MDC HOLDINGS INC
Form 10-Q/A
October 11, 2006

Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q/A
Amendment No. 1

(Mark One)

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

For the quarterly period ended June 30, 2006

OR

o **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 **Denver, Colorado** **(Address of principal executive offices)**	**80237** **(Zip code)**

(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 þ No o

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

Large Accelerated Filer þ **Accelerated Filer** o **Non-Accelerated Filer** o

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

As of June 30, 2006, 44,967,000 shares of M.D.C. Holdings, Inc. common stock were outstanding.

Table of Contents

EXPLANATORY NOTE: This Form 10-Q/A is being filed to provide additional segment reporting footnote disclosure related to our homebuilding operations. We have restated the accompanying Unaudited Consolidated Financial Statements to revise our segment disclosures for all periods presented by disaggregating our one homebuilding reportable segment into four reportable segments. See our revised disclosures in Note 11 to the Unaudited Consolidated Financial Statements. This amendment does not reflect events occurring after the filing of our Quarterly Report on Form 10-Q on August 7, 2006, nor does it modify or update those disclosures, except as discussed above or in Note 2 to the Unaudited Consolidated Financial Statements.

This Form 10-Q/A has all Items included in our Form 10-Q filed August 7, 2006. However, this Form 10-Q/A amends and restates only Part I, Items 1, 2 and 4 of the June 30, 2006 Quarterly Report on Form 10-Q, in each case solely to be responsive to certain disclosure comments, primarily relating to segment reporting, received from the Division of Corporation Finance of the Securities and Exchange Commission. The restatement has no impact for any periods presented on: our total assets, liabilities or stockholders equity included in the Consolidated Balance Sheets; net income or earnings per share amounts included in the Consolidated Statements of Income; and the Consolidated Statements of Cash Flows.

M.D.C. HOLDINGS, INC. AND SUBSIDIARIES
FORM 10-Q/A
FOR THE QUARTER ENDED JUNE 30, 2006
INDEX

		Page No.
Part I. Financial Information:		
Item 1.	Unaudited Consolidated Financial Statements:	
	Consolidated Balance Sheets at June 30, 2006 and December 31, 2005	1
	Consolidated Statements of Income for the three and six months ended June 30, 2006 and 2005	2
	Consolidated Statements of Cash Flows for the six months ended June 30, 2006 and 2005	3
	Notes to Unaudited Consolidated Financial Statements	4
Item 2.	Management s Discussion and Analysis of Financial Condition and Results of Operations	24
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	41
Item 4.	Controls and Procedures	42
Part II. Other Information:		
Item 1.	Legal Proceedings	43
Item 1A.	Risk Factors	43
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	45
Item 3.	Defaults Upon Senior Securities	45
Item 4.	Submission of Matters to a Vote of Security Holders	45
Item 5.	Other Information	46
Item 6.	Exhibits	46
Signature		47

Certification of CEO Pursuant to Section 302
Certification of CFO Pursuant to Section 302
Certification of CEO Pursuant to Section 906
Certification of CFO Pursuant to Section 906

Table of Contents

ITEM 1. Unaudited Consolidated Financial Statements

M.D.C. HOLDINGS, INC.
Consolidated Balance Sheets
(In thousands)
(Unaudited)

	June 30, 2006	December 31, 2005
ASSETS		
Cash and cash equivalents	$ 91,484	$ 214,531
Restricted cash	6,855	6,742
Home sales receivables	98,629	134,270
Mortgage loans held in inventory	163,373	237,376
Inventories, net		
Housing completed or under construction	1,512,009	1,320,106
Land and land under development	1,760,077	1,677,948
Property and equipment, net	46,277	49,119
Deferred income taxes	71,131	54,319
Prepaid expenses and other assets, net	207,101	165,439
Total Assets	$ 3,956,936	$ 3,859,850
LIABILITIES		
Accounts payable	$ 224,666	$ 201,747
Accrued liabilities	410,455	442,409
Income taxes payable	30,933	102,656
Related party liabilities (See Note 15)		8,100
Homebuilding line of credit		
Mortgage line of credit	168,163	156,532
Senior notes, net	996,486	996,297
Total Liabilities	1,830,703	1,907,741
COMMITMENTS AND CONTINGENCIES		
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; 44,981,000 and 44,967,000 issued and outstanding at June 30, 2006 and 44,642,000 and 44,630,000 issued and outstanding at December 31, 2005	450	447
Additional paid-in capital	746,637	722,291
Retained earnings	1,382,427	1,232,971
Unearned restricted stock	(2,000)	(2,478)
Accumulated other comprehensive loss	(622)	(622)
Less treasury stock, at cost; 14,000 and 12,000 shares, respectively, at June 30, 2006 and December 31, 2005	(659)	(500)

