

TOUSA INC
Form 10-Q
May 27, 2009

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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, 2008

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: 001-32322
TOUSA, INC.**

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

76-0460831
(I.R.S. Employer
Identification No.)

4000 Hollywood Blvd., Suite 400 N
Hollywood, Florida
(Address of principal executive offices)

33021
(ZIP code)

(954) 364-4000

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

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes

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 whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

(Do not check if a 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

APPLICABLE ONLY TO CORPORATE ISSUERS:

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Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 59,604,169 shares of common stock as of May 11, 2009.

**TOUSA, INC. AND SUBSIDIARIES
DEBTOR-IN-POSSESSION
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TOUSA, INC. AND SUBSIDIARIES
DEBTOR-IN-POSSESSION
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
(Dollars in millions, except par value)

	September 30, 2008 (Unaudited)	December 31, 2007
ASSETS		
HOMEBUILDING:		
Cash and cash equivalents:		
Unrestricted	\$ 277.5	\$ 67.2
Restricted	19.9	5.1
Inventory:		
Deposits	19.2	56.9
Homesites and land under development	235.7	633.0
Residences completed and under construction	282.9	555.9
Inventory not owned	9.6	26.0
	547.4	1,271.8
Property and equipment, net	15.2	24.6
Investments in unconsolidated joint ventures	3.0	9.0
Receivables from unconsolidated joint ventures		0.3
Other assets	62.0	330.0
Goodwill		11.2
Assets held for sale	2.7	6.1
	927.7	1,725.3
FINANCIAL SERVICES:		
Cash and cash equivalents:		
Unrestricted	13.6	9.3
Restricted		5.6
Mortgage loans held for sale	5.0	15.0
Other assets	4.0	6.8
	22.6	36.7
Total assets	\$ 950.3	\$ 1,762.0
LIABILITIES AND STOCKHOLDERS DEFICIT		
HOMEBUILDING:		
Accounts payable and other liabilities	\$ 121.6	\$ 401.8
Customer deposits	17.8	33.9
Obligations for inventory not owned		32.0
Notes payable		1,585.3
Bank borrowings		168.5

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Liabilities associated with assets held for sale	0.4	0.9
	139.8	2,222.4
FINANCIAL SERVICES:		
Accounts payable and other liabilities	1.3	7.3
Bank borrowings		7.8
	1.3	15.1
Total liabilities not subject to compromise	141.1	2,237.5
Liabilities subject to compromise (Note 2)	2,080.0	
Total liabilities	2,221.1	2,237.5
Commitments and contingencies		

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	September 30, 2008 (Unaudited)	December 31, 2007
Stockholders' deficit:		
Preferred stock \$0.01 par value; 3,000,000 shares authorized; 117,500 issued and outstanding at September 30, 2008 and December 31, 2007	11.6	3.9
Common stock \$0.01 par value; 975,000,000 shares authorized; 59,604,169 shares issued and outstanding at September 30, 2008 and December 31, 2007	0.6	0.6
Additional paid-in capital	565.5	570.7
Accumulated deficit	(1,848.5)	(1,050.7)
Total stockholders' deficit	(1,270.8)	(475.5)
Total liabilities and stockholders' deficit	\$ 950.3	\$ 1,762.0

See accompanying notes to unaudited consolidated financial statements.

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TOUSA, INC. AND SUBSIDIARIES
DEBTOR-IN-POSSESSION
CONSOLIDATED STATEMENTS OF OPERATIONS
(Dollars in millions, except per share amounts)
(Unaudited)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2008	2007	2008	2007
HOMEBUILDING:				
Revenues:				
Home sales	\$ 246.6	\$ 449.6	\$ 814.4	\$ 1,542.3
Land sales	0.3	43.3	22.0	77.0
	246.9	492.9	836.4	1,619.3
Cost of sales:				
Home sales	194.1	370.1	713.1	1,250.0
Land sales	1.5	56.5	18.3	85.6
Inventory impairments and abandonment costs	97.1	504.5	574.1	628.4
Other		(0.8)		(5.0)
	292.7	930.3	1,305.5	1,959.0
Gross loss	(45.8)	(437.4)	(469.1)	(339.7)
Selling, general and administrative expenses	44.0	86.0	153.8	262.4
Loss (income) from unconsolidated joint ventures, net	(0.1)	9.2	(0.4)	8.8
Impairment of investments in and receivables from unconsolidated joint ventures	9.9	23.4	1.1	28.9
Provision for settlement of loss contingency		40.7		151.6
Goodwill impairments		2.7	11.2	40.9
Interest expense (see Note 3 for contractual interest)	16.9	10.0	53.7	10.2
Other expense (income), net	(0.8)	0.6	(2.7)	(1.5)
Homebuilding pretax loss	(115.7)	(610.0)	(685.8)	(841.0)
FINANCIAL SERVICES:				
Revenues	4.1	8.3	13.2	31.3
Expenses	4.6	8.1	18.0	26.1
Financial Services pretax income (loss)	(0.5)	0.2	(4.8)	5.2
Loss from continuing operations before reorganization items and taxes	(116.2)	(609.8)	(690.6)	(835.8)
Reorganization items, net (see Note 2)	18.7		105.4	

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Provision (benefit) for income taxes	(2.7)	6.0	(2.0)	(35.7)
Loss from continuing operations, net of taxes	(132.2)	(615.8)	(794.0)	(800.1)
Discontinued operations:				
Loss from discontinued operations	(0.6)	(3.9)	(3.8)	(11.8)
Loss from disposal of discontinued operations				(13.6)
Benefit for income taxes				(7.8)
Loss from discontinued operations, net of taxes	(0.6)	(3.9)	(3.8)	(17.6)
Net loss	(132.8)	(619.7)	(797.8)	(817.7)
Dividends and accretion of discount on preferred stock	2.5	2.2	7.7	2.2
Net loss attributable to common stockholders	\$ (135.3)	\$ (621.9)	\$ (805.5)	\$ (819.9)
LOSS PER COMMON SHARE, BASIC AND DILUTED:				
Loss from continuing operations	\$ (2.26)	\$ (10.36)	\$ (13.45)	\$ (13.46)
Loss from discontinued operations	(0.01)	(0.07)	(0.07)	(0.30)
Loss per common share	\$ (2.27)	\$ (10.43)	\$ (13.52)	\$ (13.76)
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING:				
Basic	59,604,169	59,604,169	59,604,169	59,601,119
Diluted	59,604,169	59,604,169	59,604,169	59,601,119

See accompanying notes to unaudited consolidated financial statements.

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TOUSA, INC. AND SUBSIDIARIES
DEBTOR-IN-POSSESSION
CONSOLIDATED STATEMENT OF STOCKHOLDERS DEFICIT
(Dollars in millions)
(Unaudited)

	Preferred		Common Stock			Additional	Accumulated	Total
	Shares	Amount	Shares	Amount	Capital	Deficit	Stockholders	Deficit
Balance at January 1, 2008	117,500	\$ 3.9	59,604,169	\$ 0.6	\$ 570.7	\$ (1,050.7)	\$	(475.5)
Stock option compensation expense					2.5			2.5
Dividends and accretion of preferred stock discount		7.7			(7.7)			
Net loss						(797.8)		(797.8)
Balance at September 30, 2008	117,500	\$ 11.6	59,604,169	\$ 0.6	\$ 565.5	\$ (1,848.5)	\$	(1,270.8)

See accompanying notes to unaudited consolidated financial statements.

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TOUSA, INC. AND SUBSIDIARIES
DEBTOR-IN-POSSESSION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in millions)
(Unaudited)

	Nine Months Ended	
	September 30,	
	2008	2007
Cash flows from operating activities:		
Net loss	\$ (797.8)	\$ (817.7)
Loss from discontinued operations	3.8	17.6
Loss from continuing operations	(794.0)	(800.1)
Adjustments to reconcile loss from continuing operations to net cash provided by (used in) operating activities:		
Depreciation and amortization	10.4	11.2
Non-cash compensation expense	2.5	3.0
Non-cash interest expense	38.4	8.0
Reorganization items, net	105.4	
Loss on early termination of debt		2.4
Provision for settlement of loss contingency		151.6
Loss on impairments of inventory and abandonment costs	574.1	628.4
Goodwill impairments	11.2	40.9
Write-down of receivables	5.7	
Deferred income taxes		(160.6)
Loss (income) from unconsolidated joint ventures	(0.4)	19.2
Distributions of earnings from unconsolidated joint ventures	0.2	0.9
Impairment of investments in and receivables from unconsolidated joint ventures	1.1	28.9
Changes in operating assets and liabilities:		
Restricted cash	(9.2)	28.6
Inventory	143.2	(72.1)
Receivables from unconsolidated joint ventures	(1.4)	(29.9)
Other assets	216.2	82.4
Mortgage loans held for sale	10.0	10.9
Accounts payable and other liabilities	(4.5)	(26.7)
Customer deposits	(16.1)	(15.6)
Net cash provided by (used in) operating activities	292.8	(88.6)
Cash flows from investing activities:		
Acquisitions, net of cash acquired		(7.7)
Net disposals (additions) to property and equipment	0.8	(9.4)
Investments in unconsolidated joint ventures	(1.6)	(29.2)
Capital distributions from unconsolidated joint ventures		12.4
Net cash used in investing activities	(0.8)	(33.9)

Cash flows from financing activities:

Net borrowings from (repayments of) revolving credit facilities	(28.1)	150.3
Principal payments on notes payable	(37.7)	(0.5)
Net repayments of Financial Services bank borrowings	(7.8)	(13.0)
Payments for deferred financing costs	(2.9)	(32.1)
Payment for issuance of convertible preferred stock and warrants		(2.9)
Net cash provided by (used in) financing activities	(76.5)	101.8
Net cash provided by (used in) continuing operations	215.5	(20.7)
Cash flows from discontinued operations:		
Net cash used in operating activities	(0.9)	(12.4)
Net cash provided by financing activities		56.5
Net cash provided by (used in) discontinued operations	(0.9)	44.1
Increase in cash and cash equivalents	214.6	23.4
Cash and cash equivalents at beginning of period	76.5	54.2
Cash and cash equivalents at end of period	\$ 291.1	\$ 77.6

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	Nine Months Ended September 30,	
	2008	2007
Supplemental disclosure of non-cash financing activities:		
Increase (decrease) in obligations for inventory not owned	\$ (15.9)	\$ 44.5
Increase (decrease) in inventory not owned	\$ (16.4)	\$ 39.8

Supplemental disclosure of non-cash activities:

Refer to Note 3 for the consolidation of variable interest entities in accordance with FIN 46(R)

Refer to Note 4 for the settlement of the Transeastern joint venture and related acquisition of assets

See accompanying notes to unaudited consolidated financial statements.

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**TOUSA, INC. AND SUBSIDIARIES
DEBTOR-IN-POSSESSION
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2008**

1. Business and Organization

Business

TOUSA, Inc. (TOUSA , the Company , we , us and our) is a homebuilder with a geographically diversified national presence. We operate in various metropolitan markets in nine states, located in four major geographic regions: Florida, the Mid-Atlantic, Texas and the West. We design, build and market detached single-family residences, town homes and condominiums. We also provide title insurance and, through a joint venture, mortgage brokerage services to our homebuyers and others. Generally, we do not retain or service the mortgages that we originate but, rather, sell the mortgages and related servicing rights. See Mortgage Joint Venture discussion below. Technical Olympic S.A. owns approximately 67% of our outstanding common stock. Technical Olympic S.A. is a publicly-traded Greek company whose shares are traded on the Athens Stock Exchange. Our equity structure will likely change as a result of our Chapter 11 filings.

On March 20, 2009, we filed Forms 15 with the Securities and Exchange Commission terminating the registration of our debt and equity securities under Section 12(g) of the Securities Exchange Act of 1934. Our duty to file periodic reports under the Exchange Act was suspended immediately upon filing the Forms 15. We are therefore voluntarily filing this Quarterly Report on Form 10-Q and do not intend to make any further filings.

Chapter 11 Cases

On January 29, 2008, TOUSA, Inc. and certain of our subsidiaries (excluding our financial services subsidiaries and joint ventures) filed voluntary petitions for relief under Chapter 11 of Title 11 of the United States Code in the Bankruptcy Court. The Chapter 11 cases have been consolidated solely for procedural purposes and are pending as Case No. 08-10928-JKO.

The following discussion provides general background information regarding our cases under Chapter 11 of the Bankruptcy Code, and is not intended to be an exhaustive description. Additional information regarding our Chapter 11 cases, including access to court documents and other general information about the Chapter 11 cases, is available at www.kccllc.net/tousa. Financial information on the website is prepared according to requirements of federal bankruptcy law and the United States Bankruptcy Court for the Southern District of Florida, Fort Lauderdale Division (the Bankruptcy Court). While such financial information accurately reflects information required under federal bankruptcy law, such information may be unconsolidated, unaudited and prepared in a format different than that used in our unaudited consolidated financial statements prepared in accordance with generally accepted accounting principles in the United States and filed under the securities laws. Moreover, the materials filed with the Bankruptcy Court are not prepared for the purpose of providing a basis for investment decisions relating to our stock or debt or for comparison with other financial information filed with the Securities and Exchange Commission.

In March 2009, we announced that our primary focus will be on completing and delivering sold homes currently under construction and on selling our remaining inventory of speculative homes. In addition, we are seeking to sell our other assets. In certain cases, such as in the State of Florida and in Austin and Houston, Texas, we are attempting to sell our assets as a whole. We are in discussions with various parties regarding a sale of our financial services businesses, Universal Land Title, Inc., Preferred Home Mortgage Company and Alliance Insurance Information Services. We are attempting to sell all of our assets in a manner designed to maximize recovery for our creditors. Subject to, in certain situations, receiving approvals from the Bankruptcy Court, we have taken and will continue to take the following actions:

severely curtailing land purchases;

abandoning or in some cases renegotiating our rights under option and land bank contracts;

engaging in bulk sales of land and unsold homes;

reducing the number of unsold homes under construction and limiting and/or curtailing land development activities;

completing other asset dispositions; and

pursuing other initiatives designed to monetize our assets.

We continue to operate our businesses and manage our properties as debtors-in-possession under the jurisdiction of the Bankruptcy Court and in accordance with the applicable provisions of the Bankruptcy Code and orders of the Bankruptcy Court. At the onset of the Chapter 11 cases, we obtained Bankruptcy Court approval to, among other things, continue to pay certain critical vendors and vendors with lien rights, meet our pre-petition payroll obligations, maintain our cash management systems, sell homes free and clear of liens, pay our taxes, continue to provide employee benefits and maintain our insurance programs. In addition, the Bankruptcy Court has approved certain trading notification and transfer procedures designed to allow us to restrict trading in our common stock (and related securities) and has also provided for potentially retroactive application of notice and sell-down procedures for trading in claims against the debtors' estates (in the event that such procedures are approved in the future), which could negatively impact our accumulated net operating losses and other

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tax attributes. The Bankruptcy Court has also entered orders to establish procedures for the purchase and disposition of real property by us subject to certain monetary limits without specific approval for each transaction.

On February 5, 2008, pursuant to an interim order from the Bankruptcy Court dated January 31, 2008, we entered into a Senior Secured Super-Priority Debtor in Possession Credit and Security Agreement. The agreement provided for a first priority and priming secured revolving credit interim commitment of up to \$134.6 million. The agreement was subsequently amended to extend it to September 19, 2008. No funds were drawn under the agreement.

The agreement was subsequently terminated and we entered into an agreement with our prepetition secured lenders to use cash collateral on hand (cash generated by our operations, including the sale of excess inventory and the proceeds of our federal tax refund of \$207.3 million received in April 2008). We are authorized by the Bankruptcy Court to use cash collateral of our first lien and second lien lenders in a manner consistent with a budget negotiated by the parties. The order further provided for the pay-down of \$175.0 million to our first lien term secured lenders, subject to disgorgement provisions in the event that certain claims against the lenders are successful and repayment is required. We also have the right to pay-down an additional \$15.0 million to our first lien secured lenders. As of May 1, 2009, we had paid-down \$148.4 million to the first lien secured lenders. We may incur liens and enter into sale/leaseback transactions for model homes subject to certain limitations. We have granted the pre-petition agents and the lenders various forms of protection, including liens and claims to protect against any diminution of the collateral value, payment of accrued, but unpaid interest on the first priority indebtedness at the non-default rate and the payment of reasonable fees and expenses of the agents under our secured facilities.

Our right to the use of cash collateral has been extended until July 31, 2009 on terms substantially similar to those in the original cash collateral order. If we fail to comply with the order, we will not have sufficient cash to enable us to operate our business and effectuate our restructuring.

The Bankruptcy Court established May 19, 2008 as the bar date for filing proofs of claim against the Debtors relating to obligations arising before January 29, 2008. As of April 28, 2009, approximately 4,400 claims have been filed against us totaling \$7.3 billion in asserted liabilities. These claims are comprised of approximately \$5.0 billion in administrative claims, \$219.0 million in secured claims, \$75.0 million in priority claims and \$7.0 billion in unsecured claims. There are many claims (at least 700) that have been asserted in unliquidated amounts or that contain an unliquidated component. Notably, among the unliquidated claims are the claims of our secured first and second lien lenders. In addition, the indenture trustees under our approximately \$1.1 billion of unsecured debentures each filed an unliquidated claim with respect to such obligations.

On April 17, 2009, we filed with the Bankruptcy Court our First Amended Joint Plan of TOUSA, Inc. and its Affiliated Debtors and Debtors in Possession under Chapter 11 of the Bankruptcy Code (as modified or revised, the Plan) and Disclosure Statement pursuant to Section 1125 of the Bankruptcy Code relating to the Plan (as modified or revised, the Disclosure Statement). Copies of the Plan and Disclosure Statement, as filed with the Bankruptcy Court, are available at <http://www.tousa.com/reorg>. Currently, no hearing has been scheduled on the Plan or Disclosure Statement. We have the exclusive right to file a plan until July 29, 2009 and the exclusive right to solicit acceptance thereof until September 27, 2009. Pursuant to Section 1121 of the Bankruptcy Code, the exclusivity periods may be expanded or reduced by the Bankruptcy Court, but in no event can the exclusivity periods to file and solicit acceptance of a plan or plans of reorganization be extended beyond September 29, 2009.

As a result of our Chapter 11 cases and other matters described herein, including uncertainties related to the fact that our filed plan of reorganization has not been confirmed, there is substantial doubt about our ability to continue as a going concern.

Mortgage Joint Venture

On January 28, 2008, Preferred Home Mortgage Company, our wholly-owned residential mortgage lending subsidiary, entered into an Amended and Restated Agreement of Limited Liability Company with Wells Fargo Ventures, LLC. The limited liability company is known as PHMCWF, LLC but does business as Preferred Home Mortgage Company, an affiliate of Wells Fargo. Preferred Home Mortgage Company owns 49.9% of the venture with the balance owned by Wells Fargo. Effective April 1, 2008, the venture began to carry on the mortgage business of Preferred Home Mortgage Company. The venture is managed by a committee composed of six members, three from Preferred Home Mortgage Company and three from Wells Fargo. The venture entered into a revolving credit

agreement with Wells Fargo Bank, N.A. providing for advances of up to \$20.0 million. Wells Fargo Home Mortgage provides the general and administrative support (as well as all loan related processing, underwriting and closing functions), and is the end investor for the majority of the loans closed through the joint venture. Prior to the joint venture, Preferred Home Mortgage Company had a centralized operations center that provided those support functions. The majority of these support functions ceased in June 2008. Effective April 1, 2008, we began to account for the venture as an equity-method investment.

2. Summary of Significant Accounting Policies

Principles of Consolidation and Basis of Presentation

The unaudited consolidated financial statements include our accounts and those of our subsidiaries. All significant intercompany balances and transactions have been eliminated in the unaudited consolidated financial statements. For the three months ended September 30, 2008 and 2007, we have eliminated inter-segment Financial Services revenues of \$0.6 million and \$3.6 million, respectively. For the nine months ended September 30, 2008 and 2007, we have eliminated inter-segment Financial Services revenues of \$2.9 million and \$10.7 million, respectively.

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) on a going concern basis. This contemplates the realization of assets and satisfaction of liabilities in the ordinary course of business. Accordingly, we do not include any adjustments relating to the recoverability of assets and satisfaction of liabilities that might be necessary should we be unable to continue as a going concern. Due to our Chapter 11 cases, there is substantial doubt about our ability to continue as a going concern and there is uncertainty about the realization of assets and satisfaction of liabilities, without substantial adjustments and/or changes in capital structure.

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In accordance with GAAP, we have applied the provisions of American Institute of Certified Public Accountants (AICPA) Statement of Position 90-7, *Financial Reporting by Entities in Reorganization Under the Bankruptcy Code* (SOP 90-7), in preparing the unaudited consolidated financial statements. SOP 90-7 requires that the financial statements, for periods subsequent to the Chapter 11 filing, distinguish transactions and events that are directly associated with the reorganization from the ongoing operations of the business. Accordingly, certain items of income, expense, gain or loss realized or incurred because we are in Chapter 11 are recorded in reorganization items, net on the accompanying unaudited consolidated statements of operations. Also, pre-petition obligations that may be impacted by the bankruptcy reorganization process have been classified in liabilities subject to compromise on the unaudited consolidated statement of financial condition at September 30, 2008. These liabilities are reported at the amounts expected to be allowed by the Bankruptcy Court, in accordance with Statement of Financial Accounting Standards (SFAS) No. 5, *Accounting for Contingencies* (SFAS 5), even if they may be settled for lesser amounts. As of September 30, 2008, the pre-petition liabilities included in liabilities subject to compromise have not been reduced.

The following table summarizes the components included in reorganization items, net, in our unaudited consolidated statements of operations for the three and nine months ended September 30, 2008 (in millions):

	Three Months Ended September 30, 2008	Nine Months Ended September 30, 2008
Professional fees	\$ 19.7	\$ 42.5
Write-off of deferred finance costs		54.4
Write-off of debt premium and discounts		11.9
Interest income	(1.6)	(1.7)
Lease rejections	0.6	0.6
Reversal of previously recorded interest expense		(2.3)
Total reorganization items, net	\$ 18.7	\$ 105.4

Net cash paid for reorganization items totaled \$15.3 million related to professional fees and \$39.9 million (\$37.0 million of professional fees and \$2.9 million of deferred finance costs) for the three and nine months ended September 30, 2008, respectively.

The following table summarizes the components included in liabilities subject to compromise on our unaudited consolidated statement of financial condition as of September 30, 2008 (in millions):

Revolving Loan Facility ⁽¹⁾	\$ 223.1
First Lien Term Loan Facility due 2012 ⁽¹⁾	161.3
Second Lien Term Loan Facility due 2013 ⁽¹⁾	352.6
Senior notes due 2010, at 9% ⁽¹⁾	300.0
Senior notes due 2011, at 8 1/4% ⁽¹⁾	250.0
Senior subordinated notes due 2012, at 10 3/8% ⁽¹⁾	185.0
Senior subordinated notes due 2011, at 7 1/2% ⁽¹⁾	125.0
Senior subordinated notes due 2015, at 7 1/2% ⁽¹⁾	200.0
Senior Subordinated PIK Notes due 2015, at 14 3/4% ⁽¹⁾	24.0
Accrued interest on notes payable	47.2
Accounts payable and other liabilities	195.7
Obligations for inventory not owned ⁽²⁾	16.1

Total liabilities subject to compromise \$ 2,080.0

(1) See Note 9

(2) See Note 3

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. Those estimates and assumptions which, in the opinion of management, are both significant to the underlying amounts included in the financial statements and as to which future events or information could change those estimates include:

impairment assessments of investments in unconsolidated joint ventures, long-lived assets, including our inventory, and goodwill;

loss exposures associated with the abandonment of our rights under option and/or land bank contracts, the relinquishment of our rights under certain joint ventures and obligations under joint venture debt agreements and under performance bonds;

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classification of liabilities subject to compromise;

insurance and litigation related contingencies;

realization of deferred income tax assets and liability for unrecognized tax benefits; and

estimated costs associated with construction and development activities in connection with our homebuilding operations.

The accompanying unaudited consolidated financial statements do not purport to reflect or provide for the consequences of our Chapter 11 cases. In particular, the financial statements do not purport to show: (1) as to assets, their realizable value on a liquidation basis or their availability to satisfy liabilities; (2) as to stockholders' equity accounts, the effect of any changes that may be made in our capitalization; or (3) as to operations, the effect of any changes that may be made to our business. In addition, the financial statements do not reflect the amounts that may be allowed with respect to pre-petition claims and liabilities which may, as a result of the filing of proofs of claims by our creditors, result in liabilities in excess of those estimated by us in preparing the accompanying unaudited consolidated financial statements.

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

Interim Presentation

The accompanying unaudited consolidated financial statements reflect all adjustments, consisting primarily of normal recurring items that, in the opinion of management, are considered necessary for a fair presentation of the financial position, results from operations, and cash flows for the periods presented. Results of operations achieved through September 30, 2008 are not necessarily indicative of those that may be achieved for the year ending December 31, 2008. The unaudited consolidated statement of financial condition as of December 31, 2007 was derived from audited financial statements included in our 2007 Annual Report on Form 10-K, but does not include all disclosures required under GAAP and with the rules and regulations of the Securities and Exchange Commission. The unaudited consolidated financial statements included as part of this Form 10-Q should be read in conjunction with the financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2007.

Loss per Common Share

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

For the three months ended September 30, 2008 and 2007, basic and diluted weighted average shares outstanding were 59,604,169. For the nine months ended September 30, 2008 and 2007, basic and diluted weighted average shares outstanding were 59,604,169 and 59,601,119, respectively. There were no dilutive common stock equivalents during the three and nine months ended September 30, 2008 and 2007. At September 30, 2008, outstanding options to purchase 7.5 million shares of common stock were excluded from the computation of loss per common share since their inclusion would be anti-dilutive.

Revenue Recognition

Our primary source of revenue is the sale of homes to homebuyers. To a lesser degree, we engage in the sale of land to other homebuilders and other third-parties. Revenue is recognized on home sales and land sales at closing when title passes to the buyer and all of the following conditions are met: a sale is consummated, a significant down payment is received, the earnings process is complete, the receivable is not subject to future subordination, the collection of any remaining receivables is reasonably assured and we do not have substantial continuing involvement

with the sold asset.

In accordance with SFAS No. 66, *Accounting for the Sales of Real Estate* (SFAS 66), at September 30, 2008 and December 31, 2007, we deferred approximately \$0.2 million and \$1.0 million, respectively, in profit related to certain homes that were delivered for which our mortgage subsidiary originated interest-only loans or loans with high loan to value ratios which did not meet the initial and continuing investment requirements under SFAS 66, and the loans were still held for sale at the respective balance sheet date.

Fair Value Disclosures

Effective January 1, 2008, we adopted SFAS No. 157, *Fair Value Measurements* (SFAS 157), for our financial instruments measured at fair value on a recurring basis. SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, expands disclosures about fair value measurements and establishes a fair value hierarchy summarized below:

- Level 1 Fair value determined based on quoted prices in active markets for identical assets or liabilities.
- Level 2 Fair value determined using significant observable inputs either directly or indirectly through corroboration with market data.
- Level 3 Fair value determined using significant unobservable inputs, such as pricing models, discounted cash flows, or similar techniques.

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Our financial instruments measured at fair value on a recurring basis at September 30, 2008 are summarized below (in millions):

Financial Instrument	Fair Value Hierarchy	Fair Value
Assets:		
Mortgage loans held for sale	Level 2	\$ 5.0

Mortgage loans held for sale of \$5.0 million represents loans originated in prior years for which the fair value is determined by third-party opinions establishing the market sales price for the underlying collateral adjusted for customary sales and marketing costs.

Recent Accounting Pronouncements

In September 2006, the FASB issued SFAS 157. SFAS 157 was effective for financial statements issued for fiscal years beginning after November 15, 2007 (our fiscal year beginning January 1, 2008), and interim periods within those fiscal years. As discussed above, we adopted SFAS 157 effective January 1, 2008 for our financial instruments measured at fair value on a recurring basis. In February 2008, the FASB issued a final Staff Position (FSP) No. 157-2, *Effective Date of FASB Statement No. 157*, to allow a one-year deferral of adoption of SFAS 157 for nonfinancial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. The FASB also decided to amend SFAS 157 to exclude SFAS No. 13, *Accounting for Leases*, and its related interpretive accounting pronouncements that address leasing transactions. We are currently reviewing the effects, if any, of SFAS 157 related to nonfinancial assets and liabilities on our unaudited consolidated financial statements.

In November 2006, the FASB issued EITF No. 06-8, *Applicability of the Assessment of a Buyers Continuing Investment under FASB Statement No. 66, Accounting for Sales of Real Estate, for Sales of Condominiums* (EITF 06-8). EITF 06-8 establishes that a company should evaluate the adequacy of the buyer's continuing investment in determining whether to recognize profit under the percentage-of-completion method. EITF 06-8 was effective as of January 1, 2008 and had no impact on our unaudited consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*, (SFAS 159). SFAS 159 permits companies to measure many financial instruments and certain other items at fair value. While SFAS 159 became effective for us on January 1, 2008, we did not elect the fair value measurement option for any of our financial assets or liabilities.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), *Business Combinations* (SFAS 141(R)). SFAS 141(R) establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any non-controlling interest in the acquiree, and the goodwill acquired. SFAS 141(R) also establishes disclosure requirements to enable the evaluation of the nature and financial effects of the business combination. SFAS 141(R) is effective for fiscal years beginning after December 15, 2008. Adoption is prospective, and early adoption is not permitted. Adoption of SFAS 141(R) will apply to any business combination beginning January 1, 2009.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements – an amendment of Accounting Research Bulletin No. 51* (SFAS 160). SFAS 160 establishes accounting and reporting standards for ownership interests in subsidiaries held by parties other than the parent, the amount of consolidated net income attributable to the parent and to the noncontrolling interest, changes in a parent's ownership interest, and the valuation of retained, noncontrolling equity investments when a subsidiary is deconsolidated. SFAS 160 also establishes disclosure requirements that clearly identify and distinguish between the interests of the parent and the interests of the noncontrolling owners. SFAS 160 is effective for fiscal years beginning after December 15, 2008. We are currently reviewing the effect of this statement on our unaudited consolidated financial statements.

On February 20, 2008, the FASB issued FASB Staff Position (FSP) SFAS No. 140-3, *Accounting for Transfers of Financial Assets and Repurchase Financing Transactions*. The FSP addresses whether there are circumstances that would permit a transferor and a transferee to evaluate the accounting for the transfer of a financial asset separately

from a repurchase financing when the counterparties to the two transactions are the same. The FSP presumes that the initial transfer of a financial asset and a repurchase financing are considered part of the same arrangement (a linked transaction) under FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* (SFAS 140"). However, if certain criteria specified in the FSP are met, the initial transfer and repurchase financing may be evaluated separately under SFAS 140. The FSP is effective for fiscal years beginning after November 15, 2008, and interim periods within those fiscal years. Earlier application is not permitted. Adoption of the FSP is not expected to have a material effect on our unaudited consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities* (SFAS 161). SFAS 161 requires enhanced disclosures regarding derivative instruments and hedging activities to enable investors to better understand their effects on a company's financial position, financial performance and cash flows. These requirements include the disclosure of the fair values of derivative instruments and their gains and losses in a tabular format. SFAS 161 is effective for fiscal years beginning after November 15, 2008. We are currently evaluating the disclosure requirements of SFAS 161 and their impact on our unaudited consolidated financial statements.

In April 2008, the FASB issued FASB Staff Position 90-7-1, *An Amendment of AICPA Statement of Position 90-7* (FSP 90-7-1). FSP 90-7-1, which was effective immediately and amends SOP 90-7, paragraph 38 to nullify the requirement regarding changes in accounting principles. Previously under paragraph 38 of SOP 90-7, changes in accounting principles that will be required in the financial statements of an emerging entity within the 12 months following the adoption of fresh-start accounting were required to be adopted at the time fresh-start reporting was adopted. As a result of the amendment, an entity emerging from bankruptcy that applies fresh-start reporting should follow only the accounting standards in effect at the date fresh-start reporting is adopted, which include those standards eligible for early adoption if an election is made to adopt early. This will be applicable to us upon emergence from bankruptcy.

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In May 2008, the FASB issued FSP APB 14-1, *Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)* (FSP APB 14-1). This FSP clarifies the treatment of convertible debt instruments that may be settled in cash upon conversion (including partial cash settlement) that are not addressed by paragraph 12 of APB Opinion No. 14, *Accounting for Convertible Debt and Debt issued with Stock Purchase Warrants* . Additionally, this FSP specifies that issuers of such instruments should separately account for the liability and equity components in a manner that will reflect the entity's nonconvertible debt borrowing rate when interest cost is recognized in subsequent periods. This FSP is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. We are currently evaluating the impact of FSP APB 14-1 will have on our unaudited consolidated financial statements.

