------|-------------------|--------|-------------------|--------|-------------------|---|
|                                             |                   | %      |                   | %      |                   | % |
|                                             |                   | Change |                   | Change |                   |   |
| Unsold:                                     |                   |        |                   |        |                   |   |
| Completed                                   | 378               | 71 %   | 221               | 51 %   | 146               |   |
| Under construction                          | 1,038             | 72 %   | 604               | 84 %   | 328               |   |
| Total unsold started homes                  | 1,416             | 72 %   | 825               | 74 %   | 474               |   |
| Sold homes under construction or completed  | 981               | -14 %  | 1,147             | 80 %   | 638               |   |
| Model homes                                 | 258               | 17 %   | 221               | -2 %   | 226               |   |
| Total homes completed or under construction | 2,655             | 21 %   | 2,193             | 64 %   | 1,338             |   |

The increase in our total homes completed or under construction from December 31, 2012 to December 31, 2013 was driven by increases in the total number of unsold homes that were either completed or under construction. We intentionally started more speculative homes during 2013 in light of increased homebuyer demand, improving market conditions, low levels of resale and new home inventories, and the recent improvements in our speculative homes gross margins.

The increase in our total homes completed or under construction from December 31, 2011 to December 31, 2012 was primarily related to a higher number of sold homes started in light of our year-over-year increase in backlog. We also intentionally increased our inventory of unsold started homes based on the overall improvement in housing market conditions and increased demand for started homes.

*Lots Owned and Optioned (including homes completed or under construction):*

| December 31, 2013 |               |                       |                   | December 31, 2012 |               |                       |                   | December 31, 2011 |               |                       |  |
|-------------------|---------------|-----------------------|-------------------|-------------------|---------------|-----------------------|-------------------|-------------------|---------------|-----------------------|--|
| Lots Owned        | Lots Optioned | Total Lots Controlled | % Change in Total | Lots Owned        | Lots Optioned | Total Lots Controlled | % Change in Total | Lots Owned        | Lots Optioned | Total Lots Controlled |  |

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|            |        |       |        |     |   |       |       |        |     |   |       |       |        |
|------------|--------|-------|--------|-----|---|-------|-------|--------|-----|---|-------|-------|--------|
| Arizona    | 2,838  | 74    | 2,912  | 58  | % | 1,763 | 80    | 1,843  | 79  | % | 955   | 77    | 1,032  |
| California | 1,765  | 129   | 1,894  | 75  | % | 1,080 | -     | 1,080  | -22 | % | 1,384 | -     | 1,384  |
| Nevada     | 1,503  | 391   | 1,894  | 50  | % | 1,226 | 40    | 1,266  | 3   | % | 1,191 | 33    | 1,224  |
| Washington | 537    | 182   | 719    | 13  | % | 472   | 162   | 634    | 19  | % | 385   | 147   | 532    |
| West       | 6,643  | 776   | 7,419  | 54  | % | 4,541 | 282   | 4,823  | 16  | % | 3,915 | 257   | 4,172  |
| Colorado   | 4,292  | 1,093 | 5,385  | 40  | % | 3,335 | 508   | 3,843  | 9   | % | 3,220 | 321   | 3,541  |
| Utah       | 538    | 19    | 557    | 2   | % | 532   | 13    | 545    | -13 | % | 607   | 17    | 624    |
| Mountain   | 4,830  | 1,112 | 5,942  | 35  | % | 3,867 | 521   | 4,388  | 5   | % | 3,827 | 338   | 4,165  |
| Maryland   | 446    | 304   | 750    | -16 | % | 577   | 315   | 892    | -23 | % | 566   | 596   | 1,162  |
| Virginia   | 469    | 133   | 602    | -26 | % | 553   | 263   | 816    | -4  | % | 678   | 173   | 851    |
| Florida    | 650    | 423   | 1,073  | 105 | % | 365   | 159   | 524    | -22 | % | 330   | 340   | 670    |
| Illinois   | -      | -     | -      | 0   | % | -     | -     | -      | N/M |   | 125   | -     | 125    |
| East       | 1,565  | 860   | 2,425  | 9   | % | 1,495 | 737   | 2,232  | -21 | % | 1,699 | 1,109 | 2,808  |
| Total      | 13,038 | 2,748 | 15,786 | 38  | % | 9,903 | 1,540 | 11,443 | 3   | % | 9,441 | 1,704 | 11,145 |

N/M - Not meaningful

As a result of the significant increase in our land acquisition activity during 2013, we increased our owned and optioned lot supply as of December 31, 2013 by 38% year-over-year, even after a 26% year-over-year increase in new home deliveries in 2013. The majority of the increase in our lot supply occurred in Colorado in our Mountain segment and all markets in our West segment, where we experienced strong demand over the last year, as well as in Florida, where we expanded our footprint into Orlando and South Florida. We believe that these continued increases in lots owned and under option will help us generate meaningful increases in our active community count during 2014. See **"Forward-Looking Statements"** above.

We increased our supply of owned and optioned lots by 3% during the year ended December 31, 2012 to 11,443 total lots, even after a 35% year-over-year increase in new home deliveries in 2012. Our lot supply increased most significantly in the West, particularly in Arizona, which was up 79%, and in Colorado, which was up 9%. These increases were partially offset by a 21% decline in lots in our East segment due to decreases in each market within that segment.

## Financial Services

|                                         | Year Ended December 31, |                  |      |          |                  |       |          |  |
|-----------------------------------------|-------------------------|------------------|------|----------|------------------|-------|----------|--|
|                                         | 2013                    | Change<br>Amount | %    | 2012     | Change<br>Amount | %     | 2011     |  |
|                                         | (Dollars in thousands)  |                  |      |          |                  |       |          |  |
| <b>Financial services revenues</b>      |                         |                  |      |          |                  |       |          |  |
| Mortgage operations                     | \$34,976                | \$(147)          | 0 %  | \$35,123 | \$17,316         | 97 %  | \$17,807 |  |
| Other                                   | 16,283                  | 4,525            | 38 % | 11,758   | 3,479            | 42 %  | 8,279    |  |
| Total financial services revenues       | \$51,259                | \$4,378          | 9 %  | \$46,881 | \$20,795         | 80 %  | \$26,086 |  |
| <b>Financial services pretax income</b> |                         |                  |      |          |                  |       |          |  |
| Mortgage operations                     | \$21,608                | \$(2,331)        | -10% | \$23,939 | \$23,545         | 5976% | \$394    |  |
| Other                                   | 7,894                   | 3,335            | 73 % | 4,559    | 1,797            | 65 %  | 2,762    |  |
| Total financial services pretax income  | \$29,502                | \$1,004          | 4 %  | \$28,498 | \$25,342         | 803 % | \$3,156  |  |

Our financial services pretax income for the year ended December 31, 2013 was up slightly over the prior year period. The increase was driven by a \$3.3 million increase in our Other financial services segment, which consists of our insurance and title operations, and was partially offset by a \$2.3 million decrease in pretax income for our Mortgage operations segment. The decline in pretax income for Mortgage operations was primarily due to per unit reduced origination income and gains on loans locked and sold compared to a year ago resulting largely from a more competitive mortgage market and higher interest rates. In addition, higher general and administrative expenses, due to added employees hired to handle additional loan volume, and higher loan loss reserve expenses, caused by a slight increase in claims activity from our third party loan purchasers, adversely impacted the profitability of our Mortgage operations for the year ended December 31, 2013.

The increase in our financial services pretax income for the year ended December 31, 2012 from 2011 was driven primarily by a year-over-year increase of \$23.5 million in our Mortgage operations pretax income of \$23.9 million for the year ended December 31, 2012. The improvement in our mortgage operation's profitability was driven largely by year-over-year increases of: (1) \$7.1 million from the marketing gains on sales of mortgage loans; (2) \$4.7 million from the corresponding sale of servicing rights associated with those mortgage loans and; (3) \$2.3 million from origination income for the year ended December 31, 2012. These increases aggregated \$14.1 million and were due to favorable mortgage market conditions, increases in the volume of loans locked and originated, and a decrease in the level of special financing programs that we offered our homebuyers. Our mortgage operation's profitability for the year ended December 31, 2012 also benefited from a year-over-year decrease in our loan loss reserve expense by \$7.7 million due to reduced repurchase and indemnity claims received from third-party purchasers of our mortgage loans and reductions in settlement claims paid by HomeAmerican. During 2011, the Company's mortgage subsidiary entered into various settlements with third parties concerning claims and potential claims to repurchase certain previously sold mortgage loans, which resulted in an increase in its loan loss reserve of \$8.0 million. The balance of our financial services pretax income, which consisted of income from our insurance and title operations, was \$4.6 million for the year ended December 31, 2012, as compared with \$2.8 million for the year ended December 31, 2011. Because many components of the expenses for our financial services operations do not change in direct relation to revenues, the increase in our 2012 financial services revenue, combined with a decrease in loan loss reserve expenses, caused a significant increase in our financial services profit margin percentage.



The following table sets forth information for our Mortgage operations relating to mortgage loans originated and capture rate. The “capture rate” is defined as the number of mortgage loans originated by our Mortgage operations for our homebuyers as a percent of our total home closings.

|                                                               | Year Ended December 31, |                              |    |            |     |                              |    |            |     |   |
|---------------------------------------------------------------|-------------------------|------------------------------|----|------------|-----|------------------------------|----|------------|-----|---|
|                                                               | 2013                    | % or<br>Percentage<br>Change |    | 2012       |     | % or<br>Percentage<br>Change |    | 2011       |     |   |
|                                                               | (Dollars in thousands)  |                              |    |            |     |                              |    |            |     |   |
| <b>Total Originations<br/>(including transfer loans):</b>     |                         |                              |    |            |     |                              |    |            |     |   |
| Loans                                                         | 2,947                   | 15                           | %  | 2,557      | 23  | %                            |    | 2,076      |     |   |
| Principal                                                     | \$ 890,404              | 24                           | %  | \$ 715,542 | 29  | %                            |    | \$ 556,558 |     |   |
| <b>Capture Rate Data:</b>                                     |                         |                              |    |            |     |                              |    |            |     |   |
| Capture rate as % of all homes delivered                      | 61                      | %                            | -5 | %          | 66  | %                            | -6 | %          | 72  | % |
| Capture rate as % of all homes delivered excluding cash sales | 65                      | %                            | -8 | %          | 73  | %                            | -6 | %          | 79  | % |
| <b>Mortgage Loan<br/>Origination Product Mix:</b>             |                         |                              |    |            |     |                              |    |            |     |   |
| FHA loans                                                     | 24                      | %                            | -8 | %          | 32  | %                            | -8 | %          | 40  | % |
| Other government loans (VA & USDA)                            | 30                      | %                            | 0  | %          | 30  | %                            | 2  | %          | 28  | % |
| Total government loans                                        | 54                      | %                            | -8 | %          | 62  | %                            | -6 | %          | 68  | % |
| Conventional loans                                            | 46                      | %                            | 8  | %          | 38  | %                            | 6  | %          | 32  | % |
|                                                               | 100                     | %                            | 0  | %          | 100 | %                            | 0  | %          | 100 | % |
| <b>Loan Type:</b>                                             |                         |                              |    |            |     |                              |    |            |     |   |
| Fixed rate                                                    | 96                      | %                            | -3 | %          | 99  | %                            | 3  | %          | 96  | % |
| ARM                                                           | 4                       | %                            | 3  | %          | 1   | %                            | -3 | %          | 4   | % |
| <b>Credit Quality:</b>                                        |                         |                              |    |            |     |                              |    |            |     |   |
| Average FICO Score                                            | 733                     |                              | 0  | %          | 730 |                              | 0  | %          | 727 |   |
| <b>Other Data:</b>                                            |                         |                              |    |            |     |                              |    |            |     |   |
| Average combined LTV ratio                                    | 89                      | %                            | -1 | %          | 90  | %                            | -1 | %          | 91  | % |
| Full documentation loans                                      | 100                     | %                            | 0  | %          | 100 | %                            | 0  | %          | 100 | % |
| Non-full documentation loans                                  | 0                       | %                            | 0  | %          | 0   | %                            | 0  | %          | 0   | % |
| <b>Loans Sold to Third Parties:</b>                           |                         |                              |    |            |     |                              |    |            |     |   |
| Loans                                                         | 3,035                   | 24                           | %  | 2,457      | 21  | %                            |    | 2,023      |     |   |
| Principal                                                     | \$ 913,309              | 35                           | %  | \$ 675,422 | 24  | %                            |    | \$ 545,613 |     |   |

During 2012 and 2013, as a result of (1) increases in the amount that FHA charges to insure mortgages, (2) increases in home prices, which can limit a borrower's ability to use FHA insured mortgages in connection with the purchase of a home, and (3) structural changes in the FHA mortgage insurance program, which extended the period of time during which the borrower must pay a mortgage insurance premium, we have seen significant year-over-year declines in our originations of FHA loans as a percentage of our total loans originated.

## Income Taxes

We recorded an income tax benefit of \$184.6 million for the year ended December 31, 2013 compared to income tax benefits of \$1.6 million and \$9.1 million for the same periods in 2012 and 2011, respectively.

The income tax benefit for the year ended December 31, 2013 was due primarily to a \$187.6 million reversal of a significant portion of our deferred tax asset valuation allowance in the 2013 second quarter in addition to a \$6.5 million benefit from energy tax credits relating to current and prior years. These amounts were slightly offset by an \$11.9 million write-off of a deferred tax asset as a result of the termination of certain post-retirement pension benefits contained in the employment agreements of our Chief Executive Officer and Chief Operating Officer in the 2013 fourth quarter. We concluded that the reversal of a portion of our valuation allowance was appropriate after determining that it was more likely than not, after our evaluation of all relevant positive and negative evidence, that we would be able to realize most of our deferred tax assets within the allowable carryforward periods. As of December 31, 2013, we had a \$8.2 million deferred tax asset valuation allowance remaining that related to various state net operating loss carryforwards where realization is more uncertain at this time due to the more limited carryforward periods that exist in certain states. See Notes 13 and 14 of the Consolidated Financial Statements for further discussion.

The income tax benefit for the year ended December 31, 2012 was due primarily to the release of reserves related to settlements with various taxing authorities.

The income tax benefit for the year ended December 31, 2011 was primarily from settlements of various state income tax matters and our settlement with the IRS on its audit of our 2004 and 2005 federal income tax returns.

## LIQUIDITY AND CAPITAL RESOURCES

We use our liquidity and capital resources to (1) support our operations, including the purchase of land, land development and construction of homes; (2) provide working capital; and (3) provide mortgage loans for our homebuyers. Our liquidity includes our cash and cash equivalents, marketable securities, Mortgage Repurchase Facility (as defined below) and Revolving Credit Facility (as defined below). Additionally, we have an existing effective shelf registration statement that allows us to issue equity, debt or hybrid securities up to \$1.5 billion (\$1.25 billion after the issuance of our 5½% senior notes due 2024 in January of 2014). See Note 22 to the Consolidated Financial Statements.

We have marketable debt and equity securities. Our debt securities consist primarily of fixed and floating rate interest earning debt securities, which may include, among others, United States government and government agency debt and corporate debt. Our equity securities consist primarily of holdings in mutual fund securities, which invest mostly in debt securities. The remaining equity securities in our investment portfolio are holdings in corporate equities.

### Capital Resources.

Our capital structure is primarily a combination of (1) permanent financing, represented by stockholders' equity; (2) long-term financing, represented by our publicly traded 5 % senior notes due 2014 and 2015, 5 % senior notes due 2020, 5½% senior notes due 2024 issued in January of 2014 (See Note 21 to the Consolidated Financial Statements) and our 6% senior notes due 2043; (3) our Mortgage Repurchase Facility and (4) our Revolving Credit Facility. Because of our current balance of cash, cash equivalents, marketable securities, ability to access the capital markets, and available capacity under both our Mortgage Repurchase Facility and Revolving Credit Facility, we believe that our capital resources are adequate to satisfy our short and long-term capital requirements, including meeting future payments on our senior notes as they become due. See **“Forward-Looking Statements”** below.

We may from time to time seek to retire or purchase our outstanding senior notes through cash purchases, whether in open market purchases, privately negotiated transactions or otherwise. Such repurchases, if any, will depend on prevailing market conditions, our liquidity requirements, contractual restrictions and other factors. The amounts involved may be material.

### Senior Notes, Revolving Credit Facility and Mortgage Repurchase Facility

*Senior Notes.* Our senior notes are not secured and, while the senior note indentures contain some restrictions on secured debt and other transactions, they do not contain financial covenants. Our senior notes are fully and unconditionally guaranteed on an unsecured basis, jointly and severally, by most of our homebuilding segment subsidiaries. We believe that we are in compliance with the representations, warranties and covenants in the senior note indentures.

*Revolving Credit Facility.* On December 13, 2013, we entered into an unsecured revolving credit agreement (“Revolving Credit Facility”) with a group of lenders which may be used for general corporate purposes. Our Revolving Credit Facility has an aggregate commitment amount of \$450 million (the “Commitment”) and a maturity date of December 13, 2018. Each lender may issue letters of credit in an amount up to 50% of its commitment. The facility permits an increase in the maximum Commitment amount to \$1.0 billion upon our request, subject to receipt of additional commitments from existing or additional lenders. Interest rates on outstanding borrowings are determined by reference to a specified London Interbank Offered Rate (LIBOR), a specified federal funds effective rate or a specified prime rate, plus a margin that is determined based on our credit ratings and leverage ratio, as defined in the facility agreement. At any time at which the Company’s leverage ratio, as of the last day of the most recent calendar quarter, exceeds 55%, the aggregate principal amount of all consolidated senior debt borrowings outstanding may not exceed the borrowing base. If the Company’s leverage ratio, as of the last day of the most recent calendar quarter, is 55% or less, then no borrowing base requirement will exist.

The Revolving Credit Facility is fully and unconditionally guaranteed, jointly and severally, by most of our homebuilding segment subsidiaries. The facility contains various representations, warranties and covenants that we believe are customary for agreements of this type. The financial covenants include a consolidated tangible net worth test and a leverage test, along with a consolidated tangible net worth covenant, all as defined in the facility agreement. A failure to satisfy the foregoing tests does not constitute an event of default, but can trigger a “term-out” of the facility. A breach of the consolidated tangible net worth covenant (but not the consolidated tangible net worth test) would result in an event of default.

The Revolving Credit Facility is subject to acceleration upon certain specified events of default, including breach of the consolidated tangible net worth covenant, failure to make timely payments, breaches of certain representations or covenants, failure to pay other material indebtedness, or another person becoming beneficial owner of 50% or more of the MDC's outstanding common stock. We believe we were in compliance with the representations, warranties and covenants included in the Revolving Credit Facility as of December 31, 2013.

We incur costs associated with unused commitment fees pursuant to the terms of the Revolving Credit Facility. At December 31, 2013, there were no borrowings under the Revolving Credit Facility and there were \$14.9 million in letters of credit outstanding, which reduced the amounts available to be borrowed under the Revolving Credit Facility.

Upon entering into the Revolving Credit Facility on December 13, 2013, our separate letter of credit facilities terminated and our existing letters of credit were included in the Revolving Credit Facility.

*Mortgage Repurchase Facility.* HomeAmerican has a Master Repurchase Agreement, (the "Mortgage Repurchase Facility"), with U.S. Bank National Association ("USBNA"). This agreement was amended on September 20, 2013 and extended until September 19, 2014. The Mortgage Repurchase Facility provides liquidity to HomeAmerican by providing for the sale of eligible mortgage loans to USBNA with an agreement by HomeAmerican to repurchase the mortgage loans at a future date. Until such mortgage loans are transferred back to HomeAmerican, the documents relating to such loans are held by USBNA, as custodian, pursuant to the Custody Agreement ("Custody Agreement"), dated as of November 12, 2008, by and between HomeAmerican and USBNA. The Mortgage Repurchase Facility had a temporary increase in the maximum aggregate commitment from \$50 million to \$80 million from December 31, 2013 through January 30, 2014 and from December 21, 2012 through January 30, 2013. At December 31, 2013 and December 31, 2012, we had \$63.1 million and \$76.3 million, respectively, of mortgage loans that we were obligated to repurchase under our Mortgage Repurchase Facility. Mortgage loans that we are obligated to repurchase under the Mortgage Repurchase Facility are accounted for as a debt financing arrangement and are reported as mortgage repurchase facility in the consolidated balance sheets. Advances under the Mortgage Repurchase Facility carry a Pricing Rate equal to the greater of (i) the LIBOR Rate (as defined in the Mortgage Repurchase Facility) plus 2.75%, or (ii) 3.00%. The Mortgage Repurchase Facility contains various representations, warranties and affirmative and negative covenants that we believe are customary for agreements of this type. The negative covenants include, among others, (i) a minimum Adjusted Tangible Net Worth requirement, (ii) a maximum Adjusted Tangible Net Worth Ratio, (iii) a minimum Adjusted Net Income requirement, and (iv) a minimum Liquidity requirement. The foregoing terms are defined in the Mortgage Repurchase Facility. We believe we were in compliance with the representations, warranties and covenants included in the Mortgage Repurchase Facility as of December 31, 2013.

## **Dividends**

There were no dividends declared or paid for the year ended of December 31, 2013. We paid dividends of \$2.00 per share during the year ended December 31, 2012. Of the \$2.00 per share in dividends, \$1.00 was in lieu of declaring

and paying regular quarterly dividends in calendar year 2013.

### **MDC Common Stock Repurchase Program**

At December 31, 2013, we were authorized to repurchase up to 4,000,000 shares of our common stock. We did not repurchase any shares of our common stock during the year ended December 31, 2013.

### **Consolidated Cash Flow**

Our operating cash flows are primarily impacted by: (1) land purchases and construction of homes; (2) closing homes and the associated timing of collecting receivables from home closings; (3) sales of mortgage loans originated by HomeAmerican; (4) payments on accounts payables and accrued liabilities; and (5) funding for payroll. When we close on the sale of a house, our homebuilding subsidiaries will generally receive the proceeds from the sale of the homes within a few days of the home being closed. Therefore, our home sales receivable balance can increase or decrease from period to period based upon the timing of our home closings. Additionally, the amount of mortgage loans held-for-sale can be impacted period to period based upon the number of mortgage loans that were originated by HomeAmerican that have not been sold to third party purchasers and by the timing of fundings by third party mortgage purchasers. Accordingly, mortgage loans held-for-sale may increase if HomeAmerican originates more homes towards the end of one reporting period when compared with the same period in the previous year. HomeAmerican will generally sell mortgage loans it originates within 15 to 40 days after origination.

*Year Ended December 31, 2013.* We used \$269.5 million in cash for operating activities during the year ended December 31, 2013, primarily resulting from increasing our inventory from December 31, 2012, which resulted in the use of \$409.3 million in cash. The use of cash was significantly offset by consolidated pretax income of \$129.8 million and a decrease of \$27.4 million in mortgage loans held-for-sale.

We used \$30.4 million in cash from investing activities during the year ended December 31, 2013, primarily attributable to purchasing \$405.0 million of marketable securities. The use of cash was significantly offset by the maturity and sale of marketable securities that increased our cash by \$376.3 million.

We generated \$339.2 million of cash from financing activities during the year ended December 31, 2013, primarily attributable to \$346.9 million associated with the issuance of our 30-year 6% senior notes, which was partially offset by a \$13.3 million net decrease from payment and advance activity on our mortgage repurchase facility.

*Year Ended December 31, 2012.* We used \$108.8 million in cash for operating activities during the year ended December 31, 2012, primarily resulting from: (1) increasing our inventory from December 31, 2011, which resulted in the use of \$196.8 million in cash and (2) \$41.6 million used in connection with originating mortgage loans held-for-sale. These items partially were offset by net income of \$62.7 million and a \$47.5 million increase in accounts payable.

We used \$21.8 million in cash for investing activities during the year ended December 31, 2012, primarily attributable to purchasing \$478.7 million of marketable securities. These items were significantly offset by the maturity and sale of marketable securities that increased our cash by \$458.2 million.

We used \$52.7 million in cash for financing activities during the year ended December 31, 2012, primarily resulting from \$96.9 million of dividend payments. This was partially offset by net cash proceeds of \$27.6 million from mortgage repurchase facility activity.

*Year Ended December 31, 2011.* We used \$80.3 million in cash for operating activities, primarily resulting from: (1) using \$65.6 million to reduce our accrued liabilities; (2) \$13.2 million used in connection with originating mortgage loans; (3) \$6.1 million associated with changes in our inventory levels; and (4) \$5.7 million associated with net loss before non-cash items of \$93.4 million. This use of cash was partially offset by generating \$16.8 million in cash associated with reducing our income tax receivable.



We generated \$404.3 million in cash from investing activities during the year ended December 31, 2011, primarily attributable to the maturity and sale of marketable securities that increased our cash by \$942.7 million, partially offset by the purchase of \$506.6 million of marketable securities. In addition, we used \$31.9 million in cash for the purchase of property, equipment and other.

We used \$552.8 million in cash for financing activities, primarily attributable to \$537.7 million used to extinguish certain of our senior notes due 2012 and 2013 and \$47.4 million used to pay cash dividends during 2011. These items partially were offset by net proceeds from our mortgage repurchase facility, which resulted in a \$23.3 million increase in cash, and \$9.0 million in cash proceeds from the exercise of stock options.

### **Off-Balance Sheet Arrangements**

*Lot Option Purchase Contracts.* In the ordinary course of business, we enter into lot option purchase contracts in order to procure lots for the construction of homes. Lot option contracts enable us to control lot positions with a minimal capital investment, which substantially reduces the risks associated with land ownership and development. At December 31, 2013, we had deposits of \$13.4 million in the form of cash and \$2.6 million in the form of letters of credit that were at risk to secure option contracts to purchase 2,748 lots for a total estimated purchase price of \$225.0 million.

*Surety Bonds and Letters of Credit.* At December 31, 2013, we had issued and outstanding surety bonds and letters of credit totaling \$97.9 million and \$30.2 million, respectively, including \$15.3 million in letters of credit issued by HomeAmerican. The estimated cost to complete obligations related to these bonds and letters of credit was approximately \$45.5 million and \$8.1 million, respectively. We expect that the obligations secured by these performance bonds and letters of credit generally will be performed in the ordinary course of business and in accordance with the applicable contractual terms. To the extent that the obligations are performed, the related performance bonds and letters of credit should be released and we should not have any continuing obligations. However, in the event any such performance bonds or letters of credit are called, our indemnity obligations could require us to reimburse the issuer of the performance bond or letter of credit.

We have made no material guarantees with respect to third-party obligations.

### Contractual Obligations.

The table below summarizes our known contractual obligations at December 31, 2013.

|                                                       | Payments due by Period (in thousands) |                     |                |                |                  |
|-------------------------------------------------------|---------------------------------------|---------------------|----------------|----------------|------------------|
|                                                       | Total                                 | Less than<br>1 Year | 1 - 3<br>Years | 4 - 5<br>Years | After 5<br>Years |
| Senior notes                                          | \$1,100,000                           | \$250,000           | \$250,000      | \$-            | \$600,000        |
| Interest on senior notes                              | 751,220                               | 61,938              | 83,563         | 70,125         | 535,594          |
| Lump sum payment to executive officers <sup>(1)</sup> | 30,796                                | 30,796              | -              | -              | -                |
| Operating leases                                      | 14,865                                | 4,462               | 8,183          | 1,799          | 421              |
| Total <sup>(2)</sup>                                  | \$1,896,881                           | \$347,196           | \$341,746      | \$71,924       | \$1,136,015      |

Reflects deferred lump sum payments to be made on October 20, 2014 to the Company's Chief Executive Officer, Larry A. Mizel, and its Chief Operating Officer, David D. Mandarich for the early termination of the Retirement Benefits contained in their respective Employment Agreements. See Note 13 to the Consolidated Financial Statements for further information and definitions.

The table above excludes \$63.1 million of mortgage loans that we are obligated to repurchase under our Mortgage Repurchase Facility since it is not long-term indebtedness. Additionally, there were outstanding performance bonds and letters of credit totaling approximately \$97.9 million and \$30.2 million, respectively, at December 31, 2013, which have been excluded from the table above due to the uncertainty as to whether any payments may be made.

## CRITICAL ACCOUNTING ESTIMATES AND POLICIES

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

Listed below are those estimates and policies that we believe are critical and require the use of complex judgment in their application. Our critical accounting estimates and policies are as follows and should be read in conjunction with the Notes to our Consolidated Financial Statements.

*Homebuilding Inventory Valuation.* Our inventories are primarily associated with communities where we intend to construct and sell homes, including models and unsold started homes. Costs capitalized to land and land under development primarily include: (1) land costs; (2) land development costs; (3) entitlement costs; (4) capitalized interest; (5) engineering fees; and (6) title insurance, real property taxes and closing costs directly related to the purchase of the land parcel. Components of housing completed or under construction primarily include: (1) land costs transferred from land and land under development; (2) direct construction costs associated with a house; (3) real property taxes, engineering fees, permits and other fees; (4) capitalized interest; and (5) indirect construction costs, which include field construction management salaries and benefits, utilities and other construction related costs. Land costs are transferred from land and land under development to housing completed or under construction at the point in time that construction of a home on an owned lot begins.

Homebuilding inventories are carried at cost unless events and circumstances indicate that the carrying value of the underlying subdivision may not be recoverable. We determine impairments on a subdivision level basis as each such subdivision represents the lowest level of identifiable cash flows. In making this determination, we review, among other things, the following for each subdivision:

- actual and trending “Operating Margin” (which is defined as home sale revenues less home cost of sales and all direct incremental costs associated with the home closing) for homes closed;
- estimated future undiscounted cash flows and Operating Margin;
- forecasted Operating Margin for homes in backlog;
- actual and trending net and gross home orders;
-

base sales price and home sales incentive information for homes closed, homes in backlog and homes available for sale;  
market information for each sub-market, including competition levels, home foreclosure levels, the size and style of homes currently being offered for sale and lot size; and  
known or probable events indicating that the carrying value may not be recoverable.

