

MDC HOLDINGS INC
Form 10-Q
November 01, 2018

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2018

OR

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

Commission File No. 1-8951

M.D.C. HOLDINGS, INC.

(Exact name of Registrant as specified in its charter)

Delaware
(State or other jurisdiction
of incorporation or organization)

84-0622967
(I.R.S.
employer
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)

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 every Interactive Data File required to be submitted 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 such files). Yes No

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

Large Accelerated Filer	Accelerated Filer
Non-Accelerated Filer	Smaller Reporting Company
Emerging growth company	

If an emerging growth company, indicate by check mark if the registrant has elected to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of October 30, 2018, 56,614,573 shares of M.D.C. Holdings, Inc. common stock were outstanding.

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M.D.C. HOLDINGS, INC.

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FOR THE QUARTER ENDED SEPTEMBER 30, 2018

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Table of Contents**PART I****ITEM 1. Unaudited Consolidated Financial Statements**
M.D.C. HOLDINGS, INC.**Consolidated Balance Sheets.**

	September 30, 2018	December 31, 2017
	(Dollars in thousands, except per share amounts) (Unaudited)	
ASSETS		
Homebuilding:		
Cash and cash equivalents	\$ 360,947	\$ 472,957
Marketable securities	-	49,634
Restricted cash	7,866	8,812
Trade and other receivables	56,469	53,362
Inventories:		
Housing completed or under construction	1,073,909	936,685
Land and land under development	1,034,025	893,051
Total inventories	2,107,934	1,829,736
Property and equipment, net	56,693	26,439
Deferred tax asset, net	36,815	41,480
Prepaid and other assets	52,988	75,666
Total homebuilding assets	2,679,712	2,558,086
Financial Services:		
Cash and cash equivalents	49,979	32,471
Marketable securities	49,006	42,004
Mortgage loans held-for-sale, net	114,836	138,114
Other assets	14,637	9,617
Total financial services assets	228,458	222,206
Total Assets	\$ 2,908,170	\$ 2,780,292
LIABILITIES AND EQUITY		
Homebuilding:		
Accounts payable	\$ 52,070	\$ 39,655
Accrued liabilities	175,110	166,312
Revolving credit facility	15,000	15,000
Senior notes, net	987,617	986,597
Total homebuilding liabilities	1,229,797	1,207,564
Financial Services:		

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Accounts payable and accrued liabilities	54,847	53,101
Mortgage repurchase facility	90,784	112,340
Total financial services liabilities	145,631	165,441
Total Liabilities	1,375,428	1,373,005
Stockholders' Equity		
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; 56,614,726 and 56,123,228 issued and outstanding at September 30, 2018 and December 31, 2017, respectively	566	561
Additional paid-in-capital	1,162,924	1,144,570
Retained earnings	369,252	258,164
Accumulated other comprehensive income	-	3,992
Total Stockholders' Equity	1,532,742	1,407,287
Total Liabilities and Stockholders' Equity	\$2,908,170	\$2,780,292

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

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
	(Dollars in thousands, except per share amounts)			
	(Unaudited)			
Homebuilding:				
Home sale revenues	\$766,027	\$584,947	\$2,123,323	\$1,796,046
Land sale revenues	-	1,340	-	2,938
Total home and land sale revenues	766,027	586,287	2,123,323	1,798,984
Home cost of sales	(619,248)	(485,147)	(1,722,283)	(1,493,166)
Land cost of sales	-	(1,259)	-	(2,672)
Inventory impairments	(11,098)	(4,540)	(11,848)	(9,390)
Total cost of sales	(630,346)	(490,946)	(1,734,131)	(1,505,228)
Gross profit	135,681	95,341	389,192	293,756
Selling, general and administrative expenses	(83,523)	(69,102)	(236,435)	(206,109)
Interest and other income	1,953	54,548	5,586	59,722
Other expense	(1,128)	(618)	(2,562)	(1,635)
Other-than-temporary impairment of marketable securities	-	-	-	(51)
Homebuilding pretax income	52,983	80,169	155,781	145,683
Financial Services:				
Revenues	19,611	17,464	60,018	54,516
Expenses	(9,408)	(8,849)	(27,850)	(25,247)
Interest and other income	4,234	925	6,619	3,142
Other-than-temporary impairment of marketable securities	-	(29)	-	(160)
Financial services pretax income	14,437	9,511	38,787	32,251
Income before income taxes	67,420	89,680	194,568	177,934
Provision for income taxes	(14,028)	(28,517)	(38,513)	(60,651)
Net income	\$53,392	\$61,163	\$156,055	\$117,283
Other comprehensive loss related to available for sale securities, net of tax	-	(23,175)	-	(19,245)
Comprehensive income	\$53,392	\$37,988	\$156,055	\$98,038
Earnings per share:				
Basic	\$0.94	\$1.09	\$2.77	\$2.10
Diluted	\$0.93	\$1.07	\$2.72	\$2.07
Weighted average common shares outstanding:				
Basic	56,171,619	55,782,389	56,023,996	55,623,225