In November 2008, the FASB issued EITF Issue No. 08-6, *Equity Method Investment Accounting Considerations* (EITF 08-6), which clarifies the accounting for certain transactions and impairment considerations involving equity method investments. EITF 08-6 is effective for fiscal years beginning after December 15, 2008, with early adoption prohibited. We are currently evaluating the impact EITF 08-6 will have on our unaudited consolidated financial statements.

In December 2008, the FASB issued FSP FAS 140-4 and FIN 46(R)-8, *Disclosures by Public Entities (Enterprises) about Transfers of Financial Assets and Interests in Variable Interest Entities* (FSP 140-4 and FIN 46(R)-8). FSP 140-4 and FIN 46(R)-8 requires additional disclosures about transfers of financial assets and involvement with variable interest entities. FSP 140-4 and FIN 46(R)-8 is effective for the first reporting period ending after December 15, 2008. The implementation of this standard is not expected to have a material impact on our unaudited consolidated financial statements.

In April 2009, the FASB issued FSP FAS 157-4, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly* (FSP FAS 157-4), which addresses the factors that determine whether there has been a significant decrease in the volume and level of activity for an asset or liability when compared to the normal market activity. This pronouncement provides that if it has been determined that the volume and level of activity has significantly decreased and that transactions are not orderly, further analysis is required and significant adjustments to the quoted prices or transactions might be needed. FSP FAS 157-4 is effective for interim and annual reporting periods ending after June 15, 2009. We are currently evaluating the impact FSP FAS 157-4 will have on our unaudited consolidated financial statements.

In April 2009, the FASB issued FSP FAS 107-1 and APB 28-1, *Interim Disclosures about Fair Value of Financial Instruments* (FSP FAS 107-1 and APB 28-1), which provide guidance relating to required disclosures concerning the fair value of financial instruments when a publicly traded company issues financial information for interim reporting periods. The requirements are effective for interim reporting periods ending after June 15, 2009. We are currently evaluating the impact FSP FAS 107-1 and APB 28-1 will have on our unaudited consolidated financial statements.

3. Inventory

The following is a breakdown of inventory (in millions):

	September 30, 2008				
		Homesites and Land Under Development	Residences Completed and Under Construction	Inventory Not Owned	Total Inventory
Region					
Florida	\$ 0.1	\$ 105.7	\$ 105.1	\$	\$ 210.9
Mid-Atlantic	3.8	10.3	18.5		32.6
Texas	2.2	54.8	98.7	1.0	156.7
West	13.1	64.9	60.6	8.6	147.2

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Total \$ 19.2 \$ 235.7 \$ 282.9 \$ 9.6 \$ 547.4

Region	December 31, 2007				
	Deposits	Homesites and Land Under Development	Residences Completed and Under Construction	Inventory Not Owned	Total Inventory
Florida	\$ 10.2	\$ 294.7	\$ 320.1	\$ 8.1	\$ 633.1
Mid-Atlantic	7.9	21.8	28.6		58.3
Texas	15.6	73.3	111.9	3.1	203.9
West	23.2	243.2	95.3	14.8	376.5
Total	\$ 56.9	\$ 633.0	\$ 555.9	\$ 26.0	\$ 1,271.8

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A summary of homebuilding interest capitalized in inventory is as follows (in millions):

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2008	2007	2008	2007
Interest capitalized, beginning of period	\$ 70.1	\$ 81.6	\$ 77.8	\$ 68.7
Interest incurred ⁽¹⁾⁽²⁾	26.9	43.5	92.1	100.2
Less interest included in:				
Cost of sales	(8.0)	(35.2)	(43.8)	(78.6)
Interest expense	(16.9)	(10.0)	(53.7)	(10.2)
Other adjustments	0.1	(0.4)	(0.2)	(0.6)
Interest capitalized, end of period ⁽³⁾	\$ 72.2	\$ 79.5	\$ 72.2	\$ 79.5

(1) Included in interest incurred is the amortization of deferred finance costs which amounted to \$3.5 million for the three months ended September 30, 2007, and \$4.3 million and \$6.2 million for the nine months ended September 30, 2008 and September 30, 2007, respectively. There was no amortization of deferred finance costs for the three months ended September 30, 2008 due to the write-off of our deferred finance costs.

(2)

Had we not filed voluntary petitions for relief under Chapter 11, contractual interest incurred for the three and nine months ended September 30, 2008 would have been \$53.4 million and \$162.9 million, respectively, a portion of which would have been capitalized. Interest on our senior and senior subordinated notes stopped accruing upon filing for Chapter 11. See Note 9.

- (3) We have incurred significant inventory impairments in recent years, which are determined based on total inventory, including capitalized interest. However, the capitalized interest amounts above are gross amounts before allocating any portion of the

impairments to
capitalized
interest.

In the ordinary course of business, we enter into option contracts to purchase homesites and land held for development. At September 30, 2008 and December 31, 2007, we had non-refundable cash deposits totaling \$7.7 million and \$56.9 million, respectively, included in inventory in the accompanying unaudited consolidated statements of financial condition. Under these option contracts, we have the right to buy homesites at predetermined prices on a predetermined takedown schedule. Option contracts generally require the payment of a cash deposit and/or the posting of a letter of credit, which is typically less than 20% of the underlying purchase price, and may require monthly maintenance payments. These option contracts are either with land sellers or third party financial entities which have acquired the land to enter into the option contract with us. Homesite option contracts are generally non-recourse, thereby limiting our financial exposure for non-performance to our cash deposits and/or letters of credit. In certain instances, we have entered into development agreements in connection with option contracts, which require us to complete the development of the land, at a fixed reimbursable amount, even if we choose not to exercise our option and forfeit our deposit and even if our costs exceed the reimbursable amount. We have abandoned our rights under certain option contracts that require us to complete the development of land for a fixed reimbursable amount. We recorded net recoveries of \$0.6 million for the three months ended September 30, 2008 and net losses of \$3.4 million for the nine months ended September 30, 2008 for our estimated obligations under these development agreements, which is included in inventory impairments and abandonment costs in the accompanying unaudited consolidated statement of operations. At September 30, 2008 and December 31, 2007, \$13.7 million and \$10.3 million are included in liabilities subject to compromise and accounts payable and other liabilities, respectively, in the accompanying unaudited consolidated statements of financial condition related to these development agreements.

Financing Transactions under SFAS 66

Certain of our option contracts give the other party the right to require us to purchase homesites or guarantee certain minimum returns. We have abandoned our rights under certain of these option contracts and we have not complied with the notices given to us. These option contracts were previously recorded as financing transactions under SFAS 66 and the inventory was included in inventory not owned and the corresponding liability was included in obligations for inventory not owned. Since we defaulted under or terminated these contracts, we are no longer accounting for these contracts as financing transactions. During the three and nine months ended September 30, 2008, we recorded losses of \$5.0 million and \$14.5 million, respectively, in connection with the abandonment of these option contracts, for our estimated obligations, which is included in inventory impairments and abandonment costs in the accompanying unaudited consolidated statements of operations. These amounts were computed based on the estimated deficiency between the fair value of the underlying inventory compared to our required purchase price under the option contract. The total required purchase price under these option contracts at September 30, 2008 and December 31, 2007 was \$36.3 million and \$25.0 million, respectively. At September 30, 2008 and December 31, 2007, \$24.0 million and \$9.5 million is included in liabilities subject to compromise and accounts payable and other liabilities, respectively, in the accompanying unaudited consolidated statements of financial condition.

From time to time, we transfer title to certain parcels of land to unrelated third parties or enter into agreements pursuant to which third parties purchase land which we have the contractual right to acquire. We then enter into options with the purchasers to acquire fully developed homesites. As we have continuing involvement in these properties, in accordance with SFAS 66, we have accounted for these transactions as financing arrangements. At September 30, 2008 and December 31, 2007, \$7.8 million (net of \$2.1 million in impairments) and \$9.8 million (net of \$6.0 million in impairments), respectively, of inventory not owned and \$9.9 million and \$15.8 million, respectively, of obligations for inventory not owned relate to sales where we have continuing involvement.

Consolidation of Variable Interest Entities Under FIN 46(R)

Some of our option contracts for the purchase of land or homesites are with land sellers and third party financial entities, which qualify as variable interest entities (VIEs) under FASB Interpretation No. 46 (Revised), *Consolidation of Variable Interest Entities* (FIN 46(R)). FIN 46(R) addresses consolidation by business enterprises of VIEs in which an entity absorbs a majority of the expected losses, receives a majority of the entity's expected residual returns, or both, as a result of ownership, contractual or other financial interests

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in the entity. Obligations for inventory not owned in our unaudited consolidated statements of financial condition represent liabilities associated with our land banking and similar activities, including obligations in VIEs which have been consolidated by us and in which we have a less than 50% ownership interest, and the creditors have no recourse against us.

In applying FIN 46(R) to our homesite option contracts and other transactions with VIEs, we make estimates regarding cash flows and other assumptions. We believe that our critical assumptions underlying these estimates are reasonable based on historical evidence and industry practice. Based on our analysis of transactions entered into with VIEs, we determined that we are the primary beneficiary of certain of these homesite option contracts. Consequently, FIN 46(R) requires us to consolidate the assets (homesites) at their fair value, although (1) we have no legal title to the assets, (2) our maximum exposure to loss is generally limited to the deposits or letters of credit placed with these entities, and (3) creditors, if any, of these entities have no recourse against us.

The effect of FIN 46(R) at September 30, 2008 was to increase inventory by \$1.8 million (net of \$4.3 million of impairments), excluding cash deposits of \$0.2 million, which had been previously recorded, with a corresponding increase to obligations for inventory not owned of \$6.1 million in the accompanying unaudited consolidated statement of financial condition. The effect of FIN 46(R) at December 31, 2007 was to increase inventory by \$16.2 million, excluding cash deposits of \$3.8 million, which had been previously recorded, with a corresponding increase to obligations for inventory not owned of \$16.2 million in the accompanying unaudited consolidated statement of financial condition. Additionally, we have entered into arrangements with VIEs to acquire homesites in which our variable interest is insignificant and, therefore, we have determined that we are not the primary beneficiary and are not required to consolidate the assets of such VIEs. Our potential exposure to loss in VIEs where we are not the primary beneficiary would primarily be the forfeiture of our deposit and/or letters of credit placed on land purchase and option contracts. At September 30, 2008 and December 31, 2007, our non-refundable cash deposits placed on land purchase and option contracts amounted to \$7.7 million and \$56.9 million, respectively, and our letters of credit placed on land purchase and option contracts amounted to \$4.9 million and \$44.9 million, respectively.

Inventory Impairments and Abandonment Costs

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* (SFAS 144), we carry long-lived assets held for sale at the lower of the carrying amount or fair value. For active communities (communities under development and construction), we evaluate an asset for impairment when events and circumstances indicate that they may be impaired. Impairment is evaluated by estimating future undiscounted cash flows expected to result from the use of the asset and its eventual disposition. If the sum of the expected undiscounted future cash flows is less than the carrying amount of the assets, an impairment loss is recognized. Fair value, for purposes of calculating impairment, is measured based on estimated future cash flows, discounted at a market rate of interest. During the three months ended September 30, 2008 and 2007, we recorded impairment losses and abandonment costs of \$65.0 million and \$63.3 million, respectively, on active communities. During the nine months ended September 30, 2008 and 2007, we recorded impairment losses and abandonment costs of \$342.2 million and \$112.7 million, respectively, on active communities. These losses are included in cost of sales inventory impairments and abandonment costs in the accompanying unaudited consolidated statements of operations.

In accordance with SFAS 144, we performed an evaluation of impairment on a large land parcel located in Arizona, known as Red River, during the nine months ended September 30, 2008 and determined that it was impaired as the future undiscounted cash flows expected to result from the use of the asset and its eventual disposition did not exceed the carrying value. We based our computation of the future undiscounted cash flows on management estimates and projections which assume that the land parcel will be subdivided into super-pads (entitled and engineered, level but not graded with the required master plan infrastructure and utilities for merchant builders to custom finish lots for retail home construction) with super-pad sales estimated to commence in 2010 in anticipation of retail new home demand in 2012. This computation also included other assumptions related to market supply and demand, product type, homesite sizes, sales pace, sales prices, construction costs, sales and marketing expenses, the local economy, competitive conditions, labor costs and costs of materials. The undiscounted cash flows are based on a long-term project horizon of nine years; accordingly, all project costs are variable. The undiscounted cash flows used to evaluate this parcel assume a nine-year average annual retail home price appreciation of 2.5%. As a result, an

impairment charge of \$85.0 million was recognized during the nine months ended September 30, 2008 related to this parcel which is included in the write-off of deposits and abandonment costs for the West region in the table below, leaving a remaining book value of \$19.8 million.

During the three and nine months ended September 30, 2008, we also recorded charges of \$32.1 million and \$231.9 million, respectively, in write-offs of deposits and abandonment costs which are included in cost of sales inventory impairments and abandonment costs in the accompanying unaudited consolidated statements of operations, related to land that we have determined is not probable that we will purchase or build on (including land to be sold as lots), compared to \$441.2 million and \$515.7 million, respectively, for the three and nine months ended September 30, 2007. The following table summarizes information related to impairment charges on active communities and write-offs of deposits and abandonment costs by region (dollars in millions):

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	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Impairment charges on active communities:				
Florida	\$ 58.1	\$ 15.7	\$ 264.0	\$ 44.4
Mid-Atlantic	2.1	4.4	14.6	11.0
Texas	1.7		4.8	0.6
West	3.1	43.2	58.8	56.7
	65.0	63.3	342.2	112.7
Write-offs of deposits and abandonment costs:				
Florida	10.0	274.5	46.4	287.3
Mid-Atlantic	4.6	33.9	14.0	47.8
Texas	13.5		20.3	0.3
West	4.0	132.8	151.2	180.3
	32.1	441.2	231.9	515.7
Inventory impairments and abandonment costs	\$ 97.1	\$ 504.5	\$ 574.1	\$ 628.4
Remaining carrying value of inventory impaired at end of period	\$ 502.2	\$ 728.0	\$ 502.2	\$ 728.0
Number of projects impaired during the period	98	131	257	171
Total number of projects included in inventory and reviewed for impairment during the period	361	481	361	481

4. Transeastern Joint Venture

We acquired our 50% interest in the Transeastern Joint Venture (Transeastern JV) on August 1, 2005, when the Transeastern JV acquired substantially all of the homebuilding assets and operations of Transeastern Properties, Inc. including work in process, finished lots and certain land option rights. The Transeastern JV paid approximately \$826.2 million for these assets and operations (which included the assumption of \$127.1 million of liabilities and certain transaction costs, net of \$30.1 million of cash). The other member of the joint venture was an entity controlled by the former majority owners of Transeastern Properties, Inc. We functioned as the managing member of the Transeastern JV through a wholly-owned subsidiary.

On October 31, 2006 and November 1, 2006, we received demand letters from the administrative agent for the lenders to the Transeastern JV demanding payment under certain guarantees. The demand letters alleged that potential defaults and events of default had occurred under the credit agreements and that such potential defaults or events of default had triggered our obligations under the guarantees. The lenders claimed that our guarantee obligations equaled or exceeded all of the outstanding obligations under each of the credit agreements and that we were liable for default interest, costs and expenses.

On July 31, 2007, we consummated transactions to settle the disputes regarding the Transeastern JV with the lenders to the Transeastern JV, its land bankers and our joint venture partner in the Transeastern JV. As a result, the Transeastern JV became a wholly-owned subsidiary of ours by merger into one of our subsidiaries.

Pursuant to the settlement, among other things,

the Transeastern JV became a wholly-owned subsidiary of ours by merger into one of our subsidiaries, which became a guarantor on our credit facilities and note indentures (the acquisition was accounted for using the

purchase method of accounting and results of operations have been included in our consolidated results beginning on July 31, 2007);

the senior secured lenders of the Transeastern JV were repaid in full, including accrued interest (approximately \$400.0 million in cash);

the senior mezzanine lenders to the Transeastern JV received \$20.0 million in aggregate principal amount of 14.75% Senior Subordinated PIK Election Notes due 2015 and \$117.5 million in initial aggregate liquidation preference of 8% Series A Convertible Preferred PIK Preferred Stock;

the junior mezzanine lenders to the Transeastern JV received warrants to purchase shares of our common stock which had an estimated fair value of \$8.2 million at issuance (based on the Black-Scholes option pricing model and before issuance costs);

we entered into settlement and release agreements with the senior mezzanine lenders and the junior mezzanine lenders to the Transeastern JV which released us from our potential obligations to them; and

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we entered into a settlement and mutual release agreement with Falcone/Ritchie LLC and certain of its affiliates (the Falcone Entities) concerning the Transeastern JV, one of which owned 50% of the equity interests in the Transeastern JV and, among other things, released the Falcone Entities from claims under the 2005 asset purchase agreement pursuant to which we acquired our interest in the Transeastern JV. Pursuant to the settlement agreement, we remain obligated on certain indemnification obligations, including, without limitation, certain land bank arrangements.

To effect the settlement of the Transeastern JV dispute, on July 31, 2007, we also entered into: an amendment to our \$800.0 million revolving loan facility dated January 30, 2007;

a new \$200.0 million aggregate principal amount first lien term loan facility; and

a new \$300.0 million aggregate principal amount second lien term loan facility.

The proceeds from the first and second lien term loans were used to satisfy claims of the senior secured lenders against the Transeastern JV, and to pay related expenses. Our existing \$800.0 million revolving loan facility was amended and restated to reduce the revolving commitments thereunder by \$100.0 million and permit the incurrence of the first and second lien term loan facilities (and make other conforming changes relating to the facilities). Net proceeds from these financings at closing were \$470.6 million which is net of a 1% discount and transaction costs.

We also paid:

\$50.2 million in cash to purchase land under existing land bank arrangements with the former Transeastern JV partner; and

\$33.5 million in interest and expenses.

Additional descriptions of the facilities, preferred stock and the warrants are provided in Notes 9 and 12 to the unaudited consolidated financial statements.

In connection with the Transeastern JV settlement, we recognized a loss of \$426.6 million, of which \$32.0 million was recognized during the three months ended September 30, 2007, \$119.6 million was recognized during the remainder of 2007 and \$275.0 million was recognized during 2006.

The consideration paid by us in connection with the TE Acquisition approximated \$586.8 million, at the time of settlement (July 31, 2007), which included (in millions):

Purchase price:

Cash consideration paid to Senior Lenders of the Transeastern JV	\$ 400.0
Fair value of convertible preferred stock issued	84.0
Fair value of senior subordinated notes issued	10.9
Fair value of common stock warrants issued	8.2
Payment to purchase land under existing land bank arrangements	50.2
Transaction costs including accrued interest paid to the Senior Lenders	33.5
 Total estimated purchase price	 \$ 586.8

Allocation of purchase consideration:

Cash and cash equivalents	\$ 10.3
Restricted cash	28.4
Inventory ⁽¹⁾	149.8
Property and equipment	1.0
Accounts payable and other liabilities	(27.4)
Customer deposits	(1.9)
Previously accrued loss contingency ⁽²⁾	385.9
Additional loss on TE Acquisition ⁽³⁾	40.7

- (1) The fair value of the inventory was determined by estimating future cash flows expected to result from the use of the asset and its eventual disposition, discounted at a market rate of interest.
- (2) In accordance with SFAS 5 and other authoritative guidance, as of September 30, 2007, we accrued \$385.9 million for settlement of a loss contingency (determined by computing the difference between the estimated fair value of the consideration paid in connection with the global settlement less the estimated fair value of the business acquired).
- (3) There were no identifiable intangible assets or goodwill

associated with
the TE
Acquisition.

Table of Contents**5. Investments in Unconsolidated Joint Ventures**

We have entered into strategic joint ventures that acquire and develop land for our Homebuilding operations and/or that also build and market homes for sale to third parties. Our partners in these joint ventures generally are unrelated homebuilders, land sellers, financial investors or other real estate entities. In some cases our Chapter 11 filings have constituted an event of default under the joint venture lender agreements which have resulted in the debt becoming immediately due and payable, limiting the joint ventures' access to future capital. In joint ventures where the assets are being financed with debt, the borrowings are non-recourse to us except that in certain instances we have agreed to complete certain property development commitments in the event the joint ventures default and to indemnify the lenders for losses resulting from fraud, misappropriation, violations of environmental laws and similar acts. In some cases, we have agreed to make capital contributions to the joint venture sufficient to comply with a specified debt to value ratio. Our obligations become full recourse upon certain bankruptcy events with respect to the joint venture. At September 30, 2008 and December 31, 2007, we had investments in unconsolidated joint ventures of \$3.0 million and \$9.0 million, respectively. We account for these investments under the equity method of accounting. These unconsolidated joint ventures are limited liability companies or limited partnerships in which we have a limited partnership interest and a minority interest in the general partner. At December 31, 2007, we had receivables of \$0.3 million, net of allowances from these joint ventures due to loans and advances, unpaid management fees and other items. At September 30, 2008, we had no receivables from joint ventures.

In certain instances, we were appointed as the day-to-day manager of the unconsolidated entities and received management fees for performing this function. We earned management fees from these unconsolidated entities of \$0 and \$0.8 million for the three months ended September 30, 2008 and 2007, respectively, and \$0.1 million and \$9.0 million for the nine months ended September 30, 2008 and 2007, respectively. These fees are included in income (loss) from unconsolidated joint ventures in the accompanying unaudited consolidated statements of operations.

We evaluated the recoverability of our investments in and receivables from unconsolidated joint ventures under APB 18 and SFAS No. 114, *Accounting by Creditors for Impairment of a Loan* (SFAS 114), and recorded total impairments of investments in unconsolidated joint ventures of \$5.8 million and \$23.4 million for the three months ended September 30, 2008 and 2007, respectively, and \$8.6 million and \$28.9 million for the nine months ended September 30, 2008 and 2007, respectively. Additionally, during the three months ended September 30, 2008, we recorded \$5.3 million of impairments on joint venture receivables (net of a \$2.2 million recovery related to a previously written-off joint venture receivable). At September 30, 2008 and December 31, 2007, the accrual related to joint venture obligations was \$47.7 million and \$74.6 million, respectively, which primarily relates to limited guarantees we issued in connection with our unconsolidated joint ventures. As explained in further detail below, the decrease in the accrual is primarily due to the reduction of loss accruals for certain joint venture obligations totaling \$26.9 million established in 2007 and reversed during the nine months ended September 30, 2008.

Engle/Sunbelt Joint Venture

In December 2004, we entered into a joint venture agreement with Suntous Investors, LLC (Suntous) to form Engle/Sunbelt Holdings, LLC (Engle/Sunbelt). Engle/Sunbelt was formed to develop finished homesites and to build and deliver homes in the Phoenix, Arizona market. Upon its inception, the venture acquired eight of our existing communities in Phoenix, Arizona.

At December 31, 2007, the joint venture had financing arrangements with an aggregate borrowing capacity of \$230.0 million, of which \$200.0 million related to a revolving loan and \$30.0 million related to a mezzanine financing instrument. On January 16, 2008, the facility was amended to reduce the revolving loan limit to \$115.0 million and terminate the mezzanine financing instrument. While the borrowings by Engle/Sunbelt were non-recourse to us, we had obligations to complete construction of certain improvements and housing units in the event Engle/Sunbelt defaulted. Additionally, we agreed to indemnify the lenders for, among other things, potential losses resulting from violations of environmental laws, misappropriation, bankruptcy filings and similar acts by Engle/Sunbelt.

Although Engle/Sunbelt was not included in our Chapter 11 filings, our Chapter 11 filings constituted an event of default under the financing arrangements and Engle/Sunbelt's debt became immediately due and payable.

During 2007, we evaluated the recoverability of our investment in and receivables from Engle/Sunbelt for impairment under APB 18 and SFAS 114, respectively, and recorded an impairment charge of \$60.7 million,

representing the full carrying value our investment in and receivables from Engle/Sunbelt, net of deferred gains of \$22.5 million.

In April 2008, we entered into a settlement agreement with the lenders pursuant to which Engle/Sunbelt agreed to the appointment of a receiver and further agreed to either, at the election of the lenders, deliver a deed in lieu of foreclosure to its assets or consent to a judicial foreclosure. We also agreed to assist the lenders in their efforts to complete certain construction for which we would receive arm's length compensation. The Bankruptcy Court entered an order approving the settlement agreement. Pursuant to the settlement agreement, on November 20, 2008, we were relieved from our obligations under the completion and indemnity agreements.

TOUSA/Kolter Joint Venture

In January 2005, we entered into a joint venture with Kolter Real Estate Group LLC to form TOUSA/Kolter Holdings, LLC ("TOUSA/Kolter") for the purpose of acquiring, developing and selling approximately 1,900 homesites and commercial property in a master planned community in South Florida. The joint venture obtained senior and senior subordinated term loans. We entered into a Performance and Completion Agreement in favor of the lenders under which we agreed, among other things, to construct and complete the horizontal development of the lots and commercial property and related infrastructure in accordance with certain plans. The loans required, among other things, TOUSA/Kolter to have completed the development of certain lots by January 7, 2007. Due to unforeseen and unanticipated delays in the entitlement process and additional development requests by the county and water management district, TOUSA/Kolter was unable to complete the development of these certain lots by the required deadline. On September 21, 2007, and in response to missing the development deadline, TOUSA/Kolter amended the existing loan agreements and we amended the Performance and Completion Agreement to extend the Performance and Completion Agreement development deadline to May 31, 2008. The amendments to the term loan agreements increased the interest rate on the senior term loan by 100 basis points to LIBOR plus 3.25% and by 50 basis points to LIBOR plus 8.5% for the senior subordinated term loan. As a condition to the amendment, we agreed with Kolter Real Estate Group LLC to be responsible for the additional 150 basis points; accordingly, this would be a cost of the lots we acquired from

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TOUSA/Kolter. The amendment also required us to increase our existing letter of credit by an additional \$1.8 million to \$12.1 million and place an additional \$3.0 million cash deposit on the remaining lots under option. The \$3.0 million was used by TOUSA/Kolter to pay down a portion of the senior term loan.

As we had abandoned our rights under the option contract due to non-performance, we recorded an obligation of \$12.1 million for the letter of credit we anticipated would be drawn, wrote-off the \$3.0 million cash deposit and \$1.0 million in capitalized pre-acquisition costs in 2007. In 2008, the letter of credit was drawn and used to reduce the joint venture's term loan outstanding.

The lenders to the joint venture declared the loan to the venture to be in default. The Remargining Agreement required us to pay to the Administrative Agent, upon default of the joint venture, an amount necessary to decrease the principal balance of the loan so that the outstanding balance did not exceed 70% of the value of the joint venture's assets. Based on the estimated fair value of the assets of the joint venture, we recorded a \$54.0 million obligation (which included the \$12.1 million letter of credit accrual) in 2007 in connection with our obligation under the re-margining provisions of the loan agreement. We did not record any additional contingent liability under the completion guarantee as the \$54.0 million accrual represented the full debt obligation of the joint venture. At December 31, 2007, the obligation of \$54.0 million is included in accounts payable and other liabilities in the accompanying unaudited consolidated statements of financial condition. As a result of the 2009 transaction discussed below, we reduced the obligation for \$8.5 million of loan forgiveness, \$11.7 million of drawn letters of credit and \$2.3 million of escrowed interest applied to the loan balance, leaving a remaining obligation at September 30, 2008 of \$31.5 million, which is included in liabilities subject to compromise in the accompanying unaudited consolidated statement of financial condition.

During 2007, we evaluated the recoverability of our investment and receivables from TOUSA/Kolter for impairment under APB 18 and SFAS 114, respectively, and recorded an impairment charge of \$58.8 million representing the full carrying value of our investment in and receivables from TOUSA/Kolter, net of deferred gains of \$12.8 million, which were deferred as a result of the contributed assets and contract assignments to TOUSA/Kolter. Additionally, in 2007 we recorded an obligation of \$18.9 million for performance bonds and letters of credit that we placed on behalf of the joint venture, as we considered it probable that we would be required to reimburse these amounts for development remaining to be completed. At September 30, 2008 and December 31, 2007, the obligation for performance bonds and letters of credit of \$13.7 million and \$18.9 million, respectively, is included in liabilities subject to compromise and accounts payable and other liabilities, respectively, in the accompanying unaudited consolidated statements of financial condition.

On January 28, 2009, we entered into an agreement with CC Loan Acquisition LLC, which had purchased the loans to the joint venture and the Community Development District Bonds related to the project. The joint venture deeded the property to CC Loan Acquisition LLC and received an extension of the maturity of the B Bonds until May 1, 2013. A portion of the outstanding joint venture indebtedness was also satisfied and the amount collectible from CC Loan Acquisition LLC under filed proofs of claim related to the Completion Agreement was limited. This agreement was approved by the Bankruptcy Court on January 9, 2009.

Centex/TOUSA at Wellington, LLC

In December 2005, we entered into a joint venture with Centex Corporation to form Centex/TOUSA at Wellington, LLC (Centex/TOUSA at Wellington) for the purpose of acquiring, developing and selling approximately 264 homesites in a community in South Florida. The joint venture obtained a term loan of which \$31.0 million was outstanding as of September 30, 2008 and December 31, 2007. The credit agreement requires us to construct and complete the horizontal development of the lots and related infrastructure in accordance with certain agreed upon plans. On August 31, 2007, Centex/TOUSA at Wellington received a notice from the lender requiring the joint venture members to contribute approximately \$10.0 million to the joint venture to reduce the outstanding term loan in order to comply with the 60% loan-to-value ratio covenant. We have not made the required equity contribution.

We evaluated the recoverability of our investment in and receivables from Centex/TOUSA at Wellington for impairment under APB 18 and SFAS 114 respectively, and recorded an impairment of \$27.0 million representing the full carrying value of our investment in and receivables from Centex/TOUSA at Wellington during 2007. Based on the estimated fair value of the assets of the joint venture, we recorded a \$15.5 million liability in 2007, in connection

with our obligation under the re-margining provisions of the loan agreement which represents our portion of the joint venture's outstanding debt. We did not record any additional contingent liability under the completion guarantee as the \$15.5 million accrual represents our portion of the full joint venture debt obligation. At September 30, 2008 and December 31, 2007, the \$15.5 million obligation is included in liabilities subject to compromise and accounts payable and other liabilities, respectively, in the accompanying unaudited consolidated statements of financial condition.

We have entered into an agreement with our joint venture partner pursuant to which we will surrender our interest in the joint venture, be relieved from any liability owed to the venture or under the guarantees and convey our ownership interest in 44 lots to the venture for \$1.1 million, less applicable real estate taxes. The agreement is subject to Bankruptcy Court approval.

Layton Lakes Joint Venture

In connection with our joint venture with Lennar Corporation (the Layton Lakes Joint Venture) to acquire and develop land, townhome properties and commercial property in Gilbert, Arizona, we entered into a Completion and Limited Indemnity Agreement for the benefit of the lender to the joint venture.

We evaluated the recoverability of our investment in and receivables from the Layton Lakes Joint Venture for impairment under APB 18 and SFAS 114, respectively, and recorded an impairment charge of \$24.9 million representing the full carrying value of our investment in and receivables from the Layton Lakes Joint Venture during 2007. At that time, we did not record any obligation under the re-margining provision as we were not a party to the re-margining agreement. The remargining agreement required that the outstanding loan balance not exceed 65% of the value of the joint venture's assets. Additionally, in 2007 we recorded an obligation of \$4.4 million for performance bonds that we placed on behalf of the joint venture, as we considered it probable that we would be required to reimburse these amounts for development remaining to be completed. We did not record any additional contingent liability under the completion guarantee as based on

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the estimated fair value of the assets of the joint venture; we did not believe that it was probable that we would be called to perform under the completion obligation.

The joint venture also breached various other loan covenants. As a result of our defaults, including our failure to maintain a required net worth, we did not have the right to take down lots or vote as a member of the joint venture.

Tousa, Tousa Homes, Inc., Lennar and the Town of Gilbert, Arizona entered into a series of agreements pursuant to which, among other things, we surrendered our interest in the joint venture and paid \$1.3 million toward completion of certain offsite improvements. In exchange, we were granted an option to continue acquiring lots and the Town of Gilbert agreed to issue certificates of occupancy for certain homes under construction. Tousa, Tousa Homes, Inc., Lennar and Bank Midwest each agreed to mutual releases of claims related to the Layton Lakes Joint Venture. The Bankruptcy Court approved these agreements on November 25, 2008. As a result of this settlement and certain work performed by our joint venture partner, we reversed \$4.4 million of our accrual for estimated obligations under the performance bonds during the nine months ended September 30, 2008.