Total Stockholders Equity	2,126,233	1,952,109
Total Liabilities and Stockholders Equity	$ 3,956,936	$ 3,859,850

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

-1-

Table of Contents

M.D.C. HOLDINGS, INC.
Consolidated Statements of Income
(In thousands, except per share amounts)
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	**2005**	**2006**	**2005**
REVENUE				
Home sales revenue	$ 1,195,083	$ 1,029,553	$ 2,314,391	$ 1,946,384
Land sales revenue	13,639		15,476	1,296
Other revenue	24,214	16,787	45,763	32,576
Total Revenue	1,232,936	1,046,340	2,375,630	1,980,256
COSTS AND EXPENSES				
Home cost of sales	917,414	734,772	1,732,003	1,391,552
Land cost of sales	13,400		15,774	790
Marketing expense	31,568	25,008	60,603	47,326
Commission expense	37,394	28,680	70,237	54,526
General and administrative expenses	110,799	93,840	220,495	185,993
Related party expenses	127	63	1,803	163
Total Costs and Expenses	1,110,702	882,363	2,100,915	1,680,350
Income before income taxes	122,234	163,977	274,715	299,906
Provisions for income taxes	(45,743)	(61,354)	(102,803)	(112,652)
NET INCOME	$ 76,491	$ 102,623	$ 171,912	$ 187,254
EARNINGS PER SHARE				
Basic	$ 1.70	$ 2.35	$ 3.83	$ 4.30
Diluted	$ 1.66	$ 2.25	$ 3.74	$ 4.10
WEIGHTED-AVERAGE SHARES				
Basic	44,939	43,718	44,880	43,584
Diluted	45,972	45,703	45,967	45,649
DIVIDENDS DECLARED PER SHARE	$ 0.25	$ 0.18	$ 0.50	$ 0.33

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

Table of Contents

M.D.C. HOLDINGS, INC.
Consolidated Statements of Cash Flows
(In thousands)
(Unaudited)

	Six Months Ended June 30, 2006	2005
OPERATING ACTIVITIES		
Net income	$ 171,912	$ 187,254
Adjustments to reconcile net income to net cash used in operating activities		
Amortization of deferred marketing costs	19,086	14,750
Depreciation and amortization of long-lived assets	9,423	6,836
Amortization of debt discount	189	149
Deferred income taxes	(16,812)	(1,409)
Stock-based compensation expense	7,142	699
Excess tax benefits from stock-based compensation	(1,486)	
Net changes in assets and liabilities		
Home sales receivables	35,641	(38,382)
Housing completed or under construction	(191,903)	(332,028)
Land and land under development	(82,129)	(193,156)
Prepaid expenses and other assets	(14,989)	(42,255)
Mortgage loans held in inventory	74,003	16,814
Accounts payable and accrued liabilities	(72,626)	52,795
Restricted cash	(113)	(1,941)
Other, net	(49,609)	1,830
Net cash used in operating activities	(112,271)	(328,044)
INVESTING ACTIVITIES		
Net purchase of property and equipment	(4,331)	(11,724)
FINANCING ACTIVITIES		
Lines of credit		
Advances	437,531	386,300
Principal payments	(425,900)	(380,899)
Excess tax benefits from stock-based compensation	1,486	
Dividend payments	(22,456)	(14,647)
Proceeds from exercise of stock options	2,894	9,412
Net cash (used in) provided by financing activities	(6,445)	166
Net decrease in cash and cash equivalents	(123,047)	(339,602)
Cash and cash equivalents		
Beginning of period	214,531	400,959
End of period	$ 91,484	$ 61,357

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

Table of Contents

M.D.C. HOLDINGS, INC.
Notes to Unaudited Consolidated Financial Statements

1. Basis of Presentation

The Unaudited Consolidated Financial Statements of M.D.C. Holdings, Inc. (MDC or the Company, 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 accounting principles generally accepted in the United States of America 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 June 30, 2006 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 Form 10-K/A for the year ended December 31, 2005 filed October 11, 2006.