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Diluted	57,226,659	56,809,208	57,029,715	56,428,247
Dividends declared per share	\$0.30	\$0.23	\$0.90	\$0.69

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

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

	Nine Months Ended September 30, 2018 2017 (Dollars in thousands) (Unaudited)	
Operating Activities:		
Net income	\$ 156,055	\$ 117,283
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Stock-based compensation expense	8,500	3,100
Depreciation and amortization	15,406	4,205
Inventory impairments	11,848	9,390
Other-than-temporary impairment of marketable securities	-	211
Net gain on sale of available-for-sale marketable securities	-	(18,122)
Net gain on marketable equity securities	(3,129)	-
Gain on sale of metropolitan district bond securities (related party)	-	(35,847)
Amortization of discount / premiums on marketable debt securities, net	(366)	-
Deferred income tax expense	4,092	22,795
Net changes in assets and liabilities:		
Trade and other receivables	(7,049)	119
Mortgage loans held-for-sale	23,278	48,970
Housing completed or under construction	(131,657)	(101,997)
Land and land under development	(149,963)	19,886
Prepaid and other assets	(12,328)	(11,229)
Accounts payable and accrued liabilities	26,067	15,345
Net cash provided by (used in) operating activities	(59,246)	74,109
Investing Activities:		
Purchases of marketable securities	(17,183)	(17,604)
Maturities of marketable securities	50,000	-
Sales of marketable securities	13,310	83,315
Proceeds from sale of metropolitan district bond securities (related party)	-	44,253
Purchases of property and equipment	(19,899)	(1,917)
Net cash provided by investing activities	26,228	108,047
Financing Activities:		
Payments on mortgage repurchase facility, net	(21,556)	(49,382)
Dividend payments	(50,733)	(38,793)
Payments of deferred financing costs	-	(2,630)
Proceeds from exercise of stock options	9,859	8,503
Net cash used in financing activities	(62,430)	(82,302)

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Net increase (decrease) in cash, cash equivalents and restricted cash	(95,448)	99,854
Cash, cash equivalents and restricted cash:		
Beginning of period	514,240	286,687
End of period	\$418,792	\$386,541

Reconciliation of cash, cash equivalents and restricted cash:

Homebuilding:		
Cash and cash equivalents	\$360,947	\$351,399
Restricted cash	7,866	8,723
Financial Services:		
Cash and cash equivalents	49,979	26,419
Total cash, cash equivalents and restricted cash	\$418,792	\$386,541

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

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1. Basis of Presentation

The Unaudited 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) have been prepared, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC"). Accordingly, they do not include all information and footnotes required by U.S. generally accepted accounting principles ("GAAP") for complete financial statements. These statements reflect all normal and recurring adjustments which, in the opinion of management, are necessary to present fairly the financial position, results of operations and cash flows of MDC at September 30, 2018 and for all periods presented. These statements should be read in conjunction with MDC's Consolidated Financial Statements and Notes thereto included in MDC's Annual Report on Form 10-K for the year ended December 31, 2017.

On November 20, 2017, MDC's board of directors declared an 8% stock dividend that was distributed on December 19, 2017 to shareholders of record on December 5, 2017. In accordance with Accounting Standards Codification ("ASC") Topic 260, *Earnings Per Share* ("ASC 260"), basic and diluted earnings per share amounts, share amounts and dividends declared per share have been restated for any periods or dates prior to the stock dividend record date.