Other

Certain of our other ongoing unconsolidated land development joint ventures have outstanding debt obligations totaling \$12.4 million and \$20.6 million at September 30, 2008 and December 31, 2007, respectively. These joint venture borrowings are non-recourse to us except that in certain instances we have agreed to complete certain property development commitments in the event the joint venture defaults and to indemnify the lenders for losses resulting from fraud, misappropriation, violations of environmental laws and similar acts.

6. Other Assets

Other assets consist of the following (in millions):

	September 30, 2008	December 31, 2007
Homebuilding:		
Income taxes receivable	\$	\$ 218.4
Accounts receivable	26.5	34.7
Deferred finance costs, net		55.8
Prepaid expenses	13.3	20.3
Deposits and other assets	22.2	0.8
Total other assets	\$ 62.0	\$ 330.0

During the nine months ended September 30, 2008, we wrote off \$54.4 million of deferred finance costs related to our unsecured and under-secured debt obligations which have been classified as liabilities subject to compromise and are recorded at amounts expected to be allowed by the Bankruptcy Court.

In April 2008, we received a \$207.3 million refund of previously paid income taxes for 2005 and 2006 through the carryback of our taxable loss from 2007.

7. Goodwill

Goodwill represents the excess of the purchase price of our acquisitions over the fair value of the net assets acquired. Additional consideration paid in subsequent periods under the terms of purchase agreements is included as acquisition costs.

In accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*, we test goodwill for impairment annually or more frequently if certain impairment indicators are present. For purposes of the impairment test, we consider each homebuilding and financial services entity a reporting unit. Our impairment test is based on discounted cash flows derived from internal projections. This process requires us to make assumptions on future revenues, costs, and timing of expected cash flows. Due to the degree of judgment required and uncertainties surrounding such estimates, actual results could differ from such estimates. To the extent additional information arises or our strategies change, it is possible that our conclusion regarding goodwill impairment could change, which could have a material

adverse effect on our financial position and results of operations. During the nine months ended September 30, 2008, we determined that the challenging housing market and the asset impairments taken in certain of our homebuilding divisions were indicators of impairment. All goodwill was impaired as of June 30, 2008. We performed our interim impairment tests as of March 31, 2008 and June 30, 2008, which resulted in a goodwill impairment for the nine months ended September 30, 2008 of \$11.2 million (\$1.6 million related to the Mid-Atlantic region and \$9.6 million related to the Texas region). During the three months ended September 30, 2007, we recorded a goodwill impairment charge in our Southwest Florida division of \$2.7 million. During the nine months ended September 30, 2007, we recorded goodwill impairments totaling \$40.9 million in our Southwest Florida (\$2.7 million), Virginia (\$6.5 million), Mid-Atlantic (\$21.2 million) and Las Vegas (\$10.5 million) divisions. Additionally, during the nine months ended September 30, 2007, we wrote-off \$3.1 million of goodwill related to our Dallas division that has been accounted for as a discontinued operation.

At September 30, 2008, there is no remaining goodwill. At December 31, 2007, total goodwill is \$11.2 million, consisting of \$1.6 million related to the Mid-Atlantic region and \$9.6 million related to the Texas region.

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Accounts payable and other liabilities consist of the following (in millions):

	September 30, 2008	December 31, 2007
Homebuilding:		
Accounts payable	\$ 36.8	\$ 41.8
Interest	9.7	48.4
Compensation	10.7	14.8
Taxes, including income and real estate	12.7	22.6
Accrual for unpaid invoices on delivered homes	19.6	27.9
Accrued expenses	2.6	90.7
Community development district bond obligations	26.7	29.6
Obligations related to unconsolidated joint ventures		74.6
Accrued letters of credit expected to be drawn		43.6
Warranty costs	2.7	5.0
Deferred revenue	0.1	2.8
Total accounts payable and other liabilities⁽¹⁾	\$ 121.6	\$ 401.8

⁽¹⁾ Certain accounts payable and other liabilities at September 30, 2008 have been classified as liabilities subject to compromise.

In connection with the development of certain of our communities, community development or improvement districts may utilize tax-exempt bond financing to fund construction or acquisition of certain on-site and off-site infrastructure improvements. Some bonds are repaid directly by us while other bonds only require us to pay non-ad valorem assessments related to lots not yet delivered to residents. These bonds are typically secured by the property and are repaid from assessments levied on the property over time. We also guarantee district shortfalls under certain bond debt service agreements when the revenues, fees and assessments, which are designed to cover principal, interest and other operating costs of the bonds, are insufficient. In accordance with EITF 91-10, *Accounting for Special Assessments and Tax Increment Financing*, we record a liability for future assessments, which are fixed and determinable for a fixed or determinable period. In addition and in accordance with SFAS 5, we evaluate whether we are contingently liable for any of the debt related to the bond issuance. Community development district bond obligations were \$26.7 million and \$29.6 million at September 30, 2008 and December 31, 2007, respectively.

At September 30, 2008, we have total outstanding performance / surety bonds of \$140.6 million related to land development activities and have estimated our exposure on our outstanding surety bonds to be \$54.5 million based on land development remaining to be completed. At September 30, 2008 and December 31, 2007, our accrual totaled \$41.8 million and \$48.0 million, respectively, for surety bonds where we consider it probable that the surety has a claim for reimbursement for amounts drawn related to defaulted agreements, which is included as a liability subject to compromise and accounts payable and other liabilities, respectively, in the accompanying unaudited consolidated statements of financial condition.

9. Homebuilding and Financial Services Borrowings**Homebuilding Borrowings**

Homebuilding borrowings consist of the following (in millions):

	September 30, 2008	December 31, 2007
Revolving Loan Facility	\$ 223.1	\$ 168.5

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First Lien Term Loan Facility due 2012	161.3	199.0
Discount on First Lien Term Loan Facility ⁽¹⁾		(1.8)
Second Lien Term Loan Facility due 2013	352.6	317.1
Discount on Second Lien Term Loan Facility ⁽¹⁾		(2.8)
Senior notes due 2010, at 9%	300.0	300.0
Senior notes due 2011, at 8 1/4%	250.0	250.0
Discount on senior notes ⁽¹⁾		(2.5)
Senior subordinated notes due 2012, at 10 3/8%	185.0	185.0
Senior subordinated notes due 2011, at 7 1/2%	125.0	125.0
Senior subordinated notes due 2015, at 7 1/2%	200.0	200.0
Premium on senior subordinated notes ⁽¹⁾		3.7
Senior Subordinated PIK Notes due 2015, at 14 3/4%	24.0	21.3
Discount on Senior Subordinated PIK Notes ⁽¹⁾		(8.7)
	1,821.0	1,753.8
Less: Amounts classified as liabilities subject to compromise (see Note 2)	(1,821.0)	
	\$	\$ 1,753.8

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(1) During the nine months ended September 30, 2008, we wrote-off \$11.9 million of debt premium and discounts related to our debt obligations which have been classified as liabilities subject to compromise (see Note 2).

The filing of the Chapter 11 cases triggered repayment obligations under a number of instruments and agreements relating to our direct and indirect financial obligations. As a result, all our borrowings became automatically and immediately due and payable. We believe that any efforts to enforce the payment obligations are stayed as a result of the filing of the Chapter 11 cases.

We are authorized by the Bankruptcy Court order to use cash collateral of our first lien and second lien lenders in a manner consistent with a budget negotiated by the parties. The order further provided for the pay-down of \$175.0 million to our first lien term secured lenders, subject to disgorgement provisions in the event that certain claims against the lenders are successful and repayment is required. We also have the right to pay-down an additional \$15.0 million to our first lien secured lenders. As of May 1, 2009, we had paid-down \$148.4 million to the first lien secured lenders. We may incur liens and enter into sale/leaseback transactions for model homes subject to certain limitations. We have granted the pre-petition agents and the lenders various forms of protection, including liens and claims to protect against any diminution of the collateral value, payment of accrued, but unpaid interest on the first priority indebtedness at the non-default rate and the payment of reasonable fees and expenses of the agents under our secured facilities.

Our right to the use of cash collateral has been extended until July 31, 2009 on terms substantially similar to those in the original cash collateral order. If we fail to comply with the order, we will not have sufficient cash to enable us to operate our business and effectuate our restructuring.

Revolving Loan Facility and First and Second Lien Term Loan Facilities

To effect the TE Acquisition, on July 31, 2007, we entered into (1) the \$200.0 million aggregate principal amount first lien term loan facility (the First Lien Term Loan Facility) and (2) the \$300.0 million aggregate principal amount second lien term loan facility (the Second Lien Term Loan Facility), (First and Second Lien Term Loan Facilities taken together, the Facilities). At September 30, 2008 and December 31, 2007, we had \$223.1 million and \$168.5 million, respectively, outstanding under our revolving loan facility (the Revolving Loan Facility). There is no additional capacity available under the Revolving Loan Facility other than for letters of credit presented to the bank. The Revolving Loan Facility expires on March 9, 2010. The First Lien Term Loan Facility expires on July 31, 2012 and the Second Lien Term Loan Facility expires on July 31, 2013. At September 30, 2008, the Revolving Loan Facility and the Facilities are classified as liabilities subject to compromise (see Note 2).

The interest rates on the Facilities and the Revolving Loan Facility are based on LIBOR plus a margin or an alternate base rate plus a margin, at our option. For the Revolving Loan Facility, the LIBOR rates are increased by between 2.50% and 5.25% depending on our leverage ratio (as defined in the Agreement) and credit ratings. Loans bearing interest at the base rate (the rate announced by Citibank as its base rate or 0.50% above the Federal Funds Rate) increase between 1.00% and 4.25% in accordance with the same criteria. Based on our current leverage ratio and credit ratings, our LIBOR loans bear interest at LIBOR plus 5.25% and our base rate loans bear interest at the Federal Funds Rate plus 4.25%. For the First Lien Term Loan Facility, the interest rate is LIBOR plus 5.00% or base rate plus 4.00%. For the Second Lien Term Loan Facility, the interest rate is LIBOR plus 7.25% or base rate plus 6.25%. The Second Lien Term Loan Facility allows us to pay interest, at our option, (1) in cash, (2) entirely by increasing the principal amount of the Second Lien Term Loan Facility, or (3) a combination thereof. The Facilities and the Revolving Loan Facility are guaranteed by substantially all of our domestic subsidiaries (Guarantor Subsidiaries). The obligations are secured by substantially all of our assets, including those of our subsidiaries other than our mortgage and title subsidiaries.

Senior Notes and Senior Subordinated Notes

Our outstanding senior notes are guaranteed, on a joint and several basis, by the Guarantor Subsidiaries, which are all of our material domestic subsidiaries, other than our mortgage and title subsidiaries (the Non-Guarantor Subsidiaries). Our outstanding senior subordinated notes are guaranteed on a senior subordinated basis by all of the Guarantor Subsidiaries. The senior notes rank *pari passu* in right of payment with all of our existing and future unsecured senior debt and senior in right of payment to our senior subordinated notes and any future subordinated

debt. The senior subordinated notes rank *pari passu* in right of payment with all of our existing and future unsecured senior subordinated debt. The indentures governing the senior notes and senior subordinated notes generally require us to maintain a minimum consolidated net worth and place certain restrictions on our ability, among other things, to incur additional debt, pay or declare dividends or other restricted payments, sell assets, enter into transactions with affiliates, invest in joint ventures above specified amounts and merge or consolidate with other entities. Interest on our outstanding senior notes and senior subordinated notes is payable semi-annually. In accordance with SOP 90-7, as of January 29, 2008, the petition date, we ceased accruing interest on the senior notes and the senior subordinated notes as these are unsecured claims and are not entitled to interest upon filing of petitions for relief under Chapter 11. At September 30, 2008, the senior notes and senior subordinated notes are classified as liabilities subject to compromise (see Note 2).

Special Interest

In connection with the issuance of the \$250.0 million 8 1/4% senior notes, we filed within 90 days of the issuance a registration statement with the SEC covering a registered offer to exchange the notes for exchange notes of ours having terms substantially identical in all material respects to the notes. The registration statement was not declared effective within the required 180 days of issuance and was withdrawn in 2008. As a result, on October 9, 2006, in accordance with their terms, the notes became subject to special interest which accrues at a rate of 0.25% per annum during the 90-day period immediately following the occurrence of such default, and increases by 0.25% per annum at the end of each 90-day period, up to a maximum of 1.0% per annum. In accordance with SOP 90-7, as of January 29, 2008, the petition date, we ceased accruing special interest and reversed \$2.3 million of the interest expense that had been previously accrued as these are unsecured claims and not entitled to interest upon filing petitions for relief under Chapter 11.

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As part of the transactions to settle the disputes regarding the Transeastern JV, on July 31, 2007, the senior mezzanine lenders to the Transeastern JV received \$20.0 million in aggregate principal amount of 14.75% Senior Subordinated PIK Election Notes (PIK Notes) due 2015.

Interest on the PIK Notes is payable semi-annually. The PIK Notes are unsecured senior subordinated obligations of ours, and are guaranteed on an unsecured senior subordinated basis by each of our existing and future subsidiaries that guarantee our 7.5% Senior Subordinated Notes due 2015 (the Existing Notes). We are required to pay 1% of the interest in cash and the remaining 13.75%, at our option, (i) in cash, (ii) entirely by increasing the principal amount of the PIK Notes or issuing new notes, or (iii) a combination thereof. The PIK Notes mature on July 1, 2015. The indenture governing the PIK Notes contains the same covenants as contained in the indenture governing the Existing Notes and is subject, in most cases, to any change to such covenants made to the indenture governing the Existing Notes. The PIK Notes are redeemable by us at redemption prices greater than their principal amount. The PIK Notes contain an optional redemption feature that allows us to redeem up to a maximum of 35% of the aggregate principal amount of the PIK Notes using the proceeds of subsequent sales of its equity interest at 114.75% of the aggregate principal amount of the PIK Notes then outstanding, plus accrued and unpaid interest. Additionally, after July 1, 2012, subject to certain terms of our other debt agreements, we may redeem the PIK Notes at a premium to the principal amount as follows: 2012 107.375%; 2013 103.688%; 2014 and thereafter 100.000%. The call options exercisable at anytime after July 1, 2012 at a premium do not require bifurcation under SFAS 133 because they are only exercisable by us and they are not contingently exercisable. The redemption option is conditionally exercisable based on the proceeds raised from an equity offering at 114.75% of up to 35% of the aggregate outstanding PIK Notes principal and represents an embedded call option that must be bifurcated from the PIK Notes; however, the fair value of this call option is not material and has not been bifurcated from the host instrument.

The PIK Notes provide for registration rights for the holders whereby the interest rate increases by 0.25% per annum for the first 90 days of a registration default, as defined, which amount increases by an additional 0.25% every 90 days a registration default is continuing, not to exceed 1.0% in the aggregate, from and including the date of the registration default to and excluding the date on which the registration default is cured. Registration default payments may be paid, at our option, in cash, additional PIK Notes, or a combination thereof.

At September 30, 2008, the PIK Notes are classified as liabilities subject to compromise (see Note 2).

Financial Services Borrowings

On January 28, 2008, Preferred Home Mortgage Company, our wholly-owned residential mortgage lending subsidiary, entered into an Amended and Restated Agreement of Limited Liability Company with Wells Fargo Ventures, LLC. The limited liability company is known as PHMCWF, LLC but does business as Preferred Home Mortgage Company, an affiliate of Wells Fargo. Preferred Home Mortgage Company owns 49.9% of the venture with the balance owned by Wells Fargo. Effective April 1, 2008, the venture began to carry on the mortgage business of Preferred Home Mortgage Company. The venture is managed by a committee composed of six members, three from Preferred Home Mortgage Company and three from Wells Fargo. The venture entered into a revolving credit agreement with Wells Fargo Bank, N.A. providing for advances of up to \$20.0 million. Wells Fargo Home Mortgage provides the general and administrative support (as well as all loan related processing, underwriting and closing functions), and is the end investor for the majority of the loans closed through the joint venture. Prior to the joint venture, Preferred Home Mortgage Company had a centralized operations center that provided those support functions. The majority of these support functions ceased in June 2008. Effective April 1, 2008, we began to account for the venture as an equity-method investment.

Until December 4, 2008, the subsidiary had two warehouse lines of credit in place to fund the origination of residential mortgage loans. The revolving warehouse line of credit (the Warehouse Line of Credit), which was entered into on December 5, 2007, provided for revolving loans of up to \$25.0 million. The Warehouse Line of Credit replaced the \$100.0 million revolving warehouse line of credit that expired on December 8, 2007. From January 25, 2008 through December 4, 2008, the availability under the Warehouse Line of Credit was reduced to \$15.0 million. The \$150.0 million mortgage loan purchase facility (Purchase Facility) was amended to decrease the size of the facility to \$75.0 million. From January 25, 2008 through December 4, 2008, the availability under the Purchase

Facility was reduced to \$40.0 million. However, we had agreed with the lender not to utilize these facilities. The Warehouse Line of Credit bore interest at the 30-day LIBOR rate plus a margin of 2.0%, was secured by funded mortgages, which were pledged as collateral, and required our mortgage subsidiary to maintain certain financial ratios and minimums. The Warehouse Line of Credit also placed certain restrictions on, among other things, our mortgage subsidiary's ability to incur additional debt, create liens, pay or make dividends or other distributions, make equity investments, enter into transactions with affiliates, and merge or consolidate with other entities. Our mortgage subsidiary was in compliance with all covenants and restrictions at September 30, 2008. At September 30, 2008, our mortgage subsidiary had no outstanding borrowings.

10. Income Taxes

We account for income taxes in accordance with SFAS No. 109, *Accounting for Income Taxes* (SFAS 109), as interpreted by FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48). Under SFAS 109, income taxes are accounted for using the asset and liability method. Deferred tax assets and liabilities are recognized based on the anticipated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

We are subject to U.S. federal income tax as well as to income tax in multiple state jurisdictions. We have effectively closed all U.S. federal income tax matters for years through 2004. The Internal Revenue Service has concluded its review of our 2005 through 2007 consolidated tax returns and has submitted its report to the Joint Committee on Taxation under the normal procedures applicable to taxpayers with refunds in excess of \$2.0 million. As we understand, that report did not propose any changes to the returns as filed. We are awaiting the Joint Committee's acceptance of the findings included in that report. Management believes that all other tax liabilities recorded are adequate and the tax refunds received properly reflect the amounts due to us from the applicable taxing authorities.

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It is our continuing policy to account for interest and penalties associated with income tax obligations as a component of income tax expense.

SFAS 109 requires that companies assess whether valuation allowances should be established based on the consideration of all available evidence using a more likely than not standard. We assess our deferred tax assets quarterly to determine if valuation allowances are required. Pursuant to SFAS 109, we were unable to record an income tax benefit for the three and nine months ended September 30, 2008, as all recognizable tax benefits under current tax law were recorded in prior years. Our valuation allowance increased by \$47.4 million and \$279.8 million, respectively, for the three and nine months ended September 30, 2008 to \$785.5 million at September 30, 2008.

Our results of operations may be impacted in the future by our inability to realize a tax benefit for future tax losses or for items that will generate additional deferred tax assets. Our results of operations might be favorably impacted in the future by reversals of valuation allowances if we are able to demonstrate sufficient positive evidence that our deferred tax assets will be realized. However, there could be restrictions on the amount of the carryforwards that can be utilized if certain changes in our ownership should occur which would likely significantly limit potential future benefit, even if we could demonstrate sufficient positive evidence that our deferred taxes could otherwise be realized.

In April 2008, we received a \$207.3 million refund of previously paid income taxes for 2005 and 2006 through the carryback of our taxable loss from 2007.

During the three months ended September 30, 2008, we reduced our unrecognized tax benefit by \$2.7 million primarily due to a favorable ruling received from the Internal Revenue Service related to an uncertain tax position. This reduction was offset by \$0.7 million of interest on previously recorded amounts, resulting in a net \$2.0 million benefit for the nine months ended September 30, 2008.

11. Commitments and Contingencies

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

Warranty

We provide homebuyers with a limited warranty of workmanship and materials from the date of sale for up to two years. We generally have recourse against our subcontractors for claims relating to workmanship and materials. In some cases, we also provide up to a ten-year homeowner's warranty which covers major structural and design defects related to homes sold by us during the policy period, subject to a significant self-insured retention per occurrence. Estimated warranty costs are recorded at the time of sale based on historical experience and current trends. Warranty costs are included in accounts payable and other liabilities in the accompanying unaudited consolidated statements of financial condition.

During the nine months ended September 30, 2008 and 2007, the activity in our warranty cost accrual consisted of the following (in millions):

	Nine Months Ended September 30,	
	2008	2007
Accrued warranty costs at January 1	\$ 5.0	\$ 7.4
Liability recorded for warranties issued during the period	2.1	4.4
Warranty work performed	(8.4)	(4.4)
Adjustments	4.0	(2.0)
Accrued warranty costs at September 30	\$ 2.7	\$ 5.4

To address potential homebuyer concerns regarding fulfillment of warranty obligations at the inception of our Chapter 11 cases, we entered into an agreement with Professional Warranty Service Corporation to guarantee our warranty obligations for the first ten years after closing and assume all liability for structural claims in years three

through ten. Effective April 15, 2009, with Bankruptcy Court approval and to alleviate potential concerns related to our new operating model, we entered into an agreement with Professional Warranty Service Corporation to directly provide warranty service for all homes sold or delivered by us from January 21, 2008 through April 30, 2010. We paid \$4.5 million (which includes the surrender of any rights to receive a refund of premiums paid under the initial program) for this coverage plus a premium based on the sale price of each home delivered. As a result of our Chapter 11 filings, we have generally ceased performing warranty services for homes not covered by the Professional Warranty Service Corporation program.

Letters of Credit and Performance Bonds

We are subject to the normal obligations associated with entering into contracts for the purchase, development and sale of real estate in the routine conduct of our business. We are committed under various letters of credit and performance bonds which are required for certain development activities, deposits on land and deposits on homesite purchase contracts. Under these arrangements, we had total outstanding letters of credit of \$19.1 million as of September 30, 2008. As a result of abandoning our rights under option contracts, as of September 30, 2008, we accrued \$3.5 million for letters of credit which we anticipated would be drawn due to nonperformance under such contracts. From October 1, 2008 through April 30, 2009, an additional \$0.8 million of letters of credit have been drawn related to the

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abandonment of option contracts which have increased our borrowings outstanding under our Revolving Loan Facility. In certain instances, we have entered into development agreements in connection with option contracts which require us to complete the development of the land, at a fixed reimbursable amount, even if we choose not to exercise our option and forfeit our deposit and even if our costs exceed the reimbursable amount.

At September 30, 2008, we have total outstanding performance / surety bonds of \$140.6 million related to land development activities and have estimated our exposure on our outstanding surety bonds to be \$54.5 million based on land development remaining to be completed. At September 30, 2008 and December 31, 2007, our accrual totaled \$41.8 million and \$48.0 million, respectively, for surety bonds where we consider it probable that the surety has a claim for reimbursement for amounts drawn related to defaulted agreements, which is included as a liability subject to compromise and accounts payable and other liabilities, respectively, in the accompanying unaudited consolidated statements of financial condition.

Until the establishment of a surety bond program in January 2009, we had no ability to obtain new surety bonds or letters of credit and in some cases, had to post cash deposits with government entities or escrow agents. Under the program approved by the Bankruptcy Court, we have an aggregate \$15.0 million available for surety bonds. Surety bonds are issued after notice to creditors who have a right to object. The surety bonds are collateralized by cash deposits maintained in escrow accounts. At April 30, 2009, \$2.5 million was maintained as collateral for surety bonds.

Exposure on Abandoned Homesite Option Contracts

See Note 3.

Chapter 11 Cases

On January 29, 2008, TOUSA, Inc. and certain of our subsidiaries (excluding our financial services subsidiaries and joint ventures) filed voluntary petitions relief under Chapter 11 of Title 11 of the United States Code in the United States Bankruptcy Court for the Southern District of Florida, Fort Lauderdale Division. The Chapter 11 cases have been consolidated solely for procedural purposes and are pending as Case No. 08-10928-JKO. See Note 1 for additional discussion.

Securities Class Action Lawsuit

Beginning in December 2006, various stockholder plaintiffs brought lawsuits seeking class action status in the United States District Court for the Southern District of Florida. The actions were consolidated, and the consolidated suit is pending under the caption *Durgin, et al., v. TOUSA, Inc., et al., No. 06-61844-CIV*. On September 7, 2007, the Court appointed Diamondback Capital Management, L.C. (Diamondback) as the lead plaintiff and approved Diamondback's selection of counsel. Diamondback filed a consolidated complaint on November 2, 2007. The consolidated complaint set forth a proposed class period of August 1, 2005 to March 19, 2007 and alleged that TOUSA's public filings and other public statements were false and misleading in describing the financing for the Transeastern Joint Venture as non-recourse to TOUSA, and in describing the Transeastern Joint Venture's financial condition during the class period. Plaintiffs also alleged in the consolidated complaint that certain public filings and statements were misleading or suffered from material omissions in failing to fully disclose or describe the Completion and Carve-Out Guarantees that TOUSA executed in support of the Transeastern Joint Venture's financing. The consolidated complaint included claims under Section 11 of the Securities Act for strict liability and negligence regarding the registration statements and prospectus associated with the September 2005 offering of four million shares of stock. Plaintiffs asserted related claims against certain of the defendants as controlling persons responsible for the statements in the registration statements and prospectus. Finally, plaintiffs alleged claims under Section 10(b) of the Exchange Act for fraud with respect to various public statements regarding the non-recourse nature of the Transeastern debt, regarding the Completion and Carve-Out Guarantees, and regarding the financial condition of the Transeastern Joint Venture. Plaintiffs sought by way of the consolidated complaint compensatory damages, plus fees and costs, on behalf of themselves and the putative class of purchasers of TOUSA common stock and purchasers and sellers of options on TOUSA common stock.

On January 30, 2008, TOUSA and various other defendants filed motions to dismiss plaintiffs' Consolidated Complaint. On February 4, 2008, TOUSA filed a Notice of Suggestion of Bankruptcy notifying the court that TOUSA filed a bankruptcy petition. On February 5, 2008, the Court entered an order staying the action as to TOUSA pursuant to Section 362 of the United States Bankruptcy Code.

On April 30, 2008, lead plaintiff Diamondback filed a motion to withdraw as lead plaintiff, which the court granted on May 22, 2008. On July 15, 2008, the court appointed the Bricklayers & Trowel Trades International Pension Fund (the Bricklayers) as the new lead plaintiff. On July 30, 2008, the Bricklayers filed a notice of an intent to file an amended complaint and accordingly, on July 31, 2008, the court denied as moot without prejudice the defendants previously filed motions to dismiss the consolidated complaint.

On September 19, 2008, the Bricklayers filed a Consolidated Amended Class Action Complaint (the amended complaint). This amended complaint dropped many of the parties previously named as defendants in the consolidated complaint, including TOUSA, leaving only Antonio B. Mon, Tommy McAden, David J. Keller and Randy L. Kotler as defendants in the suit. The amended complaint also dropped the Section 11 and Section 15 claims, leaving the claims under Section 10(b) of the Exchange Act and Rule 10b-5, as well as the claims made under Section 20(a) of the Exchange Act. Defendants Mon, Keller and Kotler filed motions to dismiss the amended complaint on November 21, 2008. Defendant McAden had not yet been served, but his counsel recently entered an appearance and filed a motion to dismiss on March 2, 2009. The plaintiff filed its opposition to the motions to dismiss on March 24, 2009.

Defendants' replies in support of their motions to dismiss were due on May 13, 2009. A trial date has not yet been set.

Proceeding by Official Committee of Unsecured Creditors

In re TOUSA, Inc., Docket No. 08-10928-JKO; Adv. Pro No. 08-1435-JKO. We and certain of our subsidiaries are involved in an adversary proceeding brought as part of our Chapter 11 proceedings. On July 14, 2008, the Official Committee of Unsecured Creditors of TOUSA, Inc. (the Committee) commenced an adversary proceeding (the Committee Action) as part of our and certain of our

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subsidiaries (collectively, the Debtors) Chapter 11 proceedings in United States Bankruptcy Court for the Southern District of Florida. The Debtors were originally non-parties to the Committee Action, but have since been named as third-party defendants by certain of the original defendants in the Committee Action.

The Committee Action seeks to avoid certain allegedly fraudulent and preferential pre-petition transfers of up to \$800 million the Debtors made in connection with the settlement of litigation related to the Transeastern Joint Venture (the Transeastern Settlement), and further seeks to avoid as a preferential transfer any security interest that may have been granted by any of the Debtors to certain lenders in a tax refund of approximately \$207.0 million that the Debtors received in 2008. The Committee s original complaint (the Complaint) named over 60 defendants, including the lenders under the credit agreements funding the Transeastern Joint Venture (the Transeastern Lenders), as well as the original lenders (and their successors and assigns) and administrators under the credit agreements entered into as a result of the Transeastern Settlement (the New Credit Agreements). The Debtors are not defendants to the Committee s claims in the Committee Action.

The Committee s Complaint alleged that, in order to resolve certain prepetition litigation regarding the Transeastern Joint Venture, the parties to that litigation entered into a series of settlement agreements releasing all claims relating to the Transeastern acquisition. The Complaint alleges that, as part of these settlement agreements, certain of our entities agreed to pay over \$420 million to the administrator of the Transeastern loans and to issue approximately \$135 million in preferred stock, notes and warrants. The Complaint further alleged that to fund these payments, we and certain of our subsidiaries (the Conveying Subsidiaries) entered into the three New Credit Agreements. According to the Complaint, the loans issued under these New Credit Agreements were secured by liens on the property and assets of all of the Debtors, including the Conveying Subsidiaries. The Complaint alleged that the Conveying Subsidiaries were not defendants in the prepetition Transeastern litigation and were not obligated on the Transeastern debt that was released in connection with the Transeastern Settlement. Therefore, the Complaint alleged, the Conveying Subsidiaries did not receive reasonably equivalent value for the secured debt obligations that they incurred. The Complaint also alleged that the Conveying Subsidiaries were either insolvent at the time of the Transeastern Settlement or became insolvent as a result of it, and that the Conveying Subsidiaries were left with unreasonably small capital as a result of the New Credit Agreements. Based on these allegations, the Committee seeks to have the liens established under the New Credit Agreements voided and all amounts already repaid under the New Credit Agreements returned. The Committee also seeks to have the security interest the Debtors granted to the New Lenders on the Debtors tax refund voided and the New Lenders claims seeking allowance of the full amount of the New Loans disallowed in their entirety or reduced.

On September 19, 2008, the Bankruptcy Court held a hearing on motions to dismiss that had been filed by Defendants Citicorp North America, Inc., and Wells Fargo Bank, N.A. Well Fargo s motion to dismiss was denied. Citicorp s motion to dismiss sought dismissal of claims relating to only one of the three New Credit Agreements, the Second Amended And Restated Revolving Credit Agreement (the Revolver). The Court granted Citicorp s motion to dismiss, but granted the Committee leave to file an amended complaint.

On October 17, 2008, the Committee filed an Amended Complaint. The Amended Complaint contained additional allegations regarding the Revolver, and added new defendants. Citicorp moved to dismiss the claims in the Amended Complaint relating to the Revolver. In addition, the Transeastern Lenders moved to dismiss all claims against them. The Court denied the Transeastern Lenders motion to dismiss. The Court granted Citicorp s motion to dismiss the Revolver claims in the Amended Complaint, but again granted the Committee leave to file a second amended complaint consistent with the Court s specific guidance on the revolver issue. After initially filing a Second Amended Complaint again including claims related to the Revolver, on February 4, 2009, the Committee filed a Third Amended Complaint which did not include claims relating to the Revolver. The Committee has, however, appealed to the District Court the dismissal of the Revolver claims in the Amended Complaint.

In addition, on August 13, 2008, Citicorp North America, Inc., in its capacity as the Administrative Agent for the First Lien Term Loan, answered the Complaint in the Committee Action, and filed a third-party complaint (the

Citigroup Third-Party Complaint) against TOUSA, Inc. and each of the Debtor signatories, co-borrowers and co-guarantors under the First Lien Term Loan. The Citigroup Third-Party Complaint alleges that, to the extent the Committee establishes its allegations in the Committee Action, the defendants to the Citigroup Third-Party Complaint

will have materially breached the First Lien Term Loan by (a) not having assets whose fair value exceeded their debts and liabilities, subordinated, contingent or otherwise, (b) not having assets whose fair saleable value exceed their debts and other liabilities, subordinated, contingent or otherwise, (c) not being able to pay their debts and liabilities, subordinated, contingent, or otherwise, and/or (d) having unreasonably small capital with which to conduct their business. On September 30, 2008 the Debtors filed their answer to the Citigroup Third-Party Complaint, generally denying Citigroup's allegations and asserting affirmative defenses.

