BROOKFIELD HOMES CORP
Form 10-Q
November 09, 2007

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

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

For the quarterly period ended September 30, 2007
Commission File Number: 001 31524
BROOKFIELD HOMES CORPORATION
(Exact Name of Registrant as Specified in Its Charter)

Delaware	**37-1446709**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
8500 Executive Park Avenue Suite 300 Fairfax, Virginia	**22031**
(Address of Principal Executive Offices)	(Zip Code)

(703) 270-1700
(Registrant s Telephone Number, Including Area Code)

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):
Large accelerated filer o Accelerated filer þ Non-accelerated filer o

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

As of November 1, 2007, the registrant had outstanding 26,628,207 shares of its common stock, $0.01 par value per share.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

BROOKFIELD HOMES CORPORATION
CONSOLIDATED BALANCE SHEETS

(all dollar amounts are in thousands of U.S. dollars)

	Note	(Unaudited) September 30, 2007	December 31, 2006
Assets			
Housing and land inventory	2	$ 1,108,258	$ 1,075,192
Investments in housing and land joint ventures	3	108,112	90,325
Consolidated land inventory not owned	2	71,090	59,381
Receivables and other assets		36,514	37,031
Cash and cash equivalents		1,164	86,809
Deferred income taxes	6	57,057	52,715
		$ 1,382,195	$ 1,401,453
Liabilities and Equity			
Project specific and other financings		$ 690,568	$ 617,931
Accounts payable and other liabilities	4	178,988	320,061
Minority interest		104,101	92,055
Preferred stock 10,000,000 shares authorized, no shares issued			
Common stock 65,000,000 shares authorized, 32,073,781 shares issued (December 31, 2006 32,073,781 shares issued)		321	321
Additional paid-in-capital		146,060	146,730
Treasury stock, at cost 5,445,574 shares (December 31, 2006 5,519,275 shares)		(245,287)	(248,606)
Retained earnings		507,444	472,961
		$ 1,382,195	$ 1,401,453

See accompanying notes to financial statements

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BROOKFIELD HOMES CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(all dollar amounts are in thousands of U.S. dollars, except per share amounts)

		(Unaudited) Three Months Ended September 30,		*(Unaudited)* Nine Months Ended September 30,	
Revenue	**Note**	**2007**	**2006**	**2007**	**2006**
Housing		$ 117,405	$ 160,025	$ 376,077	$ 475,530
Land		3,359	15,520	9,598	67,368
		120,764	175,545	385,675	542,898
Direct Cost of Sales	2	(133,911)	(125,322)	(349,554)	(375,507)
		(13,147)	50,223	36,121	167,391
Equity in earnings / (loss) from housing and land joint ventures	3	(6,727)	11,204	(6,347)	12,874
Other (expense) / income		(5,519)	(254)	174	7,753
Selling, general and administrative expense		(16,007)	(12,699)	(50,037)	(33,771)
Minority interest		3,691	(3,737)	2,763	(9,141)
Net Income / (Loss) Before Taxes		(37,709)	44,737	(17,326)	145,106
Income tax recovery / (expense)	6	39,328	(17,134)	57,135	(55,575)
Net Income		$ 1,619	$ 27,603	$ 39,809	$ 89,531
Earnings Per Share					
Basic	5	$ 0.06	$ 1.04	$ 1.50	$ 3.32
Diluted	5	$ 0.06	$ 1.03	$ 1.48	$ 3.27
Weighted Average Common Shares Outstanding *(in thousands)*					
Basic	5	26,628	26,572	26,623	26,981
Diluted	5	26,816	26,898	26,865	27,368

See accompanying notes to financial statements

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BROOKFIELD HOMES CORPORATION
CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY
(all dollar amounts are in thousands of U.S. dollars)

	(Unaudited) Nine Months Ended September 30, 2007	2006
Common Stock	$ 321	$ 321
Additional Paid-in Capital		
Opening balance	146,730	146,249
Stock option exercises	(670)	481
Ending balance	146,060	146,730
Treasury Stock		
Opening balance	(248,606)	(217,182)
Share repurchases		(37,922)
Stock option exercises	3,319	6,498
Ending balance	(245,287)	(248,606)
Retained Earnings		
Opening balance	472,961	335,261
Net income	39,809	89,531
Dividends	(5,326)	(5,343)
Ending balance	507,444	419,449
Total stockholders equity	$ 408,538	$ 317,894

See accompanying notes to financial statements

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BROOKFIELD HOMES CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(all dollar amounts are in thousands of U.S. dollars)