If events or circumstances indicate that the carrying value of our inventory may not be recoverable, assets are reviewed for impairment by comparing the undiscounted estimated future cash flows from an individual subdivision to its carrying value. We generally determine the estimated fair value of each subdivision by determining the present value of the estimated future cash flows at discount rates that are commensurate with the risk of the subdivision under evaluation. The evaluation for the recoverability of the carrying value of the assets for each individual subdivision can be impacted significantly by the following:

- estimates of future base selling prices;
- estimates of future home sales incentives; and
- estimates of future home construction and land development costs.

These estimates are dependent on specific market or sub-market conditions for each subdivision. While we consider available information to determine what we believe to be our best estimates as of the end of a reporting period, these estimates are subject to change in future reporting periods as facts and circumstances change. Local market-specific conditions that may impact these estimates for a subdivision include:

- historical subdivision results, and actual and trending Operating Margin, base selling prices and home sales incentives;
- forecasted Operating Margin for homes in backlog;
- the intensity of competition within a market or sub-market, including publicly available home sales prices and home sales incentives offered by our competitors;
- increased levels of home foreclosures;
- the current sales pace for active subdivisions;
- subdivision specific attributes, such as location, availability and size of lots in the sub-market, desirability and uniqueness of subdivision location and the size and style of homes currently being offered;
- potential for alternative home styles to respond to local market conditions;
  - changes by management in the sales strategy of a given subdivision; and
- current local market economic and demographic conditions and related trends and forecasts.

These and other local market-specific conditions that may be present are considered by personnel in our homebuilding divisions as they prepare or update the forecasted assumptions for each subdivision. Quantitative and qualitative factors other than home sales prices could significantly impact the potential for future impairments. The sales objectives can differ among subdivisions, even within a given sub-market. For example, facts and circumstances in a given subdivision may lead us to price our homes with the objective of yielding a higher sales absorption pace, while facts and circumstances in another subdivision may lead us to price our homes to minimize deterioration in our gross margins from home sales, even though this could result in a slower sales absorption pace. Furthermore, the key assumptions included in our estimated future undiscounted cash flows may be interrelated. For example, a decrease in estimated base sales price or an increase in home sales incentives may result in a corresponding increase in sales absorption pace. Additionally, a decrease in the average sales price of homes to be sold and closed in future reporting periods for one subdivision that has not been generating what management believes to be an adequate sales absorption pace may impact the estimated cash flow assumptions of a nearby subdivision. Changes in our key assumptions, including estimated construction and land development costs, absorption pace and selling strategies could materially impact future cash flow and fair value estimates. Due to the number of possible scenarios that would result from various changes in these factors, we do not believe it is possible to develop a sensitivity analysis with a level of precision that would be meaningful to an investor.

If the undiscounted future cash flows of a subdivision are less than its carrying value, the carrying value of the subdivision is written down to its then estimated fair value.

We determine the estimated fair value of each subdivision either: (1) by determining the present value of the estimated future cash flows at discount rates that are commensurate with the risk of the subdivision under evaluation; or

(2) assessing the market value of the land in its current condition by considering the estimated price a willing buyer would pay for the land (other than in a forced liquidation), and recent land purchase transactions that we believe are indicators of fair value. The estimated future cash flows are the same for both our recoverability and fair value assessments. Factors we consider when determining the discount rate to be used for each subdivision include, among others:

- the number of lots in a given subdivision;
- the amount of future land development costs to be incurred;
- risks associated with the home construction process, including the stage of completion for the entire subdivision and
- the number of owned lots under construction; and
- the estimated remaining lifespan of the subdivision.

We allocate the impairments recorded between housing completed or under construction and land and land under development for each impaired subdivision based upon the status of construction of a home on each lot (i.e., if the lot is in housing completed or under construction, the impairment for that lot is recorded against housing completed or under construction). The allocation of impairment is the same with respect to each lot in a given subdivision. Changes in management's estimates, particularly the timing and amount of the estimated future cash inflows and outflows and forecasted average selling prices of homes to be sold and closed can materially affect any impairment calculation. Because our forecasted cash flows are impacted significantly by changes in market conditions, it is reasonably possible that actual results could differ significantly from those estimates. Please see the "Inventory Impairments" section for a detailed discussion and analysis of our asset impairments.

*Warranty Reserves.* Our homes are sold with limited third-party warranties. We record expenses and warranty reserves for general and structural warranty claims, as well as reserves for known, unusual warranty-related expenditures. Warranty reserves are established based upon historical payment experience in an amount estimated to be adequate to cover expected costs of materials and outside labor during warranty periods. The establishment of warranty reserves for closed homes and the evaluation of our warranty reserve balance is based on an internally developed analysis that includes known facts and interpretations of circumstances, including, among other things, our trends in historical warranty payment levels and warranty payments for claims not considered to be normal and recurring.

Warranty reserves are included in accrued liabilities in the Homebuilding section of our consolidated balance sheets and adjustments to our warranty reserves are recorded as an increase or reduction to home cost of sales in the Homebuilding section of our consolidated statements of operations. Additionally, it is possible that changes in the warranty payment experience used in estimating our ultimate warranty losses could have a material impact on our warranty reserve balances. Please see further discussion on the adjustments to our warranty accrual within our discussion of gross margin from home sales in the “Gross Margin” section. Also see **“Forward-Looking Statements”** above.

*Insurance Reserves.* The establishment of reserves for estimated losses associated with insurance policies issued by Allegiant and re-insurance agreements issued by StarAmerican are based on actuarial or internally developed studies that include known facts and interpretations of circumstances, including our experience with similar cases and historical trends involving claim payment patterns, pending levels of unpaid claims, product mix or concentration, claim severity, frequency patterns depending on the business conducted, and changing regulatory and legal environments.

*Litigation Accruals.* In the normal course of business, we are a defendant in claims primarily relating to construction defects, product liability and personal injury claims. These claims seek relief from us under various theories, including breach of implied and express warranty, negligence, strict liability, misrepresentation and violation of consumer protection statutes. We have accrued for losses that may be incurred with respect to legal claims based upon information provided by our legal counsel, including counsel’s on-going evaluation of the merits of the claims and defenses and the level of estimated insurance coverage. Due to uncertainties in the estimation process, actual results could vary from those accruals and could have a material impact on our results of operations.

*Income Taxes—Valuation Allowance.* A valuation allowance is recorded against a deferred tax asset if, based on the weight of available evidence, it is more-likely-than-not (a likelihood of more than 50%) that some portion, or all, of the deferred tax asset will not be realized. The realization of a deferred tax asset ultimately depends on the existence of sufficient taxable income in either the carryback or carryforward periods under tax law (generally 2 and 20 years, respectively). The four sources of taxable income to be considered in determining whether a valuation allowance is required include:

- future reversals of existing taxable temporary differences;
- taxable income in prior carryback years;
- tax planning strategies; and
- future taxable income exclusive of reversing temporary differences and carryforwards.

Determining whether a valuation allowance for deferred tax assets is necessary requires an analysis of both positive and negative evidence regarding realization of the deferred tax assets. Examples of positive evidence may include:

- a strong earnings history exclusive of the loss that created the deductible temporary differences, coupled with evidence indicating that the loss is the result of an aberration rather than a continuing condition;
- an excess of appreciated asset value over the tax basis of a company's net assets in an amount sufficient to realize the deferred tax asset; and
- existing backlog that will produce sufficient taxable income to realize the deferred tax asset based on existing sales prices and cost structures.

Examples of negative evidence may include:

- the existence of "cumulative losses" (generally defined as a pretax cumulative loss for the current and previous two years);
- an expectation of being in a cumulative loss position in a future reporting period;



- a carryback or carryforward period that is so brief that it would limit the realization of tax benefits;
- a history of operating loss or tax credit carryforwards expiring unused; and
- unsettled circumstances that, if unfavorably resolved, would adversely affect future operations and profit levels on a continuing basis.

The weight given to the potential effect of negative and positive evidence should be commensurate with the extent to which it can be objectively verified. A company must use judgment in considering the relative impact of positive and negative evidence. At December 31, 2013 and 2012, we had a valuation allowance of \$8.2 million and \$248.3 million, respectively, recorded against our net deferred tax asset. The valuation allowance as of December 31, 2013 related to various state net operating loss carryforwards where realization is more uncertain at this time due to the more limited carryforward periods that exist in certain states. The valuation allowance as of December 31, 2012 was primarily due to us experiencing a three-year cumulative operating loss as of December 31, 2012. Future adjustments to our deferred tax asset valuation allowance will be determined based upon changes in the expected realization of our net deferred tax assets. See Note 14 of the Consolidated Financial Statements for further discussion.

In the future, changes in our valuation allowance may result from, among other things, additional pretax operating losses resulting in increases in our valuation allowance or pretax operating income resulting in decreases in our valuation allowance.

*Revenue Recognition.* We recognize revenue from home deliveries and land sales when: (1) the closing has occurred; (2) title has passed to the buyer; (3) possession and other attributes of ownership have been transferred to the buyer; (4) we are not obligated to perform significant additional activities after closing and delivery; and (5) the buyer demonstrates a commitment to pay for the property through an adequate initial and continuing investment. The buyer's initial investment shall include: (1) cash paid as a down payment; (2) the buyer's notes supported by irrevocable letters of credit; (3) payments made by the buyer to third-parties to reduce existing indebtedness on the property; and (4) other amounts paid by the buyer that are part of the sales value of the property. Revenue from a home delivery includes the base sales price and any purchased options and upgrades and is reduced for any sales price incentives.

Revenues recorded by HomeAmerican primarily include origination fees and the corresponding sale of a loan and its servicing rights. Origination fees are recognized when a loan is originated. When an interest rate lock commitment is made to a customer, we record the expected gain on sale of the mortgage including servicing rights, adjusted for a pull-through percentage (which is defined as the likelihood that an interest rate lock commitment will be originated), as revenue. As the interest rate lock commitment gets closer to being originated, the expected gain on the sale of that loan plus servicing rights is updated to reflect current market value and the increase or decrease in the fair value of that interest rate lock commitment is recorded through revenues. At the same time, as the likelihood of the interest rate lock commitment being originated increases resulting in an improvement to the expected pull-through percentage, additional revenues are recognized. After origination, our mortgage loans generally are transferred to third-party purchasers in accordance with sale agreements entered into by us with a third party purchaser of the loans. We make representations and warranties with respect to the status of loans transferred in the sale agreements. The sale agreements generally include statements acknowledging the transfer of the loans is intended by both parties to constitute a sale. Sale of a mortgage loan has occurred when the following criteria, among others, have been met:

(1) fair consideration has been paid for transfer of the loan by a third party in an arms-length transaction, (2) all the usual risks and rewards of ownership that are in substance a sale have been transferred by us to the third party purchaser; and (3) we do not have a substantial continuing involvement with the mortgage loan. The related servicing rights are generally transferred by us to the third party purchaser for additional consideration. Revenue from the sale of mortgage loan servicing is recognized upon the exchange of consideration for the mortgage loans and related servicing rights between us and the third-party purchaser.

We carry interest rate lock commitments and mortgage loans held-for-sale at fair value.

*Home Cost of Sales.* Home cost of sales includes the specific construction costs of each home and all applicable land acquisition, land development and related costs, both incurred and estimated to be incurred, warranty costs and finance and closing costs. We use the specific identification method for the purpose of accumulating home construction costs and allocate costs to each lot within a subdivision associated with land acquisition and land development based upon relative fair value of the lots prior to home construction. Lots within a subdivision typically have comparable fair values, and, as such, we generally allocate costs equally to each lot within a subdivision. We record all home cost of sales when a home is closed on a house-by-house basis.

When a home is closed, we generally have not yet paid or incurred all costs necessary to complete the construction of the home and certain land development costs. At the time of a home closing, we compare the home construction budgets to actual recorded costs to determine the additional estimated costs remaining to be paid on each closed home. For amounts not incurred or paid as of the time of closing a home, we record an estimated accrual associated with certain home construction and land development costs. Generally, these accruals are established based upon contracted work that has yet to be paid, open work orders not paid at the time of home closing, as well as land completion costs more likely than not to be incurred, and represent estimates believed to be adequate to cover the expected remaining home construction and land development costs. We monitor the adequacy of these accruals on a house-by-house basis and in the aggregate on both a market-by-market and consolidated basis.

*Mortgage Loan Loss Reserves.* In the normal course of business, we establish reserves for potential losses associated with HomeAmerican's sale of mortgage loans to third-parties. These reserves are created to address repurchase and indemnity claims by third-party purchasers of the mortgage loans, which claims arise primarily out of allegations of homebuyer fraud at the time of origination of the loan. These reserves are based upon, among other matters: (1) pending claims received from third-party purchasers associated with previously sold mortgage loans; (2) a current assessment of the potential exposure associated with future claims of homebuyer fraud in mortgage loans originated in prior periods; and (3) historical loss experience. Significant changes in the number and magnitude of claims to repurchase previously sold mortgage loans could have a material impact on our results of operations. Our mortgage loan reserves are reflected as a component of accrued liabilities in the Financial Services section of the accompanying consolidated balance sheets, and the associated expenses are included in Expenses in the Financial Services section of the accompanying consolidated statements of operations.

*Stock-Based Compensation.* Accounting Standards Codification ("ASC") Topic 718, *Compensation—Stock Compensation* ("ASC 718") requires that share-based compensation expense be measured and recognized at an amount equal to the fair value of share-based payments granted under compensation arrangements. Determining the appropriate fair value model and calculating the fair value of stock option awards requires judgment, including estimating stock price volatility, annual forfeiture rates and the expected life of an award. We estimate the fair value for stock options granted using a Black-Scholes option pricing model. The Black-Scholes option pricing model calculates the estimated fair value of stock options based upon the following inputs: (1) closing price of our common stock on the measurement date (generally the date of grant); (2) exercise price; (3) expected stock option life; (4) expected volatility; (5) risk-free interest rate; and (6) expected dividend yield rate. The expected life of employee stock options represents the period for which the stock options are expected to remain outstanding and is derived primarily from historical exercise patterns. The expected volatility is based on the historical volatility in the price of our common stock over the most recent period commensurate with the estimated expected life of our employee stock options,

adjusted for the impact of unusual fluctuations not reasonably expected to recur and other relevant factors. The risk-free interest rate assumption is determined based upon observed interest rates appropriate for the expected term of our employee stock options. The expected dividend yield assumption is based on our historical dividend payouts. We determine the estimated fair value of the stock option awards on the date they were granted. The fair values of previously granted stock option awards are not adjusted as subsequent changes in the foregoing assumptions occur; for example, an increase or decrease in the price of our common stock. However, changes in the foregoing inputs, particularly the price of our common stock, expected stock option life and expected volatility, significantly change the estimated fair value of future grants of stock options.

An annual forfeiture rate is estimated at the time of grant, and revised if necessary, in subsequent periods if the actual forfeiture rate differs from our estimate.

*Segment Reporting.* The application of segment reporting requires significant judgment in determining our operating segments. Operating segments are defined as a component of an enterprise for which discrete financial information is available and is reviewed regularly by the chief operating decision-maker, or decision-making group, to evaluate performance and make operating decisions. We have identified our chief operating decision-makers as two key executives—the Chief Executive Officer and Chief Operating Officer.

We have identified each homebuilding division as an operating segment as each homebuilding division engages in business activities from which it earns revenue, primarily from the sale of single-family detached homes, generally to first-time and first-time move-up homebuyers. Divisions in the reportable segments noted below have been aggregated because they are similar in the following regards: (1) economic characteristics; (2) housing products; (3) class of homebuyer; (4) regulatory environments; and (5) methods used to manage the construction and sale of homes. In making the determination of whether or not our markets demonstrate similar economic characteristics, we review, among other things, actual and trending gross margins from home sales for homes closed within each market and forecasted gross margins from home sales. Accordingly, we may be required to reclassify our reportable segments if markets that currently are being aggregated do not continue to demonstrate similar economic characteristics.

Our homebuilding reportable segments are as follows:

- ♣West (Arizona, California, Nevada and Washington);
- ♣Mountain (Colorado and Utah); and
- ♣East (Virginia, Florida, Illinois and Maryland, which includes Pennsylvania, Delaware, and New Jersey)

Our financial services operating segments are as follows: (1) HomeAmerican Mortgage Corporation ("HomeAmerican"); (2) Allegiant Insurance Company, Inc., A Risk Retention Group ("Allegiant"); (3) StarAmerican Insurance Ltd. ("StarAmerican"); (4) American Home Insurance Agency, Inc.; and (5) American Home Title and Escrow Company. Due to its contributions to consolidated pretax income we consider HomeAmerican to be a reportable segment ("Mortgage operations"). The remaining operating segments have been aggregated into one reportable segment ("Other") because they do not individually exceed 10 percent of: (1) consolidated revenue; (2) the greater of (A) the combined reported profit of all operating segments that did not report a loss or (B) the positive value of the combined reported loss of all operating segments that reported losses; or (3) consolidated assets.

## RECENTLY ISSUED ACCOUNTING STANDARDS

See Note 1 in our accompanying consolidated financial statements.

**Item 7A. *Quantitative and Qualitative Disclosures About Market Risk.***

Our cash and investment policy and strategy is to achieve an appropriate investment return while preserving principal and managing risk. Our cash and cash equivalents may include immediately available commercial bank deposits, commercial paper, money market funds, certificates of deposit and time deposits. Our marketable securities contain both debt and equity instruments, held directly or through mutual funds. Our debt securities consist primarily of fixed and floating rate interest earning debt securities, which may include, among others, United States government and government agency debt and corporate debt. Our equity securities consist primarily of holdings in mutual fund securities, which invest mostly in debt securities. The remaining equity securities in our investment portfolio are holdings in corporate equities. The market value and/or income derived from our debt and equity securities can be negatively impacted by a number of market risk factors, including changes in interest rates, general economic conditions and equity markets. As of December 31, 2013, we had marketable securities in unrealized loss positions totaling \$1.2 million. There can be no assurances that the cost basis of these securities will be recovered in the future. If we elect to sell, or are otherwise required to sell these securities, we could be required to record losses if the market values do not increase prior to any sales. Such losses, if any, would be recorded as a component of our results of operations.

We are exposed to market risks related to fluctuations in interest rates on mortgage loans held-for-sale, mortgage interest rate lock commitments and debt. Derivative instruments utilized in the normal course of business by HomeAmerican include interest rate lock commitments, and forward sales of mortgage-backed securities, which are used to manage the price risk on fluctuations in interest rates on our mortgage loans in inventory and interest rate locked commitments to originate mortgage loans. Such contracts are the only significant financial derivative instruments utilized by MDC. HomeAmerican's mortgage loans in process for which a rate and price commitment had been made to a borrower that had not closed at December 31, 2013 had an aggregate principal balance of approximately \$69.8 million, all of which were under interest rate lock commitments at an average interest rate of 4.13%. In addition, HomeAmerican had \$91.0 million of mortgage loans held-for-sale at December 31, 2013, of which \$25.9 million had not yet been committed to a mortgage purchaser and had an average interest rate of 4.25%. In order to hedge the changes in fair value of our interest rate lock commitments and mortgage loans held-for-sale which had not yet been committed to a mortgage purchaser, we had forward sales of securities totaling \$74.5 million and \$41.5 million at December 31, 2013 and 2012, respectively.

HomeAmerican provides mortgage loans that generally are sold forward and subsequently delivered to a third-party purchaser between 15 and 40 days. Forward commitments are used for non-trading purposes to sell mortgage loans and hedge price risk due to fluctuations in interest rates on rate-locked mortgage loans in process that have not closed. Due to this economic hedging philosophy, the market risk associated with these mortgages is limited. For forward sales commitments, as well as commitments to originate mortgage loans that are still outstanding at the end of a reporting period, we record the fair value of the derivatives in the consolidated statements of operations with an offset to either derivative assets or liabilities, depending on the nature of the change.

We utilize our Revolving Credit Facility, our Mortgage Repurchase Facility and senior notes in our financing strategy. For fixed rate debt, changes in interest rates generally affect the fair value of the debt instrument, but not our earnings or cash flows. We do not have an obligation to prepay our senior notes prior to maturity and, as a result, interest rate risk and changes in fair value do not have an impact on our financial position, results of operations or cash flows. See “**Forward-Looking Statements**” above.



At December 31, 2013, we had \$63.1 million of mortgage loans that we are obligated to repurchase under our Mortgage Repurchase Facility. Mortgage loans that we are obligated to repurchase under the Mortgage Repurchase Facility are accounted for as a debt financing arrangement and are reported under Mortgage Repurchase Facility in the consolidated balance sheets. The following table provides the maturities, average interest rate and estimated fair value of significant financial instruments that are sensitive to changes in interest rates at December 31, 2013.

|                                             | Maturities through December 31, |           |      |      |      |            |             | Estimated   |   |
|---------------------------------------------|---------------------------------|-----------|------|------|------|------------|-------------|-------------|---|
|                                             | 2014                            | 2015      | 2016 | 2017 | 2018 | Thereafter | Total       | Fair Value  |   |
|                                             | (Dollars in thousands)          |           |      |      |      |            |             |             |   |
| <b>Assets:</b>                              |                                 |           |      |      |      |            |             |             |   |
| Mortgage loans held for sale <sup>(1)</sup> |                                 |           |      |      |      |            |             |             |   |
| Fixed Rate                                  | \$85,225                        | \$-       | \$ - | \$ - | \$ - | \$-        | \$85,225    | \$86,743    |   |
| Average interest rate                       | 4.11                            | %         |      |      |      |            | 4.11        | %           |   |
| Variable Interest Rate                      | 5,727                           | \$-       | \$ - | \$ - | \$ - | \$-        | \$5,727     | \$5,835     |   |
| Average interest rate                       | 3.13                            | %         |      |      |      |            | 3.13        | %           |   |
| <b>Liabilities:</b>                         |                                 |           |      |      |      |            |             |             |   |
| Fixed rate debt                             | \$250,000                       | \$250,000 | \$ - | \$ - | \$ - | \$600,000  | \$1,100,000 | \$1,086,083 |   |
| Average interest rate                       | 5.38                            | %         | 5.38 | %    |      | 5.84       | %           | 5.63        | % |
| Mortgage facility                           | \$63,074                        | \$-       | \$ - | \$ - | \$ - | \$-        | \$63,074    | \$63,074    |   |
| Average interest rate                       | 3.00                            | %         |      |      |      |            |             |             |   |
| <b>Derivative Financial Instruments:</b>    |                                 |           |      |      |      |            |             |             |   |
| Commitments to originate mortgage loans     |                                 |           |      |      |      |            |             |             |   |
| Notional amount                             | \$69,758                        | \$-       | \$ - | \$ - | \$ - | \$-        | \$69,758    | \$1,010     |   |
| Average interest rate                       | 4.13                            | %         |      |      |      |            | 4.13        | %           |   |
| Forward sales of mortgage backed securities |                                 |           |      |      |      |            |             |             |   |
| Notional amount                             | \$74,500                        | \$-       | \$ - | \$ - | \$ - | \$-        | \$74,500    | \$664       |   |
| Average interest rate                       | 3.49                            | %         |      |      |      |            | 3.49        | %           |   |

(1) All the amounts in this line reflect the expected 2013 disposition of these loans rather than the actual scheduled maturity dates of these mortgages.

**Item 8. Consolidated Financial Statements.**

**M.D.C. HOLDINGS, INC.**

**INDEX TO CONSOLIDATED FINANCIAL STATEMENTS**

|                                                                                                                                  | <b><u>Page</u></b> |
|----------------------------------------------------------------------------------------------------------------------------------|--------------------|
| Consolidated Financial Statements                                                                                                |                    |
| Report of Independent Registered Public Accounting Firm                                                                          | F-2                |
| Consolidated Balance Sheets at December 31, 2013 and December 31, 2012                                                           | F-3                |
| Consolidated Statements of Operations and Comprehensive Income for each of the Three Years in the Period Ended December 31, 2013 | F-4                |
| Consolidated Statements of Stockholders' Equity for each of the Three Years in the Period Ended December 31, 2013                | F-5                |
| Consolidated Statements of Cash Flows for each of the Three Years in the Period Ended December 31, 2013                          | F-6                |
| Notes to Consolidated Financial Statements                                                                                       | F-7                |

**Report of Independent Registered Public Accounting Firm**

**The Board of Directors and Stockholders of**

**M.D.C. Holdings, Inc.**

We have audited the accompanying consolidated balance sheets of M.D.C. Holdings, Inc. (the “Company”) as of December 31, 2013 and 2012, and the related consolidated statements of operations and comprehensive income, stockholders’ equity, and cash flows for each of the three years in the period ended December 31, 2013. These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of M.D.C. Holdings, Inc. at December 31, 2013 and 2012, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2013, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), M.D.C. Holdings, Inc.’s internal control over financial reporting as of December 31, 2013, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (1992 framework) and our report dated February 5, 2014 expressed an unqualified opinion thereon.

/s/ Ernst & Young  
LLP  
Irvine, California

February 5, 2014

F-2

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**M.D.C. HOLDINGS, INC.****Consolidated Balance Sheets**

|                                                                                                                                  | December<br>31,<br>2013                                | December<br>31,<br>2012 |
|----------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------|-------------------------|
|                                                                                                                                  | (Dollars in thousands,<br>except<br>per share amounts) |                         |
| <b>ASSETS</b>                                                                                                                    |                                                        |                         |
| <b>Homebuilding:</b>                                                                                                             |                                                        |                         |
| Cash and cash equivalents                                                                                                        | \$ 148,634                                             | \$ 129,535              |
| Marketable securities                                                                                                            | 569,021                                                | 519,465                 |
| Restricted cash                                                                                                                  | 2,195                                                  | 1,859                   |
| Trade and other receivables                                                                                                      | 23,407                                                 | 28,163                  |
| Inventories:                                                                                                                     |                                                        |                         |
| Housing completed or under construction                                                                                          | 636,700                                                | 512,949                 |
| Land and land under development                                                                                                  | 774,961                                                | 489,572                 |
| Total inventories                                                                                                                | 1,411,661                                              | 1,002,521               |
| Property and equipment, net                                                                                                      | 31,248                                                 | 33,125                  |
| Deferred tax asset, net of valuation allowance of \$8,201 and \$248,306 at December 31, 2013 and December 31, 2012, respectively | 176,262                                                | -                       |
| Metropolitan district bond securities (related party)                                                                            | 12,729                                                 | 5,818                   |
| Prepaid and other assets                                                                                                         | 53,525                                                 | 38,959                  |
| Total homebuilding assets                                                                                                        | 2,428,682                                              | 1,759,445               |
| <b>Financial Services:</b>                                                                                                       |                                                        |                         |
| Cash and cash equivalents                                                                                                        | 50,704                                                 | 30,560                  |
| Marketable securities                                                                                                            | 19,046                                                 | 32,473                  |
| Mortgage loans held-for-sale, net                                                                                                | 92,578                                                 | 119,953                 |
| Other assets                                                                                                                     | 4,439                                                  | 3,010                   |
| Total financial services assets                                                                                                  | 166,767                                                | 185,996                 |
| Total Assets                                                                                                                     | \$2,595,449                                            | \$1,945,441             |
| <b>LIABILITIES AND EQUITY</b>                                                                                                    |                                                        |                         |
| <b>Homebuilding:</b>                                                                                                             |                                                        |                         |
| Accounts payable                                                                                                                 | \$ 15,046                                              | \$ 73,055               |
| Accrued liabilities                                                                                                              | 152,821                                                | 118,456                 |
| Senior notes, net                                                                                                                | 1,095,620                                              | 744,842                 |
| Total homebuilding liabilities                                                                                                   | 1,263,487                                              | 936,353                 |
| <b>Financial Services:</b>                                                                                                       |                                                        |                         |
| Accounts payable and accrued liabilities                                                                                         | 55,639                                                 | 51,864                  |
| Mortgage repurchase facility                                                                                                     | 63,074                                                 | 76,327                  |

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|                                                                                                                                                                          |             |             |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------|-------------|
| Total financial services liabilities                                                                                                                                     | 118,713     | 128,191     |
| Total Liabilities                                                                                                                                                        | 1,382,200   | 1,064,544   |
| <b>Stockholders' Equity</b>                                                                                                                                              |             |             |
| Preferred stock, \$0.01 par value; 25,000,000 shares authorized; none issued or outstanding                                                                              | -           | -           |
| Common stock, \$0.01 par value; 250,000,000 shares authorized; 48,788,887 and 48,698,757 issued and outstanding at December 31, 2013 and December 31, 2012, respectively | 488         | 487         |
| Additional paid-in-capital                                                                                                                                               | 908,090     | 896,861     |
| Retained earnings (accumulated deficit)                                                                                                                                  | 293,096     | (21,289 )   |
| Accumulated other comprehensive income                                                                                                                                   | 11,575      | 4,838       |
| Total Stockholders' Equity                                                                                                                                               | 1,213,249   | 880,897     |
| Total Liabilities and Stockholders' Equity                                                                                                                               | \$2,595,449 | \$1,945,441 |

The accompanying Notes are an integral part of these Consolidated Financial Statements.