On November 6, 2008, Wells Fargo Bank, N.A., in its capacity as the Second Lien Term Agent, filed its answer to the Committee's Amended Complaint in the Committee Action, and filed a third-party complaint (the Wells Fargo Third-Party Complaint) against TOUSA, Inc. and each of the Debtor signatories, co-borrowers and co-guarantors under the Second Lien Term Loan (except for Engle/Gilligan, LLC, Engle Homes Delaware, Inc., Newmark Homes Business Trust, TOUSA Delaware, Inc., and TOUSA Funding, LLC). The Wells Fargo Third-Party Complaint alleges that, to the extent the Committee establishes its allegations in the Committee Action, the defendants to the Wells Fargo Third-Party Complaint will have materially breached the Second Lien Term Loan by (a) not having assets whose fair value exceeded their debts and liabilities, subordinated, contingent or otherwise, (b) not having assets whose fair saleable value exceed their debts and other liabilities, subordinated, contingent or otherwise, (c) not being able to pay their debts and liabilities, subordinated, contingent, or otherwise, and/or (d) having unreasonably small capital with which to conduct their business. On November 25, 2008, the Debtors filed their answer to the Wells Fargo Third-Party Complaint, generally denying Wells Fargo's allegations and asserting affirmative defenses.

On February 24, 2009, the Senior Transeastern Lenders and the CIT Group/Business Credit, Inc. (CIT) each filed a Counterclaim and Third-Party Complaint against certain of the Debtors. The Senior Transeastern Lenders and CIT allege that they are entitled to indemnification against any recovery the Committee receives as a result of the Committee's fraudulent transfer claims under the terms of the August 1, 2005 Senior Credit Agreement signed by certain of the Debtors in connection with the formation of the Transeastern Joint

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Venture. The Senior Transeastern Lenders and CIT seek recoupment for the full amount of any recovery against them on each of the Committee's fraudulent transfer claims. On April 1, 2009, the third-party defendant Debtors moved to strike, or in the alternative to sever and stay, the claims asserted against them in the Senior Transeastern Lenders' and CIT's Counterclaims and Third-Party Complaints. A hearing on the third-party Debtor's motion is currently scheduled for May 28, 2009.

Discovery in the Committee Action, the Citicorp Third-Party Complaint, and the Wells Fargo Third-Party Complaint is currently ongoing. Pursuant to the amended case management order entered by the Court on November 11, 2008, current and former employees of the Debtors, the parties and various non-parties have been deposed.

On February 26, 2009, the court entered an order granting the Debtors' motion to compel mediation of the case. The non-binding judicial settlement conference was conducted by Judge Laurel Isicoff on March 23, 2009 and March 24, 2009. On April 14, 2009, Judge Isicoff reported that the parties were at an impasse with respect to the Committee's claims against the First Lien Term Loan Lenders, the First Lien Revolver Lenders, and the Senior Transeastern Lenders. Judge Isicoff further reported that the other Defendants had either reached an agreement with the Committee or were continuing settlement discussions. Trial is currently scheduled for the weeks of July 13, 2009 and July 20, 2009.

Potential Claim by the Official Committee of Unsecured Creditors of TOUSA

On October 26, 2007, the TOUSA Board of Directors received a letter from counsel to a group of holders of TOUSA senior and subordinated notes (the Noteholder Group). TOUSA did not file for bankruptcy protection as requested by the Noteholder Group, but did later file for bankruptcy in January 2008. On February 27, 2009 the Official Committee of Unsecured Creditors of TOUSA filed a motion seeking standing to pursue claims against members of certain Debtor-Subsidiaries' boards of directors as well as the majority shareholder of TOUSA, Tech SA, in connection with the July 31, 2007 transaction. The Court has not yet heard or ruled upon the Committee's motion.

Vista Lakes

Plaintiffs, purchasers of homes in the Vista Lakes community near Orlando, filed a class action complaint alleging that their homes were built on the site of a former bombing range. The plaintiffs seek recovery under theories of fraud, breach of contract, strict liability, negligence, and civil conspiracy. Because the plaintiffs named debtor defendants Touse, Inc., Touse Homes, Inc., d/b/a Engle Homes Orlando and Touse Homes, LP as defendants in this action, the action was removed to federal court. The plaintiffs then agreed to dismiss the debtor defendants and the parties entered into a stipulation for remand. The state court case was re-opened and the parties remaining as defendants included Universal Land Title, Inc. and Preferred Home Mortgage Company.

Universal Land Title, Inc. and Preferred Home Mortgage Company filed a motion to dismiss the second amended complaint. On February 13, 2009, the court dismissed all nine counts of the second amended complaint as to both Universal Land Title, Inc. and Preferred Home Mortgage Company, but granted Plaintiffs leave to amend their complaint.

On March 23, 2009, Plaintiffs filed their Third Amended Complaint and, with the exception of the claim for strict liability, re-alleged eight of the previously dismissed causes of action against Universal Land Title, Inc. and Preferred Home Mortgage Company. On April 29, 2009, Preferred Home Mortgage Company and Universal Land Title, Inc. filed their motion to dismiss the Third Amended Complaint. On April 30, 2009, Plaintiffs filed a notice voluntarily dismissing certain counts, and the only claims that remain pending as to Preferred Home Mortgage Company and Universal Land Title, Inc. are counts for negligence and civil conspiracy.

Based upon the early stage of the litigation and discovery, and depending upon the success of the motion to dismiss the Third Amended Complaint, we are unable to evaluate the likelihood of an unfavorable outcome or the range of liability in such event.

Chinese Drywall

TOUSA Homes, Inc. was named as a defendant in a purported class action lawsuit pending in the United States District Court for the Southern District of Florida on behalf of certain homeowner plaintiffs in Southwest Florida. (Karen Vickers, et al., v. TOUSA Homes, Inc., et al., No. 09-20510-CIV-GOLD/MCALILEY). The complaint alleges the plaintiff homeowners were sold homes containing drywall that is inherently defective (Chinese Drywall), because

it emits various sulfide gasses and/or other chemicals through off gassing that purportedly causes property damage and potential health hazards. The plaintiffs have voluntarily withdrawn the complaint without prejudice. We are in the process of responding to notice of the alleged defect pursuant to Florida Statutes chapter 558. TOUSA Homes, Inc. was named, but has not been served in an additional purported class action lawsuit making similar allegations in the Lee County, Florida Circuit Court (Joyce Dowdy Revocable Trust, et. al v. Engle Homes, Inc. et. al, No. 09-CA-1158).

Other Litigation

We are also involved in various other claims and legal actions arising in the ordinary course of business. We do not believe that the ultimate resolution of these other matters will have a material adverse effect on our financial condition or results of operations. As of the date of the Chapter 11 filing, then pending litigation was generally stayed, and absent further order of the Bankruptcy Court, most parties may not take any action to recover on pre-petition claims against us.

Informal Inquiry

In the Matter of TOUSA, Inc. SEC Inquiry, File No. FL-3310. In September of 2007, we were contacted by the Miami Regional Office of the SEC requesting the voluntary provision of documents, and other information from us, relating primarily to corporate and financial information and communications related to the Transeastern JV. In May 2009, the SEC advised us that it has completed its investigation and does not intend to recommend any enforcement action.

Table of Contents***PHMC Settlement***

On July 10, 2008, PHMC entered into a settlement agreement with one of its primary purchasers of its mortgage loans. In connection with the settlement, we recorded a loss accrual of \$2.9 million in 2007. The settlement agreement releases PHMC of all its known and unknown obligations under the Loan Purchase Agreement.

12. Stockholders Deficit***Convertible PIK Preferred Stock***

The preferred stock ranks senior to all of our capital stock with respect to liquidation and dividends and has an initial aggregate liquidation preference of \$117.5 million and accrues dividends semi-annually at 8% per annum as follows: (i) 1% payable in cash; (ii) the remaining 7% payable, at our option, in cash, additional preferred stock, or a combination thereof. The preferred stock is mandatorily redeemable on July 1, 2015 at \$1.61 per share. The conversion price of the preferred stock will be adjusted for certain anti-dilution events including below market price or below the conversion price issuances by us of our common stock, subject to certain exceptions.

At September 30, 2008 and December 31, 2007, the preferred stock redemption amount includes amounts representing dividends not currently declared or paid but which will be payable under the redemption features. The preferred stock is currently redeemable because redemption of the instrument, absent the existence of the share settled conversion option, is certain to occur at maturity. At September 30, 2008, the accreted redemption balance is \$0.8 million.

The preferred stock contains a contingent dividend feature, which provides for an increase in the dividend rate of 0.25% during the period in which the Company fails to register the underlying common stock. This increase in the dividend rate becomes effective after 270 days. The contingent dividend feature constitutes an obligation to make future payments or otherwise transfer consideration under a registration payment arrangement. In accordance with FSP EITF No. 00-19-2, *Accounting for Registration Payment Arrangements*, the contingent dividend feature should be separately recognized and measured in accordance with SFAS 5. At September 30, 2008, \$0.4 million was accrued for our obligation under the registration payment arrangement. Although there is no limitation on the amount that could be paid under this arrangement, our estimate is based on our estimated date of exit from bankruptcy of September 2009 since this liability is expected to be extinguished as part of the Chapter 11 cases.

In accordance with EITF No. 98-5, *Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios*, the intrinsic value of the beneficial conversion feature required measurement at the commitment date by comparing our stock price at date of closing to the conversion price, which is determinable at the end of the 20 trading days commencing 60 calendar days after closing. The value attributable to the beneficial conversion features has been recognized and measured by allocating a portion of the proceeds to additional paid-in-capital (since there are no retained earnings) and a discount to the preferred stock. In accordance with EITF 00-27, *Application of Issue No. 98-5 to Certain Convertible Instruments*, \$84.0 million, representing the maximum intrinsic value of the beneficial conversion feature, is amortized from additional-paid in capital to preferred stock from October 26, 2007 to July 1, 2015.

Dividends and amortization of the discount of the preferred stock are recorded as charges to retained earnings or additional paid in capital, if there are no retained earnings, and reduce net income in the determination of income attributable to shareholders for the purposes of computing basic and diluted earnings per share. For the three and nine months ended September 30, 2008, dividends on and accretion of preferred stock was \$2.5 million and \$7.7 million, respectively, which was recorded as a charge to additional paid-in-capital.

We will determine and, if required, measure a beneficial conversion feature based on the fair value of our stock price on the date dividends are declared on the convertible preferred shares, which will be recognized as a reduction to retained earnings (or additional paid in capital if there no retained earnings) and the convertible preferred shares newly issued if the fair value of the stock on the declaration date is below the contractual conversion price. The discount on the convertible preferred shares issued as PIK dividends will then be accreted through the contractual maturity of the instrument.

The preferred stock is not a participating security, as defined in SFAS No. 128, *Earnings per Share*, and EITF No. 03-6, *Participating Securities and the Two-Class Method under FASB Statement No. 128*, and, therefore, does not require the two-class method of calculating EPS. The preferred stock provides for the adjustment to the conversion

price for common stock dividends declared. The common shares underlying the convertible preferred stock have not been included in diluted EPS as its effect is anti-dilutive.

Warrants

The warrants are exercisable for a term of five years from the date of issuance. The warrants had an estimated fair value of \$8.2 million at issuance (based on the Black-Scholes option pricing model and certain agreed upon inputs). The warrants are exercisable as follows (i) 5,045,662 shares of common stock can be purchased at \$5.31 per share, and (ii) 5,045,662 shares of common stock can be purchased at \$6.38 per share. The exercise prices of the warrants will be adjusted for certain anti-dilution events including below market price or below the conversion price issuances by us of our common stock, subject to certain exceptions. Upon exercise of the warrants by the holders thereof, we may, in our sole discretion, satisfy our obligations under any warrant being exercised by: (i) paying the holder the value of the common stock to be delivered in cash less the exercise price; (ii) paying such amount in common stock rather than cash; (iii) delivering shares of common stock upon receiving the cash exercise price therefore; or (iv) any combination of the foregoing.

NYSE Delisting

Effective November 19, 2007, NYSE Regulation, Inc. suspended our common stock and debt securities from trading on the NYSE. We appealed the suspension. Following our suspension from the NYSE, we began trading on the Pink Sheet Electronic Quotation Service. On February 15, 2008, the NYSE denied our appeal and affirmed the decision to suspend trading in our common stock and debt securities. On March 3, 2008, the NYSE filed Forms 25, Notification of Removal of Listing and/or Registration under Section 12(b) of the Securities Exchange Act of 1934, with the SEC of its intention to remove our common stock, 9% Senior Notes due July 1, 2010, 9% Senior Notes due July 1, 2010, 7 1 / 2% Senior Subordinated Notes due March 15, 2011, 7 1 / 2% Senior Subordinated Notes due January 15, 2015 and the 10 3 / 8% Senior Subordinated Notes due July 1, 2012 at the opening of business May 13, 2008. Our common stock and debt securities were delisted on that date.

Table of Contents**13. Stock-Based Compensation**

Under the TOUSA, Inc. Annual and Long-Term Incentive Plan (the Plan) employees, consultants and directors of ours, our subsidiaries and affiliated entities, (as defined in the Plan), are eligible to receive options to purchase shares of common stock. Each stock option expires on a date determined when the options are granted, but not more than ten years after the date of grant. Stock options granted have a vesting period ranging from immediate vesting to a graded vesting over five years.

During the three months ended September 30, 2008 and 2007, we recognized compensation expense related to stock options of \$0.8 million and \$1.0 million, respectively. During the nine months ended September 30, 2008 and 2007, we recognized compensation expense related to stock options of \$2.5 million and \$3.0 million, respectively. At September 30, 2008 and December 31, 2007, outstanding stock options totaled 7.5 million and 7.8 million, respectively. During the nine months ended September 30, 2008, 241,250 stock options were forfeited.

14. Operating and Reporting Segments

Our operating segments are aggregated into reportable segments in accordance with SFAS No. 131, *Disclosures About Segments of an Enterprise and Related Information*, based primarily upon similar economic characteristics, product type, geographic areas, and information used by the chief operating decision maker to allocate resources and assess performance. Our reportable segments consist of our four major Homebuilding geographic regions (Florida, Mid-Atlantic, Texas and West) and our Financial Services operations.

Through our four homebuilding regions, we design, build and market detached single-family residences, town homes and condominiums in various metropolitan markets in nine states, located as follows:

Florida: Central Florida, Jacksonville, Southeast Florida, Southwest Florida, Tampa/St. Petersburg

Mid-Atlantic: Baltimore / Southern Pennsylvania, Nashville, Northern Virginia (on September 25, 2007, we sold in bulk, home sites in our Mid-Atlantic (excluding Nashville) and Virginia divisions)

Texas: Austin, Houston, San Antonio (on September 6, 2007, we sold substantially all of our Dallas/Fort Worth division)

West: Colorado, Las Vegas, Phoenix

Evaluation of segment performance is based on the segment's results of operations without consideration of income taxes. Results of operations for our four homebuilding segments consist of revenues generated from the sales of homes and land, equity in earnings from unconsolidated joint ventures, and other income / expense less the cost of homes and land sold and selling, general and administrative expenses. The results of operations for our Financial Services segment consist of revenues generated from mortgage financing, title insurance and other ancillary services less the cost of such services and certain selling, general and administrative expenses. Effective April 1, 2008, our mortgage subsidiary became part of a joint venture and has been accounted for as an equity-method investment (see Mortgage Joint Venture discussion in Note 1).

The operational results of each of our segments are not necessarily indicative of the results that would have occurred had each segment been an independent, stand-alone entity during the periods presented. The following tables set forth the financial information relating to our operations, presented by segment (in millions)

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	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Revenues:				
Homebuilding:				
Florida ⁽²⁾	\$ 79.3	\$ 195.6	\$ 309.8	\$ 671.1
Mid-Atlantic	17.7	81.4	48.3	196.1
Texas ⁽¹⁾	101.5	149.0	313.8	469.0
West	48.4	66.9	164.5	283.1
Total Homebuilding	246.9	492.9	836.4	1,619.3
Financial Services	4.1	8.3	13.2	31.3
Total revenues	\$ 251.0	\$ 501.2	\$ 849.6	\$ 1,650.6
Loss (income) from unconsolidated joint ventures:				
Florida	\$	\$ 0.2	\$	\$ 2.1
Mid-Atlantic				(2.2)
Texas	(0.1)	(0.3)	(0.3)	(0.3)
West		9.3	(0.1)	9.2
	(0.1)	9.2	(0.4)	8.8
Impairments (recoveries) on unconsolidated joint ventures:				
Florida	(1.9)	16.4	(12.6)	20.4
Mid-Atlantic				1.5
Texas	6.6		8.9	
West ⁽³⁾	5.2	7.0	4.8	7.0
	9.9	23.4	1.1	28.9
Loss from unconsolidated joint ventures after impairments	\$ 9.8	\$ 32.6	\$ 0.7	\$ 37.7
Results of Operations:				
Homebuilding:				
Florida ⁽²⁾	\$ (53.9)	\$ (299.4)	\$ (301.4)	\$ (290.3)
Mid-Atlantic	(7.9)	(52.0)	(36.2)	(97.7)
Texas ⁽¹⁾	(11.6)	14.6	(28.9)	43.3
West	(17.1)	(199.4)	(235.5)	(276.2)
Total Homebuilding	(90.5)	(536.2)	(602.0)	(620.9)
Financial Services	(0.5)	0.2	(4.8)	5.2
Corporate and unallocated	(25.2)	(73.8)	(83.8)	(220.1)

Loss from continuing operations before reorganization items and taxes	\$ (116.2)	\$ (609.8)	\$ (690.6)	\$ (835.8)
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(1) The Texas region excludes the Dallas division, which is classified as a discontinued operation.

(2) The results of operations for Transeastern for the three and nine months ended September 30, 2008 have been included in our consolidated results. Results of operations for the three and nine months ended September 30, 2007 are included in the results for the unconsolidated joint ventures. See Note 4.

(3) We have excluded the results of the Engle/Sunbelt joint venture from our unconsolidated joint venture results for the three and nine months ended September 30, 2008 due to the settlement agreement reached in 2008.

See Note 5.

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	September 30, 2008	December 31, 2007
Assets:		
Homebuilding:		
Florida	\$ 241.7	\$ 631.3
Mid-Atlantic	42.9	73.0
Texas ⁽¹⁾	171.1	220.0
West	156.5	381.3
Assets held for sale	2.7	6.1
Financial Services	22.6	36.7
Corporate and unallocated	312.8	413.6
Total assets	\$ 950.3	\$ 1,762.0
Investments in Unconsolidated Joint Ventures:		
Mid-Atlantic	\$ 0.1	\$ 0.1
Texas	2.9	8.6
West		0.3
Total Investments in Unconsolidated Joint Ventures	\$ 3.0	\$ 9.0

(1) The Texas region excludes the Dallas division, which is classified as a discontinued operation.

15. Discontinued Operations

On September 6, 2007, we sold substantially all of our Dallas/Fort Worth division to an unrelated third-party for \$56.5 million and realized a pre-tax loss on disposal of \$13.6 million. Certain communities were not part of the sale. We are actively marketing these communities for sale.

In accordance with SFAS 144, the results of our Dallas/Fort Worth division have been classified as discontinued operations for all periods presented. Discontinued operations include Dallas/Fort Worth division revenues and net loss of \$0.2 million and \$0.6 million, respectively, for the three months ended September 30, 2008 and \$1.1 million and \$3.9 million, respectively, for the three months ended September 30, 2007. Included in the net loss of the Dallas/Fort Worth division for the three months ended September 30, 2008 and 2007 is \$0 million and \$2.8 million, respectively, of inventory impairments and abandonment costs. Discontinued operations include Dallas/Fort Worth division revenues and net loss of \$1.2 million and \$3.8 million, respectively, for the nine months ended September 30, 2008 and \$44.7 million and \$17.6 million, respectively, for the nine months ended September 30, 2007. Included in the net loss of the Dallas/Fort Worth division for the nine months ended September 30, 2008 and 2007 is \$1.9 million and \$5.7 million, respectively, of inventory impairments and abandonment costs. Additionally, during the nine months ended September 30, 2007, we wrote off \$3.1 million of goodwill which is included in loss from discontinued operations for the nine months ended September 30, 2007 related to the sale of our Dallas/Fort Worth division.

Assets held for sale, as shown on the unaudited consolidated statements of financial condition, consist primarily of \$2.7 million and \$6.1 million of inventory at September 30, 2008 and December 31, 2007, respectively.

16. Summarized Financial Information

Our outstanding senior notes and senior subordinated notes are fully and unconditionally guaranteed, on a joint and several basis, by the Guarantor Subsidiaries, which are all of the Company's material direct and indirect subsidiaries, other than our mortgage and title operations subsidiaries (the Non-guarantor Subsidiaries). Each of the Guarantor Subsidiaries is directly or indirectly 100% owned by the Company. In lieu of providing separate audited financial statements for the Guarantor Subsidiaries, consolidated condensed financial statements are presented below. Separate financial statements and other disclosures concerning the Guarantor Subsidiaries are not presented because management has determined that they are not material to investors. Substantially all of our subsidiaries are included in the Chapter 11 cases, excluding our financial services subsidiaries and unconsolidated joint ventures.

Table of Contents**Consolidated Statement of Financial Condition
September 30, 2008**

	TOUSA, Inc.	Guarantor Subsidiaries	Non- Guarantor Subsidiaries (in millions)	Intercompany Eliminations	Total
ASSETS					
HOMEBUILDING:					
Cash and cash equivalents	\$ 276.7	\$ 20.7	\$	\$	\$ 297.4
Inventory		547.4			547.4
Property and equipment, net	1.3	13.9			15.2
Investments in unconsolidated joint ventures		3.0			3.0
Investments in/ advances to consolidated subsidiaries	346.5	(404.8)	(8.2)	66.5	
Other assets	22.9	39.1			62.0
Assets held for sale		2.7			2.7
	647.4	222.0	(8.2)	66.5	927.7
FINANCIAL SERVICES:					
Cash and cash equivalents			13.6		13.6
Mortgage loans held for sale			5.0		5.0
Other assets			4.0		4.0
			22.6		22.6
Total assets	\$ 647.4	\$ 222.0	\$ 14.4	\$ 66.5	\$ 950.3
LIABILITIES AND STOCKHOLDERS EQUITY (DEFICIT)					
HOMEBUILDING:					
Accounts payable and other liabilities	\$ 27.8	\$ 93.8	\$	\$	\$ 121.6
Customer deposits		17.8			17.8
Liabilities associated with assets held for sale		0.4			0.4
	27.8	112.0			139.8
FINANCIAL SERVICES:					
Accounts payable and other liabilities			1.3		1.3
			1.3		1.3

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Total liabilities not subject to compromise	27.8	112.0	1.3		141.1
Liabilities subject to compromise	1,890.4	189.6			2,080.0
Total liabilities	1,918.2	301.6	1.3		2,221.1
Total stockholders equity (deficit)	(1,270.8)	(79.6)	13.1	66.5	(1,270.8)
Total liabilities and stockholders equity (deficit)	\$ 647.4	\$ 222.0	\$ 14.4	\$ 66.5	\$ 950.3

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Table of Contents**Consolidated Statement of Financial Condition
December 31, 2007**

	TOUSA, Inc.	Guarantor Subsidiaries	Non- Guarantor Subsidiaries	Intercompany Eliminations	Total
			(in millions)		
ASSETS					
HOMEBUILDING:					
Cash and cash equivalents	\$ 81.3	\$ (9.0)	\$	\$	\$ 72.3
Inventory		1,271.8			1,271.8
Property and equipment, net	3.3	21.3			24.6
Investments in unconsolidated joint ventures		9.0			9.0
Receivables from unconsolidated joint ventures, net		0.3			0.3
Investments in/ advances to consolidated subsidiaries	989.7	(372.5)	(5.5)	(611.7)	
Other assets	287.7	42.3			330.0
Goodwill		11.2			11.2
Assets held for sale		6.1			6.1
	1,362.0	980.5	(5.5)	(611.7)	1,725.3
FINANCIAL SERVICES:					
Cash and cash equivalents			14.9		14.9
Mortgage loans held for sale			15.0		15.0
Other assets			6.8		6.8
			36.7		36.7
Total assets	\$ 1,362.0	\$ 980.5	\$ 31.2	\$ (611.7)	\$ 1,762.0
LIABILITIES AND STOCKHOLDERS EQUITY (DEFICIT)					
HOMEBUILDING:					
Accounts payable and other liabilities	\$ 83.7	\$ 318.1	\$	\$	\$ 401.8
Customer deposits		33.9			33.9
Obligations for inventory not owned		32.0			32.0
Notes payable	1,585.3				1,585.3
Bank borrowings	168.5				168.5
Liabilities associated with assets held for sale		0.9			0.9
	1,837.5	384.9			2,222.4
FINANCIAL SERVICES:					

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Accounts payable and other liabilities			8.0	(0.7)	7.3
Bank borrowings			7.8		7.8
			15.8	(0.7)	15.1
Total liabilities not subject to compromise	1,837.5	384.9	15.8	(0.7)	2,237.5
Liabilities subject to compromise					
Total stockholders equity (deficit)	(475.5)	595.6	15.4	(611.0)	(475.5)
Total liabilities and stockholders equity (deficit)	\$ 1,362.0	\$ 980.5	\$ 31.2	\$ (611.7)	\$ 1,762.0

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Consolidated Statement of Operations
Three Months Ended September 30, 2008

	TOUSA, Inc.	Guarantor Subsidiaries	Non- Guarantor Subsidiaries	Intercompany Eliminations	Total
HOMEBUILDING:					
Revenues	\$	\$ 246.9	\$	\$	\$ 246.9
Cost of sales		292.7			292.7
Gross loss		(45.8)			(45.8)
Selling, general and administrative expenses	10.7	33.9		(0.6)	44.0
Recovery from unconsolidated joint ventures, net		(0.1)			(0.1)
Impairments on investments in unconsolidated joint ventures		9.9			9.9
Interest expense	16.9				16.9
Other expenses, net	89.2	61.2		(151.2)	(0.8)
Homebuilding pretax loss	(116.8)	(150.7)		151.8	(115.7)
FINANCIAL SERVICES:					
Revenues			4.7	(0.6)	4.1
Expenses			5.5	(0.9)	4.6
Financial Services pretax loss			(0.8)	0.3	(0.5)
Loss from continuing operations before reorganization items and taxes	(116.8)	(150.7)	(0.8)	152.1	(116.2)
Reorganization items, net	18.7				18.7
Benefit for income taxes	(2.7)				(2.7)
Loss from continuing operations, net of taxes	(132.8)	(150.7)	(0.8)	152.1	(132.2)
Discontinued operations:					
Loss from discontinued operations		(0.6)			(0.6)
Loss from discontinued operations, net of taxes		(0.6)			(0.6)
Net loss	(132.8)	(151.3)	(0.8)	152.1	(132.8)
Dividends and accretion of discount on preferred stock	2.5				2.5

Loss attributable to common stockholders	\$ (135.3)	\$ (151.3)	\$ (0.8)	\$ 152.1	\$ (135.3)
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Table of Contents**Consolidated Statement of Operations
Nine Months Ended September 30, 2008**

	TOUSA, Inc.	Guarantor Subsidiaries	Non- Guarantor Subsidiaries (in millions)	Intercompany Eliminations	Total
HOMEBUILDING:					
Revenues	\$	\$ 836.4	\$	\$	\$ 836.4
Cost of sales		1,305.5			1,305.5
Gross loss		(469.1)			(469.1)
Selling, general and administrative expenses	35.6	121.2		(3.0)	153.8
Recovery from unconsolidated joint ventures, net		(0.4)			(0.4)
Impairments on investments in unconsolidated joint ventures		1.1			1.1
Goodwill impairments		11.2			11.2
Interest expense	53.7				53.7
Other (income) expenses, net	605.1	67.4		(675.2)	(2.7)
Homebuilding pretax loss	(694.4)	(669.6)		678.2	(685.8)
FINANCIAL SERVICES:					
Revenues			16.1	(2.9)	13.2
Expenses			20.3	(2.3)	18.0
Financial Services pretax loss			(4.2)	(0.6)	(4.8)
Loss from continuing operations before reorganization items and taxes	(694.4)	(669.6)	(4.2)	677.6	(690.6)
Reorganization items, net	105.4				105.4
Benefit for income taxes	(2.0)				(2.0)
Loss from continuing operations, net of taxes	(797.8)	(669.6)	(4.2)	677.6	(794.0)
Discontinued operations:					
Loss from discontinued operations		(3.8)			(3.8)
Loss from discontinued operations, net of taxes		(3.8)			(3.8)
Net loss	(797.8)	(673.4)	(4.2)	677.6	(797.8)
Dividends and accretion of discount on preferred stock	7.7				7.7

Loss attributable to common stockholders	\$ (805.5)	\$ (673.4)	\$ (4.2)	\$ 677.6	\$ (805.5)
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Consolidated Statement of Operations
Three Months Ended September 30, 2007

	TOUSA, Inc.	Guarantor Subsidiaries	Non- Guarantor Subsidiaries (in millions)	Intercompany Eliminations	Total
HOMEBUILDING:					
Revenues	\$	\$ 492.9	\$	\$	\$ 492.9
Cost of sales		930.3			930.3
Gross loss		(437.4)			(437.4)
Selling, general and administrative expenses	23.3	66.3		(3.6)	86.0
Loss from unconsolidated joint ventures, net		9.2			9.2
Impairments on investments in unconsolidated joint ventures		23.4			23.4
Provision for settlement of loss contingency	40.7				40.7
Goodwill impairment		2.7			2.7
Interest expense	10.0				10.0
Other expenses, net	547.5	30.2		(577.1)	0.6
Homebuilding pretax loss	(621.5)	(569.2)		580.7	(610.0)
FINANCIAL SERVICES:					
Revenues			11.9	(3.6)	8.3
Expenses			8.2	(0.1)	8.1
Financial Services pretax income			3.7	(3.5)	0.2
Income (loss) from continuing operations before income taxes	(621.5)	(569.2)	3.7	577.2	(609.8)
Provision (benefit) for income taxes	(1.8)	6.0	1.8		6.0
Income (loss) from continuing operations	(619.7)	(575.2)	1.9	577.2	(615.8)
Discontinued operations:					
Loss from discontinued operations		(3.9)			(3.9)
Loss from discontinued operations, net of taxes		(3.9)			(3.9)
Net income (loss)	(619.7)	(579.1)	1.9	577.2	(619.7)
	2.2				2.2

Dividends and accretion of discount
on preferred stock

Net income (loss) attributable to common stockholders	\$ (621.9)	\$ (579.1)	\$ 1.9	\$ 577.2	\$ (621.9)
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Table of Contents**Consolidated Statement of Operations
Nine Months Ended September 30, 2007**

	TOUSA, Inc.	Guarantor Subsidiaries	Non- Guarantor Subsidiaries (in millions)	Intercompany Eliminations	Total
HOMEBUILDING:					
Revenues	\$	\$ 1,619.3	\$	\$	\$ 1,619.3
Cost of sales		1,959.0			1,959.0
Gross loss		(339.7)			(339.7)
Selling, general and administrative expenses	63.1	210.1		(10.8)	262.4
Loss from unconsolidated joint ventures, net		8.8			8.8
Impairments on investments in unconsolidated joint ventures		28.9			28.9
Provision for settlement of loss contingency	151.6				151.6
Goodwill impairment		40.9			40.9
Interest expense	10.0	0.2			10.2
Other (income) expenses, net	605.4	40.5		(647.4)	(1.5)
Homebuilding pretax loss	(830.1)	(669.1)		658.2	(841.0)
FINANCIAL SERVICES:					
Revenues			42.0	(10.7)	31.3
Expenses			30.0	(3.9)	26.1
Financial Services pretax income			12.0	(6.8)	5.2
Income (loss) from continuing operations before income taxes	(830.1)	(669.1)	12.0	651.4	(835.8)
Provision (benefit) for income taxes	(12.4)	(28.7)	5.4		(35.7)
Income (loss) from continuing operations	(817.7)	(640.4)	6.6	651.4	(800.1)
Discontinued operations:					
Loss from discontinued operations		(11.8)			(11.8)
Loss from disposal of discontinued operations		(13.6)			(13.6)
Benefit for income taxes		(7.8)			(7.8)
Loss from discontinued operations, net of taxes		(17.6)			(17.6)

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Net income (loss)	(817.7)	(658.0)	6.6	651.4	(817.7)
Dividends and accretion of discount on preferred stock	2.2				2.2
Net income (loss) attributable to common stockholders	\$ (819.9)	\$ (658.0)	\$ 6.6	\$ 651.4	\$ (819.9)

Table of Contents**Consolidated Statement of Cash Flows
Nine Months Ended September 30, 2008**

	TOUSA, Inc.	Guarantor Subsidiaries	Non- Guarantor Subsidiaries (in millions)	Intercompany Eliminations	Total
Net cash provided by (used in) operating activities	\$ (389.5)	\$ (5.3)	\$ 9.4	\$ 678.2	\$ 292.8
Cash flows from investing activities:					
Net disposals of property and equipment	0.6	0.2			0.8
Investments in unconsolidated joint ventures		(1.6)			(1.6)
Net cash provided by (used in) investing activities	0.6	(1.4)			(0.8)
Cash flows from financing activities:					
Net borrowings from revolving credit facilities	(28.1)				(28.1)
Principal payments on term loans	(37.7)				(37.7)
Net repayments of from Financial Services bank borrowings			(7.8)		(7.8)
Payments for deferred financing costs	(2.9)				(2.9)
Increase (decrease) in intercompany transactions	643.2	32.3	2.7	(678.2)	
Net cash provided by (used in) financing activities	574.5	32.3	(5.1)	(678.2)	(76.5)
Net cash provided by continuing operations	185.6	25.6	4.3		215.5
Net cash used in discontinued operations		(0.9)			(0.9)
Increase in cash and cash equivalents	185.6	24.7	4.3		214.6
Cash and cash equivalents at beginning of period	79.1	(11.9)	9.3		76.5
Cash and cash equivalents at end of period	\$ 264.7	\$ 12.8	\$ 13.6	\$	\$ 291.1

Table of Contents**Consolidated Statement of Cash Flows
Nine Months Ended September 30, 2007**

	TOUSA, Inc.	Guarantor Subsidiaries	Non- Guarantor Subsidiaries (in millions)	Intercompany Eliminations	Total
Net cash provided by (used in) operating activities	\$ (569.4)	\$ (173.9)	\$ 3.4	\$ 651.3	\$ (88.6)
Cash flows from investing activities:					
Acquisitions, net of cash acquired		(7.7)			(7.7)
Net additions to property and equipment	(0.8)	(7.9)	(0.7)		(9.4)
Investments in unconsolidated joint ventures		(29.2)			(29.2)
Capital distributions from unconsolidated joint ventures		12.4			12.4
Net cash used in investing activities	(0.8)	(32.4)	(0.7)		(33.9)
Cash flows from financing activities:					
Net borrowings from revolving credit facilities	150.3				150.3
Principal payments on notes payable	(0.5)				(0.5)
Net repayments of Financial Services bank borrowings			(13.0)		(13.0)
Payments for deferred financing costs	(32.1)				(32.1)
Payments for issuance of convertible preferred stock and warrants	(2.9)				(2.9)
Increase (decrease) in intercompany transactions	494.0	149.8	7.5	(651.3)	
Net cash provided by (used in) financing activities	608.8	149.8	(5.5)	(651.3)	101.8
Net cash provided by (used in) continuing operations	38.6	(56.5)	(2.8)		(20.7)
Net cash provided by discontinued operations		44.1			44.1
Increase (decrease) in cash and cash equivalents	38.6	(12.4)	(2.8)		23.4
Cash and cash equivalents at beginning of period	50.6	(3.2)	6.8		54.2
	\$ 89.2	\$ (15.6)	\$ 4.0	\$	\$ 77.6

Cash and cash equivalents at end of
period

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Table of Contents**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the unaudited consolidated financial statements and related notes included elsewhere in this report.