	(Unaudited) Three Months Ended September 30,		*(Unaudited)* Nine Months Ended September 30,	
	2007	**2006**	**2007**	**2006**
Cash Flows From / (used in) Operating Activities				
Net income	$ 1,619	$ 27,603	$ 39,809	$ 89,531
Adjustments to reconcile net income to net cash used in operating activities:				
Distributed / (undistributed) income from housing and land joint ventures	11	(10,977)	277	(9,987)
Minority interest	(3,691)	3,737	(2,763)	9,141
Deferred income taxes	(10,798)	898	(4,342)	4,676
Impairments and write-offs of option deposits	34,413		34,413	
Impairments from housing and land joint ventures	7,135		7,135	
Other changes in operating assets and liabilities:				
Decrease in receivables and other assets	1,529	5,130	517	57,904
Increase in housing and land inventory	(22,685)	(46,852)	(73,232)	(138,478)
(Decrease)/increase in accounts payable and other	(38,909)	1,339	(132,408)	(79,808)
Net cash used in operating activities	(31,376)	(19,122)	(130,594)	(67,021)
Cash Flows From / (used in) Investing Activities				
Investments in housing and land joint ventures	(12,006)	(30,424)	(33,063)	(49,515)
Recovery from housing and land joint ventures	4,185	3,088	7,864	9,718
Net cash used in investing activities	(7,821)	(27,336)	(25,199)	(39,797)
Cash Flows From / (used in) Financing Activities				
Net (repayments)/borrowings under revolving project specific and other financings	35,106	(15,486)	72,637	(25,692)
Distributions to minority interest		(510)	(1,750)	(14,627)
Contributions from minority interest	1,537	1,359	4,503	4,248
Repurchase of common shares		(1,251)		(37,922)
Exercise of stock options	11		84	164
Dividends paid in cash			(5,326)	(5,343)
Net cash provided by / (used in) financing activities	36,654	(15,888)	70,148	(79,172)
Decrease in cash and cash equivalents	(2,543)	(62,346)	(85,645)	(185,990)
Cash and cash equivalents at beginning of period	3,707	74,767	86,809	198,411

Cash and cash equivalents at end of period	$ 1,164	$ 12,421	$ 1,164	$ 12,421
Supplemental Cash Flow Information				
Interest paid	$ 16,386	$ 15,531	$ 48,531	$ 40,628
Income taxes paid	$	$ 13,375	$ 22,154	$ 52,185
Non-cash increase / (decrease) in consolidated land inventory not owned	$ 139	$ 531	$ 5,956	$ (6,726)

See accompanying notes to financial statements

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BROOKFIELD HOMES CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands of U.S. dollars except per share amounts)

Note 1. Significant Accounting Policies

(a) Basis of Presentation

Brookfield Homes Corporation (the Company or Brookfield Homes) was incorporated on August 28, 2002 as a wholly-owned subsidiary of Brookfield Properties Corporation (Brookfield Properties) to acquire as of October 1, 2002 all of the California and Washington D.C. Area homebuilding and land development operations (the Land and Housing Operations) of Brookfield Properties pursuant to a reorganization of its business (the Spin-off). On January 6, 2003, Brookfield Properties completed the Spin-off by distributing all of the issued and outstanding common stock it owned in the Company to its common stockholders. Brookfield Homes began trading as a separate company on the New York Stock Exchange on January 7, 2003.

The consolidated financial statements include the accounts of Brookfield Homes and its subsidiaries and investments in joint ventures and variable interests in which the Company is the primary beneficiary.

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information. Since they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements, they should be read in conjunction with the Company s consolidated financial statements and footnotes thereto included in the Company s annual report on Form 10-K for the year ended December 31, 2006. In the opinion of management, all adjustments necessary for fair presentation of the accompanying consolidated financial statements have been made.

The Company historically has experienced, and expects to continue to experience, variability in quarterly results. The consolidated statements of income for the three months and nine months ended September 30, 2007 are not necessarily indicative of the results to be expected for the full year.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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.

(b) Recent Accounting Pronouncements

In February 2007, the United States Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) 159, The Fair Value Option for Financial Assets and Financial Liabilities. SFAS 159 allows companies to choose to measure certain financial instruments and other items at fair value. Companies electing the fair value option are required to report subsequent changes in fair value in earnings. This Statement is effective for fiscal years beginning after November 15, 2007 (the Company s fiscal year beginning January 1, 2008). The Company is currently reviewing the impact of SFAS 159 on its consolidated financial statements.

In September 2006, the FASB issued SFAS 157, Fair Value Measurements. SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement is effective for fiscal years beginning after November 15, 2007 (the Company s fiscal year beginning January 1, 2008), and interim periods within those fiscal years. The Company is currently reviewing the impact of SFAS 157 on its consolidated financial statements.

In July 2006, the FASB issued FASB Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109, which clarifies the accounting for uncertainty in income taxes recognized in financial statements in accordance with FASB Statement No. 109, Accounting for Income Taxes. This Interpretation provides guidance on the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. In addition, FIN 48 provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. Under FIN 48, the impact of an uncertain tax position on the income tax return must be recognized at the largest amount that is more-likely-than-not to be sustained upon audit by the relevant taxing authority. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of

BROOKFIELD HOMES CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands of U.S. dollars except per share amounts)

being sustained. The Company adopted the provisions of FIN 48 on January 1, 2007. See Note 6 Income Taxes, for further discussions.

(c) Reclassification

Certain prior period amounts in the consolidated balance sheet and consolidated statements of income have been reclassified to conform with the September 30, 2007 presentation. Specifically, Accounts payable and other liabilities now includes deferred compensation which had previously been shown as a component of project specific and other financings, and Other (expense) / income is shown separately which had previously been shown as a component of Land and other revenues.