**M.D.C. HOLDINGS, INC.****Consolidated Statements of Operations and Comprehensive Income**

|                                                                                        | Year Ended December 31,                          |             |              |
|----------------------------------------------------------------------------------------|--------------------------------------------------|-------------|--------------|
|                                                                                        | 2013                                             | 2012        | 2011         |
|                                                                                        | (Dollars in thousands, except per share amounts) |             |              |
| <b>Homebuilding:</b>                                                                   |                                                  |             |              |
| Home sale revenues                                                                     | \$1,626,707                                      | \$1,150,998 | \$805,164    |
| Land sale revenues                                                                     | 2,468                                            | 5,144       | 11,859       |
| Total home and land sale revenues                                                      | 1,629,175                                        | 1,156,142   | 817,023      |
| Home cost of sales                                                                     | (1,336,978 )                                     | (973,120 )  | (686,661 )   |
| Land cost of sales                                                                     | (1,961 )                                         | (4,823 )    | (10,796 )    |
| Inventory impairments                                                                  | (919 )                                           | (1,105 )    | (12,965 )    |
| Total cost of sales                                                                    | (1,339,858 )                                     | (979,048 )  | (710,422 )   |
| Gross margin                                                                           | 289,317                                          | 177,094     | 106,601      |
| Selling, general and administrative expenses                                           | (213,283 )                                       | (167,295 )  | (179,105 )   |
| Interest income                                                                        | 26,938                                           | 23,398      | 26,068       |
| Interest expense                                                                       | (1,726 )                                         | (808 )      | (20,842 )    |
| Other income (expense)                                                                 | (923 )                                           | 228         | (43,350 )    |
| Homebuilding pretax income (loss)                                                      | 100,323                                          | 32,617      | (110,628 )   |
| <b>Financial Services:</b>                                                             |                                                  |             |              |
| Revenues                                                                               | 51,259                                           | 46,881      | 26,086       |
| Expenses                                                                               | (25,271 )                                        | (21,645 )   | (26,306 )    |
| Interest and other income                                                              | 3,514                                            | 3,262       | 3,376        |
| Financial services pretax income                                                       | 29,502                                           | 28,498      | 3,156        |
| Income (loss) before income taxes                                                      | 129,825                                          | 61,115      | (107,472 )   |
| Benefit from income taxes                                                              | 184,560                                          | 1,584       | 9,082        |
| Net income (loss)                                                                      | \$314,385                                        | \$62,699    | \$(98,390 )  |
| Other comprehensive income (loss) related to available for sale securities, net of tax | 6,737                                            | 12,078      | (12,124 )    |
| Comprehensive income (loss)                                                            | \$321,122                                        | \$74,777    | \$(110,514 ) |
| Earnings (loss) per share:                                                             |                                                  |             |              |
| Basic                                                                                  | \$6.39                                           | \$1.29      | \$(2.12 )    |
| Diluted                                                                                | \$6.34                                           | \$1.29      | \$(2.12 )    |
| Weighted average common shares outstanding                                             |                                                  |             |              |
| Basic                                                                                  | 48,453,119                                       | 47,660,629  | 46,796,334   |
| Diluted                                                                                | 48,831,785                                       | 47,834,156  | 46,796,334   |

|                              |     |        |        |
|------------------------------|-----|--------|--------|
| Dividends declared per share | \$- | \$2.00 | \$1.00 |
|------------------------------|-----|--------|--------|

The accompanying Notes are an integral part of these Consolidated Financial Statements.

F-4

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**M.D.C. HOLDINGS, INC.****Consolidated Statements of Stockholders' Equity****(Dollars in thousands, except share amounts)**

|                                                                                                        | <b>Common Stock</b> |               | <b>Additional<br/>Paid-in</b> | <b>Retained<br/>Earnings<br/>(Accumulated<br/>Deficit)</b> | <b>Accumulated<br/>Other<br/>Comprehensive<br/>Income<br/>(Loss)</b> | <b>Treasury<br/>Shares</b> | <b>Amount Total</b> |            |
|--------------------------------------------------------------------------------------------------------|---------------------|---------------|-------------------------------|------------------------------------------------------------|----------------------------------------------------------------------|----------------------------|---------------------|------------|
|                                                                                                        | <b>Shares</b>       | <b>Amount</b> | <b>Capital</b>                |                                                            |                                                                      |                            |                     |            |
| Balance at December 31, 2010                                                                           | 47,198,081          | \$ 472        | \$ 820,237                    | \$ 158,749                                                 | \$ 4,884                                                             | \$(55,623)                 | \$(659 )            | \$983,683  |
| Net loss                                                                                               | -                   | -             | -                             | (98,390 )                                                  | -                                                                    | -                          | -                   | (98,390 )  |
| Unrealized loss on available-for-sale investments                                                      | -                   | -             | -                             | -                                                          | (12,124 )                                                            | -                          | -                   | (12,124 )  |
| Total comprehensive loss                                                                               |                     |               |                               |                                                            |                                                                      |                            |                     | (110,514 ) |
| Shares issued upon exercise of stock options and awards of restricted stock                            | 819,027             | 8             | 9,036                         | -                                                          | -                                                                    | -                          | -                   | 9,044      |
| Cash dividends paid                                                                                    | -                   | -             | -                             | (47,432 )                                                  | -                                                                    | -                          | -                   | (47,432 )  |
| Stock-based compensation expense                                                                       | -                   | -             | 15,432                        | -                                                          | -                                                                    | -                          | -                   | 15,432     |
| Forfeiture of restricted stock                                                                         | -                   | -             | -                             | -                                                          | -                                                                    | (4,289 )                   | -                   | -          |
| Reinstatement of tax benefits on non-qualified stock options exercised in previous years (Footnote 13) | -                   | -             | 18,423                        | -                                                          | -                                                                    | -                          | -                   | 18,423     |
| Balance at December 31, 2011                                                                           | 48,017,108          | 480           | 863,128                       | 12,927                                                     | (7,240 )                                                             | (59,912)                   | (659 )              | 868,636    |
| Net Income                                                                                             | -                   | -             | -                             | 62,699                                                     | -                                                                    | -                          | -                   | 62,699     |
| Unrealized gain on available-for-sale investments                                                      | -                   | -             | -                             | -                                                          | 12,078                                                               | -                          | -                   | 12,078     |
| Total comprehensive income                                                                             |                     |               |                               |                                                            |                                                                      |                            |                     | 74,777     |
|                                                                                                        | 752,855             | 8             | 16,616                        | -                                                          | -                                                                    | -                          | -                   | 16,624     |

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|                                                                             |            |        |            |            |           |          |      |              |
|-----------------------------------------------------------------------------|------------|--------|------------|------------|-----------|----------|------|--------------|
| Shares issued upon exercise of stock options and awards of restricted stock |            |        |            |            |           |          |      |              |
| Cash dividends paid                                                         | -          | -      | -          | (96,915 )  | -         | -        | -    | (96,915 )    |
| Stock-based compensation expense                                            | -          | -      | 16,225     | -          | -         | -        | -    | 16,225       |
| Reversal of uncertain tax positions due to statute of limitations           | -          | -      | 1,551      | -          | -         | -        | -    | 1,551        |
| Retirement of treasury stock                                                | (62,230 )  | (1 )   | (659 )     | -          | -         | 62,230   | 659  | (1 )         |
| Forfeiture of restricted stock                                              | (8,976 )   | -      | -          | -          | -         | (2,318 ) | -    | -            |
| Balance at December 31, 2012                                                | 48,698,757 | 487    | 896,861    | (21,289 )  | 4,838     | -        | -    | 880,897      |
| Net Income                                                                  | -          | -      | -          | 314,385    | -         | -        | -    | 314,385      |
| Unrealized gain on available-for-sale investments                           | -          | -      | -          | -          | 6,737     | -        | -    | 6,737        |
| Total comprehensive income                                                  |            |        |            |            |           |          |      | 321,122      |
| Shares issued upon exercise of stock options and awards of restricted stock | 178,737    | 2      | 5,116      | -          | -         | -        | -    | 5,118        |
| Stock-based compensation expense                                            | -          | -      | 9,652      | -          | -         | -        | -    | 9,652        |
| Forfeiture of restricted stock                                              | (88,607 )  | (1 )   | 1          | -          | -         | -        | -    | -            |
| Net income tax deficiency from share-based compensation                     | -          | -      | (3,540 )   | -          | -         | -        | -    | (3,540 )     |
| Balance at December 31, 2013                                                | 48,788,887 | \$ 488 | \$ 908,090 | \$ 293,096 | \$ 11,575 | -        | \$ - | \$ 1,213,249 |

The accompanying Notes are an integral part of these Consolidated Financial Statements.

**M.D.C. HOLDINGS, INC.****Consolidated Statements of Cash Flows**

|                                                                                        | Year Ended December 31, |           |             |
|----------------------------------------------------------------------------------------|-------------------------|-----------|-------------|
|                                                                                        | 2013                    | 2012      | 2011        |
|                                                                                        | (Dollars in thousands)  |           |             |
| <b>Operating Activities:</b>                                                           |                         |           |             |
| Net income                                                                             | \$314,385               | \$62,699  | \$(98,390 ) |
| Adjustments to reconcile net income (loss) to net cash (used in) operating activities: |                         |           |             |
| Loss on extinguishment of senior notes                                                 |                         | -         | 38,795      |
| Stock-based compensation expense                                                       | 9,652                   | 16,225    | 15,432      |
| Depreciation and amortization                                                          | 3,864                   | 4,766     | 6,371       |
| Inventory impairments                                                                  | 919                     | 1,105     | 12,965      |
| Amortization of discount (premiums) on marketable debt securities                      | 219                     | 596       | 1,271       |
| Deferred income tax benefit                                                            | (187,171)               | -         | -           |
| Excess tax benefits from stock-based compensation                                      | (391 )                  | -         | -           |
| Net changes in assets and liabilities:                                                 |                         |           |             |
| Restricted cash                                                                        | (336 )                  | (1,192 )  | (247 )      |
| Trade and other receivables                                                            | 4,186                   | (6,223 )  | 12,078      |
| Mortgage loans held-for-sale                                                           | 27,375                  | (41,618 ) | (13,221 )   |
| Housing completed or under construction                                                | (124,211)               | (212,154) | 86,477      |
| Land and land under development                                                        | (285,070)               | 15,314    | (93,381 )   |
| Prepaid expenses and other assets                                                      | (13,562 )               | 4,388     | 17,163      |
| Accounts payable                                                                       | (58,142 )               | 47,473    | (9,012 )    |
| Accrued liabilities                                                                    | 38,734                  | (198 )    | (56,585 )   |
| Net cash used in operating activities                                                  | (269,549)               | (108,819) | (80,284 )   |
| <b>Investing Activities:</b>                                                           |                         |           |             |
| Purchases of marketable securities                                                     | (404,965)               | (478,701) | (330,968)   |
| Maturities of marketable securities                                                    | 159,592                 | 108,250   | 492,051     |
| Sales of marketable securities                                                         | 216,756                 | 349,938   | 275,038     |
| Purchases of property and equipment                                                    | (1,785 )                | (1,268 )  | (31,857 )   |
| Net cash provided by (used in) investing activities                                    | (30,402 )               | (21,781 ) | 404,264     |
| <b>Financing Activities:</b>                                                           |                         |           |             |
| Extinguishment of senior notes                                                         | -                       | -         | (537,724)   |
| Payments on mortgage repurchase facility                                               | (234,671)               | (196,402) | (91,372 )   |
| Advances on mortgage repurchase facility                                               | 221,418                 | 224,027   | 114,640     |
| Dividend payments                                                                      | -                       | (96,915 ) | (47,432 )   |
| Excess tax benefits from stock-based compensation                                      | 391                     | -         | -           |
| Proceeds from issuance of senior notes                                                 | 346,938                 | -         | -           |
| Proceeds from exercise of stock options                                                | 5,118                   | 16,624    | 9,044       |
| Net cash provided by (used in) financing activities                                    | 339,194                 | (52,666 ) | (552,844)   |

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|                                                      |            |            |            |
|------------------------------------------------------|------------|------------|------------|
| Net increase (decrease) in cash and cash equivalents | 39,243     | (183,266)  | (228,864)  |
| Cash and cash equivalents:                           |            |            |            |
| Beginning of period                                  | 160,095    | 343,361    | 572,225    |
| End of period                                        | \$ 199,338 | \$ 160,095 | \$ 343,361 |

The accompanying Notes are an integral part of these Consolidated Financial Statements.

F-6

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**M.D.C. HOLDINGS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**1. Summary of Significant Accounting Policies**

*Principles of Consolidation.* The Consolidated Financial Statements of M.D.C. Holdings, Inc. ("MDC," "the Company," "we," "us," or "our" which refers to M.D.C. Holdings, Inc. and its subsidiaries) include the accounts of MDC and its wholly owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation. Certain prior year balances have been reclassified to conform to the current year's presentation.

*Description of Business.* Our homebuilding segments have operations in Arizona, California, Colorado, Florida, Maryland, (which includes Maryland, Pennsylvania, Delaware and New Jersey), Nevada, Utah, Virginia and Washington. The primary functions of our homebuilding segments include land acquisition and development, home construction, purchasing, marketing, merchandising, sales and customer service. We build and sell primarily single-family detached homes, which are designed and built to meet local customer preferences. We are the general contractor for all of our projects and retain subcontractors for site development and home construction.

Our financial services operations consist of HomeAmerican Mortgage Corporation ("HomeAmerican"), which originates mortgage loans, primarily for our homebuyers, American Home Insurance Agency, Inc. ("American Home Insurance"), which offers third-party insurance products to our homebuyers, and American Home Title and Escrow Company ("American Home Title"), which provides title agency services to the Company and our homebuyers in Colorado, Florida, Maryland, Nevada and Virginia. The financial services operations also include Allegiant Insurance Company, Inc., A Risk Retention Group ("Allegiant"), which provides insurance coverage primarily to our homebuilding subsidiaries and certain subcontractors for homes sold by our homebuilding subsidiaries and for work performed in completed subdivisions, and StarAmerican Insurance Ltd. ("StarAmerican"), a wholly owned subsidiary of MDC which is a re-insurer of Allegiant claims.

*Presentation.* Our balance sheet presentation is unclassified due to the fact that certain assets and liabilities have both short and long-term characteristics.

*Use of Accounting Estimates.* The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

*Cash and Cash Equivalents.* The Company periodically invests funds in highly liquid investments with an original maturity of three months or less, such as commercial paper, money market funds and time deposits, which are included in cash and cash equivalents in the consolidated balance sheets and consolidated statements of cash flows.

*Marketable Securities.* We have marketable debt and equity securities. Our debt securities consist primarily of fixed and floating rate interest earning debt securities, which may include, among others, United States government and government agency debt and corporate debt. Our equity securities consist primarily of holdings in mutual fund securities, which invest mostly in debt securities. The remaining equity securities in our investment portfolio are holdings in corporate equities. As of December 31, 2013 and December 31, 2012, all of our marketable securities were treated as available-for-sale investments and, as such, we have recorded all of our marketable securities at fair value with changes in fair value being recorded as a component of accumulated other comprehensive income (loss). When a security is sold, we use specific identification to determine the cost of the security sold or the amount reclassified out of accumulated other comprehensive income (loss).

*Restricted Cash.* We receive cash earnest money deposits from our customers who enter into home sale contracts. In certain states we are restricted from using such deposits for general purposes, unless we take measures to release state imposed restrictions on such deposits received from homebuyers, which may include posting blanket security bonds. We had \$2.2 million and \$1.9 million in restricted cash related to homebuyer deposits at December 31, 2013 and 2012, respectively.

*Home Sale Receivables.* Home sale receivables primarily consist of cash to be received from title companies or outside brokers associated with closed homes. Generally, we will receive cash from title companies and outside brokers within a few days of the home being closed.

**M.D.C. HOLDINGS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

*Mortgage Loans Held-for-Sale, net.* Mortgage loans held-for-sale are recorded at fair value based on quoted market prices and estimated market prices received from an outside third-party. Using fair value allows an offset of the changes in fair values of the mortgage loans and the derivative instruments used to hedge them without the burden of complying with the requirements for hedge accounting.

*Inventories.* Our inventories are primarily associated with communities where we intend to construct and sell homes, including models and unsold started homes. Costs capitalized to land and land under development primarily include: (1) land costs; (2) land development costs; (3) entitlement costs; (4) capitalized interest; (5) engineering fees; and (6) title insurance, real property taxes and closing costs directly related to the purchase of the land parcel. Components of housing completed or under construction primarily include: (1) land costs transferred from land and land under development; (2) direct construction costs associated with a house; (3) real property taxes, engineering fees, permits and other fees; (4) capitalized interest; and (5) indirect construction costs, which include field construction management salaries and benefits, utilities and other construction related costs. Land costs are transferred from land and land under development to housing completed or under construction at the point in time that construction of a home on an owned lot begins.

In accordance with ASC Topic 360, *Property, Plant, and Equipment* (“ASC 360”), homebuilding inventories are carried at cost unless events and circumstances indicate that the carrying value of the underlying subdivision may not be recoverable. We evaluate inventories for impairment at each quarter end on a subdivision level basis as each such subdivision represents the lowest level of identifiable cash flows. In making this determination, we review, among other things, the following for each subdivision:

- actual and trending “Operating Margin” (which is defined as home sale revenues less home cost of sales and all direct incremental costs associated with the home closing, including sales commissions) for homes closed;
- estimated future undiscounted cash flows and Operating Margin;
- forecasted Operating Margin for homes in backlog;
- actual and trending net and gross home orders;
- base sales price and home sales incentive information for homes closed, homes in backlog and homes available for sale;
- market information for each sub-market, including competition levels, home foreclosure levels, the size and style of homes currently being offered for sale and lot size; and
- known or probable events indicating that the carrying value may not be recoverable.

If events or circumstances indicate that the carrying value of our inventory may not be recoverable, assets are reviewed for impairment by comparing the undiscounted estimated future cash flows from an individual subdivision

(including capitalized interest) to its carrying value. If the undiscounted future cash flows are less than the subdivision's carrying value, the carrying value of the subdivision is written down to its then estimated fair value. We generally determine the estimated fair value of each subdivision by determining the present value of the estimated future cash flows at discount rates that are commensurate with the risk of the subdivision under evaluation. For the years ended December 31, 2013, 2012 and 2011, we used discount rates ranging from 10% to 18% for the subdivisions that were impaired.

*Property and Equipment, net.* Property and equipment is carried at cost less accumulated depreciation and amortization. Depreciation and amortization is computed using the straight-line method over the estimated useful lives of the related assets, which range from 2 to 29 years. Depreciation and amortization expense for property and equipment was \$3.7 million, \$4.4 million and \$6.1 million for the years ended December 31, 2013, 2012 and 2011, respectively.



**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The following table sets forth the cost and carrying value of our property and equipment by major asset category.

|                                 | Cost     | Accumulated<br>Depreciation<br>and<br>Amortization<br>(Dollars in thousands) | Carrying<br>Value |
|---------------------------------|----------|------------------------------------------------------------------------------|-------------------|
| December 31, 2013:              |          |                                                                              |                   |
| Airplane                        | \$28,997 | \$ 6,604                                                                     | \$ 22,393         |
| Computer software and equipment | 18,436   | 11,780                                                                       | 6,656             |
| Leasehold improvements          | 8,793    | 6,787                                                                        | 2,006             |
| Other                           | 2,048    | 1,855                                                                        | 193               |
| Total                           | \$58,274 | \$ 27,026                                                                    | \$ 31,248         |
| December 31, 2012:              |          |                                                                              |                   |
| Airplane                        | \$28,997 | \$ 6,055                                                                     | \$ 22,942         |
| Computer software and equipment | 17,905   | 9,513                                                                        | 8,392             |
| Leasehold improvements          | 7,623    | 6,066                                                                        | 1,557             |
| Other                           | 1,991    | 1,757                                                                        | 234               |
| Total                           | \$56,516 | \$ 23,391                                                                    | \$ 33,125         |

*Deferred Tax Asset, net.* Deferred income taxes reflect the net tax effects of temporary differences between (1) the carrying amounts of the assets and liabilities for financial reporting purposes and (2) the amounts used for income tax purposes. Deferred tax assets and liabilities are measured using current enacted tax rates in effect in the years in which those temporary differences are expected to reverse. A valuation allowance is recorded against a deferred tax asset if, based on the weight of available evidence, it is more-likely-than-not (a likelihood of more than 50%) that some portion, or all, of the deferred tax asset will not be realized. At December 31, 2013 and 2012, based upon current facts and circumstances, we had recorded a valuation allowance of \$8.2 million and \$248.3 million, respectively, against our deferred tax assets (net of deferred tax liabilities). See Note 14 to the Consolidated Financial Statements.

*Deferred Marketing Costs.* Certain marketing costs related to model homes and sales offices are capitalized as they are: (1) reasonably expected to be recovered from the sale of the project; and (2) incurred for (a) tangible assets that are used directly throughout the selling period to aid in the sale of the project or (b) services that have been performed to obtain regulatory approval of sales. Capitalized marketing costs are included in prepaid and other assets in the Homebuilding section of the accompanying consolidated balance sheets and the associated amortization expense is

included in selling, general and administrative (“SG&A”) in the Homebuilding section of the accompanying consolidated statements of operations as the homes in the related subdivision are delivered. We allocate all capitalized marketing costs equally to each house within a subdivision and record expense as homes close over the life of a subdivision. All other marketing costs are expensed as incurred.

*Variable Interest Entities.* In accordance with ASC Topic 810, *Consolidation* (“ASC 810”), we analyze our land option contracts and other contractual arrangements to determine whether the corresponding land sellers are variable interest entities (“VIEs”) and, if so, whether we are the primary beneficiary. Although we do not have legal title to the optioned land, ASC 810 requires a company to consolidate a VIE if the company is determined to be the primary beneficiary. In determining whether we are the primary beneficiary, we consider, among other things, whether we have the power to direct the activities of the VIE that most significantly impact VIE’s economic performance, including, but not limited to, determining or limiting the scope or purpose of the VIE, selling or transferring property owned or controlled by the VIE, or arranging financing for the VIE. We also consider whether we have the obligation to absorb losses of the VIE or the right to receive benefits from the VIE. We have concluded that, as of December 31, 2013, we were not the primary beneficiary of any VIEs from which we are purchasing land under land option contracts.

*Related Party Assets.* Our related party assets are debt security bonds acquired from a quasi-municipal corporation in the state of Colorado. See Note 15 to the Consolidated Financial Statements.

**M.D.C. HOLDINGS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

*Goodwill.* In accordance with ASC Topic 350, *Intangibles—Goodwill and Other* (“ASC 350”), we evaluate goodwill for possible impairment annually or more frequently if events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. We use a three step process to assess the realizability of goodwill. The first step is a qualitative assessment that analyzes current economic indicators associated with a particular reporting unit. For example, we analyze changes in economic, market and industry conditions, business strategy, cost factors, and financial performance, among others, to determine if there would be a significant decline to the fair value of a particular reporting unit. If the qualitative assessment indicates a stable or improved fair value, no further testing is required.

If a qualitative assessment indicates that a significant decline to fair value of a reporting unit is more likely than not, or if a reporting unit’s fair value has historically been closer to its carrying value, we will proceed to the second step where we calculate the fair value of a reporting unit based on discounted future probability-weighted cash flows. If this step indicates that the carrying value of a reporting unit is in excess of its fair value, we will proceed to the third step where the fair value of the reporting unit will be allocated to assets and liabilities as they would in a business combination. Impairment occurs when the carrying amount of goodwill exceeds its estimated fair value calculated in the third step.

Based on our analysis, we have concluded as of December 31, 2013, our goodwill was not impaired.

*Liability for Unrecognized Tax Benefits.* ASC Topic 740, *Income Taxes*, regarding liabilities for unrecognized tax benefits provides guidance for the recognition and measurement in financial statements of uncertain tax positions taken or expected to be taken in a tax return.

The evaluation of a tax position is a two-step process, the first step being recognition. We determine whether it is more-likely-than-not that a tax position will be sustained upon tax examination, including resolution of any related appeals or litigation, based on the technical merits of the position. The technical merits of a tax position derive from both statutory and judicial authority (legislation and statutes, legislative intent, regulations, rulings, and case law) and their applicability to the facts and circumstances of the tax position. If a tax position does not meet the more-likely-than-not recognition threshold, the benefit of that position is not recognized in the financial statements.

The second step is measurement. A tax position that meets the more-likely-than-not recognition threshold is measured to determine the amount of benefit to recognize in the financial statements. The tax position is measured as the largest

amount of benefit that is greater than 50 percent likely of being realized upon ultimate resolution with a taxing authority. Once the gross unrecognized tax benefit is determined, we also accrue for any interest and penalties, as well as any offsets expected from resultant amendments to federal or state tax returns. We record the aggregate effect of these items in income tax expense in the consolidated statements of operations, and the corresponding liability in accrued liabilities in the Homebuilding section of our consolidated balance sheets.

*Warranty Reserves.* Our homes are sold with limited third-party warranties. Under our agreement with the issuer of the third-party warranties, we are responsible for performing all of the work for the first two years of the warranty coverage, and paying for substantially all of the work required to be performed during years three through ten of the warranties. We record expenses and warranty reserves for general and structural warranty claims, as well as reserves for known, unusual warranty-related expenditures. Warranty reserves are established based upon historical payment experience in an amount estimated to be adequate to cover expected costs of materials and outside labor during warranty periods. The establishment of warranty reserves for closed homes and the evaluation of our warranty reserve balance is based on an internally developed analysis that includes known facts and interpretations of circumstances, including, among other things, our trends in historical warranty payment levels and warranty payments for claims not considered to be normal and recurring.

Warranty payments are recorded against the warranty reserve. Additional reserves may be established for known, unusual warranty-related expenditures not covered through the independent warranty reserve analysis performed by us. Warranty payments incurred for an individual house may differ from the related reserve established for the home at the time it was closed. The actual disbursements for warranty claims are evaluated in the aggregate to determine if an adjustment to the historical warranty reserve should be recorded.

**M.D.C. HOLDINGS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

We assess the reasonableness and adequacy of the reserve and the per-unit reserve amount originally included in home cost of sales, as well as the timing of the reversal of any excess reserve on a quarterly basis, using historical payment data and other relevant information. Warranty reserves are included in accrued liabilities in the Homebuilding section of our consolidated balance sheets and adjustments to our warranty reserves are recorded as an increase or reduction to home cost of sales in the Homebuilding section of our consolidated statements of operations.

*Insurance Reserves.* The establishment of reserves for estimated losses associated with insurance policies issued by Allegiant and re-insurance agreements issued by StarAmerican are based on actuarial or internally developed studies that include known facts and interpretations of circumstances, including our experience with similar cases and historical trends involving claim payment patterns, pending levels of unpaid claims, product mix or concentration, claim severity, frequency patterns depending on the business conducted, and changing regulatory and legal environments.

*Mortgage Loan Loss Reserves.* In the normal course of business, we establish reserves for potential losses associated with HomeAmerican's sale of mortgage loans to third-parties. These reserves are created to address repurchase and indemnity claims by third-party purchasers of the mortgage loans, which claims arise primarily from various loan document manufacturing quality assertions as well as allegations of homebuyer fraud at the time of origination of the loan. These reserves are based upon, among other things: (1) pending claims received from third-party purchasers associated with previously sold mortgage loans; and (2) a current assessment of the potential exposure associated with future claims of fraud in mortgage loans originated in prior periods. In addition to reserves established for mortgage loans previously sold to third-parties, we establish reserves for loans that we have repurchased if we believe the loss is likely and estimable. Our mortgage loan reserves are reflected as a component of accrued liabilities in the Financial Services section of the accompanying consolidated balance sheets, and the associated expenses are included in Expenses in the Financial Services section of the accompanying consolidated statements of operations. See Note 17 to the Consolidated Financial Statements.

*Litigation Reserves.* We and certain of our subsidiaries have been named as defendants in various cases. We reserve for estimated exposure with respect to these cases based upon currently available information on each case. See Note 17 to the Consolidated Financial Statements.

*Derivative Financial Instruments.* The derivative instruments we utilize in the normal course of business are interest rate lock commitments and forward sales of mortgage-backed securities, both of which typically are short-term in nature. Forward sales of mortgage-backed securities are utilized to hedge changes in fair value of our interest rate lock commitments as well as mortgage loans held-for-sale not under commitments to sell. For forward sales of securities,

as well as interest rate lock commitments that are still outstanding at the end of a reporting period, we record the changes in fair value of the derivatives in revenues in the Financial Services section of our consolidated statements of operations with an offset to prepaid expenses and other assets or accounts payable and accrued liabilities in the Financial Services section of our accompanying consolidated balance sheets, depending on the nature of the change.

At December 31, 2013 and 2012, we had interest rate lock commitments with aggregate principal balances of approximately \$69.8 million and \$50.8 million, respectively, at average interest rates of 4.13% and 3.26%, respectively. In addition, we had \$25.9 million and \$11.7 million of mortgage loans held-for-sale at December 31, 2013 and 2012, respectively, that had not yet been committed to a mortgage purchaser. In order to hedge the changes in fair value of our interest rate lock commitments and mortgage loans held-for-sale which had not yet been committed to a mortgage purchaser, we had forward sales of securities totaling \$74.5 million and \$41.5 million at December 31, 2013 and 2012, respectively.

For the years ended December 31, 2013, 2012 and 2011, we recorded net gains (losses) on our derivatives of \$(0.1) million, \$1.1 million and \$0.6 million, respectively. For further discussion of our policies regarding interest rate lock commitments, see our "Revenue Recognition for HomeAmerican" accounting policy section below.

*Revenue Recognition for Homebuilding Segments.* Revenue from home closings and land sales is recognized when the closing has occurred, title has passed, adequate initial and continuing investment by the buyer is received, possession and other attributes of ownership have been transferred to the buyer and we are not obligated to perform significant additional activities after closing and delivery. If the buyer has provided sufficient initial and continuing investment, and all other revenue recognition criteria have been met, revenue is recognized on the date of closing. Revenue from a home closing includes the base sales price and any purchased options and upgrades and is reduced for any sales price incentives.