As used in this Form 10-Q, consolidated information refers only to information relating to our continuing operations which are consolidated in our financial statements and exclude the results of our Dallas/Fort Worth division which we have classified as a discontinued operation; and combined information includes consolidated information and information relating to our unconsolidated joint ventures. Unless otherwise noted, the information contained herein is shown on a consolidated basis. Our unaudited consolidated financial statements are presented on a going concern basis, which contemplates the realization of assets and satisfaction of liabilities in the normal course of business. Due to our Chapter 11 cases, there is substantial doubt about our ability to continue as a going concern and there is uncertainty about the realization of assets and satisfaction of liabilities, without material adjustments and/or changes in ownership.

Explanatory Note

In some instances we have attempted to provide information as of a date more current than September 30, 2008. The housing market has continued to deteriorate significantly since September 30, 2008 and we have not yet completed the analyses and processes required for the preparation of financial statements for any period subsequent to September 30, 2008. Therefore, the information contained herein does not include reserves or provisions for any period after the period ended September 30, 2008. As a result of the continued homebuilding and overall macroeconomic market deterioration and the impact of our Chapter 11 filing on our operations, it is likely that we will have material impairments, losses and provisions upon completion of the analyses and processes in future periods.

Executive Summary

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

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

We conduct our Homebuilding operations through our consolidated subsidiaries and through various unconsolidated joint ventures that also build and market homes.

Since 2006, the homebuilding industry has experienced a significant and sustained decrease in demand for new homes, an oversupply of new and existing homes available for sale and a more restrictive mortgage lending environment. Although we operate in a number of markets, approximately 53% of our operations are concentrated in Florida and the West, based on 2007 deliveries, which suffered particularly severe downturns in home buying activity. The weakness in the housing market has accelerated during 2008 as a result of increased foreclosures, fewer home sales, increased buyer difficulty in obtaining financing, lack of consumer confidence, inability to sell existing homes that would enable prospective buyers to purchase new homes, greater cancellations of home purchase agreements by buyers, higher inventories of unsold homes and the increased use by homebuilders, speculators, investors and others of discounts, incentives, price concessions, broker commissions and advertising to close home sales compared to the past several years. The deterioration in the homebuilding industry has been negatively impacted by significant disruptions in the broader financial markets and severe constraints in the credit markets. Further deterioration in the homebuilding industry is expected for the foreseeable future and may have a material adverse effect on our business, financial condition and results of operations.

Reflecting these trends, we, like many other homebuilders, experienced severe liquidity challenges in the credit and mortgage markets, diminished consumer confidence, increased home inventories and foreclosures and downward pressure on home prices. Potential buyers have exhibited both a reduction in confidence as to the economy in general and a willingness to delay purchase decisions based on a perception that prices will continue to decline. Prospective homebuyers continue to be concerned about interest rates and the inability to sell their current homes or to obtain appraisals at sufficient amounts to secure mortgage financing as a result of the disruption in the mortgage markets and the tightening of credit standards. Our Chapter 11 filings were a further factor contributing to decreased performance.

As a result of deteriorating market conditions and liquidity constraints, we did not exercise certain homesite option and land bank contracts and reviewed our inventories, goodwill, investments in joint ventures and other assets for possible impairment charges. We recognized charges in continuing operations totaling \$107.0 million and \$571.3 million for the three months ended September 30, 2008 and 2007, respectively, and \$586.4 million and \$849.8 million for the nine months ended September 30, 2008 and 2007, respectively related to inventory and goodwill impairments, abandonment costs, joint venture impairments and the settlement of a loss contingency.

For the three and nine months ended September 30, 2008, we reported a loss from continuing operations, net of taxes, of \$132.2 million and \$794.0 million compared to \$615.8 million and \$800.1 million for the three and nine months ended September 30, 2007. Home

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deliveries from continuing operations decreased 40% and 38%, Homebuilding revenues decreased 50% and 48%, and net sales orders from continuing operations decreased 37% and 55% for the three and nine months ended September 30, 2008 as compared to the three and nine months ended September 30, 2007. During the three and nine months ended September 30, 2008, our unconsolidated joint ventures had a decrease in deliveries and net sales orders of 100% as compared to the three and nine months ended September 30, 2007 due to the consolidation of the results of our Transeastern joint venture, previously included in our unconsolidated joint venture results, into our Florida operations for the three and nine months ended September 30, 2008. Additionally, we have excluded the results of the Engle/Sunbelt joint venture from our unconsolidated joint venture results for the three and nine months ended September 30, 2008 due to the settlement agreement reached with the lenders to the joint venture. During the three and nine months ended September 30, 2008, we also recognized \$18.7 million and \$105.4 million of reorganization expenses related to our bankruptcy cases.

Chapter 11 Cases

On January 29, 2008, TOUSA, Inc. and certain of our subsidiaries (excluding our financial services subsidiaries and joint ventures) filed voluntary petitions for relief under Chapter 11 of Title 11 of the United States Bankruptcy Code in the United States Bankruptcy Court for the Southern District of Florida, Fort Lauderdale Division. The Chapter 11 cases have been consolidated solely for procedural purposes and are pending as Case No. 08-10928-JKO.

We continue to operate our businesses and manage our properties as debtors-in-possession under the jurisdiction of the Bankruptcy Court and in accordance with the applicable provisions of the Bankruptcy Code and orders of the Bankruptcy Court. At the onset of the Chapter 11 cases, we obtained Bankruptcy Court approval to, among other things, continue to pay certain critical vendors and vendors with lien rights, meet our pre-petition payroll obligations, maintain our cash management systems, sell homes free and clear of liens, pay our taxes, continue to provide employee benefits and maintain our insurance programs. In addition, the Bankruptcy Court has approved certain trading notification and transfer procedures designed to allow us to restrict trading in our common stock (and related securities) and has also provided for potentially retroactive application of notice and sell-down procedures for trading in claims against the debtors' estates (in the event that such procedures are approved in the future), which could negatively impact our accumulated net operating losses and other tax attributes. The Bankruptcy Court has also entered orders to establish procedures for the purchase and disposition of real property by us subject to certain monetary limits without specific approval for each transaction.

In March 2009, we announced that our primary focus will be on completing and delivering sold homes currently under construction and on selling our remaining inventory of speculative homes. In addition, we are seeking to sell our other assets. In certain cases, such as in the State of Florida and in Austin and Houston, Texas, we are attempting to sell our assets as a whole. We are in discussions with various parties regarding a sale of our financial services businesses, Universal Land Title, Inc., Preferred Home Mortgage Company and Alliance Insurance Information Services. We are attempting to sell all of our assets in a manner designed to maximize recovery for our creditors. Subject to, in certain situations, receiving approvals from the Bankruptcy Court, we have taken and will continue to take the following actions:

severely curtailing land purchases;

abandoning or in some cases renegotiating our rights under option and land bank contracts;

engaging in bulk sales of land and unsold homes;

reducing the number of unsold homes under construction and limiting and/or curtailing land development activities;

completing other asset dispositions; and

pursuing other initiatives designed to monetize our assets.

On February 5, 2008, pursuant to an interim order from the Bankruptcy Court dated January 31, 2008, we entered into a Senior Secured Super-Priority Debtor in Possession Credit and Security Agreement. The agreement provided for a first priority and priming secured revolving credit interim commitment of up to \$134.6 million. The agreement was subsequently amended to extend it to September 19, 2008. No funds were drawn under the agreement.

The agreement was subsequently terminated and we entered into an agreement with our prepetition secured lenders to use cash collateral on hand (cash generated by our operations, including the sale of excess inventory and the proceeds of our federal tax refund of \$207.3 million received in April 2008). We are authorized by the Bankruptcy Court to use cash collateral of our first lien and second lien lenders in a manner consistent with a budget negotiated by the parties. The order further provided for the pay-down of \$175.0 million to our first lien term secured lenders, subject to disgorgement provisions in the event that certain claims against the lenders are successful and repayment is required. We also have the right to pay-down an additional \$15.0 million to our first lien secured lenders. As of May 1, 2009, we had paid-down \$148.4 million to the first lien secured lenders. We may incur liens and enter into sale/leaseback transactions for model homes subject to certain limitations. We have granted the pre-petition agents and the lenders various forms of protection, including liens and claims to protect against any diminution of the collateral value, payment of accrued, but unpaid interest on the first priority indebtedness at the non-default rate and the payment of reasonable fees and expenses of the agents under our secured facilities.

Our right to the use of cash collateral has been extended until July 31, 2009 on terms substantially similar to those in the original cash collateral order. If we fail to comply with the order, we will not have sufficient cash to enable us to operate our business and effectuate our restructuring.

The Bankruptcy Court established May 19, 2008 as the bar date for filing proofs of claim against the Debtors relating to obligations arising before January 29, 2008. As of April 28, 2009, approximately 4,400 claims have been filed against us totaling approximately \$7.3

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billion in asserted liabilities. These claims are comprised of approximately \$5.0 million in administrative claims, \$219.0 million in secured claims, \$75.0 million in priority claims and \$7.0 billion in unsecured claims. There are many claims (at least 700) that have been asserted in unliquidated amounts or that contain an unliquidated component. Notably, among the unliquidated claims are the claims of our secured first and second lien lenders. In addition, the indenture trustees under our approximately \$1.1 billion of unsecured debentures each filed an unliquidated claim with respect to such obligations.

On April 17, 2009, we filed with the Bankruptcy Court our First Amended Joint Plan of TOUSA, Inc. and its Affiliated Debtors and Debtors in Possession under Chapter 11 of the Bankruptcy Code (as modified or revised, the Plan) and Disclosure Statement pursuant to Section 1125 of the Bankruptcy Code relating to the Plan (as modified or revised, the Disclosure Statement). Copies of the Plan and Disclosure Statement, as filed with the Bankruptcy Court, are available at <http://www.tousa.com/reorg>. Currently, no hearing has been scheduled on the Plan or Disclosure Statement. We have the exclusive right to file a plan until July 29, 2009 and the exclusive right to solicit acceptance thereof until September 27, 2009. Pursuant to Section 1121 of the Bankruptcy Code, the exclusivity periods may be expanded or reduced by the Bankruptcy Court, but in no event can the exclusivity periods to file and solicit acceptance of a plan or plans of reorganization be extended beyond September 29, 2009.

As a result of our Chapter 11 cases and other matters described herein, including uncertainties related to the fact that our filed plan of reorganization has not been confirmed, there is substantial doubt about our ability to continue as a going concern.

On March 20, 2009, we filed Forms 15 with the Securities and Exchange Commission terminating the registration of our debt and equity securities under Section 12(g) of the Securities Exchange Act of 1934. Our duty to file periodic reports under the Exchange Act was suspended immediately upon filing the Forms 15. We are therefore voluntarily filing this Quarterly Report on Form 10-Q and do not intend to make any further filings.

The foregoing discussion provides general background information regarding our Chapter 11 cases, and is not intended to be an exhaustive description. Additional information regarding our Chapter 11 cases, including access to court documents and other general information about the Chapter 11 cases, is available at www.kccllc.net/tousa. Financial information on the website is prepared according to requirements of federal bankruptcy law and the Bankruptcy Court. While such financial information accurately reflects information required under federal bankruptcy law, such information may be unconsolidated, unaudited and prepared in a format different than that used in our unaudited consolidated financial statements prepared in accordance with generally accepted accounting principles in the United States and filed under the securities laws. Moreover, the materials filed with the Bankruptcy Court are not prepared for the purpose of providing a basis for investment decisions relating to our stock or debt or for comparison with other financial information filed with the Securities and Exchange Commission.

Total Controlled Homesites by our Homebuilding Operations

The following is a summary of our controlled homesites:

	September 30, 2008			December 31, 2007		
	Owned	Optioned	Total Controlled	Owned	Optioned	Total Controlled
Region:						
Florida	7,600		7,600	8,600	600	9,200
Mid-Atlantic	300	200	500	400	800	1,200
Texas ⁽¹⁾	2,000	700	2,700	2,500	4,000	6,500
West	9,300	200	9,500	9,900	5,400	15,300
Continuing operations	19,200	1,100	20,300	21,400	10,800	32,200
Discontinued operations ⁽¹⁾	100		100	100	100	200
Total	19,300	1,100	20,400	21,500	10,900	32,400

- (1) The Texas region excludes the Dallas division, which is classified as a discontinued operation.

The following is a summary breakdown of our owned homesites:

Region	Residences Completed or Under Construction		Homesites Finished or Under Construction		Raw Land Held for Future Development		Total	
	9/30/08	12/31/07	9/30/08	12/31/07	9/30/08	12/31/07	9/30/08	12/31/07
	Florida	700	1,400	5,900	6,600	1,000	600	7,600
Mid-Atlantic	100	100	200	300			300	400
Texas ⁽¹⁾	600	700	1,000	1,400	400	400	2,000	2,500
West	400	700	2,200	2,500	6,700	6,700	9,300	9,900
Continuing operations	1,800	2,900	9,300	10,800	8,100	7,700	19,200	21,400
Discontinued operations ⁽¹⁾					100	100	100	100
Consolidated total	1,800	2,900	9,300	10,800	8,200	7,800	19,300	21,500

- (1) The Texas region excludes the Dallas/Fort Worth division, which is classified as a discontinued operation.

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We use option contracts in addition to land joint ventures in order to acquire land whenever feasible. Option contracts allow us to control large homesite positions with reduced capital investment.

Controlled homesites represent homesites either owned or under option by our consolidated subsidiaries or by our unconsolidated joint ventures that build and market homes. We do not include as controlled homesites those homesites which are included in land development joint ventures where we do not intend to build homes. These joint ventures acquire and develop land to be sold to us for use in our homebuilding operations or sold to others. See additional discussion regarding our joint ventures located in the *Liquidity and Capital Resources* section.

Due to worsening market conditions impacting the new home industry and our liquidity constraints, we have applied increasingly conservative standards to our land retention and option exercise decisions. We have analyzed each of our communities to determine if they are aligned with our immediate and mid term goals which are focused on our ability to monetize assets within a relatively short period of time. As part of the analysis, we have reviewed our construction processes including our bid procedures, bid templates and engineering designs in an attempt to reduce costs from home construction. Preacquisition costs, development costs and the number of home starts and speculative homes have also been reduced in light of the new challenges facing the market and us.

At September 30, 2008, the number of homesites controlled by our consolidated continuing operations has decreased by 11,900 or 37%, as compared to December 31, 2007. Due to our liquidity constraints, during the three and nine months ended September 30, 2008, we did not exercise certain option contracts which resulted in a reduction of approximately 2,500 and 8,800 optioned homesites, respectively.

Homebuilding Operations

For the three and nine months ended September 30, 2008 total consolidated home deliveries from continuing operations decreased 40% and 38%, Homebuilding revenues decreased 50% and 48%, and net sales orders from continuing operations decreased 37% and 55% for the three and nine months ended September 30, 2008 as compared to the three and nine months ended September 30, 2007. We had a net loss from continuing operations of \$132.2 million and \$794.0 million for the three and nine months ended September 30, 2008, respectively, as compared to a net loss from continuing operations of \$615.8 million and \$800.1 million for the three and nine months ended September 30, 2007, respectively.

During the three and nine months ended September 30, 2008, our unconsolidated joint ventures had a decrease in deliveries and net sales orders of 100% as compared to the three and nine months ended September 30, 2007 due to the consolidation of the results of our Transeastern joint venture, previously included in our unconsolidated joint venture results, into our Florida operations for the three and nine months ended September 30, 2008. Additionally, we have excluded the results of the Engle/Sunbelt joint venture from our unconsolidated joint venture results for the three and nine months ended September 30, 2008 due to the settlement agreement reached with the lenders to the joint venture. During the three and nine months ended September 30, 2008, we also recognized \$18.7 million and \$105.4 million, respectively, of reorganization expenses related to our bankruptcy cases.

Compared to September 30, 2007, consolidated sales value in backlog from continuing operations at September 30, 2008 decreased 67% to \$364.4 million. Our sales orders cancellation rate was 40% and 49% for the three and nine months ended September 30, 2008, respectively, as compared to 46% and 34% for three and nine months ended September 30, 2007, respectively. Cancellation rates continue to be affected by worsening market conditions and our Chapter 11 cases.

We build homes for inventory (speculative homes) and on a pre-sold basis. At September 30, 2008, we had 1,800 homes completed or under construction compared to 2,900 homes at December 31, 2007. Approximately 41% of these homes were unsold at September 30, 2008, a decrease from 45% at December 31, 2007. At September 30, 2008, we had 296 completed unsold homes in our inventory, down 44% from 532 homes at December 31, 2007. Approximately 56% of our completed, unsold homes at September 30, 2008 had been completed for more than 90 days. As previously discussed, in March 2009, we announced that our primary focus will be completing and delivering sold homes currently under construction and on selling our remaining inventory of speculative homes.

Once a sales contract with a buyer has been approved, we classify the transaction as a new sales order and include the home in backlog. Such sales orders are usually subject to certain contingencies such as the buyer's ability to qualify for financing and ability to sell their existing home. At closing, title passes to the buyer and a home is considered to be

delivered and is removed from backlog. Revenues, which are net of buyer incentives and cost of sales, are recognized upon the delivery of the home, land or homesite when title is transferred to the buyer. We estimate that the average period between the execution of a sales contract for a home and closing is approximately four months to over a year for pre-sold homes; however, this varies by market. The principal expenses of our Homebuilding operations are cost of sales and selling, general and administrative (SG&A) expenses. Costs of home sales include land and land development costs, home construction costs, previously capitalized indirect costs, capitalized interest and estimated warranty costs.

SG&A expenses for our Homebuilding operations include administrative costs, advertising expenses, on-site marketing expenses, sales commission costs and closing costs. Sales commissions are included in selling, general and administrative costs when the related revenue is recognized. As used herein, Homebuilding includes results of home and land sales. Home sales includes results related only to the sale of homes.

Financial Services Operations

On January 28, 2008, Preferred Home Mortgage Company, our wholly-owned residential mortgage lending subsidiary, entered into an Amended and Restated Agreement of Limited Liability Company with Wells Fargo Ventures, LLC. The limited liability company is known as PHMCWF, LLC but does business as Preferred Home Mortgage Company, an affiliate of Wells Fargo. Preferred Home Mortgage Company owns 49.9% of the venture with the balance owned by Wells Fargo. Effective April 1, 2008, the venture began to carry on the mortgage business of Preferred Home Mortgage Company. The venture is managed by a committee composed of six members, three from Preferred Home Mortgage Company and three from Wells Fargo. The venture entered into a revolving credit agreement with Wells Fargo Bank, N.A. providing for advances of up to \$20.0 million. Wells Fargo Home Mortgage provides the general and administrative

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support (as well as all loan related processing, underwriting and closing functions), and is the end investor for the majority of the loans closed through the joint venture. Prior to the joint venture, Preferred Home Mortgage Company had a centralized operations center that provided those support functions. The majority of these support functions ceased in June 2008. Effective April 1, 2008, we began to account for the venture as an equity-method investment.

During the nine months ended September 30, 2008, approximately 1% to 2% of the homebuyers, including those in our unconsolidated joint ventures, that utilized our mortgage subsidiary and mortgage joint venture obtained sub-prime loans. We define a sub-prime loan as one where the buyer's FICO score is below 620 and is not an FHA or VA loan. At September 30, 2008, none of our backlog that utilized our mortgage joint venture included homebuyers seeking sub-prime financing. Since 2007, the mortgage markets have experienced a significant disruption, which commenced with increasing rates of default on sub-prime loans and declines in the market value of those loans. These events led to an unprecedented combination of reduced investor demand for mortgage loans and mortgage-backed securities, tighter credit underwriting standards, reduced mortgage loan liquidity and increased credit risk premiums, all of which affected the availability of nonconforming mortgage products. The tightening of credit standards in the sub-prime market had an impact on the Alt-A and prime loans and further negatively impacted current homebuilding market conditions.

Critical Accounting Policies

There have been no material changes to our critical accounting policies and estimates from the information provided in Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations. Critical Accounting Policies and Estimates included in our 2007 Form 10-K except as follows.

Impairment of Long-Lived Assets

Housing communities and land/homesites under development are stated at the lower of cost or net realizable value. Property and equipment is carried at cost less accumulated depreciation. We assess these assets for impairment in accordance with the provisions of SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. SFAS 144 requires that long-lived assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

We review inventories for impairment on a community by community basis. Recoverability of assets is measured by comparing the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If the sum of the expected undiscounted future cash flows is less than the carrying amount of the assets, an impairment loss is recognized. Our evaluation for impairment is impacted by margins on homes that have been delivered, margins in sales contracts in backlog, projected margins with regard to future home sales over the life of the community, projected margins with regard to future land sales, and the fair value of the land itself. We pay particular attention to trends that indicate a downward market such as slow-moving inventories and lower sales prices.

If the undiscounted cash flows are less than the carrying amount of inventory, then the impairment is measured based on estimated future cash flows, discounted at a market rate of interest. The projected cash flows for each community are significantly impacted by estimates related to market supply and demand, product type, homesite sizes, sales pace, sales prices, sales incentives, construction costs, sales and marketing expenses, the local economy, competitive conditions, labor costs, costs of materials and other factors for that particular community. Local economy and community factors that may affect our assumptions include current market economic and demographic conditions, competitors' presence and activities in the local market, current market trends and forecasts, historical results, specific community features such as location, amenities, unique attributes and future potential alternatives for product offerings in response to market conditions. The determination of fair value also requires discounting the estimated cash flows at a rate commensurate with the inherent risks associated with the assets and related estimated cash flow streams. The discount rate used in determining each asset's fair value depends on the community's projected life and development stage. At September 30, 2008, we used discount rates ranging from 12% to 22% with an average of 18%, depending on the perceived risks associated with the community's cash flow streams relative to its inventory. Our cash flow projection models assume either a price depreciation or no price change depending on market conditions and a minimal price appreciation in most of our markets in 2010. These assumptions are based on third-party market data, corroborated with management estimates and projections. Subsequently, during the fourth quarter of 2008 and during 2009, the weakness in the housing market was exacerbated by unforeseen significant disruptions in the broader

financial markets and severe constraints in the credit markets. As SFAS No. 144 requires that the assumptions used in the cash flow projection models reflect the conditions in effect as of the assessment date, our evaluation did not anticipate the dramatic effect of these events. Due to the continued deterioration in market conditions, we expect that our assumptions for the fourth quarter of 2008 will be correspondingly adjusted, which we expect will result in additional impairment charges.

We believe that the accounting for impairment of long-lived assets is a critical accounting policy because of the assumptions inherent in the evaluations and the impact of recognizing impairments would be material to our consolidated financial statements. Evaluations for impairment are significantly impacted by estimates of future revenues, costs and expenses and other factors involving some amount of uncertainty since they are based on current market conditions and current assumptions of future markets made by management. These assumptions include: the expected sales prices and sales incentives to be offered; the timing of sales within a community; the expected cancellation rates based on local housing market conditions and competition; the number and type of homes available and pricing and incentives being offered in other communities by us or by other builders in the surrounding areas; total costs expended to date and expected to be incurred in the future, including, sales and marketing costs; alternative products that may be offered that could have an impact on sales pace, sales price and/or building costs; and, alternative uses for the property such as the possibility of a sale of lots to a third party versus the sale of individual homes. Many of these assumptions are interdependent and changing one assumption generally requires a corresponding change to one or more of the other assumptions. For example, increasing or decreasing the sales absorption rate has a direct impact on the estimated per unit sales price of a home, the level of time sensitive costs (such as indirect construction, overhead and carrying costs), and selling and marketing costs (such as model maintenance costs and promotional and advertising campaign costs). Our objectives for a community, could have a significant impact on the community cash flow analysis. For example, if our business objective is to drive delivery levels, our community cash flow analysis will be different than if the business objective is to preserve operating margins. These objectives may vary significantly from community to community, from division to division, and over time with respect to the same community. The number of communities reviewed for impairment and the interrelationship and complexity of assumptions preclude discussion on a

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community by community basis. Continuing uncertainties in economic and market conditions and assumptions and estimates required of our management in valuing inventory during changing market conditions, could result in actual future results differing materially from management's assumptions and may require material inventory impairment charges to be recorded in the future. For example, further market deterioration may lead to additional sales incentives and decreases in sales prices and/or volumes resulting in additional impairment charges on previously impaired inventory, as well as on inventory not currently impaired but for which indicators of impairment may arise if further market deterioration occurs.

Inventory impairments and abandonment costs on active communities were \$65.0 million and \$342.2 million, respectively, for the three and nine months ended September 30, 2008 compared to \$63.3 million and \$112.7 million, respectively, for the three and nine months ended September 30, 2007. During the three and nine months ended September 30, 2008, we also recorded charges of \$32.1 million and \$231.9 million, respectively, in write-offs of deposits and abandonment costs which are included in cost of sales—inventory impairments and abandonment costs in the accompanying unaudited consolidated statements of operations, related to land that we have determined is not probable that we will purchase or build on (including land to be sold as lots), compared to \$441.2 million and \$515.7 million, respectively, for the three and nine months ended September 30, 2007. Included in the impairment charges on active communities for the three and nine months ended September 30, 2008 is \$0 million and \$4.3 million, respectively, of inventory impairments recognized on properties accounted for as financing arrangements under SFAS 66 for which we do not have title to the underlying asset.

Financial Reporting Under SOP 90-7

In accordance with GAAP, we have applied the provisions of American Institute of Certified Public Accountants (AICPA) Statement of Position 90-7, *Financial Reporting by Entities in Reorganization Under the Bankruptcy Code* (SOP 90-7), in preparing the unaudited consolidated financial statements. SOP 90-7 requires that the financial statements, for periods subsequent to the Chapter 11 filing, distinguish transactions and events that are directly associated with the reorganization from the ongoing operations of the business. Accordingly, certain items of income, expense, gain or loss realized or incurred because we are in Chapter 11 are recorded in reorganization items, net on the accompanying unaudited consolidated statements of operations. Also, pre-petition obligations that may be impacted by the bankruptcy reorganization process have been classified in liabilities subject to compromise on the unaudited consolidated statement of financial condition at September 30, 2008. These liabilities are reported at the amounts expected to be allowed by the Bankruptcy Court, in accordance with Statement of Financial Accounting Standards (SFAS) No. 5, *Accounting for Contingencies* (SFAS 5), even if they may be settled for lesser amounts. As of September 30, 2008, the pre-petition liabilities included in liabilities subject to compromise have not been reduced.

We believe that financial reporting under SOP 90-7 is a critical accounting policy because it has a significant impact on our business processes and internal control over financial reporting related to the proper separation and payment of pre-petition and post-petition obligations and the preparation of unaudited consolidated financial statements and related disclosures reflecting the accounting required for the restructuring activities and reorganization expenses resulting from our Chapter 11 proceedings. Application of SOP 90-7 involves estimates for amounts expected to be allowed claims, among other things.

Results of Operations—Consolidated***Three Months Ended September 30, 2008 Compared to Three Months Ended September 30, 2007***

Total revenues decreased 50% to \$251.0 million for the three months ended September 30, 2008, from \$501.2 million for the three months ended September 30, 2007. This decrease is primarily attributable to a decrease in Homebuilding revenues.

For the three months ended September 30, 2008, we reported a loss from continuing operations before reorganization items and the benefit for income taxes of \$116.2 million as compared to a loss from continuing operations before income taxes of \$609.8 million for the three months ended September 30, 2007. Results from continuing operations for the three months ended September 30, 2008 and 2007 include charges totaling \$107.0 million and \$571.3 million, respectively, related to inventory impairments, abandonment costs, joint venture impairments, goodwill impairments and the settlement of a loss contingency. During the three months ended September 30, 2008, we also recognized \$18.7 million of reorganization expenses related to our bankruptcy cases.

Our effective tax rate from continuing operations was (2.0)% for the three months ended September 30, 2008. The effective tax rate for the three months ended September 30, 2008 was impacted primarily by a valuation allowance on our deferred tax asset and the reduction of unrecorded tax benefits due to a favorable ruling received from the Internal Revenue Service related to an uncertain tax position.

For the three months ended September 30, 2008, we reported a loss from continuing operations, net of taxes, of \$132.2 million (or a loss of \$2.26 per basic and diluted share) compared to a loss from continuing operations, net of taxes, of \$615.8 million (or a loss of \$10.36 per basic and diluted share) for the three months ended September 30, 2007.

Homebuilding

Homebuilding revenues decreased 50% to \$246.9 million for the three months ended September 30, 2008, from \$492.9 million for the three months September 30, 2007. This decrease is primarily due to a decrease in revenue from home sales to \$246.6 million for the three months ended September 30, 2008 from \$449.6 million for the three months ended September 30, 2007. The decrease in revenue from home sales, which is net of buyer incentives, was due to a 40% decrease in the number of deliveries from continuing operations to 881 for the three months ended September 30, 2008 from 1,459 for the three months ended September 30, 2007. The average price of homes delivered from continuing operations decreased 9% to \$280,000 for the three months ended September 30, 2008, from \$308,000 for the three months ended September 30, 2007. For the three months ended September 30, 2008, our incentives from continuing operations increased 21% to \$54,800 per home delivered from \$45,300 per home delivered for the three months ended September 30, 2007. Our home sales revenues have continued to decrease through 2009 as the number of home deliveries declined as a result of severe market conditions in the new and existing home industry combined with diminished consumer confidence, the oversupply of new and existing homes available for sale, increased foreclosures and downward pressure on home prices. These factors have been exacerbated by our Chapter 11 filings.