The Company has experienced significant seasonality and quarter-to-quarter variability in homebuilding activity levels. In general, the number of homes closed and associated home sales revenue historically have increased during the third and fourth quarters, compared with the first and second quarters. The Company believes that this seasonality reflects the historical tendency of homebuyers to purchase new homes in the spring with the goal of closing in the fall or winter, as well as the scheduling of construction to accommodate seasonal weather conditions. Also, the Company has experienced seasonality in the financial services operations because loan originations correspond with the closing of homes in the homebuilding operations. The Consolidated Statements of Income for the three and six months ended June 30, 2006 and Consolidated Statements of Cash Flows for the six months ended June 30, 2006 are not necessarily indicative of the results to be expected for the full year. Refer to economic conditions described under the caption Risk Factors in Part II, Item 1A of this Quarterly Report on Form 10-Q/A and Risk Factors Relating to our Business in Item 1A of the Company s December 31, 2005 Annual Report on Form 10-K. There are no assurances as to the results of operations for the third or fourth quarter of 2006.

The following table summarizes, by quarter, information concerning the home sales revenue associated with homes closed during 2006, 2005 and 2004 (in thousands).

	Three Months Ended			
	March 31,	**June 30,**	**September 30,**	**December 31,**
2006				
Home sales revenue	$1,119,308	$1,195,083	N/A	N/A
2005				
Home sales revenue	$ 916,831	$1,029,553	$1,147,757	$1,708,734
2004				
Home sales revenue	$ 746,429	$ 861,537	$1,007,134	$1,316,913

2. Reclassifications

In conjunction with the filing of this Form 10-Q/A, the Company has reclassified the presentation of the Consolidated Balance Sheets and Consolidated Statements of Income. The Consolidated Balance Sheets and Consolidated Statements of Income previously disclosed assets, liabilities, revenue and expenses by each reportable segment. As a result of the restatement to the segment disclosures (see Note 11), assets, liabilities, revenue and expenses are now being presented on a consolidated basis. The Company s total assets, total liabilities and net income have not been affected for any periods presented as a result of this reclassification. Certain other prior year balances have been reclassified to conform to the current year s presentation.

M.D.C. HOLDINGS, INC.
Notes to Unaudited Consolidated Financial Statements

3. Recent Accounting Pronouncements

On July 13, 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation (FIN) No. 48, Accounting for Uncertainty in Income Taxes (FIN 48). FIN 48 is an interpretation of Statement of Financial Accounting Standards (SFAS) No. 109, Accounting for Income Taxes. FIN 48 provides interpretive guidance for the financial statement recognition and measurement of a tax position taken, or expected to be taken, in a tax return. FIN 48 requires the affirmative evaluation that it is more-likely-than-not, based on the technical merits of a tax position, that an enterprise is entitled to economic benefits resulting from positions taken in income tax returns. 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. FIN 48 also requires companies to disclose additional quantitative and qualitative information in their financial statements about uncertain tax positions. FIN 48 is effective for fiscal years beginning after December 15, 2006, and the cumulative effect of applying FIN 48 shall be reported as an adjustment to the opening balance of retained earnings for that fiscal year. The Company is currently evaluating the impact, if any, that FIN 48 may have on its financial position, results of operations or cash flows.

In February 2006, the FASB issued SFAS No. 155, Accounting for Certain Hybrid Financial Instruments, an amendment of FASB Statements No. 133 and 140 (SFAS 155). SFAS 155 eliminates the exemption from applying SFAS 133 to interests in securitized financial assets so that similar instruments are accounted for similarly regardless of the form of the instrument. SFAS 155 also allows a preparer to elect fair value measurement at acquisition, at issuance, or when a previously recognized financial instrument is subject to a remeasurement event, on an instrument-by-instrument basis, in cases in which a derivative would otherwise be bifurcated. At the adoption of SFAS 155, any difference between the total carrying amount of the individual components of any existing hybrid financial instrument and the fair value of the combined hybrid financial instrument should be recognized as a cumulative-effect adjustment to the Company s beginning retained earnings. SFAS 155 is effective for the Company for all financial instruments acquired or issued after January 1, 2007. The Company is currently evaluating the impact, if any, that SFAS 155 may have on its financial position, results of operations or cash flows.