**M.D.C. HOLDINGS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

We defer Operating Margin related to the sale of a home if all of the following criteria are present: (1) HomeAmerican originates the mortgage loan; (2) HomeAmerican has not sold the mortgage loan, or loans, as of the end of the pertinent reporting period; and (3) the homebuyer's down payment does not meet the initial or continuing investment criteria. The deferral is subsequently recognized at the time HomeAmerican sells the homebuyer's mortgage loan, or loans, to a third-party purchaser. In the event the Operating Margin is a loss, we recognize such loss at the time the home is closed. We did not have any homes that closed during the years ended December 31, 2013, 2012 or 2011 that failed to meet the continuing investment criteria.

*Revenue Recognition for HomeAmerican.* Revenues recorded by HomeAmerican primarily include origination fees and the corresponding sale of a loan and its servicing rights. Origination fees are recognized when a loan is originated. When an interest rate lock commitment is made to a customer, we record the expected gain on sale of the mortgage including servicing rights, adjusted for a pull-through percentage (which is defined as the likelihood that an interest rate lock commitment will be originated), as revenue. As the interest rate lock commitment gets closer to being originated, the expected gain on the sale of that loan plus servicing rights is updated to reflect current market value and the increase or decrease in the fair value of that interest rate lock commitment is recorded through revenues. At the same time, as the likelihood of the interest rate lock commitment being originated increases resulting in an improvement to the expected pull-through percentage, additional revenues are recognized. After origination, our mortgage loans generally are transferred to third-party purchasers in accordance with sale agreements entered into by us with a third party purchaser of the loans. We make representations and warranties with respect to the status of loans transferred in the sale agreements. The sale agreements generally include statements acknowledging the transfer of the loans is intended by both parties to constitute a sale. Sale of a mortgage loan has occurred when the following criteria, among others, have been met: (1) fair consideration has been paid for transfer of the loan by a third party in an arms-length transaction, (2) all the usual risks and rewards of ownership that are in substance a sale have been transferred by us to the third party purchaser; and (3) we do not have a substantial continuing involvement with the mortgage loan. The related servicing rights are generally transferred by us to the third party purchaser for additional consideration. Revenue from the sale of mortgage loan servicing is recognized upon the exchange of consideration for the mortgage loans and related servicing rights between us and the third-party purchaser.

We measure mortgage loans held-for-sale at fair value with the changes in fair value being reported in earnings at each reporting date. The impact of recording changes in fair value to earnings did not have a material impact on our financial position, results of operations or cash flows during the years ended December 31, 2013, 2012 or 2011. Gains on sales of mortgage loans, net, were \$28.7 million, \$21.7 million and \$10.0 million for the years ended December 31, 2013, 2012 and 2011, respectively, and are included as a component of revenues in the Financial Services section of the consolidated statements of operations.

*Home Cost of Sales.* Home cost of sales includes the specific construction costs of each home and all applicable land acquisition, land development and related costs, both incurred and estimated to be incurred, warranty costs and finance and closing costs, including closing cost incentives. We use the specific identification method for the purpose of accumulating home construction costs and allocate costs to each lot within a subdivision associated with land acquisition and land development based upon relative fair value of the lots prior to home construction. Lots within a subdivision typically have comparable fair values, and, as such, we generally allocate costs equally to each lot within a subdivision. We record all home cost of sales when a home is closed on a house-by-house basis.

When a home is closed, we generally have not yet paid and recorded all costs necessary to complete the construction of the home and certain land development costs. At the time of a home closing, we compare the home construction budgets to actual recorded costs to determine the additional costs remaining to be paid on each closed home. For amounts not incurred or paid as of the time of closing a home, we record an estimated accrual associated with certain home construction and land development costs. Generally, these accruals are established based upon contracted work which has yet to be paid, open work orders not paid at the time of home closing, as well as land completion costs more likely than not to be incurred, and represent estimates believed to be adequate to cover the expected remaining home construction and land development costs. We monitor the adequacy of these accruals on a house-by-house basis and in the aggregate on a subdivision-by-subdivision basis. At December 31, 2013 and 2012, we had \$9.6 million and \$9.5 million, respectively, of land development and home construction accruals for closed homes. Actual results could differ from such estimates.



**M.D.C. HOLDINGS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

*Stock-Based Compensation Expense.* Stock-based compensation expense for all share-based payment awards is based on the grant date fair value. The grant date fair value for stock option awards is estimated using the Black-Scholes option pricing model and the grant date fair value for restricted stock awards is based upon the closing price of our common stock on the date of grant. We recognize these compensation costs net of estimated forfeitures. For stock option awards with service conditions only, we recognize stock-based compensation expense on a straight-line basis over the requisite service period of the award, which is currently the vesting term of up to seven years. For our stock option awards with performance conditions, we recognize stock-based compensation expense on a straight-line basis for each performance criteria tranche (if applicable) over the period between the date that it is determined the performance conditions related to each tranche (if applicable) are probable to be met and the date the option vests.

*Earnings (Loss) Per Common Share.* For purposes of calculating earnings (loss) per share (“EPS”), a company that has participating security holders (for example, unvested restricted stock that has nonforfeitable dividend rights) is required to utilize the two-class method for calculating earnings per share unless the treasury stock method results in lower EPS. The two-class method is an allocation of earnings/(loss) between the holders of common stock and a company’s participating security holders. Under the two-class method, earnings/(loss) for the reporting period are allocated between common shareholders and other security holders based on their respective rights to receive distributed earnings (i.e., dividends) and undistributed earnings (i.e., net income/(loss)). Currently, we have one class of security and we have participating security holders consisting of shareholders of unvested restricted stock. Basic EPS is calculated by dividing income or loss attributable to common stockholders by the weighted average number of shares of common stock outstanding.

For purposes of calculating diluted EPS, basic EPS is further adjusted to include the effect of potential dilutive stock options outstanding.

*Recently Issued Accounting Standards.* In February 2013, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2013-02, *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*, (“ASU 2013-02”). ASU 2013-02 amends ASC Topic 220, *Comprehensive Income* (“ASC 220”), and requires entities to present the changes in the components of accumulated other comprehensive income for the current period. Entities are required to present separately the amount of the change that is due to reclassifications, and the amount that is due to current period other comprehensive income. These changes are permitted to be shown either before or net-of-tax and can be displayed either on the face of the financial statements or in the footnotes. ASU 2013-02 was effective for our interim and annual periods beginning January 1, 2013. The adoption of ASU 2013-02 did not have a material effect on our consolidated financial position or results of operations.

**2. Supplemental Cash Flow Disclosure**

The table below sets forth supplemental disclosures of cash flow information and non-cash investing and financing activities.

|                                                            | Year Ended December 31, |          |            |
|------------------------------------------------------------|-------------------------|----------|------------|
|                                                            | 2013                    | 2012     | 2011       |
|                                                            | (Dollars in thousands)  |          |            |
| Cash paid for:                                             |                         |          |            |
| Interest, net of interest capitalized                      | \$-                     | \$1,083  | \$25,190   |
| Income taxes                                               | \$5,161                 | \$577    | \$3,532    |
| Non-cash investing and financing activities                |                         |          |            |
| Unrealized holding gains (losses) on marketable securities | \$6,737                 | \$12,078 | \$(12,124) |

**M.D.C. HOLDINGS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**3. Segment Reporting**

Our operating segments are defined as a component of an enterprise for which discrete financial information is available and is reviewed regularly by the chief operating decision-maker, or decision-making group, to evaluate performance and make operating decisions. We have identified our chief operating decision-makers (“CODMs”) as two key executives—the Chief Executive Officer and the Chief Operating Officer.

We have identified each homebuilding division as an operating segment. Our operating segments have been aggregated into the reportable segments noted below because they are similar in the following regards: (1) economic characteristics; (2) housing products; (3) class of homebuyer; (4) regulatory environments; and (5) methods used to construct and sell homes. Our homebuilding reportable segments are as follows:

West (Arizona, California, Nevada and Washington)

Mountain (Colorado and Utah)

East (Virginia, Florida, Illinois and Maryland, which includes Pennsylvania, Delaware and New Jersey)

Our Financial Services business consists of the operations of the following operating segments: (1) HomeAmerican Mortgage Corporation (“HomeAmerican”); (2) Allegiant; (3) StarAmerican; (4) American Home Insurance Agency, Inc.; and (5) American Home Title and Escrow Company. Due to its contributions to consolidated pretax income we consider HomeAmerican to be a reportable segment (“Mortgage operations”). The remaining operating segments have been aggregated into one reportable segment (“Other”) because they do not individually exceed 10 percent of: (1) consolidated revenue; (2) the greater of (A) the combined reported profit of all operating segments that did not report a loss or (B) the positive value of the combined reported loss of all operating segments that reported losses; or (3) consolidated assets.

Corporate is a non-operating segment that develops and implements strategic initiatives and supports our operating divisions by centralizing key administrative functions such as finance and treasury, information technology, insurance and risk management, litigation and human resources. Corporate also provides the necessary administrative functions to support MDC as a publicly traded company. A portion of the expenses incurred by Corporate are allocated to the homebuilding operating segments based on their respective percentages of assets, and to a lesser degree, a portion of Corporate expenses are allocated to the financial services segments. A majority of Corporate’s personnel and resources are primarily dedicated to activities relating to the homebuilding segments, and, therefore, the balance of any unallocated Corporate expenses is included in the homebuilding segment.

The following table summarizes home and land sale revenues for our homebuilding operations and revenues for our financial services operations.

|                                   | Year Ended December 31, |             |           |
|-----------------------------------|-------------------------|-------------|-----------|
|                                   | 2013                    | 2012        | 2011      |
|                                   | (Dollars in thousands)  |             |           |
| <b>Homebuilding</b>               |                         |             |           |
| West                              | \$671,278               | \$516,079   | \$272,800 |
| Mountain                          | 546,801                 | 355,368     | 316,189   |
| East                              | 411,096                 | 284,695     | 228,034   |
| Total home and land sale revenues | \$1,629,175             | \$1,156,142 | \$817,023 |
| <b>Financial Services</b>         |                         |             |           |
| Mortgage operations               | \$34,976                | \$35,123    | \$17,807  |
| Other                             | 16,283                  | 11,758      | 8,279     |
| Total financial services revenues | \$51,259                | \$46,881    | \$26,086  |

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The following table summarizes pretax income (loss) for our homebuilding and financial services operations.

|                                         | Year Ended December 31, |          |             |
|-----------------------------------------|-------------------------|----------|-------------|
|                                         | 2013                    | 2012     | 2011        |
|                                         | (Dollars in thousands)  |          |             |
| <b>Homebuilding</b>                     |                         |          |             |
| West                                    | \$65,672                | \$27,076 | \$(16,889 ) |
| Mountain                                | 52,392                  | 24,302   | 1,397       |
| East                                    | 19,590                  | 11,011   | (7,195 )    |
| Corporate                               | (37,331 )               | (29,772) | (87,941 )   |
| Total homebuilding pretax income (loss) | \$100,323               | \$32,617 | \$(110,628) |
| <b>Financial Services</b>               |                         |          |             |
| Mortgage operations                     | \$21,608                | \$23,939 | \$394       |
| Other                                   | 7,894                   | 4,559    | 2,762       |
| Total financial services pretax income  | \$29,502                | \$28,498 | \$3,156     |
| Total pretax income (loss)              | \$129,825               | \$61,115 | \$(107,472) |

The following table summarizes total assets for our homebuilding and financial services operations. The assets in our West, Mountain and East segments consist primarily of inventory while the assets in our Corporate segment primarily include cash and cash equivalents, marketable securities, and our deferred tax asset.

|                                  | December 31,           |             |
|----------------------------------|------------------------|-------------|
|                                  | 2013                   | 2012        |
|                                  | (Dollars in thousands) |             |
| <b>Homebuilding assets</b>       |                        |             |
| West                             | \$760,450              | \$459,807   |
| Mountain                         | 418,796                | 332,939     |
| East                             | 297,627                | 274,199     |
| Corporate                        | 951,809                | 692,500     |
| Total homebuilding assets        | \$2,428,682            | \$1,759,445 |
| <b>Financial services assets</b> |                        |             |
| Mortgage operations              | \$99,065               | \$122,941   |
| Other                            | 67,702                 | 63,055      |
| Total financial services assets  | \$166,767              | \$185,996   |

|              |             |             |
|--------------|-------------|-------------|
| Total assets | \$2,595,449 | \$1,945,441 |
|--------------|-------------|-------------|

F-15

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**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****4. Earnings (Loss) Per Share**

The following table shows our basic and diluted EPS calculations:

|                                                                                                | Year Ended December 31, |            |             |
|------------------------------------------------------------------------------------------------|-------------------------|------------|-------------|
|                                                                                                | 2013                    | 2012       | 2011        |
| <b>Numerator</b>                                                                               |                         |            |             |
| Net income (loss)                                                                              | \$314,385               | \$62,699   | \$(98,390 ) |
| Less: distributed earnings allocated to participating securities                               | -                       | (1,101 )   | (711 )      |
| Less: undistributed earnings allocated to participating securities                             | (4,917 )                | -          | -           |
| Net income (loss) attributable to common stockholders (numerator for basic earnings per share) | \$309,468               | \$61,598   | \$(99,101 ) |
| Add back: undistributed earnings allocated to participating securities                         | 4,917                   | -          | -           |
| Less: undistributed earnings reallocated to participating securities                           | (4,879 )                | -          | -           |
| Numerator for diluted EPS under two class method                                               | \$309,506               | \$61,598   | \$(99,101 ) |
| <b>Denominator</b>                                                                             |                         |            |             |
| Weighted-average common shares outstanding                                                     | 48,453,119              | 47,660,629 | 46,796,334  |
| Add: dilutive effect of stock options                                                          | 378,666                 | 173,527    | -           |
| Denominator for diluted EPS under two class method                                             | 48,831,785              | 47,834,156 | 46,796,334  |
| Basic Earnings Per Common Share                                                                | 6.39                    | 1.29       | (2.12 )     |
| Diluted Earnings Per Common Share                                                              | 6.34                    | 1.29       | (2.12 )     |

Diluted EPS for the years ended December 31, 2013 and 2012 excluded options to purchase approximately 3.8 million and 4.7 million shares, respectively, of common stock because the effect of their inclusion would be anti-dilutive.

There was no dilutive effect of common stock equivalents for the year ended December 31, 2011 because the effect of their inclusion would have been anti-dilutive. Using the treasury stock method, the weighted-average common stock equivalents excluded from diluted EPS were 0.3 million shares for the year ended December 31, 2011.

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****5. Accumulated Other Comprehensive Income (Loss)**

The following table sets forth our changes in accumulated other comprehensive income (loss):

|                                                                                               | Year Ended December 31, |            |            |
|-----------------------------------------------------------------------------------------------|-------------------------|------------|------------|
|                                                                                               | 2013                    | 2012       | 2011       |
|                                                                                               | (Dollars in thousands)  |            |            |
| Unrealized gains (losses) on available-for-sale marketable securities <sup>(1)</sup> :        |                         |            |            |
| Beginning balance                                                                             | \$4,838                 | \$(7,240 ) | \$4,884    |
| Other comprehensive income before reclassifications                                           | 3,255                   | 12,473     | (12,323 )  |
| Amounts reclassified from accumulated other comprehensive income <sup>(2)</sup>               | (438 )                  | (395 )     | 199        |
| Ending balance                                                                                | \$7,655                 | \$4,838    | \$(7,240 ) |
| Unrealized gains on available-for-sale metropolitan district bond securities <sup>(1)</sup> : |                         |            |            |
| Beginning balance                                                                             | \$-                     | \$-        | \$-        |
| Other comprehensive income before reclassifications                                           | 3,920                   | -          | -          |
| Amounts reclassified from accumulated other comprehensive income                              | -                       | -          | -          |
| Ending balance                                                                                | \$3,920                 | \$-        | \$-        |
| Total ending accumulated other comprehensive income (loss)                                    | \$11,575                | \$4,838    | \$(7,240 ) |

- (1) All amounts  
net-of-tax.  
See separate  
table below for  
(2) details about  
these  
reclassifications.

The following table sets forth the activity related to reclassifications out of accumulated other comprehensive income (loss) related to available for sale securities:

|  | Year Ended   |      |      |
|--|--------------|------|------|
|  | December 31, |      |      |
|  | 2013         | 2012 | 2011 |



(Dollars in thousands)

Affected Line Item in the Statements of Operations

|                                              |        |       |         |
|----------------------------------------------|--------|-------|---------|
| Homebuilding interest income                 | \$ 580 | 823   | \$(371) |
| Financial services interest and other income | 133    | (181) | 47      |
| Income (loss) before income taxes            | 713    | 642   | (324)   |
| Benefit from income taxes                    | (275)  | (247) | 125     |
| Net income (loss)                            | \$438  | \$395 | \$(199) |

**6. Fair Value Measurements**

ASC Topic 820, *Fair Value Measurements* (“ASC 820”), defines fair value, establishes guidelines for measuring fair value and expands disclosures regarding fair value measurements. ASC 820 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs for which little or no market data exists, therefore requiring an entity to develop its own assumptions.

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The following table sets forth the fair values and methods used for measuring the fair values of financial instruments on a recurring basis:

| Financial Instrument                                                      | Hierarchy | Fair Value             |                   |
|---------------------------------------------------------------------------|-----------|------------------------|-------------------|
|                                                                           |           | December 31, 2013      | December 31, 2012 |
|                                                                           |           | (Dollars in thousands) |                   |
| Marketable securities (available-for-sale)                                |           |                        |                   |
| Equity securities                                                         | Level 1   | \$389,323              | \$208,818         |
| Debt securities - maturity less than 1 year                               | Level 2   | 72,577                 | 54,388            |
| Debt securities - maturity 1 to 5 years                                   | Level 2   | 106,566                | 277,514           |
| Debt securities - maturity greater than 5 years                           | Level 2   | 19,601                 | 11,218            |
| Total available-for-sale securities                                       |           | \$588,067              | \$551,938         |
| Mortgage loans held-for-sale, net                                         | Level 2   | \$92,578               | \$119,953         |
| Metropolitan district bond securities (available-for-sale) <sup>(1)</sup> | Level 3   | \$12,729               | \$12,920          |

(1) These securities were recorded at their cost-basis at December 31, 2012 as they were still under the cost recovery method of accounting. As such, the fair value presented for December 31, 2012 does not equal the amount we

have recorded  
in our  
accompanying  
consolidated  
balance sheets.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments.

The fair value of our cash and cash equivalents, restricted cash, trade and other receivables, inventories, prepaid and other assets, accounts payable, and accrued liabilities approximate their carrying value.

*Marketable Securities.* We have marketable debt and equity securities. Our debt securities consist primarily of fixed and floating rate interest earning debt securities, which may include, among others, United States government and government agency debt and corporate debt. Our equity securities consist primarily of holdings in mutual fund securities, which invest mostly in debt securities. The remaining equity securities in our investment portfolio are holdings in corporate equities. As of December 31, 2013 and December 31, 2012, all of our marketable securities were treated as available-for-sale investments and, as such, we have recorded all of our marketable securities at fair value with changes in fair value being recorded as a component of accumulated other comprehensive income (loss).

The following tables set forth the amortized cost and estimated fair value of our available-for-sale marketable securities.

|                                                             | December 31, 2013      |           | December 31, 2012 |           |
|-------------------------------------------------------------|------------------------|-----------|-------------------|-----------|
|                                                             | Amortized              | Fair      | Amortized         | Fair      |
|                                                             | Cost                   | Value     | Cost              | Value     |
|                                                             | (Dollars in thousands) |           |                   |           |
| <b>Homebuilding:</b>                                        |                        |           |                   |           |
| Equity securities                                           | \$375,142              | \$385,303 | \$208,279         | \$208,818 |
| Debt securities                                             | 181,635                | 183,718   | 306,793           | 310,647   |
| Total homebuilding available-for-sale securities            | \$556,777              | \$569,021 | \$515,072         | \$519,465 |
| <b>Financial Services:</b>                                  |                        |           |                   |           |
| Equity securities                                           | \$4,000                | \$4,020   | \$-               | \$-       |
| Debt securities                                             | 14,721                 | 15,026    | 32,028            | 32,473    |
| Total financial services available-for-sale debt securities | \$18,721               | \$19,046  | \$32,028          | \$32,473  |
| Total available-for-sale marketable securities              | \$575,498              | \$588,067 | \$547,100         | \$551,938 |



**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

As of December 31, 2013 and 2012, our marketable securities, were in unrealized gain positions, totaling \$12.6 million and \$4.8 million, respectively. Our marketable securities which were in unrealized loss positions aggregated to unrealized losses of \$1.1 million and \$2.7 million as of December 31, 2013 and 2012, respectively. The table below sets forth the debt and equity securities that were in an aggregate loss position. We do not believe that the aggregate unrealized loss related to our debt or equity securities as of December 31, 2013 is material to our operations.

| Type of Investment | Year Ended December 31,<br>2013                                                |                                                                      |                               | Year Ended December 31,<br>2012                      |                                                                      |                               |
|--------------------|--------------------------------------------------------------------------------|----------------------------------------------------------------------|-------------------------------|------------------------------------------------------|----------------------------------------------------------------------|-------------------------------|
|                    | Number<br>of<br>Securities<br>in<br>Loss<br>Position<br>(Dollars in thousands) | Aggregate<br>Fair Value<br>of<br>Securities<br>in a Loss<br>Position | Aggregate<br>Loss<br>Position | Number<br>of<br>Securities<br>in<br>Loss<br>Position | Aggregate<br>Fair Value<br>of<br>Securities<br>in a Loss<br>Position | Aggregate<br>Loss<br>Position |
| Debt               | 72                                                                             | \$ (430 )                                                            | \$ 46,440                     | 88                                                   | \$ (594 )                                                            | \$ 103,684                    |
| Equity             | 7                                                                              | (713 )                                                               | 14,174                        | 1                                                    | (2,060 )                                                             | 52,988                        |
| Total              | 79                                                                             | \$ (1,143 )                                                          | \$ 60,614                     | 89                                                   | \$ (2,654 )                                                          | \$ 156,672                    |

The followings table sets forth gross realized gains and gross realized losses from the sale of available-for-sale marketable securities, which were included in either interest income in the Homebuilding section or interest and other income in the Financial Services section of our consolidated statements of operations.

|                                                                 | Year Ended December 31, |            |            |
|-----------------------------------------------------------------|-------------------------|------------|------------|
|                                                                 | 2013                    | 2012       | 2011       |
|                                                                 | (Dollars in thousands)  |            |            |
| Gross realized gains on sales of available-for-sale securities  |                         |            |            |
| Equity securities                                               | \$ 1,251                | \$-        | \$-        |
| Debt securities                                                 | 83                      | 608        | 1,246      |
| Total                                                           | \$ 1,334                | \$ 608     | \$ 1,246   |
| Gross realized losses on sales of available-for-sale securities |                         |            |            |
| Equity securities                                               | \$-                     | \$-        | \$-        |
| Debt securities                                                 | (3,794)                 | (1,287)    | (1,231)    |
| Total                                                           | \$ (3,794)              | \$ (1,287) | \$ (1,231) |

Net realized gain (loss) on sales of available-for-sale securities    \$(2,460) \$(679 ) \$15

*Mortgage Loans Held-for-Sale, Net.* As of December 31, 2013, the primary components of our mortgage loans held-for-sale that are measured at fair value on a recurring basis are: (1) mortgage loans held-for-sale under commitments to sell; and (2) mortgage loans held-for-sale not under commitments to sell. At December 31, 2013 and December 31, 2012, we had \$65.1 million and \$108.3 million, respectively, of mortgage loans held-for-sale under commitments to sell for which fair value was based upon Level 2 inputs, which were the quoted market prices for those mortgage loans. At December 31, 2013 and December 31, 2012, we had \$25.9 million and \$11.7 million, respectively, of mortgage loans held-for-sale that were not under commitments to sell. The fair value for those loans was primarily based upon the estimated market price received from an outside party, which is a Level 2 fair value input.

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

*Metro District Bond Securities (Related Party).* The Metro District Bond Securities are included in other assets in the Homebuilding section of our accompanying consolidated balance sheets. We acquired the Metro District Bonds from a quasi-municipal corporation in the state of Colorado (the “Metro District”), which was formed to help fund and maintain the infrastructure associated with a master-planned community being developed by our Company. See Note 15 for further discussion related to the acquisition of these securities. Cash flows received by the Company from these securities reflect principal and interest payments from the Metro District that are supported by an annual levy on the taxable value of real estate and personal property within the Metropolitan District’s boundaries and a one-time fee assessed on permits obtained by MDC in the Metro District. The stated year of maturity for the Metro Bonds is 2037. However, if the unpaid principal and all accrued interest are not paid off by the year 2037, the Company will continue to receive principal and interest payments into perpetuity until the unpaid principal and accrued interest is paid in full. Since 2007 and through the first quarter of 2013, we accounted for these securities under the cost recovery method and they were not carried at fair value in accordance with ASC Topic 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality* (“ASC 310-30”).

In the second quarter of 2013, we determined that these securities no longer were required to be accounted for under the cost recovery method due to an increase in the number of new homes delivered in the community coupled with the stabilization of property values within the Metro District. In accordance with ASC 310-30, we will adjust the bond principal balance on a prospective basis using an interest accretion model that utilizes future cash flows expected to be collected. Furthermore, as this investment is accounted for as an available-for-sale asset, we will continue to update its fair value on a quarterly basis, with the adjustment being recorded through other comprehensive income. The fair value is based upon a discounted future cash flow model, which uses Level 3 inputs. The two primary unobservable inputs used in our discounted cash flow model are the forecasted number of homes to be closed, as they drive any increases to the tax base for the Metropolitan District, and the discount rate. The table below provides quantitative data regarding each unobservable input and the sensitivity of fair value to potential changes in those unobservable inputs.

| Unobservable Input              | Quantitative Data |     |                  | Sensitivity Analysis                          |                                               |
|---------------------------------|-------------------|-----|------------------|-----------------------------------------------|-----------------------------------------------|
|                                 | Range             |     | Weighted Average | Movement in Fair Value from Increase in Input | Movement in Fair Value from Decrease in Input |
| Discount rate                   | 6% to             | 16% | 10%              | Decrease                                      | Increase                                      |
| Number of homes closed per year | 0 to              | 155 | 88               | Increase                                      | Decrease                                      |

The table set forth below summarizes the activity for our Metro Bonds.

|                                                                 | Year Ended<br>December 31, |         |
|-----------------------------------------------------------------|----------------------------|---------|
|                                                                 | 2013                       | 2012    |
|                                                                 | (Dollars in<br>thousands)  |         |
| Balance at beginning of period                                  | \$5,818                    | \$6,663 |
| Increase in fair value (recorded in other comprehensive income) | 6,373                      | -       |
| Change due to accretion of principal                            | 1,192                      | -       |
| Cash receipts                                                   | (654 )                     | (845 )  |
| Balance at end of period                                        | \$12,729                   | \$5,818 |

*Mortgage Repurchase Facility.* The debt associated with our Mortgage Repurchase Facility is at floating rates or at fixed rates that approximate current market rates and have relatively short-term maturities, generally within 30 days. The fair value approximates carrying value and is based on Level 2 inputs.



**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

*Senior Notes.* The estimated values of the senior notes in the following table are based on Level 2 inputs, including market prices of other homebuilder bonds.

|                                         | December 31, 2013      |                         | December 31, 2012  |                            |
|-----------------------------------------|------------------------|-------------------------|--------------------|----------------------------|
|                                         | Carrying<br>Amount     | Estimated<br>Fair Value | Carrying<br>Amount | Estimated<br>Fair<br>Value |
|                                         | (Dollars in thousands) |                         |                    |                            |
| 5 % Senior Notes due December 2014, net | \$249,814              | \$258,750               | \$249,621          | \$267,208                  |
| 5 % Senior Notes due July 2015, net     | 249,935                | 262,562                 | 249,895            | 268,867                    |
| 5 % Senior Notes due February 2020, net | 245,871                | 259,688                 | 245,326            | 273,125                    |
| 6% Senior Notes due January 2043        | 350,000                | 305,083                 | -                  | -                          |
| Total                                   | \$1,095,620            | \$1,086,083             | \$744,842          | \$809,200                  |

*Inventories.* The table below sets forth the carrying value, at each year end, of all inventories that were impaired during each year presented.

|          | Carrying Value of      |          |
|----------|------------------------|----------|
|          | Impaired               |          |
|          | Inventory at           |          |
|          | December               |          |
|          | 31,                    | 31,      |
|          | 2013                   | 2012     |
|          | (Dollars in thousands) |          |
| West     | -                      | -        |
| Mountain | -                      | -        |
| East     | 4,187                  | 2,775    |
| Total    | \$4,187                | \$ 2,775 |

Inventories with carrying values prior to impairment of \$5.8 and \$3.8 million were determined to be impaired during the years ended December 31, 2013 and 2012, respectively. The carrying value for some of these inventories at their respective year ends may not represent the fair value they were impaired to due to activities that occurred subsequent

to the measurement date. The fair values of impaired inventories were determined using Level 3 inputs. We generally determine the estimated fair value of each subdivision by determining the present value of the estimated future cash flows at discount rates that are commensurate with the risk of the subdivision under evaluation.