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For the three months ended September 30, 2008, we had a homebuilding gross loss of \$45.8 million as compared to a gross loss of \$437.4 million for the three months ended September 30, 2007. This decrease is primarily due to a decrease in inventory impairments and abandonment costs during the three months ended September 30, 2008. Inventory impairments and abandonment costs were \$97.1 million for the three months ended September 30, 2008 compared to \$504.5 million for the three months ended September 30, 2007.

SG&A expenses decreased to \$44.0 million for the three months ended September 30, 2008, from \$86.0 million for the three months ended September 30, 2007. This decrease in expenses is due to a decrease of \$16.8 million in selling and marketing expenses primarily due to a \$8.1 million decrease in commissions resulting from a decrease in both deliveries and average selling prices; a decrease of \$4.0 million in professional fees related to the Transeastern JV settlement in 2007; and a reduction in overhead and related expenses due to reduced levels of business during the three months ended September 30, 2008.

SG&A expenses as a percentage of revenues from home sales for the three months ended September 30, 2008 decreased to 18% as compared to 19% for the three months ended September 30, 2007. The decrease in SG&A expenses as a percentage of home sales revenues is due to the decrease in selling and marketing expenses and an overall reduction in overhead as discussed above.

Net Sales Orders and Homes in Backlog (Consolidated)

For the three months ended September 30, 2008, net sales orders from continuing operations decreased by 37% to 559 as compared to 892 for the three months ended September 30, 2007. The decrease in net sales orders is due to decreased demand for new homes and higher cancellation rates. These factors, as well as our Chapter 11 cases, have continued to negatively impact our net sales orders through 2009.

Our cancellation rate decreased to 40% for the three months ended September 30, 2008 from 46% for the three months ended September 30, 2007. The decrease in cancellation rates is due to the reduction in sales rates.

We had 1,258 homes in backlog from continuing operations as of September 30, 2008, as compared to 3,485 homes in backlog as of September 30, 2007. The 64% decrease in backlog units is primarily due to a decline in sales orders as a result of decreased demand. The sales value of backlog from continuing operations decreased 67% to \$364.4 million at September 30, 2008, from \$1.1 billion at September 30, 2007, due to the decrease in the number of homes in backlog in addition to a decrease in the average selling price of homes in backlog to \$290,000 from \$320,000 from period to period. The decrease in the average selling price of homes in backlog was primarily due to increased incentives and a change in product mix. At April 30, 2009, our consolidated continuing operations had 536 homes in backlog representing \$142.1 million in revenue.

Net Sales Orders and Homes in Backlog (Unconsolidated Joint Ventures)

For the three months ended September 30, 2008, net sales orders decreased by 100% as compared to the three months ended September 30, 2007. The decrease in net sales orders was due to the results for the Transeastern joint venture, previously included in our unconsolidated joint venture results, being consolidated into our Florida operations for the three months ended September 30, 2008. Additionally, we have excluded the results of the Engle/Sunbelt joint venture from our unconsolidated joint venture results for the three months ended September 30, 2008 due to the settlement agreement reached with the lenders to the joint venture.

Our unconsolidated joint ventures, had no homes in backlog as of September 30, 2008, as compared to 135 homes in backlog as of September 30, 2007. The 100% decrease in backlog is due to the factors described above regarding the Engle/Sunbelt joint venture.

Discontinued Operations

On September 6, 2007, we sold substantially all of our Dallas/Fort Worth division to an independent third-party. In accordance with SFAS 144, results of our Dallas/Fort Worth division have been classified as a discontinued operation, and prior periods have been restated. Discontinued operations include Dallas/Fort Worth division revenues and a net loss \$0.2 million and \$0.6 million, respectively, for the three months ended September 30, 2008 and \$1.1 million and \$3.9 million, respectively, for the three months ended September 30, 2007.

Nine Months Ended September 30, 2008 Compared to Nine Months Ended September 30, 2007

Total revenues decreased 49% to \$849.6 million for the nine months ended September 30, 2008, from \$1.7 billion for the nine months ended September 30, 2007. This decrease is primarily attributable to a decrease in Homebuilding

revenues of 48%.

For the nine months ended September 30, 2008, we reported a loss from continuing operations before reorganization items and the benefit for income taxes of \$690.6 million as compared to a loss from continuing operations before benefit for income taxes of \$835.8 million for the nine months ended September 30, 2007. Results from continuing operations for the nine months ended September 30, 2008 and 2007 include charges totaling \$586.4 million and \$849.8 million, respectively, related to inventory impairments, abandonment costs, joint venture impairments, goodwill impairments and the settlement of a loss contingency. During the nine months ended September 30, 2008, we also recognized \$105.4 million of reorganization expenses related to our bankruptcy cases.

Our effective tax rate from continuing operations was (0.3)% for the nine months ended September 30, 2008 compared to 4.3% for the nine months ended September 30, 2007, respectively. The effective tax rate for the nine months ended September 30, 2008 was impacted primarily by a valuation allowance on our deferred tax asset and the reduction of unrecognized tax benefits due to a favorable ruling received from the Internal Revenue Service related to an uncertain tax position.

For the nine months ended September 30, 2008, we reported a loss from continuing operations, net of taxes, of \$794.0 million (or a loss of \$13.45 per basic and diluted share) compared to a loss from continuing operations, net of taxes, of \$800.1 million (or a loss of \$13.46 per basic and diluted share) for the nine months ended September 30, 2007.

Table of Contents*Homebuilding*

Homebuilding revenues decreased 48% to \$836.4 million for the nine months ended September 30, 2008, from \$1.6 billion for the nine months September 30, 2007. This decrease is primarily due to a decrease in revenue from home sales to \$814.4 million for the nine months ended September 30, 2008 from \$1.5 billion for the nine months ended September 30, 2007. The decrease in revenue from home sales, which is net of buyer incentives, was due to a 38% decrease in the number of deliveries from continuing operations to 3,020 for the nine months ended September 30, 2008 from 4,833 for the nine months ended September 30, 2007. The average price of homes delivered from continuing operations decreased 15% to \$270,000 for the nine months ended September 30, 2008, from \$319,000 for the nine months ended September 30, 2007. Our home sales revenues have continued to decrease through 2009 as the number of home deliveries declined as a result of severe market conditions in the new and existing home industry combined with diminished consumer confidence, the oversupply of new and existing homes available for sale, increased foreclosures and downward pressure on home prices. These factors have been exacerbated by our Chapter 11 filings.

For the nine months ended September 30, 2008, we had a homebuilding gross loss of \$469.1 million as compared to \$339.7 million for the nine months ended September 30, 2007. This increase is primarily due to the decrease in the number of deliveries coupled with higher incentives on homes delivered in response to challenging homebuilding market conditions partially offset by a decrease in inventory impairments and abandonment costs. For the nine months ended September 30, 2008, our incentives from continuing operations increased 46% to \$59,000 per home delivered from \$40,400 per home delivered for the nine months ended September 30, 2007.

SG&A expenses decreased to \$153.8 million for the nine months ended September 30, 2008, from \$262.4 million for the nine months ended September 30, 2007. This decrease in expenses is due to a decrease of \$52.9 million in selling and marketing expenses primarily due to a \$31.9 million decrease in commissions resulting from a decrease in both deliveries and average selling prices; a decrease of \$16.0 million in professional fees related to the Transeastern JV settlement in 2007; and a reduction in overhead and related expenses due to reduced levels of business during the nine months ended September 30, 2008.

SG&A expenses as a percentage of revenues from home sales for the nine months ended September 30, 2008 increased to 19%, as compared to 17% for the nine months ended September 30, 2007. The increase in SG&A expenses as a percentage of home sales revenues is due to the decrease in deliveries and average selling prices.

For the nine months ended September 30, 2008, we had income from unconsolidated joint ventures of \$0.4 million compared to a loss from unconsolidated joint ventures of \$8.8 million for the nine months ended September 30, 2007. The increase in our earnings from unconsolidated joint ventures is primarily due to the reduction of loss accruals totaling \$11.6 million for certain joint venture obligations established in 2007 and reversed during the nine months ended September 30, 2008.

Net Sales Orders and Homes in Backlog (Consolidated)

For the nine months ended September 30, 2008, net sales orders from continuing operations decreased by 55% to 1,899 as compared to 4,195 for the nine months ended September 30, 2007. The decrease in net sales orders is due to decreased demand for new homes and higher cancellation rates. These factors, as well as our Chapter 11 cases, have continued to negatively impact our net sales orders through 2009.

Our cancellation rate increased to 49% for the nine months ended September 30, 2008 from 34% for the nine months ended September 30, 2007. The majority of our regions experienced increases in cancellation rates for the nine months ended September 30, 2008 when compared with the same period in 2007. Our Florida and Mid-Atlantic regions had the largest increases in cancellation rate to 78% and 49%, respectively, for the nine months ended September 30, 2008 as compared to 38% and 26%, respectively, for the nine months ended September 30, 2007. The increase in cancellation rate in Florida is primarily due to contracts with a third-party that marketed homes in the United Kingdom, for 511 homes representing \$115.6 million of revenue, which were cancelled in June 2008.

Net Sales Orders and Homes in Backlog (Unconsolidated Joint Ventures)

For the nine months ended September 30, 2008, net sales orders decreased by 100% as compared to the nine months ended September 30, 2007. The decrease in net sales orders was due to the results for the Transeastern joint venture, previously included in our unconsolidated joint venture results, being consolidated into our Florida operations

for the nine months ended September 30, 2008. Additionally, we have excluded the results of the Engle/Sunbelt joint venture from our unconsolidated joint venture results for the nine months ended September 30, 2008 due to the settlement agreement reached with the lenders to the joint venture.

Discontinued Operations

On September 6, 2007, we sold substantially all of our Dallas/Fort Worth division to an independent third-party. In accordance with SFAS 144, results of our Dallas/Fort Worth division have been classified as a discontinued operation, and prior periods have been restated. Discontinued operations include Dallas/Fort Worth division revenues and net loss of \$1.2 million and \$3.8 million, respectively, for the nine months ended September 30, 2008 and \$44.7 million and \$17.6 million, respectively, for the nine months ended September 30, 2007.

Table of Contents**Reportable Segments**

Our operating segments are aggregated into reportable segments in accordance with Statement of Financial Accounting Standards No. 131, *Disclosures About Segments of an Enterprise and Related Information*, based primarily upon similar economic characteristics, product type, geographic area and information used by the chief operating decision maker to allocate resources and assess performance. Our reportable segments consist of our four major Homebuilding geographic regions (Florida, Mid-Atlantic, Texas and the West) and our Financial Services operations.

Homebuilding Operations

The reportable segments for our Homebuilding operations are as follows:

Florida: Central Florida, Jacksonville, Southeast Florida, Southwest Florida, Tampa/St. Petersburg

Mid-Atlantic: Baltimore/Southern Pennsylvania, Nashville, Northern Virginia (on September 25, 2007, we sold in bulk, home sites in our Mid-Atlantic (excluding Nashville) and Virginia divisions)

Texas: Austin, Houston, San Antonio (on September 6, 2007, we sold substantially all of our Dallas/Fort Worth division)

West: Colorado, Las Vegas, Phoenix

Selected Homebuilding Operations and Financial Data

The following tables set forth selected operational and financial data for our Homebuilding operations for the periods indicated (dollars in millions, except average price in thousands):

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2008	2007	2008	2007
Homebuilding revenues:				
Florida ⁽²⁾ :				
Sales of homes	\$ 79.3	\$ 188.3	\$ 306.7	\$ 637.4
Sales of land		7.3	3.1	33.7
Total Florida	79.3	195.6	309.8	671.1
Mid-Atlantic:				
Sales of homes	17.7	49.9	46.1	164.5
Sales of land		31.5	2.2	31.6
Total Mid-Atlantic	17.7	81.4	48.3	196.1
Texas ⁽¹⁾ :				
Sales of homes	101.5	147.8	306.7	461.7
Sales of land		1.2	7.1	7.3
Total Texas	101.5	149.0	313.8	469.0
West:				
Sales of homes	48.1	63.6	154.9	278.7
Sales of land	0.3	3.3	9.6	4.4
Total West	48.4	66.9	164.5	283.1
Total homebuilding revenues	\$ 246.9	\$ 492.9	\$ 836.4	\$ 1,619.3

(1) The Texas region excludes

the Dallas division, which is classified as a discontinued operation.

- (2) The results of operations for Transeastern for the three and nine months ended September 30, 2008 have been included in our consolidated results. Results of operations for the three and nine months ended September 30, 2007 are included in the results for the unconsolidated joint ventures. See Note 4 of the notes to the unaudited consolidated financial statements.

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	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Results of Operations:				
Homebuilding:				
Florida ⁽²⁾	\$ (53.9)	\$ (299.4)	\$ (301.4)	\$ (290.3)
Mid-Atlantic	(7.9)	(52.0)	(36.2)	(97.7)
Texas ⁽¹⁾	(11.6)	14.6	(28.9)	43.3
West	(17.1)	(199.4)	(235.5)	(276.2)
Total Homebuilding	(90.5)	(536.2)	(602.0)	(620.9)
Financial Services	(0.5)	0.2	(4.8)	5.2
Corporate and unallocated	(25.2)	(73.8)	(83.8)	(220.1)
Loss from continuing operations before reorganization items and taxes	\$ (116.2)	\$ (609.8)	\$ (690.6)	\$ (835.8)

(1) The Texas region excludes the Dallas division, which is classified as a discontinued operation.

(2) The results of operations for Transeastern for the three and nine months ended September 30, 2008 have been included in our consolidated results. Results of operations for the three and nine months ended September 30, 2007 are included in the results for the unconsolidated joint ventures. See Note 4 of

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	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Impairment charges on active communities:				
Florida	\$ 58.1	\$ 15.7	\$ 264.0	\$ 44.4
Mid-Atlantic	2.1	4.4	14.6	11.0
Texas	1.7		4.8	0.6
West	3.1	43.2	58.8	56.7
	65.0	63.3	342.2	112.7
Write-offs of deposits and abandonment costs:				
Florida	10.0	274.5	46.4	287.3
Mid-Atlantic	4.6	33.9	14.0	47.8
Texas	13.5		20.3	0.3
West	4.0	132.8	151.2	180.3
	32.1	441.2	231.9	515.7
Inventory impairments and abandonment costs	\$ 97.1	\$ 504.5	\$ 574.1	\$ 628.4
Remaining carrying value of inventory impaired at end of period	\$ 502.2	\$ 728.0	\$ 502.2	\$ 728.0
Number of projects impaired during the period	98	131	257	171
Total number of projects included in inventory and reviewed for impairment during the period	361	481	361	481

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	Three Months Ended September 30,				Nine Months Ended September 30,			
	2008		2007		2008		2007	
	Homes	\$	Homes	\$	Homes	\$	Homes	\$
Deliveries:								
Consolidated:								
Florida ⁽²⁾	270	\$ 79.3	551	\$ 188.3	1,132	\$ 306.7	1,780	\$ 637.4
Mid-Atlantic	61	17.7	138	49.9	147	46.1	458	164.5
Texas ⁽¹⁾	369	101.5	563	147.8	1,170	306.7	1,784	461.7
West	181	48.1	207	63.6	571	154.9	811	278.7
Continuing operations	881	246.6	1,459	449.6	3,020	814.4	4,833	1,542.3
Discontinued operations ⁽¹⁾	1	0.2	7	1.1	8	1.2	189	44.7
Consolidated total	882	246.8	1,466	450.7	3,028	815.6	5,022	1,587.0
Unconsolidated joint ventures:								
Florida (excluding Transeastern)							40	11.3
Transeastern ⁽²⁾			132	28.5			739	174.8
Mid-Atlantic			6	1.1			16	4.0
West ⁽³⁾			136	36.5			774	230.9
Total unconsolidated joint ventures			274	66.1			1,569	421.0
Combined total	882	\$ 246.8	1,740	\$ 516.8	3,028	\$ 815.6	6,591	\$ 2,008.0

(1) The Texas region excludes the Dallas division, which is classified as a discontinued operation.

(2) The results of operations for Transeastern for the three and nine months ended September 30, 2008 have been included in our consolidated results. Results of operations for the three and

nine months ended September 30, 2007 are included in the results for the unconsolidated joint ventures. See Note 4 of the notes to the unaudited consolidated financial statements.

- (3) We have excluded the results of the Engle/Sunbelt joint venture from our unconsolidated joint venture results for the three and nine months ended September 30, 2008 due to the settlement agreement reached in 2008. See Note 5 of the notes to the unaudited consolidated financial statements.

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2008		2007		2008		2007	
	Homes	\$	Homes	\$	Homes	\$	Homes	\$
Net Sales Orders⁽¹⁾:								
Consolidated:								
Florida ⁽³⁾⁽⁴⁾	172	\$ 32.8	226	\$ 43.6	295	\$ 19.5	1,263	\$ 398.9
Mid-Atlantic	2	(2.3)	57	17.4	139	42.0	485	170.0
Texas ⁽²⁾	226	61.8	376	99.1	1,019	267.0	1,658	417.3
West	159	39.4	233	59.5	446	114.0	789	219.4
Continuing operations	559	131.7	892	219.6	1,899	442.5	4,195	1,205.6

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Discontinued operations ⁽²⁾				(0.5)	9	1.0	70	18.9
Consolidated total	559	131.7	892	219.1	1,908	443.5	4,265	1,224.5
Unconsolidated joint ventures:								
Florida (excluding Transeastern)							12	1.7
Transeastern ⁽³⁾			54	9.2			248	27.1
Mid-Atlantic			6	1.0			19	3.8
West ⁽⁵⁾			93	21.5			480	116.8
Total unconsolidated joint ventures			153	31.7			759	149.4
Combined total	559	\$ 131.7	1,045	\$ 250.8	1,908	\$ 443.5	5,024	\$ 1,373.9

- (1) Net of cancellations.
- (2) The Texas region excludes the Dallas division, which is classified as a discontinued operation.
- (3) The results of operations for Transeastern for the three and nine months ended September 30, 2008 have been included in our consolidated results. Results of operations for the three and nine months ended September 30, 2007 are included in the results for the unconsolidated joint ventures. See Note 4 of the notes to the unaudited consolidated financial

statements.

- (4) In June 2008, we cancelled 511 contracts, representing \$115.6 million of revenue, with a third-party that marketed homes to customers in the United Kingdom. Of the 511 contracts, 398 contracts were entered into in 2005 and 113 contracts were entered into in June 2007. Accordingly, included in net sales orders for the three and nine months ended September 30, 2008 are 511 cancellations related to these contracts.
- (5) We have excluded the results of the Engle/Sunbelt joint venture from our unconsolidated joint venture results for the three and nine months ended September 30, 2008 due to the settlement agreement reached in 2008. See Note 5 of

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	September 30, 2008			September 30, 2007		
	Homes	\$	Average Price	Homes	\$	Average Price
Sales Backlog:						
Consolidated:						
Florida ⁽³⁾	493	\$ 148.5	\$ 301	1,935	\$ 664.4	\$ 343
Mid-Atlantic	72	24.0	\$ 334	239	87.1	\$ 365
Texas ⁽¹⁾	398	115.1	\$ 289	848	229.2	\$ 270
West	295	76.8	\$ 260	463	135.3	\$ 292
Continuing operations	1,258	364.4	\$ 290	3,485	1,116.0	\$ 320
Discontinued operations ⁽¹⁾	4	0.6	\$ 148	14	4.3	\$ 305
Consolidated total	1,262	365.0	\$ 289	3,499	1,120.3	\$ 320
Unconsolidated joint ventures:						
West ⁽²⁾				135	37.0	\$ 274
Total unconsolidated joint ventures				135	37.0	\$ 274
Combined total	1,262	\$ 365.0	\$ 289	3,634	\$ 1,157.3	\$ 318

(1) The Texas region excludes the Dallas division, which is classified as a discontinued operation.

(2) We have excluded the results of the Engle/Sunbelt joint venture from our unconsolidated joint venture results for the three and nine months ended September 30, 2008 due to the settlement agreement reached in 2008.

See Note 5 of the notes to the unaudited consolidated financial statements.

- (3) In June 2008, we cancelled 511 contracts, representing \$115.6 million of revenue, with a third-party that marketed homes to customers in the United Kingdom. Of the 511 contracts, 398 contracts were entered into in 2005 and 113 contracts were entered into in June 2007.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Cancellation rates:				
Consolidated:				
Florida ⁽²⁾	38%	56%	78%	38%
Mid-Atlantic	97%	59%	49%	26%
Texas ⁽¹⁾	35%	43%	27%	33%
West	36%	35%	40%	36%
Continuing Operations	40%	46%	49%	34%

- (1) The Texas region excludes the Dallas division, which is classified as a discontinued operation.

- (2) In June 2008, we cancelled 511 contracts,

representing \$115.6 million of revenue, with a third-party that marketed homes to customers in the United Kingdom. Of the 511 contracts, 398 contracts were entered into in 2005 and 113 contracts were entered into in June 2007. Accordingly, included in cancellation rates for the three and nine months ended September 30, 2008 are 511 cancellations related to these contracts.

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	Three Months Ended September 30,				Nine Months Ended September 30,			
	2008		2007		2008		2007	
	Sales		Sales		Sales		Sales	
Average Price:	Deliveries	Orders	Deliveries	Orders	Deliveries	Orders	Deliveries	Orders
Consolidated:								
Florida ⁽²⁾⁽⁴⁾	\$294	\$ 190	\$342	\$193	\$271	\$ 66	\$358	\$316
Mid-Atlantic ⁽⁵⁾	\$290	\$(1,132)	\$362	\$305	\$313	\$302	\$359	\$351
Texas ⁽¹⁾	\$275	\$ 273	\$262	\$264	\$262	\$262	\$259	\$252
West	\$266	\$ 248	\$308	\$255	\$271	\$256	\$344	\$278
Continuing operations	\$280	\$ 236	\$308	\$246	\$270	\$233	\$319	\$287
Discontinued operations ⁽¹⁾	\$160		\$158		\$146	\$112	\$237	\$270
Consolidated total	\$280	\$ 236	\$307	\$246	\$269	\$232	\$316	\$287
Unconsolidated joint ventures:								
Florida (excluding Transeastern)							\$282	\$142
Transeastern ⁽²⁾			\$216	\$171			\$237	\$109
Mid-Atlantic			\$193	\$172			\$249	\$202
West ⁽³⁾			\$268	\$231			\$298	\$243
Total unconsolidated joint ventures			\$241	\$207			\$268	\$197
Combined total	\$280	\$ 236	\$297	\$240	\$269	\$232	\$305	\$273

(1) The Texas region excludes the Dallas division, which is classified as a discontinued operation.

(2) The results of operations for Transeastern for the three and nine months ended September 30, 2008 have been included in our consolidated results. Results of operations for the three and nine months ended September 30, 2007 are

included in the results for the unconsolidated joint ventures. See Note 4 of the notes to the unaudited consolidated financial statements.

- (3) We have excluded the results of the Engle/Sunbelt joint venture from our unconsolidated joint venture results for the three and nine months ended September 30, 2008 due to the settlement agreement reached in 2008. See Note 5 of the notes to the unaudited consolidated financial statements.
- (4) In June 2008, we cancelled 511 contracts, representing \$115.6 million of revenue, with a third-party that marketed homes to customers in the United Kingdom. Of the 511 contracts, 398 contracts were entered into in 2005 and 113

contracts were entered into in June 2007.

Accordingly, included in net sales orders for the three and nine months ended September 30, 2008 are 511 cancellations related to these contracts.

- (5) During the three months ended September 30, 2008, our Mid-Atlantic region experienced a 97% cancellation rate with only two net sales.

Three Months Ended September 30, 2008 compared to Three Months Ended September 30, 2007

Florida: Homebuilding revenues decreased 59% to \$79.3 million for the three months ended September 30, 2008 from \$195.6 million for the three months ended September 30, 2007. The decrease in Homebuilding revenues was due to a 58% decrease in revenues from home sales to \$79.3 million for the three months ended September 30, 2008 from \$188.3 million for the three months ended September 30, 2007 and a decrease in revenue from land sales of \$7.3 million compared to the three months ended September 30, 2007. The decrease in home sales revenues during the three months ended September 30, 2008 is the result of a 51% decrease in the number of home deliveries to 270 for the three months ended September 30, 2008 from 551 homes delivered for the three months ended September 30, 2007, and a 14% decrease in the average selling price of homes to \$294,000 for the three months ended September 30, 2008 from \$342,000 for the three months ended September 30, 2007.

During the three months ended September 30, 2008, we recognized \$58.1 million in impairment charges compared to \$15.7 million for the three months ended September 30, 2007. Gross margin on home sales, excluding impairments, was 29% for the three months ended September 30, 2008, compared to 19% for the three months ended September 30, 2007. This increase in gross margin was primarily due to the recovery of previously recorded impairments on homes delivered partially offset by an increase in sales incentives offered to home buyers coupled with a decline in the base price of the homes delivered. The average sales incentive per home delivered increased 26% to \$93,600 per home for the three months ended September 30, 2008, from \$74,500 for the three months ended September 30, 2007.

For the three months ended September 30, 2008 and 2007, we incurred losses of \$10.0 million and \$275.1 million from land sales, respectively, which included land impairments and abandonment costs of \$10.0 million and \$274.5 million, respectively.

Mid-Atlantic: Homebuilding revenues decreased 78% to \$17.7 million for the three months ended September 30, 2008 from \$81.4 million for the three months ended September 30, 2007. The decrease in Homebuilding revenues was due to a 65% decrease in revenues from home sales to \$17.7 million for the three months ended September 30, 2008 from \$49.9 million for the three months ended September 30, 2007 and a decrease in revenue from land sales of \$31.5 million compared to the three months ended September 30, 2007. Home sales revenues decreased as a result of

a 56% decrease in the number of home deliveries to 61 for the three months ended September 30, 2008 from 138 homes delivered for the three months ended September 30, 2007, and a 20% decrease in the average selling price of homes to \$290,000 for the three months ended September 30, 2008 from \$362,000 for the three months ended September 30, 2007.

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During the three months ended September 30, 2008, we recognized \$2.1 million in impairment charges compared to \$4.4 million for the three months ended September 30, 2007. Gross margin on home sales, excluding impairments, increased to 12% for the three months ended September 30, 2008 compared to 11% for the three months ended September 30, 2007. This slight increase in gross margin was primarily due to a decrease in cost of sales and the recovery of previously recorded impairments on homes delivered, partially offset by an increase in sales incentives offered to home buyers coupled with a decline in the base price of the homes delivered. Average sales incentive per home delivered increased 5% to \$29,400 per home for the three months ended September 30, 2008, from \$27,800 for the three months ended September 30, 2007.

For the three months ended September 30, 2008 and 2007, we incurred losses of \$4.6 million and \$46.9 million from land sales, respectively, which included land impairments and abandonment costs of \$4.6 million and \$33.9 million, respectively.

Texas: Homebuilding revenues decreased 32% to \$101.5 million for the three months ended September 30, 2008 from \$149.0 million for the three months ended September 30, 2007. The decrease in Homebuilding revenues was primarily due to a 31% decrease in revenues from home sales to \$101.5 million for the three months ended September 30, 2008 from \$147.8 million for the three months ended September 30, 2007. The decrease in revenue from home sales was primarily due to a 34% decrease in the number of home deliveries to 369 for the three months ended September 30, 2008 from 563 homes delivered for the three months ended September 30, 2007. The average selling price of homes increased 5% to \$275,000 for the three months ended September 30, 2008 from \$262,000 for the three months ended September 30, 2007. Our Texas region has been less affected by the challenging market conditions experienced in other regions. We believe that this is the result of the overall moderate growth rates and price appreciation experienced in Texas in prior periods and the relative health of the Texas economy as compared to other markets in which we sell.

During the three months ended September 30, 2008, we recognized \$1.7 million in impairment charges and no impairment charges during the three months ended September 30, 2007. Gross margin on home sales, excluding impairments, was unchanged at 23% for the three months ended September 30, 2008 and 2007.

For the three months ended September 30, 2008 and 2007, we incurred (losses)/gains of \$(13.5) million and \$0.3 million from land sales, respectively, which included land impairments and abandonment costs of \$13.5 million for the three months ended September 30, 2008.

West: Homebuilding revenues decreased 28% to \$48.4 million for the three months ended September 30, 2008 from \$66.9 million for the three months ended September 30, 2007. The decrease in Homebuilding revenues was due to a 25% decrease in revenues from home sales to \$48.1 million for the three months ended September 30, 2008 from \$63.6 million for the three months ended September 30, 2007, and a decrease in revenue from land sales to \$0.3 million for the three months ended September 30, 2008 from \$3.3 million for the three months ended September 30, 2007. The decrease in revenue from home sales was due to a 13% decrease in the number of home deliveries to 181 for the three months ended September 30, 2008 from 207 homes delivered for the three months ended September 30, 2007, and a 14% decrease in the average selling price of homes to \$266,000 for the three months ended September 30, 2008 from \$308,000 for the three months ended September 30, 2007.

During the three months ended September 30, 2008, we recognized \$3.1 million in impairment charges compared to \$43.2 million for the three months ended September 30, 2007. Gross margin on home sales, excluding impairments, was 8% for the three months ended September 30, 2008, compared to 9% for the three months ended September 30, 2007. This decrease in gross margin was primarily due to the decrease in average selling prices discussed above and an increase in sales incentives, partially offset by the recovery of previously recorded impairments on homes delivered. The average sales incentive per home delivered increased 6% to \$55,600 for the three months ended September 30, 2008 from \$52,400 for the three months ended September 30, 2007.

For the three months ended September 30, 2008 and 2007, we incurred losses of \$5.2 million and \$132.0 million from land sales, respectively, which included land impairments and abandonment costs of \$4.0 million and \$132.8 million, respectively.

Nine Months Ended September 30, 2008 compared to Nine Months Ended September 30, 2007

Florida: Homebuilding revenues decreased 54% to \$309.8 million for the nine months ended September 30, 2008 from \$671.1 million for the nine months ended September 30, 2007. The decrease in Homebuilding revenues was due to a 52% decrease in revenues from home sales to \$306.7 million for the nine months ended September 30, 2008 from \$637.4 million for the nine months ended September 30, 2007 and a decrease in revenue from land sales to \$3.1 million for the nine months ended September 30, 2008 from \$33.7 million for the nine months ended September 30, 2007. The decrease in home sales during the nine months ended September 30, 2008 was the result of a 36% decrease in the number of home deliveries to 1,132 for the nine months ended September 30, 2008 from 1,780 homes delivered for the nine months ended September 30, 2007, and a 24% decrease in the average selling price of homes to \$271,000 for the nine months ended September 30, 2008 from \$358,000 for the nine months ended September 30, 2007.

During the nine months ended September 30, 2008, we recognized \$264.0 million in impairment charges compared to \$44.4 million for the nine months ended September 30, 2007. Gross margin on home sales, excluding impairments, was 11% for the nine months ended September 30, 2008, compared to 21% for the nine months ended September 30, 2007. This decrease in gross margin was primarily due to an increase in sales incentives offered to home buyers coupled with a decline in the base price of the homes delivered, partially offset by the recovery of previously recorded impairments on homes delivered. The average sales incentive per home delivered increased 64% to \$97,800 per home for the nine months ended September 30, 2008, from \$59,600 for the nine months ended September 30, 2007.

For the nine months ended September 30, 2008 and 2007, we incurred a loss of \$44.9 million and \$284.5 million from land sales, respectively, which included land impairments and abandonment costs of \$46.4 million and \$287.3 million, respectively.

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Mid-Atlantic: Homebuilding revenues decreased 75% to \$48.3 million for the nine months ended September 30, 2008 from \$196.1 million for the nine months ended September 30, 2007. The decrease in Homebuilding revenues was due to a 72% decrease in revenues from home sales to \$46.1 million for the nine months ended September 30, 2008 from \$164.5 million for the nine months ended September 30, 2007 and a decrease in revenue from land sales to \$2.2 million for the nine months ended September 30, 2008 from \$31.6 million for the nine months ended September 30, 2007. The decrease in home sales was due to a 68% decrease in the number of home deliveries to 147 homes delivered for the nine months ended September 30, 2008 from 458 homes delivered for the nine months ended September 30, 2007, and a 13% decrease in the average selling price of homes to \$313,000 for the nine months ended September 30, 2008 from \$359,000 for the nine months ended September 30, 2007.