Included in these footnotes are certain statements that 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 operations, 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 section 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.

When necessary, reclassifications have been made to our prior period financial information to conform to the current year presentation.

2. Recently Issued Accounting Standards

Adoption of New Accounting Standards

Accounting Standards Update (“ASU”) 2018-02, *Income Statement – Reporting Comprehensive Income (Topic 220)* (“ASU 2018-02”). ASU 2018-02 allows for a reclassification from accumulated other comprehensive income to retained earnings for certain tax effects resulting from the Tax Cuts and Jobs Act that was signed into law in December of 2017 (the “Act”). ASU 2018-02 is effective for our interim and annual reporting periods beginning January 1, 2018, and is to be applied either (a) at the beginning of the period of adoption or (b) retrospectively to each period in which the income tax effects of the Act related to items remaining in accumulated other comprehensive income are recognized. On January 1, 2018, we adopted ASU 2018-02 by recognizing an adjustment to the opening balance of retained earnings for certain tax effects related to net unrealized gains on equity investments. The comparative information has not been restated and continues to be reported under the accounting standards in effect for the period. Please see the table below for a summary of all transition adjustments from adoption of new accounting guidance.

ASU 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash* (a consensus of the FASB Emerging Issues Task Force (“ASU 2016-18”). ASU 2016-18 amends ASC 830, *Statement of Cash Flows* and requires restricted cash to be included with cash and cash equivalents when reconciling the beginning and ending amounts on the statement of cash flows. In certain states, we are restricted from using deposits received from our customers who enter into home sale contracts for general purposes unless we take measures to release state imposed restrictions on such deposits received from homebuyers, which may include posting blanket surety bonds. As a result, cash deposits with such restrictions are classified as restricted cash. On January 1, 2018, we adopted ASU 2016-18 using the retrospective transition method. The comparative information in our statement of cash flows has been restated and the impact from adoption of this guidance was not material to our statement of cash flows.

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ASU 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (a consensus of the Emerging Issues Task Force)* (“ASU 2016-15”). ASU 2016-15 amends ASC 830, *Statement of Cash Flows* and clarifies guidance on the classification of certain cash receipts and payments in the statement of cash flows. On January 1, 2018, we adopted ASU 2016-15 using the retrospective transition method. There were no items in our comparative statement of cash flows that required restatement as a result of the adoption of ASU 2016-15 and the impact from adoption of this guidance was not material to our statement of cash flows.

ASU 2016-01, *Financial Instruments-Overall: Recognition and Measurement of Financial Assets and Financial Liabilities* (“ASU 2016-01”). On January 1, 2018, we adopted ASU 2016-01 using a modified retrospective transition method. Prior to this amendment, our equity investments with readily determinable fair values were classified as available for sale with changes in fair value being reported through other comprehensive income. Under the amended standard, any changes in fair value of equity investments with readily determinable fair values are now recognized in net income. We adopted the changes from ASU 2016-01 by recognizing an adjustment to beginning retained earnings for our net unrealized gains/losses on equity investments with readily determinable fair values. The comparative information has not been restated and continues to be reported under the accounting standards in effect for the period. Please see the table below for a summary of all transition adjustments from adoption of new accounting guidance. The effect of the change on income before income taxes for the three and nine months ended September 30, 2018 was an increase of approximately \$2.9 million and \$3.0 million, respectively.

ASU 2014-09, *Revenue from Contracts with Customers* (“ASU 2014-09”). In May 2014, ASU 2014-09 was issued which created ASC Topic 606, *Revenue from Contracts with Customers* (“ASC 606”) and is a comprehensive new revenue recognition model. In addition, ASU 2014-09 amended ASC 340, *Other Assets and Deferred Costs*, by adding ASC 340-40, *Other Assets and Deferred Costs – Contracts with Customers* (“ASC 340-40”). On January 1, 2018, we adopted ASC 606 and ASC 340-40 using the modified retrospective transition method applied to contracts that were not completed as of January 1, 2018. We recognized the cumulative effect of initially applying ASC 606 and ASC 340-40 as an adjustment to the opening balance of retained earnings. The comparative information has not been restated and continues to be reported under the accounting standards in effect for the period. Please see the table below for a summary of all transition adjustments from adoption of the new accounting guidance. As a result of adopting ASC 606 and ASC 340-40, there was not a material impact to our consolidated balance sheets or consolidated statements of operations and comprehensive income. Furthermore, there were no significant changes to our internal controls, processes, or systems as a result of adoption of this new guidance.