## 7. Inventories

The following table sets forth, by reportable segment, information relating to our homebuilding inventories:

|                                          | December 31,           |             |
|------------------------------------------|------------------------|-------------|
|                                          | 2013                   | 2012        |
|                                          | (Dollars in thousands) |             |
| Housing Completed or Under Construction: |                        |             |
| West                                     | \$270,778              | \$200,858   |
| Mountain                                 | 194,101                | 183,522     |
| East                                     | 171,821                | 128,569     |
| Subtotal                                 | 636,700                | 512,949     |
| Land and Land Under Development:         |                        |             |
| West                                     | 459,512                | 230,344     |
| Mountain                                 | 211,526                | 137,221     |
| East                                     | 103,923                | 122,007     |
| Subtotal                                 | 774,961                | 489,572     |
| Total Inventories                        | \$1,411,661            | \$1,002,521 |

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

In accordance with ASC 360, homebuilding inventories are carried at cost unless events and circumstances indicate that the carrying value of the underlying subdivision may not be recoverable. We evaluate inventories for impairment at each quarter end. Please see “*Inventories*” in Note 1 for more detail on the methods and assumptions that were used to estimate the fair value of our inventories.

Inventory impairments recognized by segment for the years ended December 31, 2013, 2012 and 2011 are shown in the table below:

|                                          | Year Ended December<br>31,<br>2013 2012 2011<br>(Dollars in thousands) |         |          |
|------------------------------------------|------------------------------------------------------------------------|---------|----------|
| Housing Completed or Under Construction: |                                                                        |         |          |
| West                                     | \$-                                                                    | \$-     | \$7,270  |
| Mountain                                 | -                                                                      | -       | 1,850    |
| East                                     | 802                                                                    | 295     | 1,804    |
| Subtotal                                 | 802                                                                    | 295     | 10,924   |
| Land and Land Under Development:         |                                                                        |         |          |
| West                                     | -                                                                      | -       | 1,499    |
| Mountain                                 | -                                                                      | -       | 449      |
| East                                     | 117                                                                    | 810     | 93       |
| Subtotal                                 | 117                                                                    | 810     | 2,041    |
| Total Inventories                        | \$919                                                                  | \$1,105 | \$12,965 |

During the year ended December 31, 2013, we recorded \$0.9 million of inventory impairments related to three projects in our Maryland division in our East segment. During the year ended December 31, 2012, we recorded \$1.1 million of inventory impairments related to two projects in Maryland. Based on the slow sales absorption rates experienced during both 2012 and 2013 as well as the estimated sales price reductions required to sell the remaining lots and houses in these communities, it was determined that the fair values were less than the carrying values.

During the year ended December 31, 2011, we recorded \$13.0 million of inventory impairments. These impairments primarily were incurred during the 2011 second and third quarters in select subdivisions primarily in the California and Nevada markets of our West segment, and the Utah market of our Mountain segment. The impairment of these specific subdivisions, most of which were purchased during 2010, primarily resulted from lowering anticipated home sales prices from those that were expected at the time we purchased the land, based on our experience with homes sold

or closed in these subdivisions. As a result of lower than anticipated home sales prices, we determined based upon our impairment evaluation, that the fair market values of the land and homes in these subdivisions were less than their carrying values.

For the years ended December 31, 2013, 2012 and 2011, we used discount rates ranging from 10% to 18% for the subdivisions that were impaired.

## **8. Capitalization of Interest**

We capitalize interest to inventories during the period of development in accordance with ASC Topic 835, *Interest* (“ASC 835”). Homebuilding interest capitalized as a cost of inventories is included in cost of sales as related units or lots are sold. To the extent our homebuilding debt exceeds our qualified assets as defined in ASC 835, we expense a portion of the interest incurred by us. Qualified homebuilding assets consist of all lots and homes, excluding finished unsold homes or finished models, within projects that are actively selling or under development. The table set forth below summarizes homebuilding interest activity.

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The homebuilding interest expensed in the table below relates to the portion of interest incurred where our homebuilding debt exceeded our qualified inventory for such periods in accordance with ASC 835.

|                                                                      | Year Ended December 31, |          |          |
|----------------------------------------------------------------------|-------------------------|----------|----------|
|                                                                      | 2013                    | 2012     | 2011     |
|                                                                      | (Dollars in thousands)  |          |          |
| Homebuilding interest incurred                                       | \$61,634                | \$42,315 | \$62,290 |
| Less: Interest capitalized                                           | (59,908)                | (41,507) | (41,448) |
| Homebuilding interest expensed                                       | \$1,726                 | \$808    | \$20,842 |
| Interest capitalized, beginning of year                              | \$68,508                | 58,107   | \$37,811 |
| Interest capitalized during year                                     | 59,908                  | 41,507   | 41,448   |
| Less: Previously capitalized interest included in home cost of sales | (54,261)                | (31,106) | (21,152) |
| Interest capitalized, end of year                                    | \$74,155                | \$68,508 | \$58,107 |

**9. Homebuilding Prepaid Expenses and Other Assets**

The following table sets forth the components of homebuilding prepaid and other assets.

|                                                | December 31,           |          |
|------------------------------------------------|------------------------|----------|
|                                                | 2013                   | 2012     |
|                                                | (Dollars in thousands) |          |
| Land option deposits                           | \$15,221               | \$8,246  |
| Deferred marketing costs                       | 15,830                 | 13,874   |
| Metro district bond securities (related party) | 12,729                 | 5,818    |
| Prepaid expenses                               | 10,046                 | 5,575    |
| Goodwill                                       | 6,008                  | 6,008    |
| Deferred debt issuance costs, net              | 5,830                  | 2,641    |
| Other                                          | 590                    | 2,615    |
| Total                                          | \$66,254               | \$44,777 |

**10. Homebuilding Accrued Liabilities and Financial Services Accounts Payable and Accrued Liabilities**

The following table sets forth information relating to homebuilding accrued liabilities.

|                                                 | December 31,           |           |
|-------------------------------------------------|------------------------|-----------|
|                                                 | 2013                   | 2012      |
|                                                 | (Dollars in thousands) |           |
| Accrued compensation and related expenses       | \$35,990               | \$16,864  |
| Accrued executive deferred compensation         | 30,796                 | 28,475    |
| Accrued interest payable                        | 24,198                 | 13,698    |
| Warranty reserves                               | 22,238                 | 23,151    |
| Customer and escrow deposits                    | 10,759                 | 9,413     |
| Land development and home construction accruals | 9,592                  | 9,545     |
| Other accrued liabilities                       | 19,248                 | 17,310    |
| Total accrued liabilities                       | \$152,821              | \$118,456 |

F-23

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**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The following table sets forth information relating to financial services accounts payable and accrued liabilities.

|                                                | December 31,           |          |
|------------------------------------------------|------------------------|----------|
|                                                | 2013                   | 2012     |
|                                                | (Dollars in thousands) |          |
| Insurance reserves                             | \$49,637               | \$47,852 |
| Accounts payable and other accrued liabilities | 6,002                  | 4,012    |
| Total accounts payable and accrued liabilities | \$55,639               | \$51,864 |

**11. Warranty Accrual**

The following table summarizes the warranty reserve activity for the years ended December 31, 2013, 2012 and 2011.

|                                | Year Ended December 31, |          |          |
|--------------------------------|-------------------------|----------|----------|
|                                | 2013                    | 2012     | 2011     |
|                                | (Dollars in thousands)  |          |          |
| Balance at beginning of period | \$23,151                | \$25,525 | \$34,704 |
| Expense provisions             | 5,562                   | 4,216    | 4,224    |
| Cash payments                  | (6,475 )                | (6,590 ) | (7,925 ) |
| Adjustments                    | -                       | -        | (5,478 ) |
| Balance at end of period       | \$22,238                | \$23,151 | \$25,525 |

We recorded adjustments to reduce our warranty reserve by \$5.5 million for the year ended December 31, 2011 primarily as a result of favorable warranty payment experience relative to our estimates at the time of home closing as we continued to experience lower than anticipated warranty payments on previously closed homes. We believe the lower warranty payment experience rate in 2011 as compared to those in prior year was driven by, among other things, tighter focus and controls over our warranty expenditures, a significant drop in sales volumes over the last several years leading up to 2011, which resulted in fewer homes under warranty, and better quality controls and construction practices. There were no such adjustments required for 2012 or 2013. Furthermore, our warranty expense provision rates for 2013 and 2012 were lowered as a result of improved warranty payment experience over the last several years.

**12. Insurance Reserves**

The following table summarizes the insurance reserve activity for the years ended December 31, 2013, 2012 and 2011. The insurance reserve is included as a component of accounts payable and accrued liabilities in the Financial Services section of the accompanying consolidated balance sheets.

|                                  | Year Ended December 31, |          |          |
|----------------------------------|-------------------------|----------|----------|
|                                  | 2013                    | 2012     | 2011     |
|                                  | (Dollars in thousands)  |          |          |
| Balance at beginning of period   | \$47,852                | \$49,376 | \$51,576 |
| Expense provisions               | 7,065                   | 4,565    | 2,506    |
| Cash payments, net of recoveries | (5,280 )                | (8,020 ) | (7,115 ) |
| Adjustments                      | -                       | 1,931    | 2,409    |
| Balance at end of period         | \$49,637                | \$47,852 | \$49,376 |

The \$1.9 million and \$2.4 million of adjustments to increase our insurance reserves during the years ended December 31, 2012 and 2011, respectively, primarily resulted from increases in the severity and frequency of insurance claim experience relative to prior period estimates. No such adjustments were required for the year ended December 31, 2013.



**M.D.C. HOLDINGS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

In the ordinary course of business, we make payments from our insurance reserves to settle litigation claims arising primarily from our homebuilding activities. These payments are irregular in both their timing and their magnitude. As a result, the cash payments, net of recoveries shown for the years ended December 31, 2013, 2012, and 2011, are not necessarily indicative of what future cash payments will be for subsequent periods.

**13. Deferred Compensation Retirement Plans**

Effective August 1, 2008, the Company entered into amended and restated employment agreements (as amended on March 8, 2012, the "Employment Agreements") with Larry A. Mizel, Chairman of the Board and Chief Executive Officer, and David D. Mandarich, President and Chief Operating Officer (collectively, the "Executive Officers"), which provided certain annual post-retirement pension benefits (the "Retirement Benefits") depending on the year of retirement. In response to concerns expressed by significant institutional investors, and in accordance with the recommendation of an independent compensation consultant to the Company's Compensation Committee, the Company announced that it had reached agreements (collectively, the "Second Amendments") with the Executive Officers for the early termination, effective on October 18, 2013, of the Retirement Benefits contained in their respective Employment Agreements. Pursuant to the Second Amendments, the Company will pay each of Mr. Mizel and Mr. Mandarich a deferred lump sum in the amount of \$14.8 million and \$16.0 million, respectively, in full satisfaction of their past, present and future Retirement Benefits. The Company's termination of the Retirement Benefits is irrevocable. These payments, which equal the amounts accrued on the books of the Company as of June 30, 2013 with respect to the Company's estimated liability to pay Retirement Benefits, will be made to the Executive Officers on October 20, 2014. As a result of the termination of the Retirement Benefits, the Company will no longer incur ongoing Retirement Benefit accruals.

The deductibility of the Second Amendment payments for tax purposes under Internal Revenue Code ("IRC") Section 162(m) will be determined at the end of the taxable year in which the payments are made. However, because the Company believes that it is more likely than not that the payments will not be deductible, we wrote off approximately \$11.9 million of our deferred tax asset. Whether or not the payments are deductible under IRC Section 162(m), the Board of Directors believed that the early termination of the Retirement Benefits was in the best interests of the Company and its shareholders.

**14. Income Taxes**

Our provision for (benefit from) income taxes for the years ended December 31, 2013, 2012 and 2011 consisted of the following:

|                           | Year Ended December 31, |          |           |
|---------------------------|-------------------------|----------|-----------|
|                           | 2013                    | 2012     | 2011      |
|                           | (Dollars in thousands)  |          |           |
| Current tax benefit:      |                         |          |           |
| Federal                   | \$2,611                 | \$(374 ) | \$(3,652) |
| State                     | -                       | (1,210)  | (5,430)   |
| Total Current             | 2,611                   | (1,584)  | (9,082)   |
| Deferred expense          |                         |          |           |
| Federal                   | \$(171,037)             | \$-      | \$-       |
| State                     | (16,134 )               | -        | -         |
| Total deferred            | (187,171)               | -        | -         |
| Benefit from income taxes | (184,560)               | (1,584)  | (9,082)   |

F-25

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**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The provision for (benefit from) income taxes differs from the amount that would be computed by applying the statutory federal income tax rate of 35% to income before income taxes as a result of the following:

|                                                                            | Year Ended December 31, |            |            |
|----------------------------------------------------------------------------|-------------------------|------------|------------|
|                                                                            | 2013                    | 2012       | 2011       |
|                                                                            | (Dollars in thousands)  |            |            |
| Tax expense (benefit) computed at federal statutory rate                   | \$45,439                | \$21,390   | \$(37,615) |
| State income tax expense (benefit), net of federal benefit                 | 4,544                   | 2,139      | (3,762 )   |
| Permanent differences                                                      | (358 )                  | 1,771      | 93         |
| Expiration of state net operating loss                                     | 3,874                   | 2,634      | -          |
| Liability for unrecognized tax benefits                                    | (552 )                  | (1,857 )   | (9,173 )   |
| Write-off of deferred tax asset for deferred compensation retirement plans | 11,856                  | -          | -          |
| Federal Energy Credits                                                     | (6,530 )                | -          | -          |
| Change in valuation allowance                                              | (242,833)               | (27,661)   | 41,375     |
| Benefit from income taxes                                                  | \$(184,560)             | \$(1,584 ) | \$(9,082 ) |
| Effective tax (benefit) rate                                               | -142.2 %                | -2.6 %     | -8.5 %     |

We recorded income tax benefits of \$184.6 million, \$1.6 million and \$9.1 million for the years ended December 31, 2013, 2012 and 2011, respectively.

The income tax benefit for the year ended December 31, 2013 was due primarily to a \$187.6 million reversal of a portion of our deferred tax asset valuation allowance in the 2013 second quarter in addition to a \$6.5 million benefit from energy credits relating to current and prior years. These amounts were slightly offset by an \$11.9 million write-off of a deferred tax asset related to the termination of certain post-retirement pension benefits contained in the employment agreements of our Chief Executive Officer and Chief Operating Officer as discussed in Note 13 to the Consolidated Financial Statements.

In our evaluation of the need for, and level of, a valuation allowance recorded against our deferred tax assets at June 30, 2013, the most significant piece of evidence considered was the objective and direct positive evidence related to our recent financial results. Through June 30, 2013, we had generated pretax income in each of the six consecutive preceding quarters totaling \$121.7 million, with our second quarter 2013 pretax income being higher than any of the five previous quarters. In prior periods, a significant part of the negative evidence we considered was our three-year cumulative loss position. However, at June 30, 2013, when including expected earnings from homes currently in our backlog, we no longer anticipated being in a cumulative loss position at December 31, 2013. Lastly, if our quarterly

income in future years remained consistent with earnings levels experienced in recent quarters, we estimated that we would utilize all of our current federal net operating losses by 2016. Other negative evidence considered was the recent rise in mortgage interest rates, caused largely by an expectation that the Federal Reserve may taper its use of quantitative easing as early as the second half of 2013. However, the Federal Reserve has also indicated that such tapering would likely only occur if economic conditions continue to improve, which would help to offset the impact of rising interest rates on the homebuilding industry.

Based on our evaluation of both positive and negative evidence as of June 30, 2013, we concluded that the objective and direct positive evidence related to operating results achieved during the recent challenging economic and housing market conditions and the sustainability of current pretax income levels outweighed the negative evidence and that it is more likely than not that the substantial majority of the Company's deferred tax assets will be realized. After considering the results of the year ended December 31, 2013, we have determined that these conclusions reached during the second quarter of 2013 remain appropriate. In addition, the Company was out of a three year cumulative loss position as of September 30, 2013. A portion of our remaining valuation allowance as of June 30, 2013 was related to amounts expected to be reversed in the third and fourth quarters of 2013 as pretax income is realized as required by ASC 740-270, *Income Taxes - Interim Reporting*, when a change in a valuation allowance is recognized in an interim period. As a result of the valuation allowance release in the 2013 second quarter and the utilization of a portion of our remaining valuation allowance during the second half of 2013, our effective tax rate in 2013 is not meaningful as the income tax benefit is not directly correlated to the amount of pretax income or loss.

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

At December 31, 2013 we have a remaining valuation allowance of \$8.2 million related to various state net operating loss carryforwards where realization is more uncertain at this time due to the more limited carryforward periods that exist in certain states.

The income tax benefit for the year ended December 31, 2012 was due primarily to the release of reserves related to settlements with various taxing authorities.

The income tax benefit for the year ended December 31, 2011 was primarily from settlements of various state income tax matters and our settlement with the IRS on its audit of our 2004 and 2005 federal income tax returns.

Due to the effects of the deferred tax valuation allowance and changes in unrecognized tax benefits, our effective tax rates in 2012 and 2011 were not meaningful as the income tax benefit is not directly correlated to the amount of pretax income or loss generated in such periods.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of the assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The tax effects of significant temporary differences that give rise to the net deferred tax asset are as follows:

|                                                            | December 31,           |           |
|------------------------------------------------------------|------------------------|-----------|
|                                                            | 2013                   | 2012      |
|                                                            | (Dollars in thousands) |           |
| Deferred tax assets:                                       |                        |           |
| Federal net operating loss carryforwards                   | \$72,915               | \$129,695 |
| State net operating loss carryforwards                     | 40,227                 | 49,551    |
| Alternative minimum tax and other tax credit carryforwards | 24,196                 | 10,988    |
| Stock-based compensation expense                           | 26,651                 | 29,196    |
| Warranty, litigation and other reserves                    | 15,543                 | 14,556    |
| Deferred compensation retirement plans                     | -                      | 11,252    |
| Accrued compensation                                       | 11,136                 | -         |
| Asset impairment charges                                   | 5,889                  | 14,080    |
| Inventory, additional costs capitalized for tax purposes   | 7,064                  | 3,930     |
| Other, net                                                 | 3,446                  | 2,063     |

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|                                                       |           |           |
|-------------------------------------------------------|-----------|-----------|
| Total deferred tax assets                             | 207,067   | 265,311   |
| Valuation allowance                                   | (8,201 )  | (248,306) |
| Total deferred tax assets, net of valuation allowance | 198,866   | 17,005    |
| Deferred tax liabilities:                             |           |           |
| Property, equipment and other assets                  | 5,512     | 5,753     |
| Discount on notes receivable                          | 4,204     | 4,204     |
| Deferred revenue                                      | 3,985     | 3,796     |
| Unrealized gain on marketable securities              | 7,368     | 1,863     |
| Other, net                                            | 1,535     | 1,389     |
| Total deferred tax liabilities                        | 22,604    | 17,005    |
| Net deferred tax asset                                | \$176,262 | \$-       |

At December 31, 2013, we had \$72.9 million in tax effected federal net operating loss carryforwards. These operating loss carryforwards, if unused, will begin to expire in 2030. Additionally, we had \$40.2 million in tax-effected state net operating loss carryforwards and \$3.3 million of these operating loss carryforwards are at risk to expire in 2014 if they remain unused. The remaining operating loss carryforwards, if unused, will begin to expire in 2018.

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

At December 31, 2013 and 2012, our total liability for uncertain tax positions was \$0.3 million and \$0.8 million, respectively, which is included in accrued liabilities in the Homebuilding section of our consolidated balance sheets. The following table summarizes activity for the gross unrecognized tax benefit component of our total liability for uncertain tax positions for the years ended December 31, 2013, 2012 and 2011:

|                                                      | Year Ended December 31, |         |          |
|------------------------------------------------------|-------------------------|---------|----------|
|                                                      | 2013                    | 2012    | 2011     |
|                                                      | (Dollars in thousands)  |         |          |
| Gross unrecognized tax benefits at beginning of year | \$575                   | \$2,712 | \$48,963 |
| Increases related to prior year tax positions        | 124                     | 63      | -        |
| Decreases related to prior year tax positions        | (53 )                   | (84 )   | (286 )   |
| Increases related to current year tax positions      | -                       | -       | 85       |
| Decreases related to current year tax positions      | -                       | -       | -        |
| Settlements with taxing authorities                  | -                       | -       | (38,543) |
| Lapse of applicable statute of limitations           | (275)                   | (2,116) | (7,507 ) |
| Gross unrecognized tax benefits at end of year       | \$371                   | \$575   | \$2,712  |

Our liability for gross unrecognized tax benefits was \$0.3 million and \$0.6 million at December 31, 2013 and 2012, respectively, all of which, if recognized, would reduce our effective tax rate.

The net expense (benefit) for interest and penalties reflected in the consolidated statements of operations for the years ended December 31, 2013, 2012 and 2011 was \$0, (\$0.4) million and (\$4.8) million, respectively. The corresponding liabilities in the consolidated balance sheets were \$0.3 million and \$0.4 million at December 31, 2013 and 2012, respectively.

We have taken positions in certain taxing jurisdictions for which it is reasonably possible that the total amounts of unrecognized tax benefits may decrease within the next twelve months. The possible decrease could result from the expiration of various statutes of limitation and the finalization of various state income tax matters. The estimated range of the reasonably possible decrease is \$0 to \$0.3 million.

The Company and its subsidiaries file income tax returns in the U.S. federal jurisdiction and various state jurisdictions. We are subject to U.S. federal income tax examination for calendar tax years ending 2010 through 2013. Additionally, we are subject to various state income tax examinations for the 2007 through 2012 calendar tax years.

**15. Related Party Transactions**

We previously entered into a transaction (the “Transaction”) with the Villages at Castle Rock Metropolitan District No. 6 (the “District”). The District is a quasi-municipal corporation and political subdivision of the State of Colorado. The Board of Directors of the District currently is comprised of employees of the Company. The District was formed to provide funding for certain land development costs associated with the construction of homes in our Cobblestone subdivision. Pursuant to the terms of the Transaction, the District sold to the Company approximately \$22.5 million in Limited Tax General Obligation Capital Appreciation Bonds Series 2007 (the “2007 Bonds”) and a \$1.6 million Limited Tax General Obligation Subordinate Bond (the “Subordinate Bond”) in exchange for title to approximately \$28.6 million in land development improvements to the District.

We initially recorded the 2007 Bonds and Subordinate Bond at an estimated \$8.9 million and \$0 fair value, respectively, based upon discounted cash flows. During the year ended December 31, 2009, we updated our evaluation of the estimated fair value of the 2007 Bonds and through this evaluation, we determined there was a decrease in the estimated cash flows from this asset and, as a result, recorded a \$1.0 million other-than-temporary-impairment associated with the 2007 Bonds in 2009. As discussed in Note 6, in the second quarter of 2013 we determined the 2007 Bonds were no longer required to be accounted for under the cost recovery method. We adjusted the bond principal balance based on the valuation to \$12.7 million as of December 31, 2013.



**M.D.C. HOLDINGS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

During the years ended December 31, 2013, 2012 and 2011, we received payments from the District in the amount of \$0.7 million, \$0.8 million and \$0.7 million, respectively. In 2012 and 2011, these payments were recorded as a reduction to the carrying value of the 2007 Bonds and Subordinate Bond. As discussed in Note 6, the principal payments going forward are included in an interest accretion model with the appropriate interest income and increase or decrease to the carrying value being recorded.

During the years ended December 31, 2013, 2012, and 2011 we contributed \$1 million, \$1 million, and \$0 respectively, in cash to the MDC/Richmond American Homes Foundation (the "Foundation"). The Foundation is a Delaware non-profit corporation that was incorporated on September 30, 1999.

The Foundation is a non-profit organization operated exclusively for charitable, educational and other purposes beneficial to social welfare within the meaning of Section 501(c)(3) of the Internal Revenue Code. The following Directors and/or officers of the Company are the trustees of the Foundation at December 31, 2013, all of whom serve without compensation:

| Name               | MDC Title                            |
|--------------------|--------------------------------------|
| Larry A. Mizel     | Chairman and Chief Executive Officer |
| David D. Mandarich | President                            |
| Raymond T. Baker   | Director                             |

**16. Lines of Credit and Total Debt Obligations**

*Revolving Credit Facility.* On December 13, 2013, we entered into an unsecured revolving credit agreement ("Revolving Credit Facility") with a group of lenders which may be used for general corporate purposes. Our Revolving Credit Facility has an aggregate commitment amount of \$450 million (the Commitment") and a maturity date of December 13, 2018. Each lender may issue letters of credit in an amount up to 50% of its commitment. The facility permits an increase in the maximum Commitment amount to \$1.0 billion upon our request, subject to receipt of additional commitments from existing or additional lenders. Interest rates on outstanding borrowings are determined by reference to a specified London Interbank Offered Rate (LIBOR), a specified federal funds effective rate or a specified prime rate, plus a margin that is determined based on our credit ratings and leverage ratio, as defined in the facility agreement. At any time at which the Company's leverage ratio, as of the last day of the most recent calendar quarter, exceeds 55%, the aggregate principal amount of all consolidated senior debt borrowings outstanding may not exceed the borrowing base. If the Company's leverage ratio, as of the last day of the most recent calendar quarter, is

55% or less, then no borrowing base requirement will exist.

The Revolving Credit Facility is fully and unconditionally guaranteed, jointly and severally, by most of our homebuilding segment subsidiaries. The facility contains various representations, warranties and covenants that we believe are customary for agreements of this type. The financial covenants include a consolidated tangible net worth test and a leverage test, along with a consolidated tangible net worth covenant, all as defined in the facility agreement. A failure to satisfy the foregoing tests does not constitute an event of default, but can trigger a “term-out” of the facility. A breach of the consolidated tangible net worth covenant (but not the consolidated tangible net worth test) would result in an event of default.

The Revolving Credit Facility is subject to acceleration upon certain specified events of default, including breach of the consolidated tangible net worth covenant, failure to make timely payments, breaches of certain representations or covenants, failure to pay other material indebtedness, or another person becoming beneficial owner of 50% or more of the MDC's outstanding common stock. We believe we were in compliance with the representations, warranties and covenants included in the Revolving Credit Facility as of December 31, 2013.

We incur costs associated with unused commitment fees pursuant to the terms of the Revolving Credit Facility. At December 31, 2013, there were no borrowings under the Revolving Credit Facility and there were \$14.9 million in letters of credit outstanding, which reduced the amounts available to be borrowed under the Revolving Credit Facility.

Upon entering into the Revolving Credit Facility on December 13, 2013, our separate letter of credit facilities terminated and our existing letters of credit were included in the Revolving Credit Facility.

**M.D.C. HOLDINGS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

*Mortgage Repurchase Facility.* HomeAmerican has a Master Repurchase Agreement, (the “Mortgage Repurchase Facility”), with U.S. Bank National Association (“USBNA”). This agreement was amended on September 20, 2013 and extended until September 19, 2014. The Mortgage Repurchase Facility provides liquidity to HomeAmerican by providing for the sale of eligible mortgage loans to USBNA with an agreement by HomeAmerican to repurchase the mortgage loans at a future date. Until such mortgage loans are transferred back to HomeAmerican, the documents relating to such loans are held by USBNA, as custodian, pursuant to the Custody Agreement (“Custody Agreement”), dated as of November 12, 2008, by and between HomeAmerican and USBNA. The Mortgage Repurchase Facility had a temporary increase in the maximum aggregate commitment from \$50 million to \$80 million from December 31, 2013 through January 30, 2014 and from December 21, 2012 through January 30, 2013. At December 31, 2013 and December 31, 2012, we had \$63.1 million and \$76.3 million, respectively, of mortgage loans that we were obligated to repurchase under our Mortgage Repurchase Facility. Mortgage loans that we are obligated to repurchase under the Mortgage Repurchase Facility are accounted for as a debt financing arrangement and are reported as mortgage repurchase facility in the consolidated balance sheets. Advances under the Mortgage Repurchase Facility carry a Pricing Rate equal to the greater of (i) the LIBOR Rate (as defined in the Mortgage Repurchase Facility) plus 2.75%, or (ii) 3.00%. The Mortgage Repurchase Facility contains various representations, warranties and affirmative and negative covenants that we believe are customary for agreements of this type. The negative covenants include, among others, (i) a minimum Adjusted Tangible Net Worth requirement, (ii) a maximum Adjusted Tangible Net Worth Ratio, (iii) a minimum Adjusted Net Income requirement, and (iv) a minimum Liquidity requirement. The foregoing terms are defined in the Mortgage Repurchase Facility. We believe we were in compliance with the representations, warranties and covenants included in the Mortgage Repurchase Facility as of December 31, 2013.

*Senior Notes.* Our senior notes are not secured and, while the senior note indentures contain some restrictions on secured debt and other transactions, they do not contain financial covenants. Our senior notes are fully and unconditionally guaranteed on an unsecured basis, jointly and severally, by most of our homebuilding segment subsidiaries.

During 2011, we completed a debt tender offer and redemptions of our 7% Senior Notes due 2012 and 5½% Senior Notes due 2013. As a result of these transactions, we paid \$537.7 million to extinguish \$500 million in debt principal with a carrying amount of \$498.9 million and recorded a \$38.8 million expense for loss on extinguishment of debt.

On January 10, 2013, we issued \$250 million of 6% Senior Notes due 2043. On May 8, 2013, we issued an additional \$100 million of 6% Senior Notes due 2043, which are of the same series and have the same terms as the notes issued on January 10, 2013 (collectively the “6% Notes”). The 6% Notes, which pay interest semi-annually in arrears on January 15 and July 15 of each year, commencing July 15, 2013, are general unsecured obligations of MDC and rank equally and ratably with our other general unsecured and unsubordinated indebtedness. We received total proceeds of \$346.9 million, net of underwriting fees of \$3.1 million.