During the nine months ended September 30, 2008, we recognized \$14.6 million in impairment charges compared to \$11.0 million for the nine months ended September 30, 2007. Gross margin on home sales, excluding impairments, was 10% for the nine months ended September 30, 2008, compared to 14% for the nine months ended September 30, 2007. This decrease in gross margin was primarily due to an increase in sales incentives offered to home buyers coupled with a decline in the base price of the homes delivered, partially offset by the recovery of previously recorded impairments on homes delivered. The average sales incentive per home delivered increased 11% to \$30,400 per home for the nine months ended September 30, 2008, from \$27,300 for the nine months ended September 30, 2007.

For the nine months ended September 30, 2008 and 2007, we incurred a loss of \$13.9 million and \$61.0 million, respectively, from land sales, which included land impairments and abandonment costs of \$14.0 million and \$47.8 million, respectively.

Texas: Homebuilding revenues decreased 33% to \$313.8 million for the nine months ended September 30, 2008 from \$469.0 million for the nine months ended September 30, 2007. The decrease in Homebuilding revenues was primarily due to a decrease in revenues from home sales to \$306.7 million for the nine months ended September 30, 2008 from \$461.7 million for the nine months ended September 30, 2007. The decrease in revenue from home sales was primarily due to a 34% decrease in the number of home deliveries to 1,170 for the nine months ended September 30, 2008 from 1,784 homes delivered for the nine months ended September 30, 2007. The average selling price of homes remained relatively unchanged at \$262,000 for the nine months ended September 30, 2008 from \$259,000 for the nine months ended September 30, 2007. Our Texas region has been less affected by the challenging market conditions experienced in other regions. We believe that this is the result of the overall moderate growth rates and price appreciation experienced in Texas in prior periods and the relative health of the Texas economy as compared to other markets in which we sell.

During the nine months ended September 30, 2008, we recognized \$4.8 million in impairment charges compared to \$0.6 million for the nine months ended September 30, 2007. Gross margin on home sales, excluding impairments, was 18% for the nine months ended September 30, 2008, compared to 22% for the nine months ended September 30, 2007. This decrease in gross margin was primarily due to an increase in sales incentives offered to home buyers. The average sales incentive per home delivered increased 62% to \$27,800 per home for the nine months ended September 30, 2008, from \$17,100 for the nine months ended September 30, 2007.

For the nine months ended September 30, 2008 and 2007, we incurred a (loss)/gain of \$(20.2) million and \$0.7 million, respectively, from land sales, which included land impairments and abandonment costs of \$20.3 million and \$0.3 million, respectively.

West: Homebuilding revenues decreased 42% to \$164.5 million for the nine months ended September 30, 2008 from \$283.1 million for the nine months ended September 30, 2007. The decrease in Homebuilding revenues was due to a 44% decrease in revenues from home sales to \$154.9 million for the nine months ended September 30, 2008 from \$278.7 million for the nine months ended September 30, 2007, partially offset by an increase in revenue from land sales to \$9.6 million for the nine months ended September 30, 2008 from \$4.4 million for the nine months ended September 30, 2007. The decrease in revenue from home sales was due to a 30% decrease in the number of home deliveries to 571 for the nine months ended September 30, 2008 from 811 homes delivered for the nine months ended September 30, 2007, and a 21% decrease in the average selling price of homes to \$271,000 for the nine months ended September 30, 2008 from \$344,000 for the nine months ended September 30, 2007.

During the nine months ended September 30, 2008, we recognized \$58.8 million in impairment charges compared to \$56.7 million for the nine months ended September 30, 2007. Gross margin on home sales, excluding impairments, was 4% for the nine months ended September 30, 2008, compared to 12% for the nine months ended September 30, 2007. This decrease in gross margin was primarily due to the decrease in average selling prices discussed above, partially offset by the recovery of previously recorded impairments on homes delivered. The average sales incentive per home delivered decreased slightly to \$56,800 for the nine months ended September 30, 2008 compared to \$57,100 for the nine months ended September 30, 2007 as incentives were factored into a reduction in the base price of the home.

For the nine months ended September 30, 2008, we incurred a loss of \$149.3 million from land sales primarily due to land improvements and the write-offs of deposits and abandonment costs totaling \$151.2 million, as compared to a loss on land sales of \$174.6 million during the nine months ended September 30, 2007, which included \$180.3 million of land impairments and abandonment costs. Land impairment and abandonment charges during the nine months ended September 30, 2008 include an \$85.0 million impairment on a parcel of land as discussed in Note 3 to the unaudited consolidated financial statements.

Seasonality

The homebuilding industry tends to be seasonal, as generally there are more homes sold in the spring and summer months when the weather is milder. Because new home deliveries trail new home contracts by a number of months, we typically have the greatest percentage of home deliveries in the fall and winter, and slow sales in the spring and summer months could negatively affect our full year results. We operate primarily in the Southwest and Southeast, where weather conditions are more suitable to a year-round construction process than in other parts of the country. Our operations in Florida and Texas are at risk of repeated and potentially prolonged disruptions during the Atlantic hurricane season, which lasts from September 1 until November 30.

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FINANCIAL CONDITION, LIQUIDITY AND CAPITAL RESOURCES

Sources and Uses of Cash

Our Homebuilding operations primary uses of cash have been for land acquisitions, construction and development expenditures, joint venture investments and SG&A expenditures. Our sources of cash to finance these uses have been primarily cash generated from operations and cash from our financing activities.

Our Financial Services operations primarily used cash to fund mortgages, prior to their sale, and SG&A expenditures. We relied primarily on internally generated funds, which included the proceeds generated from the sale of mortgages, and the mortgage operations warehouse lines of credit to fund these operations.

Our income before non-cash charges generally is our most significant source of operating cash flow.

At September 30, 2008, our homebuilding operations had unrestricted cash and cash equivalents of \$277.5 million as compared to \$67.2 million at December 31, 2007.

We are operating our businesses as debtors-in-possession under the jurisdiction of the Bankruptcy Court and in accordance with the applicable provisions of the Bankruptcy Code and orders of the Bankruptcy Court. As a result, we are subject to the risks and uncertainties associated with our Chapter 11 cases which include, among other things:

the availability of and our ability to operate subject to the terms of the cash collateral order and related budget;

limitations on our ability to implement and execute our business plans and strategy;

our ability to obtain and maintain normal terms with existing and potential homebuyers, vendors and service providers and maintain contracts and leases that are critical to our operations;

our ability to obtain needed approval from the Bankruptcy Court for transactions outside of the ordinary course of business, which may limit our ability to respond on a timely basis to certain events or take advantage of certain opportunities;

limitations on our ability to obtain Bankruptcy Court approval with respect to motions in the Chapter 11 cases that we may seek from time to time or potentially adverse decisions by the Bankruptcy Court with respect to such motions, including as a result of the actions of our creditors and other third parties, who may oppose our requested relief or who may seek to require us to take actions that we oppose;

limitations on our ability to reject contracts or leases that are burdensome or uneconomical;

limitations on our ability to raise capital, including through sales of assets; and

our ability to motivate and retain key and essential personnel is impacted by the Bankruptcy Code which limits our ability to implement a retention program or take other measures intended to motivate employees to remain with us.

These risks and uncertainties could negatively affect our business and operations in various ways. For example, events or publicity associated with our Chapter 11 cases could adversely affect our relationships with existing and potential homebuyers, vendors and employees, which in turn could adversely affect our operations and financial condition, particularly if such proceedings are protracted.

As a result of our Chapter 11 cases and the other matters described herein, including the uncertainties related to the fact that our filed plan of reorganization has not been confirmed, there is substantial doubt about our ability to continue as a going concern.

As a result of severe market conditions and our liquidity constraints, during the nine months ended September 30, 2008, we abandoned our rights under certain option agreements which resulted in an approximately 8,800 unit decline in our optioned homesites. Abandonment decisions were made following in depth community by community analyses of all option contracts based on projected returns, amount and timing of incremental cash flow, and owned homesites. As a result of abandoning our rights under option contracts, as of September 30, 2008, we accrued \$3.5 million for

letters of credit which we anticipated would be drawn due to nonperformance under such contracts. From October 1, 2008 through April 30, 2009, an additional \$0.8 million of letters of credit have been drawn related to the abandonment of option contracts which have increased our borrowings outstanding under our Revolving Loan Facility. In certain instances, we have entered into development agreements in connection with option contracts which require us to complete the development of the land, at a fixed reimbursable amount, even if we choose not to exercise our option and forfeit our deposit and even if our costs exceed the reimbursable amount. We recorded net recoveries of \$0.6 million for the three months ended September 30, 2008 and net losses of \$3.4 million for the nine months ended September 30, 2008 for our estimated obligations under these development agreements, which is included in inventory impairments and abandonment costs in the accompanying unaudited consolidated statement of operations. Through the first quarter of 2009, we have continued to reduce inventory in an attempt to further align our inventory levels to housing demand in those markets we serve, reduce our cost of sales relating to construction and labor costs for the homes we build and reduce our selling, general and administrative costs to levels consistent with fewer home deliveries to operate within our liquidity constraints. These or future actions may not be sufficient to allow us to continue our operations.

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Our unaudited consolidated financial statements are presented on a going concern basis, which contemplates the realization of assets and satisfaction of liabilities in the normal course of business. We have \$1.8 billion in borrowings and have experienced significant operating losses. For the nine months ended September 30, 2008, we incurred a loss from continuing operations, net of taxes, of \$794.0 million and had stockholders' deficit of \$1.3 billion. There is substantial doubt about our ability to continue as a going concern. Our ability to continue as a going concern and emerge successfully from our Chapter 11 cases will depend upon our development and consummation of a plan of reorganization. The accompanying unaudited consolidated financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets.

For the nine months ended September 30, 2008, cash provided by/(used in) operating activities was \$292.8 million, as compared to \$(88.6) million during the nine months ended September 30, 2007. The improvement in the use of cash by our operating activities is primarily a result of a decrease in our inventory and other assets. The decrease in other assets is primarily due to a \$207.3 million refund of previously paid income taxes. In addition to this refund, during the nine months ended September 2008, we have received refunds of overpayments of federal estimated tax payments totaling \$12.0 million.

Cash used in investing activities was \$0.8 million during the nine months ended September 30, 2008, as compared to \$33.9 million during the nine months ended September 30, 2007. The decrease in cash used in investing activities is primarily due to the reduction in the investments in our unconsolidated joint ventures during the nine months ended September 30, 2008 of \$1.6 million compared to \$29.2 million for the nine months ended September 30, 2007.

Financing Activities

Our consolidated borrowings at September 30, 2008 were \$1.8 billion (see Note 9 to the unaudited consolidated financial statements).

The filing of the Chapter 11 cases triggered repayment obligations under a number of instruments and agreements relating to our direct and indirect financial obligations. As a result, all our borrowings became automatically and immediately due and payable. We believe that any efforts to enforce the payment obligations are stayed as a result of the filing of the Chapter 11 cases.

On February 5, 2008, pursuant to an interim order from the Bankruptcy Court dated January 31, 2008, we entered into a Senior Secured Super-Priority Debtor in Possession Credit and Security Agreement. The agreement provided for a first priority and priming secured revolving credit interim commitment of up to \$134.6 million. The agreement was subsequently amended to extend it to September 19, 2008. No funds were drawn under the agreement.

The agreement was subsequently terminated and we entered into an agreement with our prepetition secured lenders to use cash collateral on hand (cash generated by our operations, including the sale of excess inventory and the proceeds of our federal tax refund of \$207.3 million received in April 2008). We are authorized by the Bankruptcy Court to use cash collateral of our first lien and second lien lenders in a manner consistent with a budget negotiated by the parties. The order further provided for the pay-down of \$175.0 million to our first lien term secured lenders, subject to disgorgement provisions in the event that certain claims against the lenders are successful and repayment is required. We also have the right to pay-down an additional \$15.0 million to our first lien secured lenders. As of May 1, 2009, we had paid-down \$148.4 million to the first lien secured lenders. We may incur liens and enter into sale/leaseback transactions for model homes subject to certain limitations. We have granted the pre-petition agents and the lenders various forms of protection, including liens and claims to protect against any diminution of the collateral value, payment of accrued, but unpaid interest on the first priority indebtedness at the non-default rate and the payment of reasonable fees and expenses of the agents under our secured facilities.

Our right to the use of cash collateral has been extended until July 31, 2009 on terms substantially similar to those in the original cash collateral order. If we fail to comply with the order, we will not have sufficient cash to enable us to operate our business and effectuate our restructuring.

Revolving Loan Facility and First and Second Lien Term Loan Facilities

To effect the TE Acquisition, on July 31, 2007, we entered into (1) the \$200.0 million aggregate principal amount first lien term loan facility (the *First Lien Term Loan Facility*) and (2) the \$300.0 million aggregate principal amount second lien term loan facility (the *Second Lien Term Loan Facility*), (First and Second Lien Term Loan Facilities taken together, the *Facilities*). At September 30, 2008 and December 31, 2007, we had \$223.1 million and \$168.5

million, respectively, outstanding under our revolving loan facility (the Revolving Loan Facility). There is no additional capacity available under the Revolving Loan Facility other than for letters of credit presented to the bank. The Revolving Loan Facility expires on March 9, 2010. The First Lien Term Loan Facility expires on July 31, 2012 and the Second Lien Term Loan Facility expires on July 31, 2013. At September 30, 2008, the Revolving Loan Facility and the Facilities are classified as liabilities subject to compromise (see Note 2 to the unaudited consolidated financial statements).

The interest rates on the Facilities and the Revolving Loan Facility are based on LIBOR plus a margin or an alternate base rate plus a margin, at our option. For the Revolving Loan Facility, the LIBOR rates are increased by between 2.50% and 5.25% depending on our leverage ratio (as defined in the Agreement) and credit ratings. Loans bearing interest at the base rate (the rate announced by Citibank as its base rate or 0.50% above the Federal Funds Rate) increase between 1.00% and 4.25% in accordance with the same criteria. Based on our current leverage ratio and credit ratings, our LIBOR loans bear interest at LIBOR plus 5.25% and our base rate loans bear interest at the Federal Funds Rate plus 4.25%. For the First Lien Term Loan Facility, the interest rate is LIBOR plus 5.00% or base rate plus 4.00%. For the Second Lien Term Loan Facility, the interest rate is LIBOR plus 7.25% or base rate plus 6.25%. The Second Lien Term Loan Facility allows us to pay interest, at our option, (i) in cash, (ii) entirely by increasing the principal amount of the Second Lien Term Loan Facility, or (iii) a combination thereof. The Facilities and the Revolving Loan Facility are guaranteed by substantially all of our domestic subsidiaries. The obligations are secured by substantially all of our assets, including those of our subsidiaries other than our mortgage and title subsidiaries.

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In connection with the issuance of the \$250.0 million 8 1 / 4% senior notes, we filed within 90 days of the issuance a registration statement with the SEC covering a registered offer to exchange the notes for exchange notes of ours having terms substantially identical in all material respects to the notes. The registration statement was not declared effective within the required 180 days of issuance and was withdrawn in 2008. As a result, on October 9, 2006, in accordance with their terms, the notes became subject to special interest which accrues at a rate of 0.25% per annum during the 90-day period immediately following the occurrence of such default, and increases by 0.25% per annum at the end of each 90-day period, up to a maximum of 1.0% per annum. In accordance with SOP 90-7, as of January 29, 2008, the petition date, we ceased accruing special interest and reversed \$2.3 million of the interest expense that had been previously accrued as these are unsecured claims and not entitled to interest upon filing petitions for relief under Chapter 11.

Our outstanding senior notes are guaranteed, on a joint and several basis, by the Guarantor Subsidiaries, which are all of our material domestic subsidiaries, other than our mortgage and title subsidiaries (the Non-Guarantor Subsidiaries). Our outstanding senior subordinated notes are guaranteed on a senior subordinated basis by all of the Guarantor Subsidiaries. The senior notes rank *pari passu* in right of payment with all of our existing and future unsecured senior debt and senior in right of payment to our senior subordinated notes and any future subordinated debt. The senior subordinated notes rank *pari passu* in right of payment with all of our existing and future unsecured senior subordinated debt. The indentures governing the senior notes and senior subordinated notes generally require us to maintain a minimum consolidated net worth and place certain restrictions on our ability, among other things, to incur additional debt, pay or declare dividends or other restricted payments, sell assets, enter into transactions with affiliates, invest in joint ventures above specified amounts and merge or consolidate with other entities. Interest on our outstanding senior notes and senior subordinated notes is payable semi-annually. In accordance with SOP 90-7, as of January 29, 2008, the petition date, we ceased accruing interest on the senior notes and the senior subordinated notes as these are unsecured claims and are not entitled to interest upon filing petitions for relief under Chapter 11. At September 30, 2008, the senior notes and senior subordinated notes are classified as liabilities subject to compromise (see Note 2 to the unaudited consolidated financial statements).

Senior Subordinated PIK Notes

As part of the transactions to settle the disputes regarding the Transeastern JV, on July 31, 2007, the senior mezzanine lenders to the Transeastern JV received \$20.0 million in aggregate principal amount of 14.75% Senior Subordinated PIK Election Notes (PIK Notes) due 2015.

Interest on the PIK Notes is payable semi-annually. The PIK Notes are unsecured senior subordinated obligations of ours, and are guaranteed on an unsecured senior subordinated basis by each of our existing and future subsidiaries that guarantee our 7.5% Senior Subordinated Notes due 2015 (the Existing Notes). We are required to pay 1% of the interest in cash and the remaining 13.75%, at our option, (i) in cash, (ii) entirely by increasing the principal amount of the PIK Notes or issuing new notes, or (iii) a combination thereof. The PIK Notes mature on July 1, 2015. The indenture governing the PIK Notes contains the same covenants as contained in the indenture governing the Existing Notes and is subject, in most cases, to any change to such covenants made to the indenture governing the Existing Notes. The PIK Notes are redeemable by us at redemption prices greater than their principal amount. The PIK Notes contain an optional redemption feature that allows us to redeem up to a maximum of 35% of the aggregate principal amount of the PIK Notes using the proceeds of subsequent sales of its equity interest at 114.75% of the aggregate principal amount of the PIK Notes then outstanding, plus accrued and unpaid interest. Additionally, after July 1, 2012, subject to certain terms of our other debt agreements, we may redeem the PIK Notes at a premium to the principal amount as follows: 2012 107.375%; 2013 103.688%; 2014 and thereafter 100.000%. The call options exercisable at anytime after July 1, 2012 at a premium do not require bifurcation under SFAS 133 because they are only exercisable by us and they are not contingently exercisable. The redemption option is conditionally exercisable based on the proceeds raised from an equity offering at 114.75% of up to 35% of the aggregate outstanding PIK Notes principal and represents an embedded call option that must be bifurcated from the PIK Notes; however, the fair value of this call option is not material and has not been bifurcated from the host instrument.

The PIK Notes provide for registration rights for the holders whereby the interest rate increases by 0.25% per annum for the first 90 days of a registration default, as defined, which amount increases by an additional 0.25% every 90 days a registration default is continuing, not to exceed 1.0% in the aggregate, from and including the date of the registration default to and excluding the date on which the registration default is cured. Registration default payments may be paid, at our option, in cash, additional PIK Notes, or a combination thereof. For the three months ended September 30, 2008, we have not incurred additional interest expense as a result of such default.

At September 30, 2008, the PIK Notes are classified as liabilities subject to compromise (see Note 2 to the unaudited consolidated financial statements).

Financial Services Borrowings

On January 28, 2008, Preferred Home Mortgage Company, our wholly-owned residential mortgage lending subsidiary, entered into an Amended and Restated Agreement of Limited Liability Company with Wells Fargo Ventures, LLC. The limited liability company is known as PHMCWF, LLC but does business as Preferred Home Mortgage Company, an affiliate of Wells Fargo. Preferred Home Mortgage Company owns 49.9% of the venture with the balance owned by Wells Fargo. Effective April 1, 2008, the venture began to carry on the mortgage business of Preferred Home Mortgage Company. The venture is managed by a committee composed of six members, three from Preferred Home Mortgage Company and three from Wells Fargo. The venture entered into a revolving credit agreement with Wells Fargo Bank, N.A. providing for advances of up to \$20.0 million. Effective April 1, 2008, we began to account for the venture as an equity-method investment.

Until December 4, 2008, the subsidiary had two warehouse lines of credit in place to fund the origination of residential mortgage loans. The revolving warehouse line of credit (the Warehouse Line of Credit), which was entered into on December 5, 2007, provided for revolving loans of up to \$25.0 million. The Warehouse Line of Credit replaced the \$100.0 million revolving warehouse line of credit that expired on December 8, 2007. From January 25, 2008 through December 4, 2008, the availability under the Warehouse Line of Credit was reduced to \$15.0 million. The \$150.0 million mortgage loan purchase facility (Purchase Facility) was amended to decrease the size of the

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facility to \$75.0 million. From January 25, 2008 through December 4, 2008, the availability under the Purchase Facility was reduced to \$40.0 million. However, we had agreed with the lender not to utilize these facilities. The Warehouse Line of Credit bore interest at the 30-day LIBOR rate plus a margin of 2.0%, was secured by funded mortgages, which were pledged as collateral, and required our mortgage subsidiary to maintain certain financial ratios and minimums. The Warehouse Line of Credit also placed certain restrictions on, among other things, our mortgage subsidiary's ability to incur additional debt, create liens, pay or make dividends or other distributions, make equity investments, enter into transactions with affiliates, and merge or consolidate with other entities. Our mortgage subsidiary was in compliance with all covenants and restrictions at September 30, 2008. At September 30, 2008, our mortgage subsidiary had no outstanding borrowings.

Liquidity Needs

We continue to have substantial liquidity needs in the operation of our business and face liquidity challenges. Our business depends upon our ability to obtain financing for the development of our residential communities and to provide bonds to ensure the completion of our projects. We expect to have sufficient resources and borrowing capacity to meet all of our commitments throughout the projected term of our Chapter 11 cases as a result of an agreement we entered in September 2008 with our secured lenders to use cash collateral on hand (cash generated by our operations, including the sale of excess inventory and the proceeds of our federal tax refund of \$207.3 million received in April 2008). Pursuant to a Bankruptcy Court order dated September 20, 2008, we are authorized by the Bankruptcy Court to use cash collateral of our first lien and second lien lenders (approximately \$358.0 million at the time of the order) in a manner consistent with a budget negotiated by the parties. The order further provided for the pay-down of \$175.0 million of the \$358.0 million to our first lien term secured lenders, subject to disgorgement provisions in the event that certain claims against the lenders are successful and repayment is required. The order also reserves our sole right to pay-down an additional \$15.0 million to our first lien secured lenders. As of May 1, 2009, we had paid-down \$148.4 million to the first lien secured lenders. We are permitted under the order to incur liens and enter into sale/leaseback transactions for model homes subject to certain limitations. As part of the order, we have granted the pre-petition agents and the lenders various forms of protection, including liens and claims to protect against any diminution of the collateral value, payment of accrued, but unpaid interest on the first priority indebtedness at the non-default rate and the payment of reasonable fees and expenses of the agents under our secured facilities.

Our right to the use of cash collateral has been extended until July 31, 2009 on terms substantially similar to those in the original cash collateral order. If we fail to comply with the order, we will not have sufficient cash to enable us to operate our business and effectuate our restructuring.

The Bankruptcy Court established May 19, 2008 as the bar date for filing proofs of claim against the Debtors relating to obligations arising before January 29, 2008. As of April 28, 2009, approximately 4,400 claims have been filed against us totaling approximately \$7.3 billion in asserted liabilities. These claims are comprised of approximately \$5.0 billion in administrative claims, \$219.0 million in secured claims, \$75.0 million in priority claims and \$7.0 billion in unsecured claims. There are many claims (at least 700) that have been asserted in unliquidated amounts or that contain an unliquidated component. Notably, among the unliquidated claims are the claims of our secured first and second lien lenders. In addition, the indenture trustees under our approximately \$1.1 billion of unsecured debentures each filed an unliquidated claim with respect to such obligations.

On April 17, 2009, we filed with the Bankruptcy Court our First Amended Joint Plan of TOUSA, Inc. and its Affiliated Debtors and Debtors in Possession under Chapter 11 of the Bankruptcy Code (as modified or revised, the Plan) and Disclosure Statement pursuant to Section 1125 of the Bankruptcy Code relating to the Plan (as modified or revised, the Disclosure Statement). Copies of the Plan and Disclosure Statement, as filed with the Bankruptcy Court, are available at <http://www.tousa.com/reorg>. Currently, no hearing has been scheduled for the Plan or Disclosure Statement. We have the exclusive right to file a plan until July 29, 2009 and the exclusive right to solicit acceptance thereof until September 27, 2009. Pursuant to Section 1121 of the Bankruptcy Code, the exclusivity periods may be expanded or reduced by the Bankruptcy Court, but in no event can the exclusivity periods to file and solicit acceptance of a plan or plans of reorganization be extended beyond September 29, 2009.

Off Balance Sheet Arrangements*Land and Homesite Option Contracts*

In the ordinary course of business, we enter into option contracts to purchase homesites and land held for development. At September 30, 2008 and December 31, 2007, we had non-refundable cash deposits totaling \$7.7 million and \$56.9 million, respectively, included in inventory in the accompanying unaudited consolidated statements of financial condition. Under these option contracts, we have the right to buy homesites at predetermined prices on a predetermined takedown schedule. Option contracts generally require the payment of a cash deposit and/or the posting of a letter of credit, which is typically less than 20% of the underlying purchase price, and may require monthly maintenance payments. These option contracts are either with land sellers or third party financial entities which have acquired the land to

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enter into the option contract with us. Homesite option contracts are generally non-recourse, thereby limiting our financial exposure for non-performance to our cash deposits and/or letters of credit. In certain instances, we have entered into development agreements in connection with option contracts, which require us to complete the development of the land, at a fixed reimbursable amount, even if we choose not to exercise our option and forfeit our deposit and even if our costs exceed the reimbursable amount. We have abandoned our rights under certain option contracts that require us to complete the development of land for a fixed reimbursable amount. We recorded net recoveries of \$0.6 million for the three months ended September 30, 2008 and net losses of \$3.4 million for the nine months ended September 30, 2008 for our estimated obligations under these development agreements, which is included in inventory impairments and abandonment costs in the accompanying unaudited consolidated statement of operations. At September 30, 2008 and December 31, 2007, \$13.7 million and \$10.3 million are included in liabilities subject to compromise and accounts payable and other liabilities, respectively, in the accompanying unaudited consolidated statements of financial condition related to these development agreements.

Certain of our option contracts give the other party the right to require us to purchase homesites or guarantee certain minimum returns. We have abandoned our rights under certain of these option contracts and we have not complied with the notices given to us. These option contracts were previously recorded as financing transactions under SFAS 66 and the inventory was included in inventory not owned and the corresponding liability was included in obligations for inventory not owned. Since we defaulted under or terminated these contracts, we are no longer accounting for these contracts as financing transactions. During the three and nine months ended September 30, 2008, we recorded losses of \$5.0 million and \$14.5 million, respectively, in connection with the abandonment of these option contracts, for our estimated obligations, which is included in inventory impairments and abandonment costs in the accompanying unaudited consolidated statements of operations. These amounts were computed based on the estimated deficiency between the fair value of the underlying inventory compared to our required purchase price under the option contract. The total required purchase price under these option contracts at September 30, 2008 and December 31, 2007 was \$36.3 million and \$25.0 million, respectively. At September 30, 2008 and December 31, 2007, \$24.0 million and \$9.5 million is included in liabilities subject to compromise and accounts payable and other liabilities, respectively, in the accompanying unaudited consolidated statements of financial condition.

We are subject to the normal obligations associated with entering into contracts for the purchase, development and sale of real estate in the routine conduct of our business. We are committed under various letters of credit and performance bonds which are required for certain development activities, deposits on land and deposits on homesite purchase contracts. Under these arrangements, we had total outstanding letters of credit of \$19.1 million as of September 30, 2008. As a result of abandoning our rights under option contracts, as of September 30, 2008, we accrued \$3.5 million for letters of credit which we anticipated would be drawn due to nonperformance under such contracts. From October 1, 2008 through April 30, 2009, an additional \$0.8 million of letters of credit have been drawn related to the abandonment of option contracts which have increased our borrowings outstanding under our Revolving Loan Facility. As discussed, in certain instances, we have entered into development agreements in connection with option contracts which require us to complete the development of the land, at a fixed reimbursable amount, even if we choose not to exercise our option and forfeit our deposit and even if our costs exceed the reimbursable amount.

At September 30, 2008, we have total outstanding performance / surety bonds of \$140.6 million related to land development activities and have estimated our exposure on our outstanding surety bonds to be \$54.5 million based on land development remaining to be completed. At September 30, 2008 and December 31, 2007, our accrual totaled \$41.8 million and \$48.0 million, respectively, for surety bonds where we consider it probable that the surety has a claim for reimbursement for amounts drawn related to defaulted agreements, which is included as a liability subject to compromise and accounts payable and other liabilities, respectively, in the accompanying unaudited consolidated statements of financial condition.

Until the establishment of a surety bond program in January 2009, we had no ability to obtain new surety bonds or letters of credit and in some cases, had to post cash deposits with government entities or escrow agents. Under the program approved by the Bankruptcy Court, we have an aggregate \$15.0 million available for surety bonds. Surety bonds are issued after notice to creditors who have a right to object. The surety bonds are collateralized by cash

deposits maintained in escrow accounts. At April 30, 2009, \$2.5 million was maintained as collateral for surety bonds.
Investments in Unconsolidated Joint Ventures

We have entered into strategic joint ventures that acquire and develop land for our Homebuilding operations and/or that also build and market homes for sale to third parties. Our partners in these joint ventures generally are unrelated homebuilders, land sellers, financial investors or other real estate entities. In some cases our Chapter 11 filings have constituted an event of default under the joint venture lender agreements which have resulted in the debt becoming immediately due and payable, limiting the joint ventures' access to future capital. In joint ventures where the assets are being financed with debt, the borrowings are non-recourse to us except that in certain instances we have agreed to complete certain property development commitments in the event the joint ventures default and to indemnify the lenders for losses resulting from fraud, misappropriation, violations of environmental laws and similar acts. In some cases, we have agreed to make capital contributions to the joint venture sufficient to comply with a specified debt to value ratio. Our obligations become full recourse upon certain bankruptcy events with respect to the joint venture. At September 30, 2008 and December 31, 2007, we had investments in unconsolidated joint ventures of \$3.0 million and \$9.0 million, respectively. We account for these investments under the equity method of accounting. These unconsolidated joint ventures are limited liability companies or limited partnerships in which we have a limited partnership interest and a minority interest in the general partner. At December 31, 2007, we had receivables of \$0.3 million, net of allowances from these joint ventures due to loans and advances, unpaid management fees and other items. At September 30, 2008, we had no receivables from joint ventures.

In certain instances, we were appointed as the day-to-day manager of the unconsolidated entities and received management fees for performing this function. We earned management fees from these unconsolidated entities of \$0 and \$0.8 million for the three months ended September 30, 2008 and 2007, respectively, and \$0.1 million and \$9.0 million for the nine months ended September 30, 2008 and 2007, respectively. These fees are included in income (loss) from unconsolidated joint ventures in the accompanying unaudited consolidated statements of operations.

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We evaluated the recoverability of our investments in and receivables from unconsolidated joint ventures under APB 18 and SFAS No. 114, *Accounting by Creditors for Impairment of a Loan* (SFAS 114), and recorded total impairments of investments in unconsolidated joint ventures of \$5.8 million and \$23.4 million for the three months ended September 30, 2008 and 2007, respectively, and \$8.6 million and \$28.9 million for the nine months ended September 30, 2008 and 2007, respectively. Additionally, during the three months ended September 30, 2008, we recorded \$5.3 million of impairments on joint venture receivables (net of a \$2.2 million recovery related to a previously written-off joint venture receivable). At September 30, 2008 and December 31, 2007, the accrual related to joint venture obligations was \$47.7 million and \$74.6 million, respectively, which primarily relates to limited guarantees we issued in connection with our unconsolidated joint ventures. As explained in further detail below, the decrease in the accrual is primarily due to the reduction of loss accruals for certain joint venture obligations totaling \$26.9 million established in 2007 and reversed during the nine months ended September 30, 2008.

Engle/Sunbelt Joint Venture

In December 2004, we entered into a joint venture agreement with Suntous Investors, LLC (Suntous) to form Engle/Sunbelt Holdings, LLC (Engle/Sunbelt). Engle/Sunbelt was formed to develop finished homesites and to build and deliver homes in the Phoenix, Arizona market. Upon its inception, the venture acquired eight of our existing communities in Phoenix, Arizona.