As substantially all of our contracts are completed within a year, we will not disclose the value of unsatisfied performance obligations. At January 1, 2018 and September 30, 2018, receivables from contracts with customers were \$32.6 million and \$37.9 million, respectively, and are included in trade and other receivables on the accompanying consolidated balance sheets.

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The cumulative effect of the changes made to our consolidated January 1, 2018 balance sheet for the adoption of ASU 2018-02, ASU 2016-01 and ASU 2014-09 was as follows:

	Balance at	Adjustments	Adjustments	Adjustments	Balance at
	December 31, 2017 (Dollars in thousands)	due to ASU 2018-02	due to ASU 2016-01	due to ASU 2014-09	January 1, 2018
Balance Sheet					
Assets:					
Homebuilding:					
Housing completed or under construction	\$936,685	\$ -	\$ -	\$ 7,406	\$944,091
Property and equipment, net	26,439	-	-	25,270	51,709
Prepaid and other assets	75,666	-	-	(34,227)	41,439
Deferred tax asset, net	41,480	-	-	(573)	40,907
Financial Services:					
Other assets	9,617	-	-	3,898	13,515
Stockholders' Equity:					
Retained earnings	258,164	(860)	4,852	1,774	263,930
Accumulated other comprehensive income	3,992	860	(4,852)	-	-

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As a result of our adoption of ASU 2014-09, our significant accounting policies have been updated as follows:

Revenue Recognition for Homebuilding Segments. We recognize home sale revenues from home deliveries when we have satisfied the performance obligations within the sales agreement, which is generally when title to and possession of the home are transferred to the buyer at the home closing date. Revenue from a home delivery includes the base sales price and any purchased options and upgrades and is reduced for any sales price incentives.

We generally do not record the sale of a home or recognize the associated revenue if all of the following criteria are present: (1) HomeAmerican Mortgage Corporation (“HomeAmerican”) originates the mortgage loan and has not sold the mortgage loan, or loans, as of the end of the pertinent reporting period; and (2) the homebuyer does not meet certain collectability thresholds, based on the type of mortgage loan, related to their credit score, debt to income ratio and loan to value ratio. The deferral is subsequently recognized at the time HomeAmerican sells the respective loan to a third-party purchaser. In the event the gross margin is a loss, we recognize such loss at the time the home is closed.

In certain states that we build, we are not always able to complete certain outdoor features (such as landscaping or pools) prior to closing the home. To the extent these separate deliverables are not complete upon the closing of a home, we defer home sale revenues related to incomplete outdoor features, and recognize revenue upon completion of the outdoor features.

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, 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 and performance obligations have been completed on a house-by-house basis.

When a home is closed, we may not have paid for all costs necessary to complete the construction of the home. This includes (1) construction that has been completed on a house but has not yet been billed or (2) work still to be performed on a home (such as limited punch-list items or certain outdoor features). For each of these items, we create an estimate of the total expected costs to be incurred and, with the exclusion of outdoor features, the estimated total costs for those items, less any amounts paid to date, are included in home cost of sales. Actual results could differ from such estimates. For incomplete outdoor features, we will defer the revenue and any cost of sales on this separate stand-alone deliverable until complete.

Costs Related to Sales Facilities. Certain marketing costs related to model homes or on-site sales facilities are either recorded as inventory, capitalized as property and equipment, or expensed as incurred. Costs related to interior and exterior upgrades to the home that will be sold as part of the home, such as wall treatments and additional upgraded landscaping, are recorded as housing completed or under construction. Costs to furnish and ready the model home or on-site sales facility that will not be sold as part of the model home, such as furniture, construction of the sales facility parking lot or construction of the sales center, are capitalized as property and equipment, net. Other costs incurred related to the marketing of the community and readying the model home for sale are expensed as incurred.