Our debt obligations at December 31, 2013 and December 31, 2012 were as follows:

|                                         | December 31,           |            |
|-----------------------------------------|------------------------|------------|
|                                         | 2013                   | 2012       |
|                                         | (Dollars in thousands) |            |
| 5 % Senior Notes due December 2014, net | \$ 249,814             | \$ 249,621 |
| 5 % Senior Notes due July 2015, net     | 249,935                | 249,895    |
| 5 % Senior Notes due February 2020, net | 245,871                | 245,326    |
| 6% Senior Notes due January 2043        | 350,000                | -          |
| Total                                   | \$ 1,095,620           | \$ 744,842 |

F-30

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**M.D.C. HOLDINGS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**17. Commitments and Contingencies**

*Surety Bonds and Letter of Credit Facilities.* At December 31, 2013, we had issued and outstanding surety bonds and letters of credit totaling \$97.9 million and \$30.2 million, respectively, including \$15.3 in letters of credit issued by HomeAmerican. The estimated cost to complete obligations related to these bonds and letters of credit was approximately \$45.5 million and \$8.1 million, respectively. The letters of credit as of December 31, 2013, excluding those issued by HomeAmerican, were included under the Revolving Credit Facility while the letters of credit as of December 31, 2012 were outstanding under our previous letter of credit facilities. We expect that the obligations secured by these performance bonds and letters of credit generally will be performed in the ordinary course of business and in accordance with the applicable contractual terms. To the extent that the obligations are performed, the related performance bonds and letters of credit should be released and we should not have any continuing obligations. However, in the event any such performance bonds or letters of credit are called, our indemnity obligations could require us to reimburse the issuer of the performance bond or letter of credit.

We have made no material guarantees with respect to third-party obligations.

*Mortgage Loan Loss Reserves.* In the normal course of business, we establish reserves for potential losses associated with HomeAmerican's sale of mortgage loans to third-parties. These reserves are created to address repurchase and indemnity claims by third-party purchasers of the mortgage loans, which claims arise primarily out of allegations of homebuyer fraud at the time of origination of the loan. These reserves are based upon, among other things: (1) pending claims received from third-party purchasers associated with previously sold mortgage loans; and (2) a current assessment of the potential exposure associated with future claims of fraud in mortgage loans originated in prior periods. In addition to reserves established for mortgage loans previously sold to third-parties, we establish reserves for loans that we have repurchased if we believe the loss is likely and estimable. Our mortgage loan reserves are reflected as a component of accrued liabilities in the Financial Services section of the accompanying consolidated balance sheets, and the associated expenses are included in expenses in the Financial Services section of the accompanying consolidated statements of operations.

The following table sets forth, by reportable segment, information relating to our homebuilding inventories:

| Year Ended December 31, |      |      |  |
|-------------------------|------|------|--|
| 2013                    | 2012 | 2011 |  |

|                              | (Dollars in thousands) |        |          |
|------------------------------|------------------------|--------|----------|
| Balance at beginning of year | \$976                  | \$830  | \$7,120  |
| Expense provisions           | 1,172                  | 437    | 149      |
| Cash payments                | (734 )                 | (226 ) | (14,450) |
| Adjustments                  | (44 )                  | (65 )  | 8,011    |
| Balance at end of year       | \$1,370                | \$976  | \$830    |

During 2011, HomeAmerican reached settlements with third parties concerning claims and potential claims to repurchase certain previously sold mortgage loans, including a comprehensive settlement with Bank of America. As a result of these settlements, we increased our loan loss reserve \$8.0 million during the year ended December 31, 2011. We made payments of \$14.5 million during the year ended December 31, 2011 primarily associated with the foregoing settlements. We believe that those settlements substantially reduced our future exposure to liabilities associated with previously sold mortgage loans.

*Legal Reserves.* Because of the nature of the homebuilding business, we have been named as defendants in various claims, complaints and other legal actions arising in the ordinary course of business, including product liability claims and claims associated with the sale and financing of homes. In the opinion of management, the outcome of these ordinary course matters will not have a material adverse effect upon our financial condition, results of operations or cash flows. At December 31, 2013 and 2012, respectively, we had \$5.9 million and \$2.3 million of legal accruals.

For the year ended December 31, 2012, we had various significant legal recoveries totaling \$9.8 million, respectively, which were included in selling, general and administrative expenses in the Homebuilding section of our consolidated statements of operations. These recoveries were realized primarily from prior claims we had made in connection with various construction defect cases.

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

*Operating Leases.* We have non-cancelable operating leases primarily associated with our office facilities. Rent expense under cancelable and non-cancelable operating leases totaled \$5.2 million, \$6.6 million and \$7.7 million in 2013, 2012 and 2011, respectively, and is included in either selling, general and administrative expenses in the Homebuilding section or expenses in the Financial Services section of our consolidated statements of operations. The table below shows the future minimum payments under non-cancelable operating leases at December 31, 2013.

|            | Year<br>Ended                                |
|------------|----------------------------------------------|
|            | December<br>31,<br>(Dollars in<br>thousands) |
| 2014       | \$ 4,462                                     |
| 2015       | 4,435                                        |
| 2016       | 3,748                                        |
| 2017       | 1,161                                        |
| 2018       | 638                                          |
| Thereafter | 421                                          |
| Total      | \$ 14,865                                    |

**18. Concentration of Third-Party Mortgage Purchasers**

The following table sets forth the percent of mortgage loans sold by HomeAmerican to its primary third party purchasers during 2013, 2012 and 2011.

|                            | Year Ended<br>December 31, |      |      |
|----------------------------|----------------------------|------|------|
|                            | 2013                       | 2012 | 2011 |
| Wells Fargo Funding, Inc.  | 40%                        | 58%  | 52%  |
| JP Morgan Chase Bank, N.A. | 46%                        | 36%  | 29%  |
| Bank of America, N.A.      | 0%                         | 0%   | 17%  |

On August 31, 2011, Bank of America, one of our former primary third-party purchasers, announced its intention to sell its third-party mortgage operation and exit its correspondent mortgage lending business. Subsequently, Bank of America amended its prior announcement and indicated that no sale of the third-party mortgage operation was forthcoming, but that it would proceed with its original plan to exit its correspondent mortgage lending business, with the last date that they would purchase a mortgage being December 15, 2011.

**19. Stockholders' Equity**

*Common Stock Repurchase Program.* At December 31, 2013, we were authorized to repurchase up to 4,000,000 shares of our common stock. We did not repurchase any shares of our common stock during the years ended December 31, 2013, 2012 or 2011. We did not hold any treasury stock at December 31, 2013. At December 31, 2011, we held 59,912 shares of treasury stock with an average cost of \$11.00.



**M.D.C. HOLDINGS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**20. Equity Incentive and Employee Benefit Plans**

A summary of our equity incentive plans follows.

*Employee Equity Incentive Plans.* Effective March 2001, we adopted the M.D.C. Holdings, Inc. 2001 Equity Incentive Plan (the “2001 Equity Incentive Plan”). On March 26, 2011, the 2001 Equity Incentive Plan terminated and all stock option grants and restricted stock awards outstanding at the time of the plan termination may continue to be exercised, or become free of restrictions, in accordance with their terms. Non-qualified option awards previously granted generally vest over periods of up to seven years and expire ten years after the date of grant. Restricted stock awards generally were granted with vesting terms of up to five years. A total of 3.0 million shares of MDC common stock were reserved for issuance under the 2001 Equity Incentive Plan as of December 31, 2013.

On April 27, 2011, our shareholders approved the M.D.C Holdings, Inc. 2011 Equity Incentive Plan (the “2011 Equity Incentive Plan”), which provides for the grant of non-qualified stock options, incentive stock options, stock appreciation rights, restricted stock, restricted stock units and other equity awards to employees of the Company. Stock options granted under the 2011 Equity Incentive Plan have an exercise price that is at least equal to the fair market value of our common stock on the date the stock option is granted, generally vest in periods up to five years and expire ten years after the date of grant. At December 31, 2013, a total of 2.5 million shares of MDC common stock were reserved for issuance under the 2011 Equity Incentive Plan, of which 1.2 million shares remained available for grant under this plan as of December 31, 2013.

*Director Equity Incentive Plans.* Effective March 2001, we adopted the M.D.C. Holdings, Inc. Stock Option Plan for Non-Employee Directors (the “2001 Director Stock Option Plan”). The 2001 Director Stock Option Plan terminated on May 21, 2012 and stock options outstanding at the time of plan termination may continue to be exercised in accordance with their terms. Each option granted under the Director Stock Option Plan vested immediately and expires ten years from the date of grant. A total of 0.8 million shares of MDC common stock were reserved for issuance under this plan as of December 31, 2013.

Effective April 27, 2011, our shareholders approved the M.D.C. Holdings, Inc. 2011 Stock Option Plan for Non-Employee Directors (the “2011 Director Stock Option Plan”). Under the 2011 Director Stock Option Plan, non-employee directors of the Company are granted non-qualified stock options. Pursuant to the 2011 Director Stock Option Plan, on August 1 of each year, each non-employee director is granted options to purchase 25,000 shares of

MDC common stock. Each option granted under the 2011 Director Stock Option Plan vests immediately, becomes exercisable six months after grant, and expires ten years from the date of grant. The option exercise price must be equal to the fair market value (as defined in the plan) of our common stock on the date of grant of the option. At December 31, 2013, a total of 0.8 million shares of MDC common stock were reserved for issuance under the 2011 Director Stock Option Plan and 0.6 million shares remained available for grant under this plan as of December 31, 2013.

*Employee Benefit Plan.* We have a defined contribution plan pursuant to Section 401(k) of the Internal Revenue Code where each employee may elect to make before-tax contributions up to the current tax limits. We match employee contributions on a discretionary basis and, as of December 31, 2013 we had accrued \$0.9 million related to the match that is to be contributed in the first quarter of 2014 for 2013 activity. For the year ended December 31, 2012 we contributed \$0.2 million. We did not make any matching contributions during the year ended December 31, 2011.

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****21. Stock Based Compensation**

*Determining Fair Value of Share-Based Payment Awards.* We examine our historical pattern of option exercises in an effort to determine if there are any discernable activity patterns based on certain employee and non-employee populations. Based upon this evaluation, we have identified three distinct populations: (1) executives currently consisting of our Chief Executive Officer, Chief Operating Officer, Chief Financial Officer, and General Counsel (collectively, the “Executives”); (2) Non-Executive employees (“Non-Executives”); and (3) non-employee members of our board of directors (“Directors”). Accordingly, during 2013, 2012 and 2011 the Company used separate Black-Scholes option pricing model assumptions for each of the aforementioned employee and non-employee populations. The fair values for stock options granted for the years ended December 31, 2013, 2012 and 2011 were estimated using the Black-Scholes option pricing model with the following weighted-average assumptions.

|                                   | Year Ended December<br>31, |       |       |
|-----------------------------------|----------------------------|-------|-------|
|                                   | 2013                       | 2012  | 2011  |
| Expected lives of options (years) | 4.0                        | 7.8   | 4.6   |
| Expected volatility               | 45.3%                      | 44.6% | 47.8% |
| Risk free interest rate           | 0.8%                       | 1.7%  | 1.3%  |
| Dividend yield rate               | 3.0%                       | 4.0%  | 4.1%  |

Based on calculations using the Black-Scholes option pricing model, the weighted-average grant date fair values of stock options granted during 2013, 2012 and 2011 were \$9.75, \$7.54 and \$7.42, respectively. No stock options were granted to our CEO and COO during the years ended December 31, 2013 and 2011. As a result, the weighted average expected life of our options are higher in 2012 when compared to 2013 and 2011 as options were granted to our CEO and COO in 2012.

The expected life of employee stock options represents the weighted-average period for which the stock options are expected to remain outstanding and are derived primarily from historical exercise patterns. The expected volatility is based on the historical volatility in the price of our common stock over the most recent period commensurate with the estimated expected life of our stock options. The risk-free interest rate assumption is determined based upon observed interest rates appropriate for the expected term of our employee stock options. The dividend yield assumption is based on our history of dividend payouts.

An annual forfeiture rate is estimated at the time of grant for all share-based payment awards with service conditions only. That rate is revised, if necessary, in subsequent periods if the actual forfeiture rate differs from our estimate. For grants made in the year ended December 31, 2013, we estimated a forfeiture rate between 20% and 45% for those share-based payment awards granted to Non-Executives. We estimate the annual forfeiture rate to be 0% for share-based payment awards with service conditions only granted to our Executives.

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

*Stock Option Award Activity.* Stock option activity under our option plans for the years ended December 31, 2013, 2012 and 2011 were as follows.

|                                          | Year Ended December 31,<br>2013 |          | 2012       |          | 2011       |          |
|------------------------------------------|---------------------------------|----------|------------|----------|------------|----------|
|                                          | Weighted-                       |          | Weighted-  |          | Weighted-  |          |
|                                          | Number of                       | Average  | Number of  | Average  | Shares     | Average  |
|                                          | Shares                          | Exercise | Shares     | Exercise |            | Exercise |
|                                          |                                 | Price    |            | Price    |            | Price    |
| <b>Outstanding Stock Option Activity</b> |                                 |          |            |          |            |          |
| Outstanding, beginning of year           | 5,879,573                       | \$ 41.29 | 5,306,506  | \$ 42.69 | 6,002,174  | \$ 40.72 |
| Granted <sup>(1)</sup>                   | 237,500                         | 33.82    | 1,382,500  | 25.33    | 265,000    | 25.07    |
| Exercised                                | (153,665 )                      | 32.94    | (704,242 ) | 23.69    | (489,324 ) | 18.47    |
| Forfeited                                | (10,000 )                       | 37.25    | (55,710 )  | 27.46    | (124,710 ) | 32.20    |
| Cancelled                                | (671,042 )                      | 44.25    | (49,481 )  | 44.75    | (346,634 ) | 33.87    |
| Outstanding, end of year                 | 5,282,366                       | \$ 40.83 | 5,879,573  | \$ 41.29 | 5,306,506  | \$ 42.69 |

|                                       | Year Ended December 31,<br>2013 |            | 2012       |            | 2011       |            |
|---------------------------------------|---------------------------------|------------|------------|------------|------------|------------|
|                                       | Weighted-                       |            | Weighted-  |            | Weighted-  |            |
|                                       | Number of                       | Average    | Number of  | Average    | Number of  | Average    |
|                                       | Shares                          | Fair Value | Shares     | Fair Value | Shares     | Fair Value |
| <b>Unvested Stock Option Activity</b> |                                 |            |            |            |            |            |
| Outstanding, beginning of year        | 2,045,000                       | \$ 8.63    | 1,251,328  | \$ 10.74   | 1,790,425  | \$ 12.65   |
| Granted <sup>(1)</sup>                | 237,500                         | 9.75       | 1,382,500  | 7.54       | 265,000    | 7.42       |
| Vested                                | (1,433,959)                     | 8.28       | (533,118 ) | 8.61       | (679,387 ) | 13.31      |
| Forfeited                             | (10,000 )                       | 12.72      | (55,710 )  | 8.45       | (124,710 ) | 10.13      |
| Unvested, end of year                 | 838,541                         | \$ 9.50    | 2,045,000  | \$ 8.63    | 1,251,328  | \$ 10.74   |

(1) Total shares granted in 2012 include 1,000,000 performance

based  
options  
granted to  
our CEO and  
COO. See  
further  
discussion  
regarding  
these grants  
in the  
“Performance  
Based Stock  
Award  
Activity”  
section  
below.

The total intrinsic value of options (difference between price per share as of the exercise date and the strike price, times the number of options outstanding) exercised during the years ended December 31, 2013, 2012 and 2011 was \$1.1 million, \$7.0 million and \$0.2 million, respectively.

The following table provides data for our stock options that are vested or expected to vest as of December 31, 2013.

**Exercisable or expected to vest**

|                                                     |           |
|-----------------------------------------------------|-----------|
| Number outstanding                                  | 5,238,762 |
| Weighted-average exercise price                     | \$40.92   |
| Aggregate intrinsic value (in thousands)            | \$11,798  |
| Weighted-average remaining contractual term (years) | 5.07      |

**Exercisable**

|                                                     |           |
|-----------------------------------------------------|-----------|
| Number outstanding                                  | 4,443,825 |
| Weighted-average exercise price                     | \$42.84   |
| Aggregate intrinsic value (in thousands)            | \$8,786   |
| Weighted-average remaining contractual term (years) | 4.59      |

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The aggregate intrinsic values in the tables above represent the total pre-tax intrinsic values (the difference between the closing price of MDC's common stock on the last trading day of fiscal 2013 and the exercise price, multiplied by the number of in-the-money stock option shares) that would have been received by the option holders had all in-the-money outstanding stock options been exercised on December 31, 2013.

The following table summarizes information associated with outstanding and exercisable stock options at December 31, 2013.

| Range of Exercise Price | Options Outstanding |             |           | Options Exercisable |             |           |
|-------------------------|---------------------|-------------|-----------|---------------------|-------------|-----------|
|                         | Weighted-           |             | Weighted- | Weighted-           |             | Weighted- |
|                         | Average             |             |           | Average             |             |           |
|                         | Number              | Remaining   | Average   | Number              | Remaining   | Average   |
|                         | Outstanding         | Contractual | Exercise  | Outstanding         | Contractual | Exercise  |
|                         |                     | Life (in    | Price     |                     | Life (in    | Price     |
|                         |                     | years)      |           |                     | years)      |           |
| \$ 15.84 - \$ 23.77     | 175,500             | 7.98        | \$ 20.91  | 45,500              | 7.75        | \$ 21.70  |
| \$ 23.78 - \$ 39.61     | 2,981,666           | 6.90        | 29.74     | 2,323,125           | 6.68        | 29.30     |
| \$ 39.62 - \$ 47.53     | 615,700             | 3.70        | 43.01     | 565,700             | 3.22        | 43.30     |
| \$ 47.54 - \$ 63.38     | 892,500             | 2.06        | 60.41     | 892,500             | 2.06        | 60.41     |
| \$ 63.39 - \$ 71.30     | 492,000             | 1.30        | 67.17     | 492,000             | 1.30        | 67.17     |
| \$ 71.31 - \$ 78.89     | 125,000             | 1.75        | 79.89     | 125,000             | 1.75        | 78.89     |
| Total                   | 5,282,366           | 5.10        | \$ 40.83  | 4,443,825           | 4.59        | \$ 42.84  |

Total compensation expense relating to stock options granted by the Company was \$5.6 million, \$10.6 million and \$9.0 million for the years ended December 31, 2013, 2012 and 2011, respectively. Our recognized tax benefit from this expense for the year ended December 31, 2013 was \$2.2 million. We did not have any recognized tax benefits from compensation expense for stock options for the years ended December 31, 2012 or 2011 as we were in a full valuation allowance position.

As of December 31, 2013, \$4.2 million of total unrecognized compensation cost related to stock options expected to be recognized as an expense by the Company in the future over a weighted-average period of approximately 1.9 years.

We did not have any net tax benefit realized for stock options exercised during the years ended December 31, 2012 or 2011 as we were in a full valuation allowance position.

*Performance Based Stock Award Activity.* On March 8, 2012, we granted a long term performance-based non-qualified stock option to each of our Chief Executive Officer and our Chief Operating Officer for 500,000 shares of common stock under our 2011 Equity Incentive Plan. The terms of the performance-based options provide that, over a three year period, one third of the option shares would vest as of March 1 following any fiscal year in which, in addition to the Company achieving a gross margin from home sales of at least 16.7% (as calculated in our 2011 Form 10-K, excluding warranty adjustments and interest), the Company achieved: (1) at least a 10% increase in total revenue over 2011 (166,667 option shares vest); (2) at least a 15% increase in total revenue over 2011 (166,667 option shares vest); or (3) at least a 20% increase in total revenue over 2011 (166,666 option shares vest). Any of the three tranches of option shares that are not performance vested by March 1, 2015 would be forfeited. ASC Topic 718, *Compensation – Stock Compensation* (“ASC 718”) prohibits recognition of expense associated with performance based stock awards until achievement of the performance targets are probable of occurring.

In accordance with ASC 718, the performance-based awards were assigned a fair value of \$7.42 per share on the date of grant. The maximum potential expense that would be recognized by the Company if all of the performance targets were met was approximately \$7.4 million. At December 31, 2012 all performance targets had been achieved. Therefore, \$6.2 million of compensation expense was recognized related to the grant of these awards during the year ended December 31, 2012. The balance of the unamortized stock-based compensation expense was amortized during the first two months of 2013, based on the vesting date of March 1, 2013.



**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

*Restricted and Unrestricted Stock Award Activity.* Non-vested restricted stock awards at December 31, 2013, 2012 and 2011 and changes during those years were as follows:

|                             | Year Ended December 31,<br>2013 |                          | 2012                   |                          | 2011                   |                          |
|-----------------------------|---------------------------------|--------------------------|------------------------|--------------------------|------------------------|--------------------------|
|                             | Weighted-                       |                          | Weighted-              |                          | Weighted-              |                          |
|                             | Number<br>of<br>Shares          | Average<br>Grant<br>Date | Number<br>of<br>Shares | Average<br>Grant<br>Date | Number<br>of<br>Shares | Average<br>Grant<br>Date |
|                             |                                 | Fair Value               |                        | Fair Value               |                        | Fair Value               |
| Unvested, beginning of year | 507,367                         | \$ 31.69                 | 667,849                | \$ 33.19                 | 443,112                | \$ 36.15                 |
| Granted                     | 25,072                          | 37.52                    | 48,613                 | 27.85                    | 329,703                | 30.24                    |
| Vested                      | (144,841)                       | 31.88                    | (197,801)              | 35.88                    | (100,677)              | 36.34                    |
| Forfeited                   | (88,607 )                       | 29.02                    | (11,294 )              | 30.62                    | (4,289 )               | 38.88                    |
| Unvested, end of year       | 298,991                         | \$ 32.87                 | 507,367                | \$ 31.69                 | 667,849                | \$ 33.19                 |

Total compensation expense relating to restricted stock awards was \$4.0 million, \$5.6 million and \$6.4 million for the years ended December 31, 2013, 2012 and 2011, respectively. Our recognized tax benefit from this expense for the year ended December 31, 2013 was \$1.6 million. We did not have any recognized tax benefits from compensation expense for restricted stock awards for the years ended December 31, 2012 or 2011 as we were in a full valuation allowance position.

At December 31, 2013, there was \$3.9 million of unrecognized compensation expense related to non-vested restricted stock awards that is expected to be recognized as an expense by us in the future over a weighted-average period of approximately 1.3 years. The total intrinsic value of unvested restricted stock awards (the difference between the closing price of MDC's common stock on the last trading day of fiscal 2013 and the grant date award price, multiplied by the number of shares) at December 31, 2013 was \$9.6 million. The total intrinsic value of restricted stock which vested during each of the years ended December 31, 2013, 2012 and 2011 was \$5.5 million, \$5.9 million and \$1.9 million, respectively.

**22. Subsequent Events**

On January 15, 2014, we completed a public offering of \$250 million principal amount of 5½% senior notes due 2024 (the “5½% Notes”). The 5½% Notes, which pay interest semi-annually in arrears on January 15 and July 15 of each year, commencing July 15, 2014, are general unsecured obligations of MDC and rank equally and ratably with our other general unsecured and unsubordinated indebtedness. In addition, the 5½% Notes are fully guaranteed on an unsecured basis, jointly and severally, by most of our homebuilding subsidiaries. We received proceeds of \$248.4 million, net of underwriting fees of \$1.6 million. We intend to use the net proceeds from this offering for general corporate purposes, which may include repayment of our 5 % Senior Notes due 2014 and 5 % Senior Notes due 2015 in whole or in part.

F-37

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**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****23. Results of Quarterly Operations (Unaudited)**

|                                                      | Quarter                                          |   |           |   |           |   |           |   |
|------------------------------------------------------|--------------------------------------------------|---|-----------|---|-----------|---|-----------|---|
|                                                      | First                                            |   | Second    |   | Third     |   | Fourth    |   |
|                                                      | (Dollars in thousands, except per share amounts) |   |           |   |           |   |           |   |
| <b>2013</b>                                          |                                                  |   |           |   |           |   |           |   |
| Home sales revenue                                   | \$331,748                                        |   | \$400,327 |   | \$433,693 |   | \$460,939 |   |
| Total revenue                                        | \$344,254                                        |   | \$416,018 |   | \$448,000 |   | \$472,162 |   |
| Asset impairments                                    | \$-                                              |   | \$-       |   | \$(350 )  |   | \$(569 )  |   |
| Gross margin from home sales (including impairments) | 17.4                                             | % | 18.1      | % | 18.1      | % | 17.4      | % |
| Selling, general and administrative expenses         | \$48,201                                         |   | \$51,908  |   | \$57,753  |   | \$55,421  |   |
| Income before income taxes                           | \$22,586                                         |   | \$38,012  |   | \$34,909  |   | \$34,318  |   |
| Net income                                           | \$22,516                                         |   | \$224,909 |   | \$36,251  |   | \$30,709  |   |
| Earnings per share:                                  |                                                  |   |           |   |           |   |           |   |
| Basic                                                | \$0.46                                           |   | \$4.60    |   | \$0.73    |   | \$0.62    |   |
| Diluted                                              | \$0.45                                           |   | \$4.56    |   | \$0.73    |   | \$0.62    |   |
| <b>2012</b>                                          |                                                  |   |           |   |           |   |           |   |
| Home sales revenue                                   | \$184,678                                        |   | \$256,532 |   | \$320,647 |   | \$389,141 |   |
| Total revenue                                        | \$193,988                                        |   | \$268,934 |   | \$334,330 |   | \$405,773 |   |
| Asset impairments                                    | \$-                                              |   | \$-       |   | \$-       |   | \$1,105   |   |
| Gross margin from home sales (including impairments) | 14.1                                             | % | 14.2      | % | 15.5      | % | 16.7      | % |
| Selling, general and administrative expenses         | \$34,124                                         |   | \$39,223  |   | \$44,788  |   | \$49,160  |   |
| Income before income taxes                           | \$2,125                                          |   | \$9,655   |   | \$19,484  |   | \$29,851  |   |
| Net income                                           | \$2,265                                          |   | \$10,638  |   | \$20,126  |   | \$29,670  |   |
| Earnings per share:                                  |                                                  |   |           |   |           |   |           |   |
| Basic                                                | \$0.04                                           |   | \$0.22    |   | \$0.41    |   | \$0.60    |   |
| Diluted                                              | \$0.04                                           |   | \$0.22    |   | \$0.41    |   | \$0.59    |   |

**24. Supplemental Guarantor Information**

Our senior notes are fully and unconditionally guaranteed on an unsecured basis, jointly and severally, by the following subsidiaries (collectively, the "Guarantor Subsidiaries"), which are 100%-owned subsidiaries of the Company.

M.D.C. Land Corporation

RAH of Florida, Inc.

Richmond American Construction, Inc.

Richmond American Homes of Arizona, Inc.

Richmond American Homes of Colorado, Inc.

Richmond American Homes of Delaware, Inc.

Richmond American Homes of Florida, LP

Richmond American Homes of Illinois, Inc.

Richmond American Homes of Maryland, Inc.

Richmond American Homes of Nevada, Inc.

Richmond American Homes of New Jersey, Inc.

Richmond American Homes of Pennsylvania, Inc.

Richmond American Homes of Utah, Inc.

Richmond American Homes of Virginia, Inc.

Richmond American Homes of Washington, Inc.

**M.D.C. HOLDINGS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The senior note indentures do not provide for a suspension of the guarantees, but do provide that any Guarantor may be released from its guarantee so long as (1) no default or event of default exists or would result from release of such guarantee, (2) the Guarantor being released has consolidated net worth of less than 5% of the Company's consolidated net worth as of the end of the most recent fiscal quarter, (3) the Guarantors released from their guarantees in any year-end period comprise in the aggregate less than 10% (or 15% if and to the extent necessary to permit the cure of a default) of the Company's consolidated net worth as of the end of the most recent fiscal quarter, (4) such release would not have a material adverse effect on the homebuilding business of the Company and its subsidiaries and (5) the Guarantor is released from its guarantee(s) under all Specified Indebtedness (other than by reason of payment under its guarantee of Specified Indebtedness). Upon delivery of an officers' certificate and an opinion of counsel stating that all conditions precedent provided for in the indenture relating to such transactions have been complied with and the release is authorized, the guarantee will be automatically and unconditionally released. "Specified Indebtedness" means indebtedness under the senior notes, the Company's Indenture dated as of December 3, 2002, the Revolving Credit Facility, and any refinancing, extension, renewal or replacement of any of the foregoing.

We have determined that separate, full financial statements of the Guarantor Subsidiaries would not be material to investors and, accordingly, supplemental financial information for the Guarantor and Non-Guarantor Subsidiaries is presented below. As a result of our Richmond American Homes of Washington, Inc. subsidiary becoming a guarantor subsidiary in 2013, we have revised the 2011 and 2012 Supplemental Condensed Combining Statements of Operations and Cash Flows and the 2012 Supplemental Condensed Combining Balance Sheet to reflect this subsidiary's results in the guarantor column.