At December 31, 2007, the joint venture had financing arrangements with an aggregate borrowing capacity of \$230.0 million, of which \$200.0 million related to a revolving loan and \$30.0 million related to a mezzanine financing instrument. On January 16, 2008, the facility was amended to reduce the revolving loan limit to \$115.0 million and terminate the mezzanine financing instrument. While the borrowings by Engle/Sunbelt were non-recourse to us, we had obligations to complete construction of certain improvements and housing units in the event Engle/Sunbelt defaulted. Additionally, we agreed to indemnify the lenders for, among other things, potential losses resulting from violations of environmental laws, misappropriation, bankruptcy filings and similar acts by Engle/Sunbelt.

Although Engle/Sunbelt was not included in our Chapter 11 filings, our Chapter 11 filings constituted an event of default under the financing arrangements and Engle/Sunbelt's debt became immediately due and payable.

During 2007, we evaluated the recoverability of our investment in and receivables from Engle/Sunbelt for impairment under APB 18 and SFAS 114, respectively, and recorded an impairment charge of \$60.7 million, representing the full carrying value our investment in and receivables from Engle/Sunbelt, net of deferred gains of \$22.5 million.

In April 2008, we entered into a settlement agreement with the lenders pursuant to which Engle/Sunbelt agreed to the appointment of a receiver and further agreed to either, at the election of the lenders, deliver a deed in lieu of foreclosure to its assets or consent to a judicial foreclosure. We also agreed to assist the lenders in their efforts to complete certain construction for which we would receive arm's length compensation. The Bankruptcy Court entered an order approving the settlement agreement. Pursuant to the settlement agreement, on November 20, 2008, we were relieved from our obligations under the completion and indemnity agreements.

TOUSA/Kolter Joint Venture

In January 2005, we entered into a joint venture with Kolter Real Estate Group LLC to form TOUSA/Kolter Holdings, LLC (TOUSA/Kolter) for the purpose of acquiring, developing and selling approximately 1,900 homesites and commercial property in a master planned community in South Florida. The joint venture obtained senior and senior subordinated term loans. We entered into a Performance and Completion Agreement in favor of the lenders under which we agreed, among other things, to construct and complete the horizontal development of the lots and commercial property and related infrastructure in accordance with certain plans. The loans required, among other things, TOUSA/Kolter to have completed the development of certain lots by January 7, 2007. Due to unforeseen and unanticipated delays in the entitlement process and additional development requests by the county and water management district, TOUSA/Kolter was unable to complete the development of these certain lots by the required deadline. On September 21, 2007, and in response to missing the development deadline, TOUSA/Kolter amended the existing loan agreements and we amended the Performance and Completion Agreement to extend the Performance and Completion Agreement development deadline to May 31, 2008. The amendments to the term loan agreements increased the interest rate on the senior term loan by 100 basis points to LIBOR plus 3.25% and by 50 basis points to

LIBOR plus 8.5% for the senior subordinated term loan. As a condition to the amendment, we agreed with Kolter Real Estate Group LLC to be responsible for the additional 150 basis points; accordingly, this would be a cost of the lots we acquired from TOUSA/Kolter. The amendment also required us to increase our existing letter of credit by an additional \$1.8 million to \$12.1 million and place an additional \$3.0 million cash deposit on the remaining lots under option. The \$3.0 million was used by TOUSA/Kolter to pay down a portion of the senior term loan.

As we had abandoned our rights under the option contract due to non-performance, we recorded an obligation of \$12.1 million for the letter of credit we anticipated would be drawn, wrote-off the \$3.0 million cash deposit and \$1.0 million in capitalized pre-acquisition costs in 2007. In 2008, the letter of credit was drawn and used to reduce the joint venture's term loan outstanding.

The lenders to the joint venture declared the loan to the venture to be in default. The Remargining Agreement required us to pay to the Administrative Agent, upon default of the joint venture, an amount necessary to decrease the principal balance of the loan so that the outstanding balance did not exceed 70% of the value of the joint venture's assets. Based on the estimated fair value of the assets of the joint venture, we recorded a \$54.0 million obligation (which included the \$12.1 million letter of credit accrual) in 2007 in connection with our obligation under the re-margining provisions of the loan agreement. We did not record any additional contingent liability under the completion guarantee as the \$54.0 million accrual represented the full debt obligation of the joint venture. At December 31, 2007, the obligation of \$54.0 million is included in accounts payable and other liabilities in the accompanying unaudited consolidated statements of financial condition. As a result of the 2009 transaction discussed below, we reduced the obligation for \$8.5 million of loan forgiveness, \$11.7 million of drawn letters of credit and \$2.3 million of escrowed interest applied to the loan balance, leaving a remaining obligation at September 30, 2008 of \$31.5 million, which is included in liabilities subject to compromise in the accompanying unaudited consolidated statement of financial condition.

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During 2007, we evaluated the recoverability of our investment and receivables from TOUSA/Kolter for impairment under APB 18 and SFAS 114, respectively, and recorded an impairment charge of \$58.8 million representing the full carrying value of our investment in and receivables from TOUSA/Kolter, net of deferred gains of \$12.8 million, which were deferred as a result of the contributed assets and contract assignments to TOUSA/Kolter. Additionally, in 2007 we recorded an obligation of \$18.9 million for performance bonds and letters of credit that we placed on behalf of the joint venture, as we considered it probable that we would be required to reimburse these amounts for development remaining to be completed. At September 30, 2008 and December 31, 2007, the obligation for performance bonds and letters of credit of \$13.7 million and \$18.9 million, respectively, is included in liabilities subject to compromise and accounts payable and other liabilities, respectively, in the accompanying unaudited consolidated statements of financial condition.

On January 28, 2009, we entered into an agreement with CC Loan Acquisition LLC, which had purchased the loans to the joint venture and the Community Development District Bonds related to the project. The joint venture deeded the property to CC Loan Acquisition LLC and received an extension of the maturity of the B Bonds until May 1, 2013. A portion of the outstanding joint venture indebtedness was also satisfied and the amount collectible from CC Loan Acquisition LLC under filed proofs of claim related to the Completion Agreement was limited. This agreement was approved by the Bankruptcy Court on January 9, 2009.

Centex/TOUSA at Wellington, LLC

In December 2005, we entered into a joint venture with Centex Corporation to form Centex/TOUSA at Wellington, LLC (Centex/TOUSA at Wellington) for the purpose of acquiring, developing and selling approximately 264 homesites in a community in South Florida. The joint venture obtained a term loan of which \$31.0 million was outstanding as of September 30, 2008 and December 31, 2007. The credit agreement requires us to construct and complete the horizontal development of the lots and related infrastructure in accordance with certain agreed upon plans. On August 31, 2007, Centex/TOUSA at Wellington received a notice from the lender requiring the joint venture members to contribute approximately \$10.0 million to the joint venture to reduce the outstanding term loan in order to comply with the 60% loan-to-value ratio covenant. We have not made the required equity contribution.

We evaluated the recoverability of our investment in and receivables from Centex/TOUSA at Wellington for impairment under APB 18 and SFAS 114 respectively, and recorded an impairment of \$27.0 million representing the full carrying value of our investment in and receivables from Centex/TOUSA at Wellington during 2007. Based on the estimated fair value of the assets of the joint venture, we recorded a \$15.5 million liability in 2007, in connection with our obligation under the re-margining provisions of the loan agreement which represents our portion of the joint venture's outstanding debt. We did not record any additional contingent liability under the completion guarantee as the \$15.5 million accrual represents our portion of the full joint venture debt obligation. At September 30, 2008 and December 31, 2007, the \$15.5 million obligation is included in liabilities subject to compromise and accounts payable and other liabilities, respectively, in the accompanying unaudited consolidated statements of financial condition.

We have entered into an agreement with our joint venture partner pursuant to which we will surrender our interest in the joint venture, be relieved from any liability owed to the venture or under the guarantees and convey our ownership interest in 44 lots to the venture for \$1.1 million, less applicable real estate taxes. The agreement is subject to Bankruptcy Court approval.

Layton Lakes Joint Venture

In connection with our joint venture with Lennar Corporation (the Layton Lakes Joint Venture) to acquire and develop land, townhome properties and commercial property in Gilbert, Arizona, we entered into a Completion and Limited Indemnity Agreement for the benefit of the lender to the joint venture.

We evaluated the recoverability of our investment in and receivables from the Layton Lakes Joint Venture for impairment under APB 18 and SFAS 114, respectively, and recorded an impairment charge of \$24.9 million representing the full carrying value of our investment in and receivables from the Layton Lakes Joint Venture during 2007. At that time, we did not record any obligation under the re-margining provision as we were not a party to the re-margining agreement. The remargining agreement required that the outstanding loan balance not exceed 65% of the value of the joint venture's assets. Additionally, in 2007 we recorded an obligation of \$4.4 million for performance bonds that we placed on behalf of the joint venture, as we considered it probable that we would be required to

reimburse these amounts for development remaining to be completed. We did not record any additional contingent liability under the completion guarantee as based on the estimated fair value of the assets of the joint venture; we did not believe that it was probable that we would be called to perform under the completion obligation.

The joint venture also breached various other loan covenants. As a result of our defaults, including our failure to maintain a required net worth, we did not have the right to take down lots or vote as a member of the joint venture.

Tousa, Tousa Homes, Inc., Lennar and the Town of Gilbert, Arizona entered into a series of agreements pursuant to which, among other things, we surrendered our interest in the joint venture and paid \$1.3 million toward completion of certain offsite improvements. In exchange, we were granted an option to continue acquiring lots and the Town of Gilbert agreed to issue certificates of occupancy for certain homes under construction. Tousa, Tousa Homes, Inc., Lennar and Bank Midwest each agreed to mutual releases of claims related to the Layton Lakes Joint Venture. The Bankruptcy Court approved these agreements on November 25, 2008. As a result of this settlement and certain work performed by our joint venture partner, we reversed \$4.4 million of our accrual for estimated obligations under the performance bonds during the nine months ended September 30, 2008.

Other

Certain of our other ongoing unconsolidated land development joint ventures have outstanding debt obligations totaling \$12.4 million and \$20.6 million at September 30, 2008 and December 31, 2007, respectively. These joint venture borrowings are non-recourse to us except that in certain instances we have agreed to complete certain property development commitments in the event the joint venture defaults and to indemnify the lenders for losses resulting from fraud, misappropriation, violations of environmental laws and similar acts.

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DISCLOSURE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, including in the material set forth in the sections entitled Business and Management's Discussion and Analysis of Financial Condition and Results of Operations. These statements concern expectations, beliefs, projections, future plans and strategies, anticipated events or trends and similar expressions concerning matters that are not historical facts, and typically include the words anticipate, believe, expect, estimate, project, and future. Specifically, this 10-Q contains forward-looking statements including with respect to:

our expectations regarding future land sales;

our expectations regarding the housing market in 2009 and beyond.

We do not undertake any obligation to update any forward-looking statements.

These forward-looking statements reflect our current views about future events and are subject to risks, uncertainties and assumptions. As a result, actual results may differ significantly from those expressed in any forward-looking statement. The most important factors that could prevent us from achieving our goals, and cause the assumptions underlying forward-looking statements and the actual results to differ materially from those expressed in or implied by those forward-looking statements include, but are not limited to, the following:

economic or other business conditions that affect the desire or ability of our customers to purchase new homes in markets in which we conduct our business, such as increases in interest rates or unemployment rates or declines in median income growth, consumer confidence or the demand for, or the price of, housing;

the risks and uncertainties associated with our Chapter 11 cases;

the inability to obtain confirmation of our Chapter 11 plan;

our ability to motivate and retain key and essential personnel is impacted by the Bankruptcy Code which limits our ability to implement a retention program or take other measures intended to motivate employees to remain with us;

we require a significant amount of cash, which may not be available to us;

a further decline in the value of our land and home inventories;

our ability to dispose successfully of developed properties or undeveloped land or homesites at expected prices and within anticipated time frames;

our ability to compete in our existing markets;

the impact of hurricanes, tornadoes or other natural disasters or weather conditions on our business, including the potential for shortages and increased costs of materials and qualified labor and the potential for delays in construction and obtaining government approvals;

an increase or change in government regulations or in the interpretation and/or enforcement of existing government regulations;

a change in ownership of our stock, as defined in Section 382 of the Internal Revenue Code, which would limit our ability to receive anticipated income tax refunds.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As a result of our senior and senior subordinated notes offerings, as of September 30, 2008, \$1.1 billion of our outstanding borrowings are based on fixed interest rates. We are exposed to market risk primarily related to potential adverse changes in interest rates on our revolving credit facility, term loans and warehouse lines. The interest rates relative to these borrowings fluctuate with the prime, Federal Funds, LIBOR, and Eurodollar lending rates. As of September 30, 2008, we had an aggregate of \$737.0 million drawn under our Revolving Loan Facility and term loans that are subject to changes in interest rates. An increase or decrease of 1% in interest rates will change our annual debt service payments by \$7.4 million per year.

The failure to pay interest on certain notes and the filing of the Chapter 11 cases has constituted events of default or otherwise triggered repayment obligations under a number of instruments and agreements relating to our direct and indirect financial obligations. As a result of the events of default, all our obligations became automatically and immediately due and payable and have been reflected as such in the following table. We believe that any efforts to enforce the payment obligations are stayed as a result of the filing of the Chapter 11 cases and therefore, are not entitled to interest.

Our operations are interest rate sensitive as overall housing demand is adversely affected by increases in interest rates. If mortgage interest rates increase significantly, this may negatively affect the ability of homebuyers to secure adequate financing. Higher interest rates also increase our borrowing costs because, as indicated above, our bank loans will fluctuate with the prime, Federal Funds, LIBOR, and Eurodollar lending rates.

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Our Annual Report on Form 10-K for the year ended December 31, 2007 contains further information regarding our market risk. As of September 30, 2008, there have been no material changes in our market risk since December 31, 2007.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

To ensure that the information we must disclose in our filings with the Securities and Exchange Commission is recorded, processed, summarized, and reported on a timely basis, we have formalized our disclosure controls and procedures. Our principal executive officer and principal financial officer have reviewed and evaluated the effectiveness of our disclosure controls and procedures, as defined in Exchange Act Rules 13a-15(e) and 15d-15(e), as of September 30, 2008. Based on such evaluation, such officers have concluded that, as of September 30, 2008, our disclosure controls and procedures were not effective solely due to our failure to file this Form 10-Q on a timely basis. This failure was the result of our Chapter 11 bankruptcy process and our reorganization plans which have required substantial effort from our limited finance, accounting and management personnel. We continue to apply controls and procedures consistent with prior periods.

Changes In Internal Control

During the three months ended September 30, 2008, we made the following change in our internal control over financial reporting that has materially affected or is reasonably likely to materially affect, our internal control over financial reporting:

Our Chapter 11 proceedings have had a significant impact on our business processes and internal control over financial reporting related to the proper separation and payment of pre-petition and post-petition obligations and the preparation of unaudited consolidated financial statements reflecting the accounting required for the restructuring activities and reorganization expenses resulting from the Chapter 11 proceedings. Management continues to take actions necessary to address the resources, processes and controls related to these restructuring activities, while maintaining controls over routine daily operations.

Table of Contents**PART II. OTHER INFORMATION****ITEM 1. LEGAL PROCEEDINGS*****Chapter 11 Cases***

On January 29, 2008, TOUSA, Inc. and certain of our subsidiaries (excluding our financial services subsidiaries and joint ventures) filed voluntary petitions for relief under Chapter 11 of Title 11 of the United States Bankruptcy Code in the United States Bankruptcy Court for the Southern District of Florida, Fort Lauderdale Division. The Chapter 11 cases have been consolidated solely for procedural purposes and are pending as Case No. 08-10928-JKO. See Part I, Item 2 for additional information.

Securities Class Action Lawsuit

Beginning in December 2006, various stockholder plaintiffs brought lawsuits seeking class action status in the United States District Court for the Southern District of Florida. The actions were consolidated, and the consolidated suit is pending under the caption *Durgin, et al., v. TOUSA, Inc., et al., No. 06-61844-CIV*. On September 7, 2007, the Court appointed Diamondback Capital Management, L.C. (Diamondback) as the lead plaintiff and approved Diamondback's selection of counsel. Diamondback filed a consolidated complaint on November 2, 2007. The consolidated complaint set forth a proposed class period of August 1, 2005 to March 19, 2007 and alleged that TOUSA's public filings and other public statements were false and misleading in describing the financing for the Transeastern Joint Venture as non-recourse to TOUSA, and in describing the Transeastern Joint Venture's financial condition during the class period. Plaintiffs also alleged in the consolidated complaint that certain public filings and statements were misleading or suffered from material omissions in failing to fully disclose or describe the Completion and Carve-Out Guarantees that TOUSA executed in support of the Transeastern Joint Venture's financing. The consolidated complaint included claims under Section 11 of the Securities Act for strict liability and negligence regarding the registration statements and prospectus associated with the September 2005 offering of four million shares of stock. Plaintiffs asserted related claims against certain of the defendants as controlling persons responsible for the statements in the registration statements and prospectus. Finally, plaintiffs alleged claims under Section 10(b) of the Exchange Act for fraud with respect to various public statements regarding the non-recourse nature of the Transeastern debt, regarding the Completion and Carve-Out Guarantees, and regarding the financial condition of the Transeastern Joint Venture. Plaintiffs sought by way of the consolidated complaint compensatory damages, plus fees and costs, on behalf of themselves and the putative class of purchasers of TOUSA common stock and purchasers and sellers of options on TOUSA common stock.

On January 30, 2008, TOUSA and various other defendants filed motions to dismiss plaintiffs' Consolidated Complaint. On February 4, 2008, TOUSA filed a Notice of Suggestion of Bankruptcy notifying the court that TOUSA filed a bankruptcy petition. On February 5, 2008, the Court entered an order staying the action as to TOUSA pursuant to Section 362 of the United States Bankruptcy Code.

On April 30, 2008, lead plaintiff Diamondback filed a motion to withdraw as lead plaintiff, which the court granted on May 22, 2008. On July 15, 2008, the court appointed the Bricklayers & Trowel Trades International Pension Fund (the Bricklayers) as the new lead plaintiff. On July 30, 2008, the Bricklayers filed a notice of an intent to file an amended complaint and accordingly, on July 31, 2008, the court denied as moot without prejudice the defendants' previously filed motions to dismiss the consolidated complaint.

On September 19, 2008, the Bricklayers filed a Consolidated Amended Class Action Complaint (the amended complaint). This amended complaint dropped many of the parties previously named as defendants in the consolidated complaint, including TOUSA, leaving only Antonio B. Mon, Tommy McAden, David J. Keller and Randy L. Kotler as defendants in the suit. The amended complaint also dropped the Section 11 and Section 15 claims, leaving the claims under Section 10(b) of the Exchange Act and Rule 10b-5, as well as the claims made under Section 20(a) of the Exchange Act. Defendants Mon, Keller and Kotler filed motions to dismiss the amended complaint on November 21, 2008. Defendant McAden had not yet been served, but his counsel recently entered an appearance and filed a motion to dismiss on March 2, 2009. The plaintiffs filed its opposition to the motions to dismiss on March 24, 2009.

Defendants' replies in support of their motions to dismiss were due on May 13, 2009. A trial date has not yet been set.

Proceeding by Official Committee of Unsecured Creditors

In re TOUSA, Inc., Docket No. 08-10928-JKO; Adv. Pro No. 08-1435-JKO. We and certain of our subsidiaries are involved in an adversary proceeding brought as part of our Chapter 11 proceedings. On July 14, 2008, the Official

Committee of Unsecured Creditors of TOUSA, Inc. (the Committee) commenced an adversary proceeding (the Committee Action) as part of our and certain of our subsidiaries (collectively, the Debtors) Chapter 11 proceedings in United States Bankruptcy Court for the Southern District of Florida. The Debtors were originally non-parties to the Committee Action, but have since been named as third-party defendants by certain of the original defendants in the Committee Action.

The Committee Action seeks to avoid certain allegedly fraudulent and preferential pre-petition transfers of up to \$800 million the Debtors made in connection with the settlement of litigation related to the Transeastern Joint Venture (the Transeastern Settlement), and further seeks to avoid as a preferential transfer any security interest that may have been granted by any of the Debtors to certain lenders in a tax refund of approximately \$207.0 million that the Debtors received in 2008. The Committee s original complaint (the Complaint) named over 60 defendants, including the lenders under the credit agreements funding the Transeastern Joint Venture (the Transeastern Lenders), as well as the original lenders (and their successors and assigns) and administrators under the credit agreements entered into as a result of the Transeastern Settlement (the New Credit Agreements). The Debtors are not defendants to the Committee s claims in the Committee Action.

The Committee s Complaint alleged that, in order to resolve certain prepetition litigation regarding the Transeastern Joint Venture, the parties to that litigation entered into a series of settlement agreements releasing all claims relating to the Transeastern acquisition. The Complaint alleges that, as part of these settlement agreements, certain of our entities agreed to pay over \$420 million to the administrator of the Transeastern loans and to issue approximately \$135 million in preferred stock, notes and warrants. The Complaint further alleged that to fund these payments, we and certain of our subsidiaries (the Conveying Subsidiaries) entered into the three New Credit Agreements.

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According to the Complaint, the loans issued under these New Credit Agreements were secured by liens on the property and assets of all of the Debtors, including the Conveying Subsidiaries. The Complaint alleged that the Conveying Subsidiaries were not defendants in the prepetition Transeastern litigation and were not obligated on the Transeastern debt that was released in connection with the Transeastern Settlement. Therefore, the Complaint alleged, the Conveying Subsidiaries did not receive reasonably equivalent value for the secured debt obligations that they incurred. The Complaint also alleged that the Conveying Subsidiaries were either insolvent at the time of the Transeastern Settlement or became insolvent as a result of it, and that the Conveying Subsidiaries were left with unreasonably small capital as a result of the New Credit Agreements. Based on these allegations, the Committee seeks to have the liens established under the New Credit Agreements voided and all amounts already repaid under the New Credit Agreements returned. The Committee also seeks to have the security interest the Debtors granted to the New Lenders on the Debtors' tax refund voided and the New Lenders' claims seeking allowance of the full amount of the New Loans disallowed in their entirety or reduced.

On September 19, 2008, the Bankruptcy Court held a hearing on motions to dismiss that had been filed by Defendants Citicorp North America, Inc., and Wells Fargo Bank, N.A. Wells Fargo's motion to dismiss was denied. Citicorp's motion to dismiss sought dismissal of claims relating to only one of the three New Credit Agreements, the Second Amended And Restated Revolving Credit Agreement (the "Revolver"). The Court granted Citicorp's motion to dismiss, but granted the Committee leave to file an amended complaint.

On October 17, 2008, the Committee filed an Amended Complaint. The Amended Complaint contained additional allegations regarding the Revolver, and added new defendants. Citicorp moved to dismiss the claims in the Amended Complaint relating to the Revolver. In addition, the Transeastern Lenders moved to dismiss all claims against them. The Court denied the Transeastern Lenders' motion to dismiss. The Court granted Citicorp's motion to dismiss the Revolver claims in the Amended Complaint, but again granted the Committee leave to file a second amended complaint consistent with the Court's specific guidance on the revolver issue. After initially filing a Second Amended Complaint again including claims related to the Revolver, on February 4, 2009, the Committee filed a Third Amended Complaint which did not include claims relating to the Revolver. The Committee has, however, appealed to the District Court the dismissal of the Revolver claims in the Amended Complaint.

In addition, on August 13, 2008, Citicorp North America, Inc., in its capacity as the Administrative Agent for the First Lien Term Loan, answered the Complaint in the Committee Action, and filed a third-party complaint (the "Citigroup Third-Party Complaint") against TOUSA, Inc. and each of the Debtor signatories, co-borrowers and co-guarantors under the First Lien Term Loan. The Citigroup Third-Party Complaint alleges that, to the extent the Committee establishes its allegations in the Committee Action, the defendants to the Citigroup Third-Party Complaint will have materially breached the First Lien Term Loan by (a) not having assets whose fair value exceeded their debts and liabilities, subordinated, contingent or otherwise, (b) not having assets whose fair saleable value exceed their debts and other liabilities, subordinated, contingent or otherwise, (c) not being able to pay their debts and liabilities, subordinated, contingent, or otherwise, and/or (d) having unreasonably small capital with which to conduct their business. On September 30, 2008 the Debtors filed their answer to the Citigroup Third-Party Complaint, generally denying Citigroup's allegations and asserting affirmative defenses.

On November 6, 2008, Wells Fargo Bank, N.A., in its capacity as the Second Lien Term Agent, filed its answer to the Committee's Amended Complaint in the Committee Action, and filed a third-party complaint (the "Wells Fargo Third-Party Complaint") against TOUSA, Inc. and each of the Debtor signatories, co-borrowers and co-guarantors under the Second Lien Term Loan (except for Engle/Gilligan, LLC, Engle Homes Delaware, Inc., Newmark Homes Business Trust, TOUSA Delaware, Inc., and TOUSA Funding, LLC). The Wells Fargo Third-Party Complaint alleges that, to the extent the Committee establishes its allegations in the Committee Action, the defendants to the Wells Fargo Third-Party Complaint will have materially breached the Second Lien Term Loan by (a) not having assets whose fair value exceeded their debts and liabilities, subordinated, contingent or otherwise, (b) not having assets whose fair saleable value exceed their debts and other liabilities, subordinated, contingent or otherwise, (c) not being able to pay their debts and liabilities, subordinated, contingent, or otherwise, and/or (d) having unreasonably small capital with which to conduct their business. On November 25, 2008, the Debtors filed their answer to the Wells Fargo Third-Party Complaint, generally denying Wells Fargo's allegations and asserting affirmative defenses.

On February 24, 2009, the Senior Transeastern Lenders and the CIT Group/Business Credit, Inc. (CIT) each filed a Counterclaim and Third-Party Complaint against certain of the Debtors. The Senior Transeastern Lenders and CIT allege that they are entitled to indemnification against any recovery the Committee receives as a result of the Committee s fraudulent transfer claims under the terms of the August 1, 2005 Senior Credit Agreement signed by certain of the Debtors in connection with the formation of the Transeastern Joint Venture. The Senior Transeastern Lenders and CIT seek recoupment for the full amount of any recovery against them on each of the Committee s fraudulent transfer claims. On April 1, 2009, the third-party defendant Debtors moved to strike, or in the alternative to sever and stay, the claims asserted against them in the Senior Transeastern Lenders and CIT s Counterclaims and Third-Party Complaints. A hearing on the third-party Debtor s motion is currently scheduled for May 28, 2009.

Discovery in the Committee Action, the Citicorp Third-Party Complaint, and the Wells Fargo Third-Party Complaint is currently ongoing. Pursuant to the amended case management order entered by the Court on November 11, 2008, current and former employees of the Debtors, the parties and various non-parties have been deposed.

On February 26, 2009, the court entered an order granting the Debtors motion to compel mediation of the case. The non-binding judicial settlement conference was conducted by Judge Laurel Isicoff on March 23, 2009 and March 24, 2009. On April 14, 2009, Judge Isicoff reported that the parties were at an impasse with respect to the Committee s claims against the First Lien Term Loan Lenders, the First Lien Revolver Lenders, and the Senior Transeastern Lenders. Judge Isicoff further reported that the other Defendants had either reached an agreement with the Committee or were continuing settlement discussions. Trial is currently scheduled for the weeks of July 13, 2009 and July 20, 2009.

Table of Contents***Potential Claim by the Official Committee of Unsecured Creditors of TOUSA***

On October 26, 2007, the TOUSA Board of Directors received a letter from counsel to a group of holders of TOUSA senior and subordinated notes (the Noteholder Group). TOUSA did not file for bankruptcy protection as requested by the Noteholder Group, but did later file for bankruptcy in January 2008. On February 27, 2009 the Official Committee of Unsecured Creditors of TOUSA filed a motion seeking standing to pursue claims against members of certain Debtor-Subsidiaries boards of directors as well as the majority shareholder of TOUSA, Tech SA, in connection with the July 31, 2007 transaction. The Court has not yet heard or ruled upon the Committee's motion.

Vista Lakes

Plaintiffs, purchasers of homes in the Vista Lakes community near Orlando, filed a class action complaint alleging that their homes were built on the site of a former bombing range. The plaintiffs seek recovery under theories of fraud, breach of contract, strict liability, negligence, and civil conspiracy. Because the plaintiffs named debtor defendants Touse, Inc., Touse Homes, Inc., d/b/a Engle Homes Orlando and Touse Homes, LP as defendants in this action, the action was removed to federal court. The plaintiffs then agreed to dismiss the debtor defendants and the parties entered into a stipulation for remand. The state court case was re-opened and the parties remaining as defendants included Universal Land Title, Inc. and Preferred Home Mortgage Company.

Universal Land Title, Inc. and Preferred Home Mortgage Company filed a motion to dismiss the second amended complaint. On February 13, 2009, the court dismissed all nine counts of the second amended complaint as to both Universal Land Title, Inc. and Preferred Home Mortgage Company, but granted Plaintiffs leave to amend their complaint.

On March 23, 2009, Plaintiffs filed their Third Amended Complaint and, with the exception of the claim for strict liability, re-alleged eight of the previously dismissed causes of action against Universal Land Title, Inc. and Preferred Home Mortgage Company. On April 29, 2009, Preferred Home Mortgage Company and Universal Land Title, Inc. filed their motion to dismiss the Third Amended Complaint. On April 30, 2009, Plaintiffs filed a notice voluntarily dismissing certain counts, and the only claims that remain pending as to Preferred Home Mortgage Company and Universal Land Title, Inc. are counts for negligence and civil conspiracy.

Based upon the early stage of the litigation and discovery, and depending upon the success of the motion to dismiss the Third Amended Complaint, we are unable to evaluate the likelihood of an unfavorable outcome or the range of liability in such event.

Chinese Drywall

TOUSA Homes, Inc. was named as a defendant in a purported class action lawsuit pending in the United States District Court for the Southern District of Florida on behalf of certain homeowner plaintiffs in Southwest Florida. (Karen Vickers, et al., v. TOUSA Homes, Inc., et al., No. 09-20510-CIV-GOLD/MCALILEY). The complaint alleges the plaintiff homeowners were sold homes containing drywall that is inherently defective (Chinese Drywall), because it emits various sulfide gasses and/or other chemicals through off gassing that purportedly causes property damage and potential health hazards. The plaintiff's have voluntarily withdrawn the complaint without prejudice. We are in the process of responding to notice of the alleged defect pursuant to Florida Statutes chapter 558. TOUSA Homes, Inc. was named, but has not been served in an additional purported class action lawsuit making similar allegations in the Lee County, Florida Circuit Court (Joyce Dowdy Revocable Trust, et. al v. Engle Homes, Inc. et. al, No. 09-CA-1158).

Other Litigation

We are also involved in various other claims and legal actions arising in the ordinary course of business. We do not believe that the ultimate resolution of these other matters will have a material adverse effect on our financial condition or results of operations. As of the date of the Chapter 11 filing, then pending litigation was generally stayed, and absent further order of the Bankruptcy Court, most parties may not take any action to recover on pre-petition claims against us.

ITEM 1A. RISK FACTORS

Set forth below is a discussion of the material changes in our risk factors as previously disclosed in Item 1A of Part 1 of our Annual Report on Form 10-K for the fiscal year ended December 31, 2007 (2007 Form 10-K).

The information presented below updates, and should be read in conjunction with, the risk factors and other information disclosed in our 2007 Form 10-K.

Our cash collateral order includes operating budgets and financial covenants that limit our operating flexibility.

The cash collateral order requires us to comply with certain financial budgets and covenants that, among other things, restrict our ability to take specific actions, even if we believe such actions are in our best interest. These include, among other things, restrictions on our ability to:

incur indebtedness;

incur liens and enter sale/leaseback transactions except for model homes subject to certain limitations;

make or own investments;

enter into transactions with affiliates;

engage in new lines of business;

consolidate, merge, sell all or substantially all of our assets;

issue guarantees of debt;

agree to amendment or modification to our organizational documents;

incur or create claims; and

make additional payments on pre-petition indebtedness.

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If we fail to comply with the new order, we will not have sufficient cash to enable us to operate our business and effectuate our restructuring.

ITEM 6. EXHIBITS

Exhibit

Number Description

31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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SIGNATURES

Pursuant to the requirements 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.

TOUSA, Inc.

Date: May 26, 2009

By: /s/ Tommy L. McAden

Name: Tommy L. McAden

Title: Executive Vice President, Director
and Chief Financial Officer

Date: May 26, 2009

By: /s/ Angela F. Valdes

Name: Angela F. Valdes

Title: Vice President and Chief Accounting
Officer