Property and Equipment, net. Property and equipment is carried at cost less accumulated depreciation. For property and equipment related to on-site sales facilities, depreciation is recorded using the units of production method as homes are delivered. For all other property and equipment, depreciation is recorded using a straight-line method over the estimated useful lives of the related assets, which range from 2 to 29 years.

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Accounting Standards Issued But Not Yet Adopted

In February 2016, the Financial Accounting Standards Board (“FASB”) issued ASU 2016-02, *Leases* (“ASU 2016-02”), which requires a lessee to recognize a right-of-use asset and a corresponding lease liability for virtually all leases. The liability will be equal to the present value of the remaining lease payments while the right-of-use asset will be based on the liability, subject to adjustment, such as for initial direct costs. In addition, ASU 2016-02 expands the disclosure requirements for lessees. The Company is still evaluating the impact of the new standard and has begun evaluating the population of all leases and related systems and internal control considerations. The Company will be required to adopt the new standard effective January 1, 2019, and the Company’s consolidated balance sheets will be impacted by the recording of a lease liability and right of use asset for virtually all of its current operating leases. As of September 30, 2018, the Company had remaining contractual obligations for operating leases, primarily associated with our office facilities, of \$43.1 million. The amount of which and the potential impact on the consolidated statements of operations and comprehensive income and consolidated statements of cash flows has yet to be determined.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments—Credit Losses (Topic 326) Measurement of Credit Losses on Financial Instruments* (“ASU 2016-13”), which requires measurement and recognition of expected credit losses for financial assets held. The amendments in ASU 2016-13 eliminate the probable threshold for initial recognition of a credit loss in current GAAP and reflect an entity’s current estimate of all expected credit losses. ASU 2016-13 is effective for our interim and annual reporting periods beginning January 1, 2021, and is to be applied using a modified retrospective transition method. Earlier adoption is permitted. We do not plan to early adopt ASU 2016-13 and with our current holdings of financial instruments that are subject to credit losses, we do not believe adoption of this guidance will be material to our financial statements.

3. Segment Reporting

An operating segment is defined as a component of an enterprise for which discrete financial information is available and is reviewed regularly by the Chief Operating Decision Maker (“CODM”), or decision-making group, to evaluate performance and make operating decisions. We have identified our CODM as two key executives—the Chief Executive Officer (“CEO”) and the Chief Operating Officer (“COO”).

We have identified each homebuilding division as an operating segment. Our homebuilding 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, Washington and Oregon)

Mountain (Colorado and Utah)
East (Virginia, Florida and Maryland)

Our financial services business consists of the operations of the following operating segments: (1) 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.

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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, treasury, information technology, insurance, 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 operations section of our consolidated statements of operations and comprehensive income.

The following table summarizes revenues for our homebuilding and financial services operations:

	Three Months Ended September 30, 2018		Nine Months Ended September 30, 2018	
	2017		2017	
	(Dollars in thousands)			
Homebuilding				
West	\$409,001	\$326,804	\$1,120,316	\$959,641
Mountain	272,989	167,066	750,162	564,558
East	84,037	92,417	252,845	274,785
Total homebuilding revenues	\$766,027	\$586,287	\$2,123,323	\$1,798,984
Financial Services				
Mortgage operations	\$11,919	\$11,176	\$39,162	\$36,056
Other	7,692	6,288	20,856	18,460
Total financial services revenues	\$19,611	\$17,464	\$60,018	\$54,516

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

	Three Months Ended September 30, 2018 2017		Nine Months Ended September 30, 2018 2017	
	(Dollars in thousands)			
Homebuilding				
West	\$28,947	\$17,746	\$91,028	\$54,335
Mountain	34,697	18,326	94,736	61,097
East	3,771	2,613	11,287	9,989
Corporate	(14,432)	41,484	(41,270)	20,262
Total homebuilding pretax income	\$52,983	\$80,169	\$155,781	\$145,683
Financial Services				
Mortgage operations	\$6,702	\$5,857	\$23,262	\$21,093
Other	7,735	3,654	15,525	11,158
Total financial services pretax income	\$14,437	\$9,511	\$38,787	\$32,251
Total pretax income	\$67,420	\$89,680	\$194,568	\$177,934

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 our cash and cash equivalents, marketable securities and deferred tax assets. The assets in our financial services segment consist mostly of cash and cash equivalents, marketable securities and mortgage loans held-for-sale.