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****M.D.C. Holdings, Inc.****Supplemental Condensed Combining Balance Sheet**

|                                         | December 31, 2013    |                           |                                   |                        |                     |
|-----------------------------------------|----------------------|---------------------------|-----------------------------------|------------------------|---------------------|
|                                         | MDC                  | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminating<br>Entries | Consolidated<br>MDC |
|                                         | Dollars in thousands |                           |                                   |                        |                     |
| <b>ASSETS</b>                           |                      |                           |                                   |                        |                     |
| <b>Homebuilding:</b>                    |                      |                           |                                   |                        |                     |
| Cash and cash equivalents               | \$ 145,180           | \$ 3,454                  | \$ -                              | \$-                    | \$ 148,634          |
| Marketable securities                   | 569,021              | -                         | -                                 | -                      | 569,021             |
| Restricted cash                         | -                    | 2,195                     | -                                 | -                      | 2,195               |
| Trade Receivables                       | 915                  | 27,951                    | -                                 | (5,459 )               | 23,407              |
| Inventories:                            |                      |                           |                                   |                        |                     |
| Housing completed or under construction | -                    | 636,700                   | -                                 | -                      | 636,700             |
| Land and land under development         | -                    | 774,961                   | -                                 | -                      | 774,961             |
| Total inventories                       | -                    | 1,411,661                 | -                                 | -                      | 1,411,661           |
| Intercompany receivables                | 1,144,292            | 2,576                     | 1,899                             | (1,148,767)            | -                   |
| Investment in subsidiaries              | 335,870              | -                         | -                                 | (335,870 )             | -                   |
| Deferred tax asset                      | 172,975              | -                         | -                                 | 3,287                  | 176,262             |
| Other assets, net                       | 53,933               | 43,569                    | -                                 | -                      | 97,502              |
| Total Homebuilding Assets               | 2,422,186            | 1,491,406                 | 1,899                             | (1,486,809)            | 2,428,682           |
| <b>Financial Services:</b>              |                      |                           |                                   |                        |                     |
| Cash and cash equivalents               | -                    | -                         | 50,704                            | -                      | 50,704              |
| Marketable securities                   | -                    | -                         | 19,046                            | -                      | 19,046              |
| Intercompany receivables                | -                    | -                         | 11,216                            | (11,216 )              | -                   |
| Mortgage loans held-for-sale, net       | -                    | -                         | 92,578                            | -                      | 92,578              |
| Other assets, net                       | -                    | -                         | 7,726                             | (3,287 )               | 4,439               |
| Total Financial Services Assets         | -                    | -                         | 181,270                           | (14,503 )              | 166,767             |
| Total Assets                            | \$ 2,422,186         | \$ 1,491,406              | \$ 183,169                        | \$ (1,501,312)         | \$ 2,595,449        |

**LIABILITIES AND EQUITY****Homebuilding:**

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|                                |           |           |        |              |           |
|--------------------------------|-----------|-----------|--------|--------------|-----------|
| Accounts payable               | \$13      | \$15,033  | \$ -   | \$-          | \$ 15,046 |
| Accrued liabilities            | 97,612    | 56,334    | 82     | (1,207 )     | 152,821   |
| Intercompany payables          | 15,692    | 1,121,581 | 19,668 | (1,156,941 ) | -         |
| Senior notes, net              | 1,095,620 | -         | -      | -            | 1,095,620 |
| Total Homebuilding Liabilities | 1,208,937 | 1,192,948 | 19,750 | (1,158,148)  | 1,263,487 |

**Financial Services:**

|                                        |           |           |         |             |           |
|----------------------------------------|-----------|-----------|---------|-------------|-----------|
| Accounts payable and other liabilities | -         | -         | 59,891  | (4,252 )    | 55,639    |
| Intercompany payables                  | -         | -         | 3,042   | (3,042 )    | -         |
| Mortgage repurchase facility           | -         | -         | 63,074  | -           | 63,074    |
| Total Financial Services Liabilities   | -         | -         | 126,007 | (7,294 )    | 118,713   |
| Total Liabilities                      | 1,208,937 | 1,192,948 | 145,757 | (1,165,442) | 1,382,200 |

**Equity:**

|                                            |             |             |            |               |             |
|--------------------------------------------|-------------|-------------|------------|---------------|-------------|
| Total Stockholders' Equity                 | 1,213,249   | 298,458     | 37,412     | (335,870 )    | 1,213,249   |
| Total Liabilities and Stockholders' Equity | \$2,422,186 | \$1,491,406 | \$ 183,169 | \$(1,501,312) | \$2,595,449 |

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****M.D.C. Holdings, Inc.****Supplemental Condensed Combining Balance Sheet**

|                                         | December 31, 2012      |                           |                                   |                        |                     |
|-----------------------------------------|------------------------|---------------------------|-----------------------------------|------------------------|---------------------|
|                                         | MDC                    | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminating<br>Entries | Consolidated<br>MDC |
|                                         | (Dollars in thousands) |                           |                                   |                        |                     |
| <b>ASSETS</b>                           |                        |                           |                                   |                        |                     |
| <b>Homebuilding:</b>                    |                        |                           |                                   |                        |                     |
| Cash and cash equivalents               | \$ 125,904             | \$ 3,631                  | \$ -                              | \$-                    | \$ 129,535          |
| Marketable securities                   | 519,465                | -                         | -                                 | -                      | 519,465             |
| Restricted cash                         | -                      | 1,859                     | -                                 | -                      | 1,859               |
| Trade Receivables                       | 6,563                  | 21,600                    | -                                 | -                      | 28,163              |
| Inventories:                            |                        |                           |                                   |                        |                     |
| Housing completed or under construction | -                      | 512,949                   | -                                 | -                      | 512,949             |
| Land and land under development         | -                      | 489,572                   | -                                 | -                      | 489,572             |
| Total inventories                       | -                      | 1,002,521                 | -                                 | -                      | 1,002,521           |
| Intercompany receivables                | 812,731                | 2,589                     | -                                 | (815,320 )             | -                   |
| Investment in subsidiaries              | 198,465                | -                         | -                                 | (198,465 )             | -                   |
| Other assets, net                       | 40,565                 | 37,337                    | -                                 | -                      | 77,902              |
| Total Homebuilding Assets               | 1,703,693              | 1,069,537                 | -                                 | (1,013,785)            | 1,759,445           |
| <b>Financial Services:</b>              |                        |                           |                                   |                        |                     |
| Cash and cash equivalents               | -                      | -                         | 30,560                            | -                      | 30,560              |
| Marketable securities                   | -                      | -                         | 32,473                            | -                      | 32,473              |
| Intercompany receivables                | -                      | -                         | 9,779                             | (9,779 )               | -                   |
| Mortgage loans held-for-sale, net       | -                      | -                         | 119,953                           | -                      | 119,953             |
| Other assets, net                       | -                      | -                         | 4,710                             | (1,700 )               | 3,010               |
| Total Financial Services Assets         | -                      | -                         | 197,475                           | (11,479 )              | 185,996             |
| Total Assets                            | \$ 1,703,693           | \$ 1,069,537              | \$ 197,475                        | \$ (1,025,264 )        | \$ 1,945,441        |

**LIABILITIES AND EQUITY****Homebuilding:**

|                  |      |           |      |      |           |
|------------------|------|-----------|------|------|-----------|
| Accounts payable | \$ - | \$ 73,055 | \$ - | \$ - | \$ 73,055 |
|------------------|------|-----------|------|------|-----------|



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|                                |         |         |        |            |         |
|--------------------------------|---------|---------|--------|------------|---------|
| Accrued liabilities            | 63,886  | 48,980  | 5,590  | -          | 118,456 |
| Intercompany payables          | 14,068  | 794,179 | 16,815 | (825,062 ) | -       |
| Senior notes, net              | 744,842 | -       | -      | -          | 744,842 |
| Total Homebuilding Liabilities | 822,796 | 916,214 | 22,405 | (825,062 ) | 936,353 |

**Financial Services:**

|                                        |         |         |         |            |           |
|----------------------------------------|---------|---------|---------|------------|-----------|
| Accounts payable and other liabilities | -       | -       | 51,864  | -          | 51,864    |
| Intercompany payables                  | -       | -       | 1,737   | (1,737 )   | -         |
| Mortgage repurchase facility           | -       | -       | 76,327  | -          | 76,327    |
| Total Financial Services Liabilities   | -       | -       | 129,928 | (1,737 )   | 128,191   |
| Total Liabilities                      | 822,796 | 916,214 | 152,333 | (826,799 ) | 1,064,544 |

**Equity:**

|                                            |              |              |            |               |              |
|--------------------------------------------|--------------|--------------|------------|---------------|--------------|
| Total Stockholders' Equity                 | 880,897      | 153,323      | 45,142     | (198,465 )    | 880,897      |
| Total Liabilities and Stockholders' Equity | \$ 1,703,693 | \$ 1,069,537 | \$ 197,475 | \$(1,025,264) | \$ 1,945,441 |

F-41

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**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****M.D.C. Holdings, Inc.****Supplemental Condensed Combining Statements of Operations**

|                                                                                    | Year Ended December 31, 2013 |                           |                                   |                        |                     |
|------------------------------------------------------------------------------------|------------------------------|---------------------------|-----------------------------------|------------------------|---------------------|
|                                                                                    | MDC                          | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminating<br>Entries | Consolidated<br>MDC |
|                                                                                    | (Dollars in thousands)       |                           |                                   |                        |                     |
| <b>Homebuilding:</b>                                                               |                              |                           |                                   |                        |                     |
| Revenues                                                                           | \$-                          | \$1,630,423               | \$-                               | \$(1,248 )             | \$1,629,175         |
| Cost of Sales                                                                      | -                            | (1,340,187)               | -                                 | 1,248                  | (1,338,939 )        |
| Inventory impairments                                                              | -                            | (919 )                    | -                                 | -                      | (919 )              |
| Gross margin                                                                       | -                            | 289,317                   | -                                 | -                      | 289,317             |
| Selling, general, and administrative expenses                                      | (63,506 )                    | (149,424 )                | -                                 | (353 )                 | (213,283 )          |
| Equity income of subsidiaries                                                      | 163,157                      | -                         | -                                 | (163,157 )             | -                   |
| Interest income                                                                    | 26,928                       | 10                        | -                                 | -                      | 26,938              |
| Interest expense                                                                   | (1,726 )                     | -                         | -                                 | -                      | (1,726 )            |
| Other income (expense), net                                                        | 1,387                        | (2,276 )                  | 14                                | (48 )                  | (923 )              |
| Homebuilding pretax income (loss)                                                  | 126,240                      | 137,627                   | 14                                | (163,558 )             | 100,323             |
| <b>Financial Services:</b>                                                         |                              |                           |                                   |                        |                     |
| Financial services pretax income                                                   | -                            | -                         | 29,101                            | 401                    | 29,502              |
| Income before income taxes                                                         | 126,240                      | 137,627                   | 29,115                            | (163,157 )             | 129,825             |
| (Provision for) benefit for income taxes                                           | 188,145                      | 7,507                     | (11,092 )                         | -                      | 184,560             |
| Net income                                                                         | \$314,385                    | \$145,134                 | \$18,023                          | \$(163,157 )           | \$314,385           |
| Other comprehensive income related to available<br>for sale securities, net of tax | 6,737                        | -                         | (119 )                            | 119                    | 6,737               |
| Comprehensive income                                                               | \$321,122                    | \$145,134                 | \$17,904                          | \$(163,038 )           | \$321,122           |

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****M.D.C. Holdings, Inc.****Supplemental Condensed Combining Statements of Operations**

|                                                                                    | Year Ended December 31, 2012 |               |              |              | Consolidated<br>MDC |
|------------------------------------------------------------------------------------|------------------------------|---------------|--------------|--------------|---------------------|
|                                                                                    | Guarantor                    | Non-Guarantor | Eliminating  |              |                     |
|                                                                                    | MDC                          | Subsidiaries  | Subsidiaries | Entries      |                     |
|                                                                                    | (Dollars in thousands)       |               |              |              |                     |
| <b>Homebuilding:</b>                                                               |                              |               |              |              |                     |
| Revenues                                                                           | \$-                          | \$ 1,162,676  | \$ -         | \$ (6,534 )  | \$ 1,156,142        |
| Cost of Sales                                                                      | -                            | (984,477 )    | -            | 6,534        | (977,943 )          |
| Inventory impairments                                                              | -                            | (1,105 )      | -            | -            | (1,105 )            |
| Gross margin                                                                       | -                            | 177,094       | -            | -            | 177,094             |
| Selling, general, and administrative expenses                                      | (52,880)                     | (119,135 )    | 4,720        | -            | (167,295 )          |
| Equity income of subsidiaries                                                      | 81,836                       | -             | -            | (81,836 )    | -                   |
| Interest income                                                                    | 23,381                       | 16            | 1            | -            | 23,398              |
| Interest expense                                                                   | (778 )                       | (30 )         | -            | -            | (808 )              |
| Other income (expense), net                                                        | 528                          | (306 )        | 6            | -            | 228                 |
| Homebuilding pretax income (loss)                                                  | 52,087                       | 57,639        | 4,727        | (81,836 )    | 32,617              |
| <b>Financial Services:</b>                                                         |                              |               |              |              |                     |
| Financial services pretax income                                                   | -                            | -             | 28,498       | -            | 28,498              |
| Income before income taxes                                                         | 52,087                       | 57,639        | 33,225       | (81,836 )    | 61,115              |
| (Provision for) benefit for income taxes                                           | 10,612                       | 1,435         | (10,463 )    | -            | 1,584               |
| Net income                                                                         | \$62,699                     | \$59,074      | \$ 22,762    | \$ (81,836 ) | \$62,699            |
| Other comprehensive income related to<br>available for sale securities, net of tax | 12,078                       | -             | 100          | (100 )       | 12,078              |
| Comprehensive income                                                               | \$74,777                     | \$59,074      | \$ 22,862    | \$ (81,936 ) | \$74,777            |

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****M.D.C. Holdings, Inc.****Supplemental Condensed Combining Statements of Operations**

|                                                                                    | Year Ended December 31, 2011 |                           |                                   |                        |                     |
|------------------------------------------------------------------------------------|------------------------------|---------------------------|-----------------------------------|------------------------|---------------------|
|                                                                                    | MDC                          | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminating<br>Entries | Consolidated<br>MDC |
|                                                                                    | (Dollars in thousands)       |                           |                                   |                        |                     |
| <b>Homebuilding:</b>                                                               |                              |                           |                                   |                        |                     |
| Revenues                                                                           | \$-                          | \$ 826,656                | \$ -                              | \$ (9,633 )            | \$ 817,023          |
| Cost of Sales                                                                      | -                            | (707,576 )                | 486                               | 9,633                  | (697,457 )          |
| Inventory impairments                                                              | -                            | (12,965 )                 | -                                 | -                      | (12,965 )           |
| Gross margin                                                                       | -                            | 106,115                   | 486                               | -                      | 106,601             |
| Selling, general, and administrative expenses                                      | (57,811 )                    | (123,095 )                | 1,801                             | -                      | (179,105 )          |
| Equity income of subsidiaries                                                      | (18,966 )                    | -                         | -                                 | 18,966                 | -                   |
| Interest income                                                                    | 26,039                       | 29                        | -                                 | -                      | 26,068              |
| Interest expense                                                                   | (20,687 )                    | (155 )                    | -                                 | -                      | (20,842 )           |
| Other income (expense), net                                                        | (35,479 )                    | (7,894 )                  | 23                                | -                      | (43,350 )           |
| Homebuilding pretax income (loss)                                                  | (106,904)                    | (25,000 )                 | 2,310                             | 18,966                 | (110,628 )          |
| <b>Financial Services:</b>                                                         |                              |                           |                                   |                        |                     |
| Financial services pretax income                                                   | -                            | -                         | 3,156                             | -                      | 3,156               |
| Income before income taxes                                                         | (106,904)                    | (25,000 )                 | 5,466                             | 18,966                 | (107,472 )          |
| (Provision for) benefit for income taxes                                           | 8,514                        | 2,027                     | (1,459 )                          | -                      | 9,082               |
| Net income                                                                         | \$(98,390 )                  | \$(22,973 )               | \$ 4,007                          | \$ 18,966              | \$(98,390 )         |
| Other comprehensive income related to available<br>for sale securities, net of tax | (12,124 )                    | -                         | (154 )                            | 154                    | (12,124 )           |
| Comprehensive income                                                               | \$(110,514)                  | \$(22,973 )               | \$ 3,853                          | \$ 19,120              | \$(110,514 )        |

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****M.D.C. Holdings, Inc.****Supplemental Condensed Combining Statements of Cash Flows**

|                                                     | Year Ended December 31, 2013 |                           |                                   |                        |                     |
|-----------------------------------------------------|------------------------------|---------------------------|-----------------------------------|------------------------|---------------------|
|                                                     | MDC                          | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminating<br>Entries | Consolidated<br>MDC |
|                                                     | (Dollars in thousands)       |                           |                                   |                        |                     |
| Net cash provided by (used in) operating activities | \$ 11,994                    | \$ (324,812 )             | \$ 43,269                         | \$ -                   | \$ (269,549 )       |
| Net cash used in investing activities               | (345,165)                    | (1,260 )                  | 13,151                            | 302,872                | (30,402 )           |
| Financing activities:                               |                              |                           |                                   |                        |                     |
| Intercompany advances (repayments)                  | -                            | 325,895                   | (23,023 )                         | (302,872 )             | -                   |
| Mortgage repurchase facility                        | -                            | -                         | (13,253 )                         | -                      | (13,253 )           |
| Proceeds from issuance of senior notes              | 346,938                      | -                         | -                                 | -                      | 346,938             |
| Excess tax benefit from share-based awards          | 391                          | -                         | -                                 | -                      | 391                 |
| Proceeds from the exercise of stock options         | 5,118                        | -                         | -                                 | -                      | 5,118               |
| Net cash provided by (used in) financing activities | 352,447                      | 325,895                   | (36,276 )                         | (302,872 )             | 339,194             |
| Net increase in cash and cash equivalents           | 19,276                       | (177 )                    | 20,144                            | -                      | 39,243              |
| Cash and cash equivalents:                          |                              |                           |                                   |                        |                     |
| Beginning of period <sup>(1)</sup>                  | 125,904                      | 3,631                     | 30,560                            | -                      | 160,095             |
| End of period                                       | \$ 145,180                   | \$ 3,454                  | \$ 50,704                         | \$ -                   | \$ 199,338          |

As a result of our Richmond American Homes of Washington, Inc. subsidiary becoming a guarantor subsidiary in 2013, cash and cash equivalents at the beginning of 2013 in the guarantor and non-guarantor columns will not equal the cash and cash equivalents at December 31, 2012 in the Supplemental Condensed Combining Balance Sheet.



**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****M.D.C. Holdings, Inc.****Supplemental Condensed Combining Statements of Cash Flows**

|                                                     | Year Ended December 31, 2012 |                           |                                   |                        |                     |
|-----------------------------------------------------|------------------------------|---------------------------|-----------------------------------|------------------------|---------------------|
|                                                     | MDC                          | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminating<br>Entries | Consolidated<br>MDC |
|                                                     | (Dollars in thousands)       |                           |                                   |                        |                     |
| Net cash provided by (used in) operating activities | \$ 1,961                     | \$ (96,947 )              | \$ (13,833 )                      | \$ -                   | \$ (108,819 )       |
| Net cash used in investing activities               | (109,332)                    | (841 )                    | 2,059                             | 86,333                 | (21,781 )           |
| Financing activities:                               |                              |                           |                                   |                        |                     |
| Intercompany advances (repayments)                  | -                            | 98,567                    | (12,234 )                         | (86,333 )              | -                   |
| Mortgage repurchase facility                        | -                            | -                         | 27,625                            | -                      | 27,625              |
| Dividend payments                                   | (96,915 )                    | -                         | -                                 | -                      | (96,915 )           |
| Proceeds from the exercise of stock options         | 16,624                       | -                         | -                                 | -                      | 16,624              |
| Net cash provided by (used in) financing activities | (80,291 )                    | 98,567                    | 15,391                            | (86,333 )              | (52,666 )           |
| Net increase in cash and cash equivalents           | (187,662)                    | 779                       | 3,617                             | -                      | (183,266 )          |
| Cash and cash equivalents:                          |                              |                           |                                   |                        |                     |
| Beginning of period                                 | 313,566                      | 2,852                     | 26,943                            | -                      | 343,361             |
| End of period                                       | \$ 125,904                   | \$ 3,631                  | \$ 30,560                         | \$ -                   | \$ 160,095          |

**M.D.C. HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****M.D.C. Holdings, Inc.****Supplemental Condensed Combining Statements of Cash Flows**

|                                                     | Year Ended December 31, 2011 |              |                           |             |              |
|-----------------------------------------------------|------------------------------|--------------|---------------------------|-------------|--------------|
|                                                     | Guarantor                    |              | Non-                      | Eliminating | Consolidated |
|                                                     | MDC                          | Subsidiaries | Guarantor<br>Subsidiaries | Entries     | MDC          |
|                                                     | (Dollars in thousands)       |              |                           |             |              |
| Net cash provided by (used in) operating activities | \$(20,496 )                  | \$(37,048 )  | \$(22,740 )               | \$ -        | \$(80,284 )  |
| Net cash used in investing activities               | 375,139                      | (30,541 )    | (4,261 )                  | 63,927      | 404,264      |
| Financing activities:                               |                              |              |                           |             |              |
| Intercompany advances (repayments)                  | -                            | 66,154       | (2,227 )                  | (63,927 )   | -            |
| Extinguishment of senior notes                      | (537,724)                    | -            | -                         | -           | (537,724 )   |
| Mortgage repurchase facility                        | -                            | -            | 23,268                    | -           | 23,268       |
| Dividend payments                                   | (47,432 )                    | -            | -                         | -           | (47,432 )    |
| Proceeds from the exercise of stock options         | 9,044                        | -            | -                         | -           | 9,044        |
| Net cash provided by (used in) financing activities | (576,112)                    | 66,154       | 21,041                    | (63,927 )   | (552,844 )   |
| Net increase in cash and cash equivalents           | (221,469)                    | (1,435 )     | (5,960 )                  | -           | (228,864 )   |
| Cash and cash equivalents:                          |                              |              |                           |             |              |
| Beginning of period                                 | 535,035                      | 4,287        | 32,903                    | -           | 572,225      |
| End of period                                       | \$313,566                    | \$2,852      | \$26,943                  | \$ -        | \$343,361    |



**Item 9. *Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.***

None.

**Item 9A. *Controls and Procedures.***

**Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures**

An evaluation of the effectiveness of the design and operation of our disclosure controls and procedures was performed under the supervision, and with the participation, of our management, including the principal executive officer and the principal financial officer. Based on that evaluation, our management, including the principal executive officer and principal financial officer, concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.

**Management's Report on Internal Control Over Financial Reporting**

Management is responsible for establishing and maintaining adequate internal control over financial reporting. Under the supervision and with the participation of our management, including the principal executive officer and the principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in the *Internal Control—Integrated Framework* (1992 framework) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation under this framework, management concluded that our internal control over financial reporting was effective at December 31, 2013.

Ernst & Young LLP, the independent registered public accounting firm that audited the consolidated financial statements included in this annual report on Form 10-K, has issued an attestation report on our internal control over financial reporting, which is included herein.

**Changes in Internal Control over Financial Reporting**

There were no changes in our internal control over financial reporting that occurred during the fourth quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**Report of Independent Registered Public Accounting Firm**

**The Board of Directors and Stockholders of**

**M.D.C. Holdings, Inc.**

We have audited M.D.C. Holdings, Inc.'s (the "Company") internal control over financial reporting as of December 31, 2013, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (1992 framework) (the COSO criteria). The Company's management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Annual Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, M.D.C. Holdings, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2013, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of M.D.C. Holdings, Inc. as of December 31, 2013 and 2012, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2013, and our report dated February 5, 2014 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Irvine, California

February 5, 2014

**Item 9B. Other Information.**

None

**PART III**

**Item 10. Directors. Executive Officers and Corporate Governance.**

Information not disclosed below that is required with respect to directors, executive officers, filings under Section 16(a) of the Securities and Exchange Act of 1934, as amended (the “Exchange Act”) and corporate governance is incorporated herein by reference, when filed, from our proxy statement (the “Proxy Statement”) for the Annual Meeting of Shareholders to be held on or about May 19, 2014, to be filed with the Securities and Exchange Commission pursuant to Regulation 14A under the Exchange Act.

We will provide to any shareholders or other person without charge, upon request, a copy of our Corporate Code of Conduct, Corporate Governance Guidelines, code of ethics applicable to our principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions (collectively “senior financial officers”) and the charters for our Audit Committee, Compensation Committee and Corporate Governance/Nominating Committee. You may obtain these documents on our website at <http://www.richmondamerican.com>, under our Investor Relations section or by contacting our Investor Relations department at 303-977-3451. Our intention is to post on our website any amendments to or waivers from our code of ethics applicable to our senior financial officers if such disclosure is required.

**Item 11. Executive Compensation.**

Information required to be set forth hereunder has been omitted and will be incorporated by reference, when filed, from our Proxy Statement.

**Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.**

Information required to be set forth hereunder has been omitted and will be incorporated by reference, when filed, from our Proxy Statement

***Item 13. Certain Relationships and Related Transactions, and Director Independence.***

Information required to be set forth hereunder has been omitted and will be incorporated by reference, when filed, from our Proxy Statement.

***Item 14. Principal Accountant Fees and Services.***

Information required to be set forth hereunder has been omitted and will be incorporated by reference, when filed, from our Proxy Statement.

## PART IV

### Item 15. *Exhibits, Financial Statement Schedules.*

#### (a)(1) Financial Statements.

The following Consolidated Financial Statements of the Company and its subsidiaries are included in Part II, Item 8.

|                                                                                                                                  | <b><u>Page</u></b> |
|----------------------------------------------------------------------------------------------------------------------------------|--------------------|
| M.D.C. Holdings, Inc. and Subsidiaries                                                                                           |                    |
| Report of Independent Registered Public Accounting Firm                                                                          | F-2                |
| Consolidated Balance Sheets at December 31, 2013 and December 31, 2012                                                           | F-3                |
| Consolidated Statements of Operations and Comprehensive Income for each of the Three Years in the Period Ended December 31, 2013 | F-4                |
| Consolidated Statements of Stockholders' Equity for each of the Three Years in the Period Ended December 31, 2013                | F-5                |
| Consolidated Statements of Cash Flows for each of the Three Years in the Period Ended December 31, 2013                          | F-6                |
| Notes to Consolidated Financial Statements                                                                                       | F-7                |

#### (a)(2) Financial Statement Schedules.

All schedules are omitted because they are not applicable, not material, not required or the required information is included in the applicable Consolidated Financial Statements or notes thereto.