In March 2006, the FASB issued SFAS No. 156, Accounting for Servicing of Financial Assets (SFAS 156), an amendment of SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. SFAS 156 requires that servicing assets and servicing liabilities be recognized at fair value, if practicable, when the Company enters into a servicing agreement and allows two alternatives, the amortization and fair value measurement methods, as subsequent measurement methods. This accounting standard is effective for all new transactions occurring as of the beginning of fiscal years beginning after September 15, 2006. The Company is currently evaluating the impact, if any, that SFAS 156 may have on its financial position, results of operations or cash flows.

4. Stock-Based Compensation

Stock-Based Compensation Policy - Effective January 1, 2006, the Company adopted the fair value recognition provisions of SFAS No. 123 (revised 2004), Share-Based Payment (SFAS 123(R)), using the modified prospective transition method and, therefore, has not restated results for prior periods. Under this transition method, stock-based compensation expense for the three and six months ended June 30, 2006 includes compensation expense for all share-based payment awards granted prior to, but not yet vested at December 31, 2005, based on the grant date fair value estimated in accordance with the provisions of SFAS No. 123, Accounting for Stock-Based Compensation (SFAS 123). Stock-based compensation expense for all share-based payment awards granted after December 31, 2005 is based on the grant date fair value estimated in accordance with the provisions of SFAS 123(R). The Company recognizes these compensation costs net of an estimated annual forfeiture rate and recognizes the compensation costs for only those awards expected to vest on a straight-line basis over the requisite

M.D.C. HOLDINGS, INC.
Notes to Unaudited Consolidated Financial Statements (Continued)

service period of the award, which is currently the option vesting term of up to seven years. Prior to the adoption of SFAS 123(R), the Company recognized stock-based compensation expense in accordance with Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees (APB 25).

In March 2005, the SEC issued Staff Accounting Bulletin No. 107, Share-Based Payment (SAB 107), regarding the SEC s interpretation of SFAS 123(R) and the valuation of share-based payment awards for public companies. The Company has applied the provisions of SAB 107 in its adoption of SFAS 123(R). Additionally, upon the adoption of SFAS 123(R), tax benefits resulting from tax deductions in excess of the compensation cost recognized for those options are classified as financing cash flows. Prior to the adoption of SFAS 123(R), the Company presented the tax benefit of stock option exercises as operating cash flows.

As a result of adopting SFAS 123(R), income before income taxes for the three and six months ended June 30, 2006 were $3.0 million and $6.0 million lower, respectively, and net income for the three and six months ended June 30, 2006 were $1.9 million and $3.8 million lower, respectively, than if the Company had continued to account for share-based payment awards under APB 25. The Company has recorded all stock-based compensation expense to general and administrative expense in the Consolidated Statements of Income.

Pro Forma Disclosures Pursuant to SFAS 123 - As of December 31, 2005, the Company had only granted stock options with exercise prices that were equal to or greater than the fair market value of the Company s common stock on the date of grant. Accordingly, prior to January 1, 2006, stock-based compensation expense was recorded only in association with the vesting of restricted stock and unrestricted stock awards and was recorded to expense ratably over the associated service period, which was generally the vesting term. Additionally, prior to January 1, 2006, the Company provided pro forma disclosure amounts in accordance with SFAS No. 148, Accounting for Stock-Based Compensation Transition and Disclosure (SFAS 148), as if the fair value method defined by SFAS 123 had been applied to all share-based payment awards. The following table illustrates the effect on net income and earnings per share if the fair value method prescribed by SFAS 123, as amended by SFAS 148, had been applied to all outstanding and unvested share-based payment awards during the three and six months ended June 30, 2005 (in thousands, except per share amounts).