	September 30, 2018	December 31, 2017
	(Dollars in thousands)	
Homebuilding assets		
West	\$1,274,955	\$1,084,756
Mountain	795,767	674,057
East	181,253	201,684
Corporate	427,737	597,589
Total homebuilding assets	\$2,679,712	\$2,558,086
Financial services assets		
Mortgage operations	\$127,725	\$152,345
Other	100,733	69,861
Total financial services assets	\$228,458	\$222,206
Total assets	\$2,908,170	\$2,780,292

Table of Contents**4. Earnings Per Share**

ASC 260 requires a company that has participating security holders (for example, holders of unvested restricted stock that have non-forfeitable dividend rights) to utilize the two-class method for calculating earnings per share ("EPS") 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)). Our common shares outstanding are comprised of shareholder owned common stock and shares of unvested restricted stock held by participating security holders. Basic EPS is calculated by dividing income or loss attributable to common stockholders by the weighted average number of shares of common stock outstanding, excluding participating shares in accordance with ASC 260. To calculate diluted EPS, basic EPS is adjusted to include the effect of potentially dilutive stock options outstanding. The table below shows our basic and diluted EPS calculations.

	Three Months Ended September 30, 2018		2017		Nine Months Ended September 30, 2018		2017	
	(Dollars in thousands, except per share amounts)							
Numerator								
Net income	\$53,392		\$61,163		\$156,055		\$117,283	
Less: distributed earnings allocated to participating securities	(106)	(68)	(307)	(196)
Less: undistributed earnings allocated to participating securities	(222)	(244)	(613)	(375)
Net income attributable to common stockholders (numerator for basic earnings per share)	53,064		60,851		155,135		116,712	
Add back: undistributed earnings allocated to participating securities	222		244		613		375	
Less: undistributed earnings reallocated to participating securities	(218)	(240)	(602)	(369)
Numerator for diluted earnings per share under two class method	\$53,068		\$60,855		\$155,146		\$116,718	
Denominator								
Weighted-average common shares outstanding	56,171,619		55,782,389		56,023,996		55,623,225	
Add: dilutive effect of stock options	1,055,040		1,026,819		1,005,719		805,022	
Denominator for diluted earnings per share under two class method	57,226,659		56,809,208		57,029,715		56,428,247	
Basic Earnings Per Common Share	\$0.94		\$1.09		\$2.77		\$2.10	
Diluted Earnings Per Common Share	\$0.93		\$1.07		\$2.72		\$2.07	

Diluted EPS for the three and nine months ended September 30, 2018 excluded options to purchase approximately 0.6 and 0.6 million shares of common stock, respectively, because the effect of their inclusion would be anti-dilutive. For the same periods in 2017, diluted EPS excluded options to purchase approximately 0.7 and 1.1 million shares, respectively.

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Table of Contents**5. Accumulated Other Comprehensive Income**

The following table sets forth our changes in accumulated other comprehensive income (“AOCI”):

	Three Months Ended September 30, 2018	Three Months Ended September 30, 2017	Nine Months Ended September 30, 2018	Nine Months Ended September 30, 2017
	(Dollars in thousands)			
Beginning balance ¹	\$- \$11,176	\$3,992	\$7,730	
Adoption of accounting standards (Note 2)	- -	(3,992)	-	
Other comprehensive income before reclassifications	- 1,778	-	6,201	
Amounts reclassified from AOCI ²	- (10,128)	-	(11,105)	
Ending balance	\$- \$2,826	\$-	\$2,826	
Unrealized gains on available-for-sale metropolitan district bond securities ¹ :				
Beginning balance	\$- \$14,825	\$-	\$14,341	
Other comprehensive income (loss) before reclassifications	- 7,400	-	7,884	
Amounts reclassified from AOCI	- (22,225)	-	(22,225)	
Ending balance	\$- \$-	\$-	\$-	
Total ending AOCI	\$- \$2,826	\$-	\$2,826	

(1) All amounts net-of-tax.