#### (a)(3) Exhibits.

## INDEX TO EXHIBITS

### Exhibit Description

**Number**

- 3.1 Certificate of Amendment to the Certificate of Incorporation of M.D.C. Holdings, Inc. (hereinafter sometimes referred to as "MDC", the "Company" or the "Registrant"), filed with the Delaware Secretary of State on April 27, 2006, and Certificate of Incorporation, dated May 17, 1985, as amended (incorporated by reference to Exhibit 3.1 of the Company's Quarterly Report on Form 10-Q dated March 31, 2006). \*
- 3.2 Form of Bylaws of MDC, as amended (incorporated by reference to Exhibit 3.2(b) of the Company's Quarterly Report on Form 10-Q dated June 30, 1987). \*
- 3.3 Form of Amendment to the Bylaws of MDC regarding indemnification adopted by its board of directors and effective as of March 20, 1987 (incorporated by reference to Exhibit 3.2(a) of the Company's Quarterly Report on Form 10-Q dated June 30, 1987). \*
- 4.1 Indenture dated as of December 3, 2002, by and among MDC and U.S. Bank National Association (incorporated by reference to Exhibit 4.2 of the Company's Form S-3/A filed September 1, 2004). \*
- 4.2 Supplemental Indenture, dated as of October 6, 2004, by and among MDC, the Guarantors party thereto and U.S. Bank National Association, as Trustee, with respect to MDC's Medium-Term Senior Notes (incorporated by reference to Exhibit 10.3 of the Company's Current Report on Form 8-K filed October 7, 2004). \*



- 4.3 Pricing Supplement No. 1, dated December 6, 2004, with respect to MDC's 5.375% Medium-Term Senior Notes due 2014 (incorporated by reference to the Company's Rule 424(b)(2) filing on December 8, 2004). \*
- 4.4 Pricing Supplement No. 2, dated June 28, 2005, with respect to MDC's 5.375% Medium-Term Senior Notes due July 1, 2015 (incorporated by reference to the Company's Rule 424(b)(2) filing on June 29, 2005). \*
- 4.5 Amendment No. 1 dated as of July 20, 2005 to Supplemental Indenture dated as of October 6, 2004, with respect to MDC's Medium-Term Senior Notes (incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8-K filed July 20, 2005). \*
- 4.6 Amendment No. 2 dated as of January 9, 2006 to Supplemental Indenture dated as of October 6, 2004, with respect to MDC's Medium-Term Senior Notes (incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8-K filed January 9, 2006). \*
- 4.7 Second Supplemental Indenture (5.375% Senior Notes due 2014 and 2015), dated as of January 3, 2013, by and among the Company, U.S. Bank National Association, as Trustee, and Richmond American Homes of Washington, Inc., a wholly owned subsidiary of the Company, as Additional Guarantor, including the form of Guaranty signed by the Additional Guarantor (incorporated by reference to Exhibit 4.7 of the Company's Annual Report on Form 10-K dated December 31, 2012). \*
- 4.8 Supplemental Indenture (5.625% Senior Notes due 2020), dated as of January 15, 2010, among the Company, the guarantors named therein and U.S. Bank National Association, as Trustee (incorporated by reference to Exhibit 4.1 of the Company's Current Report on Form 8-K filed January 15, 2010). \*
- 4.9 Second Supplemental Indenture (5.625% Senior Notes due 2020), dated as of January 3, 2013, by and among the Company, U.S. Bank National Association, as Trustee, and Richmond American Homes of Washington, Inc., a wholly owned subsidiary of the Company, as Additional Guarantor, including the form of Guaranty signed by the Additional Guarantor (incorporated by reference to Exhibit 4.9 of the Company's Annual Report on Form 10-K dated December 31, 2012). \*
- 4.10 Supplemental Indenture (6.000% Senior Notes due 2043), dated as of January 10, 2013, among the Company, the guarantors named therein and U.S. Bank National Association, as Trustee (incorporated by reference to Exhibit 4.1 of the Company's Current Report on Form 8-K filed January 10, 2013). \*
- 4.11 Supplemental Indenture (5.500% Senior Notes due 2024), dated as of January 15, 2014, among the Company, the guarantors named therein and U.S. Bank National Association, as Trustee (incorporated by reference to Exhibit 4.2 of the Company's Current Report on Form 8-K filed January 15, 2014). \*
- 10.1 Credit Agreement by and among M.D.C. Holding, Inc., U.S. Bank National Association, as designated agent and co-administrative agent, Citibank, N.A., as co-administrative agent, and the other Lenders identified therein, dated as of December 13, 2013 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed December 16, 2013). \*
- 10.2 Master Repurchase Agreement among HomeAmerican Mortgage Corporation, U.S. Bank National Association as Agent, and the other Buyers party thereto, dated as of November 12, 2008 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed November 17, 2008). \*
- 10.3

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First Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of October 29, 2009 (incorporated by reference to Exhibit 10.3 of the Company's Quarterly Report on Form 10-Q dated September 30, 2009). \*

- 10.4 Second Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of October 21, 2010 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed October 25, 2010). \*
- 10.5 Third Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of September 14, 2011 (incorporated by reference to Exhibit 10.1 of the Company's Quarterly Report on Form 10-Q dated September 30, 2011). \*
- 10.6 Fourth Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of September 29, 2011 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed September 30, 2011).\*
- 10.7 Fifth Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of January 31, 2012 (incorporated by reference to Exhibit 10.1 of the Company's Quarterly Report on Form 10-Q dated September 30, 2012). \*
- 10.8 Sixth Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of September 21, 2012 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed September 24, 2012).\*
- 10.9 Seventh Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of December 21, 2012 (incorporated by reference to Exhibit 10.8 of the Company's Annual Report on Form 10-K dated December 31, 2012). \*
- 10.10 Eight Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of September 20, 2013 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed September 20, 2013). \*
- 10.11 Ninth Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of December 31, 2013.
- 10.12 Custody Agreement by and between HomeAmerican Mortgage Corporation and U.S. Bank National Association as Agent and Custodian, dated as of November 12, 2008 (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed November 17, 2008). \*
- 10.13 M.D.C. Holdings, Inc. 2001 Equity Incentive Plan Effective March 26, 2001 (incorporated by reference to Exhibit B of the Company's Proxy Statement dated March 31, 2001 relating to the 2001 Annual Meeting of Stockholders). \*
- 10.14 First Amendment to M.D.C. Holdings, Inc. 2001 Equity Incentive Plan, effective April 28, 2003 (incorporated by reference to Exhibit 10.2 of the Company's Quarterly Report on Form 10-Q dated March 31, 2003). \*
- 10.15 Second Amendment to M.D.C. Holdings, Inc. 2001 Equity Incentive Plan, effective April 29, 2008 (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed May 1, 2008). \*
- 10.16 Third Amendment to M.D.C. Holdings, Inc. 2001 Equity Incentive Plan, effective April 29, 2008 (incorporated by reference to Exhibit 10.3 to the Company's Form 8-K filed May 1, 2008). \*



- Fourth Amendment to M.D.C. Holdings, Inc. 2001 Equity Incentive Plan, dated December 31, 2008  
10.17 (incorporated by reference to Exhibit 10.11 of the Company's Annual Report on Form 10-K dated December 31, 2008). \*
- 10.18 Form of Non-Qualified Stock Option Certificate (2001 Equity Incentive Plan) (incorporated by reference to Exhibit 10.10 of the Company's Annual Report on Form 10-K dated December 31, 2004). \*
- 10.19 Form of Restricted Stock Agreement (2001 Equity Incentive Plan) (incorporated by reference to Exhibit 10.11 of the Company's Annual Report on Form 10-K dated December 31, 2004). \*
- M.D.C. Holdings, Inc. Stock Option Plan for Non-Employee Directors Effective March 26, 2001 (incorporated  
10.20 by reference to Exhibit C of the Company's Proxy Statement dated March 31, 2001 relating to the 2001 Annual Meeting of Stockholders). \*
- First Amendment to M.D.C. Holdings, Inc. Stock Option Plan for Non-Employee Directors, October 20, 2003  
10.21 (incorporated by reference to Exhibit 10.13 of the Company's Annual Report on Form 10-K dated December 31, 2004). \*
- Second Amendment to M.D.C. Holdings, Inc. Stock Option Plan for Non-Employee Directors, dated December  
10.22 16, 2008 (incorporated by reference to Exhibit 10.16 of the Company's Annual Report on Form 10-K dated December 31, 2008). \*
- Form of Non-Qualified Stock Option Agreement (Stock Option Plan for Non-Employee Directors)  
10.23 (incorporated by reference to Exhibit 10.14 of the Company's Annual Report on Form 10-K dated December 31, 2004). \*
- 10.24 M.D.C. Holdings, Inc. 2011 Equity Incentive Plan, effective April 27, 2011 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed April 29, 2011). \*
- 10.25 First Amendment to the M.D.C. Holdings, Inc. 2011 Equity Incentive Plan (incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8-K filed March 19, 2013).\*
- 10.26 Form of 2011 Stock Option Agreement (2011 Equity Incentive Plan) (incorporated by reference to Exhibit 10.3 of the Company's Quarterly Report on Form 10-Q dated June 30, 2011). \*
- 10.27 Form of 2011 Restricted Stock Agreement (2011 Equity Incentive Plan) (incorporated by reference to Exhibit 10.4 of the Company's Quarterly Report on Form 10-Q dated June 30, 2011). \*
- 10.28 Form of Executive Officer Stock Option Agreement under the 2011 Equity Incentive Plan (incorporated by reference to Exhibit 10.3 of the Company's Current Report on Form 8-K filed March 9, 2012).\*

- 10.29 M.D.C. Holdings, Inc. 2011 Stock Option Plan for Non-Employee Directors effective April 27, 2011 (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed April 29, 2011). \*
- 10.30 Form of 2011 Stock Option Agreement (2011 Stock Option Plan for Non-Employee Directors) (incorporated by reference to Exhibit 10.2 of the Company's Quarterly Report on Form 10-Q dated June 30, 2011). \*
- 10.31 Form of Indemnification Agreement entered into between the Company and members of its Board of Directors (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed October 26, 2006).\*
- 10.32 Form of Indemnification Agreement entered into between the Company and certain of its officers (incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8-K filed October 26, 2006).\*
- 10.33 M.D.C. Holdings, Inc. Amended Executive Officer Performance-Based Compensation Plan, approved April 29, 2008 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed May 1, 2008). \*
- 10.34 First Amendment to the M.D.C. Holdings, Inc. Amended Executive Officer Performance-Based Compensation Plan, dated December 31, 2008 (incorporated by reference to Exhibit 10.21 of the Company's Annual Report on Form 10-K dated December 31, 2008). \*
- 10.35 Second Amendment to the M.D.C. Holdings, Inc. Amended Executive Officer Performance-Based Compensation Plan, dated as of June 1, 2011 (incorporated by reference to Exhibit 10.1 of the Company's Quarterly Report on Form 10-Q dated June 30, 2011). \*
- 10.36 Third Amendment to the M.D.C. Holdings, Inc. Amended Executive Officer Performance-Based Compensation Plan, dated March 8, 2012 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed March 9, 2012).\*
- 10.37 Fourth Amendment to the M.D.C. Holdings, Inc. Amended Executive Officer Performance-Based Compensation Plan, executed May 21, 2012 effective as of January 1, 2012 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed May 22, 2012).\*
- 10.38 Waiver Agreement among M.D.C. Holdings, Inc., Larry A. Mizel and David D. Mandarich, dated as of October 13, 2011 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed October 13, 2011).\*
- 10.39 M.D.C. Holdings, Inc. 2013 Executive Officer Performance-Based Compensation Plan, approved March 18, 2013 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed March 19, 2013). \*
- 10.40 Employment Agreement, Larry A. Mizel, amended and restated as of August 1, 2008 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed September 26, 2008). \*
- 10.41 Amendment to Employment Agreement of Larry A. Mizel, dated March 8, 2012 (incorporated by reference to Exhibit 10.4 of the Company's Current Report on Form 8-K filed March 9, 2012).\*
- 10.42 Second Amendment to Employment Agreement of Larry A. Mizel, dated October 18, 2013 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed October 18, 2013).\*



- 10.43 Employment Agreement, David D. Mandarich, amended and restated as of August 1, 2008 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed September 26, 2008). \*
- 10.44 Amendment to Employment Agreement of David D. Mandarich, dated March 8, 2012 (incorporated by reference to Exhibit 10.5 of the Company's Current Report on Form 8-K filed March 9, 2012).\*
- 10.45 Second Amendment to Employment Agreement of David D. Mandarich, dated October 18, 2013 (incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8-K filed October 18, 2013).\*
- 10.46 Employment offer letter by the Company to John M. Stephens, dated January 27, 2012 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed January 30, 2012). \*
- 10.47 Lease Agreement among MDC, Richmond American Homes of Colorado, Inc. and Larry A. Mizel, August 2, 2007 (incorporated by reference to Exhibit 10.4 of the Company's Quarterly Report on Form 10-Q dated June 30, 2007). \*
- 10.48 Lease Agreement among MDC, Richmond American Homes of Colorado, Inc. and David D. Mandarich, August 2, 2007 (incorporated by reference to Exhibit 10.5 of the Company's Quarterly Report on Form 10-Q dated June 30, 2007). \*
- 10.49 Change in Control and Separation Agreement between the Company and John M. Stephens, dated as of February 1, 2012 (incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8-K filed January 30, 2012).\*
- 10.50 Change in Control and Separation Agreement between the Company and Michael Touff, dated as of July 30, 2008 (incorporated by reference to Exhibit 10.8 of the Company's Quarterly Report on Form 10-Q filed July 31, 2008). \*
- 10.51 Form of Change in Control Agreement between the Company and certain employees of M.D.C. Holdings, Inc. (incorporated by reference to Exhibit 10.3 of the Company's Current Report on Form 8-K filed March 27, 1998). \*
- 10.52 Independent Contractor Agreement between Mizel Design and Decorating Company and the Company effective as of January 1, 2005 (incorporated by reference to Exhibit 10.26 of the Company's Annual Report on Form 10-K dated December 31, 2004). \*
- 10.53 Sub-Sublease agreement between MDC and CVentures, Inc., executed July 25, 2005 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed July 27, 2005). \*
- 10.54 First Amendment to Sub-Sublease agreement between MDC and CVentures, Inc., executed on March 28, 2006 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed March 29, 2006). \*
- 12 Ratio of Earnings to Fixed Charges Schedule.
- 21 Subsidiaries of the Company.
- 23 Consent of Ernst & Young LLP.



- 31.1 Certification of principal executive officer required by 17 CFR 240.13a-14(a), pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

- 31.2 Certification of principal financial officer required by 17 CFR 240.13a-14(a), pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of principal executive officer required by 17 CFR 240.13a-14(b), pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of principal financial officer required by 17 CFR 240.13a-14(b), pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

101 The following financial statements filed on February 5, 2014, formatted in XBRL(Extensible Business Reporting Language): (i) Consolidated Balance Sheets at December 31, 2013 and December 31, 2012, (ii) Consolidated Statements of Operations for each of the three years in the period ended December 31, 2013, (iii) Consolidated Statements of Stockholders' Equity for each of the three years in the period ended December 31, 2013, (iv) Consolidated Statements of Cash Flows for each of the three years in the period ended December 31, 2013; and (v) Notes to the Consolidated Financial Statements, tagged as blocks of text.

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\*Incorporated by reference.

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

M.D.C. HOLDINGS, INC.  
(Registrant)

Date: February 5, 2014 By: /s/ John M. Stephens  
John M. Stephens  
*Senior Vice President, Chief Financial  
Officer and Principal  
Accounting Officer (duly authorized officer)*

## POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that the undersigned officers and/or directors of the Registrant, by virtue of their signatures to this report, appearing below, hereby constitute and appoint Larry A. Mizel and David D. Mandarich, or any one of them, with full power of substitution, as attorneys-in-fact in their names, places and steads to execute any and all amendments to this report in the capacities set forth opposite their names and hereby ratify all that said attorneys-in-fact do by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

| <u>Signature</u>   | <u>Title</u>                                                   | <u>Date</u>         |
|--------------------|----------------------------------------------------------------|---------------------|
| /s/ Larry A. Mizel | Chairman of the Board of Directors and                         |                     |
| Larry A. Mizel     | Chief Executive Officer ( <i>principal executive officer</i> ) | February 5,<br>2014 |
|                    | Director, President and Chief Operating Officer                |                     |

|                                                   |                                                                                                                                                              |                     |
|---------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------|
| /s/ David D.<br>Mandarich<br>David D. Mandarich   |                                                                                                                                                              | February 5,<br>2014 |
| /s/ John M. Stephens<br>John M. Stephens          | Senior Vice President, Chief Financial<br>Officer & Principal Accounting Officer ( <i>principal financial officer and<br/>principal accounting officer</i> ) | February 5,<br>2014 |
| /s/ Raymond T.<br>Baker<br>Raymond T. Baker       | Director                                                                                                                                                     | February 5,<br>2014 |
| /s/ Michael A.<br>Berman<br>Michael A. Berman     | Director                                                                                                                                                     | February 5,<br>2014 |
| /s/ David E.<br>Blackford<br>David E. Blackford   | Director                                                                                                                                                     | February 5,<br>2014 |
| /s/ Herbert T.<br>Buchwald<br>Herbert T. Buchwald | Director                                                                                                                                                     | February 5,<br>2014 |
| /s/ Paris G. Reece III<br>Paris G. Reece III      | Director                                                                                                                                                     | February 5,<br>2014 |
| /s/ David Siegel<br>David Siegel                  | Director                                                                                                                                                     | February 5,<br>2014 |

## INDEX TO EXHIBITS

| Exhibit<br>Number | Description                                                                                                                                                                                                                                                                                                                                                                                                                |
|-------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 3.1               | Certificate of Amendment to the Certificate of Incorporation of M.D.C. Holdings, Inc. (hereinafter sometimes referred to as "MDC", the "Company" or the "Registrant"), filed with the Delaware Secretary of State on April 27, 2006, and Certificate of Incorporation, dated May 17, 1985, as amended (incorporated by reference to Exhibit 3.1 of the Company's Quarterly Report on Form 10-Q dated March 31, 2006). *    |
| 3.2               | Form of Bylaws of MDC, as amended (incorporated by reference to Exhibit 3.2(b) of the Company's Quarterly Report on Form 10-Q dated June 30, 1987). *                                                                                                                                                                                                                                                                      |
| 3.3               | Form of Amendment to the Bylaws of MDC regarding indemnification adopted by its board of directors and effective as of March 20, 1987 (incorporated by reference to Exhibit 3.2(a) of the Company's Quarterly Report on Form 10-Q dated June 30, 1987). *                                                                                                                                                                  |
| 4.1               | Indenture dated as of December 3, 2002, by and among MDC and U.S. Bank National Association (incorporated by reference to Exhibit 4.2 of the Company's Form S-3/A filed September 1, 2004). *                                                                                                                                                                                                                              |
| 4.2               | Supplemental Indenture, dated as of October 6, 2004, by and among MDC, the Guarantors party thereto and U.S. Bank National Association, as Trustee, with respect to MDC's Medium-Term Senior Notes (incorporated by reference to Exhibit 10.3 of the Company's Current Report on Form 8-K filed October 7, 2004). *                                                                                                        |
| 4.3               | Pricing Supplement No. 1, dated December 6, 2004, with respect to MDC's 5.375% Medium-Term Senior Notes due 2014 (incorporated by reference to the Company's Rule 424(b)(2) filing on December 8, 2004). *                                                                                                                                                                                                                 |
| 4.4               | Pricing Supplement No. 2, dated June 28, 2005, with respect to MDC's 5.375% Medium-Term Senior Notes due July 1, 2015 (incorporated by reference to the Company's Rule 424(b)(2) filing on June 29, 2005). *                                                                                                                                                                                                               |
| 4.5               | Amendment No. 1 dated as of July 20, 2005 to Supplemental Indenture dated as of October 6, 2004, with respect to MDC's Medium-Term Senior Notes (incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8-K filed July 20, 2005). *                                                                                                                                                             |
| 4.6               | Amendment No. 2 dated as of January 9, 2006 to Supplemental Indenture dated as of October 6, 2004, with respect to MDC's Medium-Term Senior Notes (incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8-K filed January 9, 2006). *                                                                                                                                                         |
| 4.7               | Second Supplemental Indenture (5.375% Senior Notes due 2014 and 2015), dated as of January 3, 2013, by and among the Company, U.S. Bank National Association, as Trustee, and Richmond American Homes of Washington, Inc., a wholly owned subsidiary of the Company, as Additional Guarantor, including the form of Guaranty signed by the Additional Guarantor (incorporated by reference to Exhibit 4.7 of the Company's |

Annual Report on Form 10-K dated December 31, 2012). \*

- 4.8 Supplemental Indenture (5.625% Senior Notes due 2020), dated as of January 15, 2010, among the Company, the guarantors named therein and U.S. Bank National Association, as Trustee (incorporated by reference to Exhibit 4.1 of the Company's Current Report on Form 8-K filed January 15, 2010). \*

- 4.9 Second Supplemental Indenture (5.625% Senior Notes due 2020), dated as of January 3, 2013, by and among the Company, U.S. Bank National Association, as Trustee, and Richmond American Homes of Washington, Inc., a wholly owned subsidiary of the Company, as Additional Guarantor, including the form of Guaranty signed by the Additional Guarantor (incorporated by reference to Exhibit 4.9 of the Company's Annual Report on Form 10-K dated December 31, 2012). \*
- 4.10 Supplemental Indenture (6.000% Senior Notes due 2043), dated as of January 10, 2013, among the Company, the guarantors named therein and U.S. Bank National Association, as Trustee (incorporated by reference to Exhibit 4.1 of the Company's Current Report on Form 8-K filed January 10, 2013). \*
- 4.11 Supplemental Indenture (5.500% Senior Notes due 2024), dated as of January 15, 2014, among the Company, the guarantors named therein and U.S. Bank National Association, as Trustee (incorporated by reference to Exhibit 4.2 of the Company's Current Report on Form 8-K filed January 15, 2014). \*
- 10.1 Credit Agreement by and among M.D.C. Holding, Inc., U.S. Bank National Association, as designated agent and co-administrative agent, Citibank, N.A., as co-administrative agent, and the other Lenders identified therein, dated as of December 13, 2013 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed December 16, 2013). \*
- 10.2 Master Repurchase Agreement among HomeAmerican Mortgage Corporation, U.S. Bank National Association as Agent, and the other Buyers party thereto, dated as of November 12, 2008 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed November 17, 2008). \*
- 10.3 First Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of October 29, 2009 (incorporated by reference to Exhibit 10.3 of the Company's Quarterly Report on Form 10-Q dated September 30, 2009). \*
- 10.4 Second Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of October 21, 2010 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed October 25, 2010). \*
- 10.5 Third Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of September 14, 2011 (incorporated by reference to Exhibit 10.1 of the Company's Quarterly Report on Form 10-Q dated September 30, 2011). \*
- 10.6 Fourth Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of September 29, 2011 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed September 30, 2011).\*
- 10.7 Fifth Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of January 31, 2012 (incorporated by reference to Exhibit 10.1 of the Company's Quarterly Report on Form 10-Q dated September 30, 2012). \*
- 10.8 Sixth Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of September 21, 2012 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed September 24, 2012).\*





- 10.9 Seventh Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of December 21, 2012 (incorporated by reference to Exhibit 10.8 of the Company's Annual Report on Form 10-K dated December 31, 2012). \*
- 10.10 Eight Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of September 20, 2013 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed September 20, 2013). \*
- 10.11 Ninth Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of December 31, 2013.
- 10.12 Custody Agreement by and between HomeAmerican Mortgage Corporation and U.S. Bank National Association as Agent and Custodian, dated as of November 12, 2008 (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed November 17, 2008). \*
- 10.13 M.D.C. Holdings, Inc. 2001 Equity Incentive Plan Effective March 26, 2001 (incorporated by reference to Exhibit B of the Company's Proxy Statement dated March 31, 2001 relating to the 2001 Annual Meeting of Stockholders). \*
- 10.14 First Amendment to M.D.C. Holdings, Inc. 2001 Equity Incentive Plan, effective April 28, 2003 (incorporated by reference to Exhibit 10.2 of the Company's Quarterly Report on Form 10-Q dated March 31, 2003). \*
- 10.15 Second Amendment to M.D.C. Holdings, Inc. 2001 Equity Incentive Plan, effective April 29, 2008 (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed May 1, 2008). \*
- 10.16 Third Amendment to M.D.C. Holdings, Inc. 2001 Equity Incentive Plan, effective April 29, 2008 (incorporated by reference to Exhibit 10.3 to the Company's Form 8-K filed May 1, 2008). \*
- 10.17 Fourth Amendment to M.D.C. Holdings, Inc. 2001 Equity Incentive Plan, dated December 31, 2008 (incorporated by reference to Exhibit 10.11 of the Company's Annual Report on Form 10-K dated December 31, 2008). \*
- 10.18 Form of Non-Qualified Stock Option Certificate (2001 Equity Incentive Plan) (incorporated by reference to Exhibit 10.10 of the Company's Annual Report on Form 10-K dated December 31, 2004). \*
- 10.19 Form of Restricted Stock Agreement (2001 Equity Incentive Plan) (incorporated by reference to Exhibit 10.11 of the Company's Annual Report on Form 10-K dated December 31, 2004). \*
- 10.20 M.D.C. Holdings, Inc. Stock Option Plan for Non-Employee Directors Effective March 26, 2001 (incorporated by reference to Exhibit C of the Company's Proxy Statement dated March 31, 2001 relating to the 2001 Annual Meeting of Stockholders). \*
- 10.21 First Amendment to M.D.C. Holdings, Inc. Stock Option Plan for Non-Employee Directors, October 20, 2003 (incorporated by reference to Exhibit 10.13 of the Company's Annual Report on Form 10-K dated December 31, 2004). \*



- 10.22 Second Amendment to M.D.C. Holdings, Inc. Stock Option Plan for Non-Employee Directors, dated December 16, 2008 (incorporated by reference to Exhibit 10.16 of the Company's Annual Report on Form 10-K dated December 31, 2008). \*
- 10.23 Form of Non-Qualified Stock Option Agreement (Stock Option Plan for Non-Employee Directors) (incorporated by reference to Exhibit 10.14 of the Company's Annual Report on Form 10-K dated December 31, 2004). \*
- 10.24 M.D.C. Holdings, Inc. 2011 Equity Incentive Plan, effective April 27, 2011 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed April 29, 2011). \*
- 10.25 First Amendment to the M.D.C. Holdings, Inc. 2011 Equity Incentive Plan (incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8-K filed March 19, 2013).\*
- 10.26 Form of 2011 Stock Option Agreement (2011 Equity Incentive Plan) (incorporated by reference to Exhibit 10.3 of the Company's Quarterly Report on Form 10-Q dated June 30, 2011). \*
- 10.27 Form of 2011 Restricted Stock Agreement (2011 Equity Incentive Plan) (incorporated by reference to Exhibit 10.4 of the Company's Quarterly Report on Form 10-Q dated June 30, 2011). \*
- 10.28 Form of Executive Officer Stock Option Agreement under the 2011 Equity Incentive Plan (incorporated by reference to Exhibit 10.3 of the Company's Current Report on Form 8-K filed March 9, 2012).\*
- 10.29 M.D.C. Holdings, Inc. 2011 Stock Option Plan for Non-Employee Directors effective April 27, 2011 (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed April 29, 2011). \*
- 10.30 Form of 2011 Stock Option Agreement (2011 Stock Option Plan for Non-Employee Directors) (incorporated by reference to Exhibit 10.2 of the Company's Quarterly Report on Form 10-Q dated June 30, 2011). \*
- 10.31 Form of Indemnification Agreement entered into between the Company and members of its Board of Directors (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed October 26, 2006).\*
- 10.32 Form of Indemnification Agreement entered into between the Company and certain of its officers (incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8-K filed October 26, 2006).\*
- 10.33 M.D.C. Holdings, Inc. Amended Executive Officer Performance-Based Compensation Plan, approved April 29, 2008 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed May 1, 2008). \*
- 10.34 First Amendment to the M.D.C. Holdings, Inc. Amended Executive Officer Performance-Based Compensation Plan, dated December 31, 2008 (incorporated by reference to Exhibit 10.21 of the Company's Annual Report on Form 10-K dated December 31, 2008). \*
- 10.35 Second Amendment to the M.D.C. Holdings, Inc. Amended Executive Officer Performance-Based Compensation Plan, dated as of June 1, 2011 (incorporated by reference to Exhibit 10.1 of the Company's Quarterly Report on Form 10-Q dated June 30, 2011). \*



10.36 Third Amendment to the M.D.C. Holdings, Inc. Amended Executive Officer Performance-Based Compensation Plan, dated March 8, 2012 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed March 9, 2012).\*

10.37 Fourth Amendment to the M.D.C. Holdings, Inc. Amended Executive Officer Performance-Based Compensation Plan, executed May 21, 2012 effective as of January 1, 2012 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed May 22, 2012).\*

10.38 Waiver Agreement among M.D.C. Holdings, Inc., Larry A. Mizel and David D. Mandarich, dated as of October 13, 2011 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed October 13, 2011).\*

10.39 M.D.C. Holdings, Inc. 2013 Executive Officer Performance-Based Compensation Plan, approved March 18, 2013 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed March 19, 2013). \*

10.40 Employment Agreement, Larry A. Mizel, amended and restated as of August 1, 2008 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed September 26, 2008). \*

10.41 Amendment to Employment Agreement of Larry A. Mizel, dated March 8, 2012 (incorporated by reference to Exhibit 10.4 of the Company's Current Report on Form 8-K filed March 9, 2012).\*

10.42 Second Amendment to Employment Agreement of Larry A. Mizel, dated October 18, 2013 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed October 18, 2013).\*

10.43 Employment Agreement, David D. Mandarich, amended and restated as of August 1, 2008 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed September 26, 2008). \*

10.44 Amendment to Employment Agreement of David D. Mandarich, dated March 8, 2012 (incorporated by reference to Exhibit 10.5 of the Company's Current Report on Form 8-K filed March 9, 2012).\*

10.45 Second Amendment to Employment Agreement of David D. Mandarich, dated October 18, 2013 (incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8-K filed October 18, 2013).\*

10.46 Employment offer letter by the Company to John M. Stephens, dated January 27, 2012 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed January 30, 2012). \*

10.47 Lease Agreement among MDC, Richmond American Homes of Colorado, Inc. and Larry A. Mizel, August 2, 2007 (incorporated by reference to Exhibit 10.4 of the Company's Quarterly Report on Form 10-Q dated June 30, 2007). \*

10.48 Lease Agreement among MDC, Richmond American Homes of Colorado, Inc. and David D. Mandarich, August 2, 2007 (incorporated by reference to Exhibit 10.5 of the Company's Quarterly Report on Form 10-Q dated June 30, 2007). \*

10.49 Change in Control and Separation Agreement between the Company and John M. Stephens, dated as of February 1, 2012 (incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8-K filed January 30, 2012).\*



- 10.50 Change in Control and Separation Agreement between the Company and Michael Touff, dated as of July 30, 2008 (incorporated by reference to Exhibit 10.8 of the Company's Quarterly Report on Form 10-Q filed July 31, 2008). \*
- 10.51 Form of Change in Control Agreement between the Company and certain employees of M.D.C. Holdings, Inc. (incorporated by reference to Exhibit 10.3 of the Company's Current Report on Form 8-K filed March 27, 1998). \*
- 10.52 Independent Contractor Agreement between Mizel Design and Decorating Company and the Company effective as of January 1, 2005 (incorporated by reference to Exhibit 10.26 of the Company's Annual Report on Form 10-K dated December 31, 2004). \*
- 10.53 Sub-Sublease agreement between MDC and CVentures, Inc., executed July 25, 2005 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed July 27, 2005). \*
- 10.54 First Amendment to Sub-Sublease agreement between MDC and CVentures, Inc., executed on March 28, 2006 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed March 29, 2006). \*
- 12 Ratio of Earnings to Fixed Charges Schedule.
- 21 Subsidiaries of the Company.
- 23 Consent of Ernst & Young LLP.
- 31.1 Certification of principal executive officer required by 17 CFR 240.13a-14(a), pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of principal financial officer required by 17 CFR 240.13a-14(a), pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of principal executive officer required by 17 CFR 240.13a-14(b), pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of principal financial officer required by 17 CFR 240.13a-14(b), pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101 The following financial statements filed on February 5, 2014, formatted in XBRL(Extensible Business Reporting Language): (i) Consolidated Balance Sheets at December 31, 2013 and December 31, 2012, (ii) Consolidated Statements of Operations for each of the three years in the period ended December 31, 2013, (iii) Consolidated Statements of Stockholders' Equity for each of the three years in the period ended December 31, 2013, (iv) Consolidated Statements of Cash Flows for each of the three years in the period ended December 31, 2013; and (v) Notes to the Consolidated Financial Statements, tagged as blocks of text.

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\*Incorporated by reference.