	Three Months Ended June 30, 2005	Six Months Ended June 30, 2005
Net income, as reported	$ 102,623	$ 187,254
Deduct stock-based compensation expense determined using the fair value method, net of related tax effects	(2,599)	(5,016)
Pro forma net income	$ 100,024	$ 182,238
Earnings per share		
Basic as reported	$ 2.35	$ 4.30
Basic pro forma	$ 2.29	$ 4.18
Diluted as reported	$ 2.25	$ 4.10
Diluted pro forma	$ 2.19	$ 3.99

Determining Fair Value of Share-Based Awards - As part of the adoption of SFAS 123(R), the Company examined its historical pattern of option exercises in an effort to determine if there were any discernable activity patterns based on certain employee and non-employee populations. Based upon this evaluation, the Company identified three distinct populations: (1) executives consisting of the Company s Chief Executive Officer, Chief Operating Officer, Chief Financial Officer and General Counsel

Table of Contents

M.D.C. HOLDINGS, INC.
Notes to Unaudited Consolidated Financial Statements (Continued)

(collectively, the Executives); (2) non-executive employees (Non-Executives); and (3) non-employee members of the Company s board of directors (Directors). The Company has used the Black-Scholes option pricing model to value stock options for each of these populations.

The fair values for stock options granted during the three and six months ended June 30, 2006 and 2005 were estimated using the Black-Scholes option pricing model with the following weighted-average assumptions.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Expected volatility	46.1%	44.2%	46.0%	44.6%
Risk-free interest rate	4.7%	3.8%	4.7%	3.8%
Dividend yield rate	1.2%	0.6%	1.2%	0.7%
Expected lives of options	3.8 yrs.	6.0 yrs.	3.8 yrs.	6.0 yrs.

Based on calculations using the Black-Scholes option pricing models, the weighted average grant date fair value of stock options was $22.03 and $30.50 for the three months ended June 30, 2006 and 2005, respectively, and $22.41 and $31.79 for the six months ended June 30, 2006 and 2005, respectively. These assumptions were used for the stock options granted only to Non-Executives during the three and six months ended June 30, 2006 and 2005. No stock option awards were granted during these periods to Executives or Directors.

The expected volatility is based on the historical volatility in the price of the Company s common stock over the most recent period commensurate with the estimated expected life of the Company s 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 the Company s employee stock options. The dividend yield assumption is based on the Company s history and expectation of dividend payouts. 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.

SFAS 123(R) requires an annual forfeiture rate to be estimated at the time of grant for all share-based payment awards granted subsequent to January 1, 2006, and revised, if necessary, in subsequent periods if the actual forfeiture rate differs from the Company s estimate. Additionally, in accordance with SFAS 123(R), the Company has estimated an annual forfeiture rate to be applied to all share-based payment awards which were unvested as of December 31, 2005 in determining the number of awards expected to vest in the future. The Company estimated the annual forfeiture rate to be 25% for share-based payment awards granted to Non-Executives and 0% for share-based payment awards granted to Executives and Directors, based on the terms of their awards, as well as historical forfeiture experience. In the Company s pro forma information required under SFAS 123 for the periods prior to 2006, the Company accounted for forfeitures as they occurred.

M.D.C. HOLDINGS, INC.
Notes to Unaudited Consolidated Financial Statements (Continued)

Stock Option Award Activity - Stock option activity under the Company s option plans at June 30, 2006 and changes during the six months ended June 30, 2006 were as follows.

	Number of Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2005	5,659,766	$ 40.54		
Granted	25,000	$ 60.15		
Exercised	(133,610)	$ 21.66		
Cancelled	(200,669)	$ 54.16		
Outstanding at June 30, 2006	5,350,487	$ 40.59	6.40	$ 62,407

The following table summarizes information concerning stock options granted to Executives, Non-Executives and Directors that are vested at June 30, 2006, as well as stock options granted but unvested at June 30, 2006 that the Company expects will vest in future periods.

	Vested and Expected to Vest at June 30, 2006			
	Number of Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in thousands)
Executives	3,875,815	$ 36.24		
Non-Executives	523,887	$ 43.48		
Directors	303,325	$ 61.41		
Total	4,703,027	$ 38.67	6.22	$ 62,363

The following table summarizes information concerning stock options granted to Executives, Non-Executives and Directors that are exercisable at June 30, 2006.