(2) See separate table below for details about these reclassifications.

During the first quarter of 2018, an election was made to reclassify the income tax effects of the Act related to net unrealized gains on equity investments from accumulated other comprehensive income to retained earnings. See Note 2 for further discussion of adoption of new accounting standards.

The Metropolitan District Limited Tax General Obligation Capital Appreciation Bonds Series 2007 (the “Metro Bonds”) were acquired from a quasi-municipal corporation in the state of Colorado, which was formed to help fund and maintain the infrastructure associated with a master-planned community developed by our Company. During the 2017 third quarter, we sold the Metro Bonds for net proceeds of \$44.3 million. With a cost basis of \$8.4 million, we recorded a realized gain of \$35.8 million, which is included in interest and other income in the homebuilding section of our consolidated statements of operations and comprehensive income for the three and nine months ended

September 30, 2017.

The following table sets forth the activity, including the Metro Bonds discussed above, related to reclassifications out of accumulated other comprehensive income:

Affected Line Item in the Statements of Operations	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2018
	2017	2017
	(Dollars in thousands)	
Homebuilding: Interest and other income	\$- \$52,211	\$- \$53,622
Homebuilding: Other-than-temporary impairment of marketable securities	- -	- (51)
Financial services: Interest and other income	- -	- 347
Financial services: Other-than-temporary impairment of marketable securities	- (29)	- (160)
Income before income taxes	- 52,182	- 53,758
Provision for income taxes	- (19,829)	- (20,428)
Net income	\$- \$32,353	\$- \$33,330

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Table of Contents**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.

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	
		September 30, 2018	December 31, 2017
		(Dollars in thousands)	
Cash and cash equivalents			
Debt securities (available-for-sale)	Level 1	\$ 34,882	\$ 99,863
Marketable securities			
Equity securities	Level 1	\$ 49,006	\$ 42,004
Debt securities (available-for-sale)	Level 1	-	49,634
Total marketable securities		\$ 49,006	\$ 91,638
Mortgage loans held-for-sale, net	Level 2	\$ 114,836	\$ 138,114

The following methods and assumptions were used to estimate the fair value of each class of financial instruments as of September 30, 2018 and December 31, 2017.

Cash and cash equivalents (excluding debt securities with an original maturity of three months or less), restricted cash, trade and other receivables, prepaid and other assets, accounts payable, accrued liabilities and borrowings on our revolving credit facility. Fair value approximates carrying value.

Equity securities. Our equity securities consist of holdings in common stock, preferred stock and exchange traded funds. As of September 30, 2018, all of our equity securities were recorded at fair value with all changes in fair value recorded to either interest and other income or other expense, dependent upon whether there was a net gain or loss, respectively, in the homebuilding section or financial services section of our consolidated statements of operations and comprehensive income. As of December 31, 2017, all of our equity securities were treated as available-for-sale investments and as such, were recorded at fair value with all changes in fair value initially recorded through AOCI, subject to an assessment to determine if an unrealized loss, if applicable, was other-than-temporary. See Note 2 for further discussion of adoption of new accounting standards.

Debt securities. Our debt securities consist of U.S. government securities. As of September 30, 2018 and December 31, 2017, all of our debt securities were treated as available-for-sale investments and, as such, are recorded at fair value with all changes in fair value initially recorded through AOCI, subject to an assessment to determine if any unrealized loss, if applicable, is other-than-temporary.

Each quarter we assess all of our securities in an unrealized loss position (excluding marketable equity securities subsequent to the adoption of ASU 2016-01 – see Note 2 for further discussion of adoption of new accounting standards) for a potential other-than-temporary impairment (“OTTI”). If the unrealized loss is determined to be other-than-temporary, an OTTI is recorded in other-than-temporary impairment of marketable securities in the homebuilding or financial services sections of our consolidated statements of operations and comprehensive income. During the three and nine months ended September 30, 2017, we recorded pretax OTTI’s of \$0.0 million and \$0.2 million, respectively. No such impairments were recorded during the three and n