Note 2. Housing and Land Inventory

Housing and land inventory includes homes completed and under construction and lots ready for construction, model homes and land under and held for development which will be used in the Company s homebuilding operations or sold as building lots to other homebuilders. The following summarizes the components of housing and land inventory:

	September 30, 2007	December 31, 2006
Housing inventory	$ 540,624	$ 571,352
Model homes	51,111	42,706
Land and land under development	516,523	461,134
	$ 1,108,258	$ 1,075,192

The Company capitalizes interest which is expensed as housing units and building lots are sold. For the three months ended September 30, 2007 and 2006, and for the nine months ended September 30, 2007 and 2006, interest incurred and capitalized by the Company was $16.4 million and $15.5 million, $48.5 million and $40.6 million, respectively. Capitalized interest expensed for the same periods was $6.0 million and $4.5 million, $20.9 million and $10.8 million, respectively.

Capitalized costs are expensed as costs of sales on a specific identification basis or on a relative value basis in proportion to anticipated revenue depending on the nature of the cost. Included in direct cost of sales is $96.1 million and $306.5 million of costs related to housing revenue for the three months and nine months ended September 30, 2007 (September 30, 2006 $118.2 million and $343.5 million, respectively) and $3.4 million and $8.6 million of costs related to land revenues (September 30, 2006 $7.1 million and $32.0 million, respectively).

In accordance with SFAS 144 Accounting for the Impairment or Disposal of Long-Lived Assets, the Company has reviewed its housing and land assets for recoverability. Recoverability is measured by comparing the carrying amount of an asset to future undiscounted cash flows expected to be generated by the asset. To arrive at this amount, the Company estimates the cash flow for the life of each project. These projections take into account the specific business plans for each project and management s best estimate of the most probable set of economic conditions anticipated to prevail in the market area. Such projections assume current home selling prices, cost estimates and sales rates for short term projects are consistent with recent sales activity. For longer term projects, sales rates for 2007 and 2008 assume recent sales activity and normalized sales rates beyond 2008. If these assets are considered to be impaired, they are then written down to fair value less estimated selling costs. The ultimate fair values for the Company s housing and land inventory are dependent upon future market and economic conditions. For the three months and nine months ended September 30, 2007, the Company recognized $31.4 million of impairment charges related to 555 finished lots in the Inland Empire of California the Company directly owns and this amount is included in direct cost of sales (September 30, 2006 nil). In addition, the Company wrote-off $3.0 million primarily related to 875 unentitled optioned lots in the Central Valley of California the Company is no longer pursuing and this amount is included in direct cost of sales (September 30, 2006 nil). Should the ongoing challenges of the housing market not stabilize in the near future, it is possible further impairment charges will be recognized in future results.

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BROOKFIELD HOMES CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands of U.S. dollars except per share amounts)

In the ordinary course of business, the Company has entered into a number of option contracts to acquire lots in the future in accordance with specific terms and conditions of such agreements. Under these option agreements, the Company will fund deposits to secure the right to purchase land or lots at a future point in time. The Company has evaluated its option contracts and determined that for those entities considered to be variable interest entities (VIEs), it is the primary beneficiary of options for 1,089 lots with an aggregate exercise price of $71.1 million (December 31, 2006 1,083 lots with an aggregate exercise price of $59.4 million), which are required to be consolidated. In these cases, the only asset recorded is the Company s exercise price for the option to purchase, with an increase in minority interest of $46.5 million (December 31, 2006 $40.5 million) for the assumed third party investment in the VIE. Where the land sellers are not required to provide the Company financial information related to the VIE, certain assumptions by the Company were required in its assessment as to whether or not it is the primary beneficiary.

Housing and land inventory includes non-refundable deposits and other entitlement costs totaling $86.7 million (December 31, 2006 $76.6 million) in connection with options that are not required to be consolidated under the provisions of FASB Interpretation No. 46R (FIN 46R), Consolidation of Variable Interest Entities . The total exercise price of these options is $584.2 million (December 31, 2006 $670.3 million) including the non-refundable deposits identified above. The number of lots for which the Company has obtained an option to purchase, excluding those already consolidated, and their respective dates of expiry and their exercise price are as follows:

Year of Expiry	Number of Lots	Total Exercise Price
2007	2,069	$ 134,400
2008	3,502	98,943
2009	634	69,158
Thereafter	6,468	281,742
	12,673	$ 584,243

The Company holds agreements for a further 3,862 acres of longer term land, with non-refundable deposits and other entitlement costs of $11.0 million which is included in housing and land inventory that may provide additional lots upon obtaining entitlements with an aggregate exercise price of $249.2 million. However, given that the Company is in the initial stage of land entitlement, the Company has concluded at this time that the level of uncertainty in entitling these properties does not warrant including them in the above totals.

Note 3. Investments in Housing and Land Joint Ventures

The Company participates in a number of joint ventures in which it has less than a controlling interest. Summarized condensed financial information on a combined 100% basis of the joint ventures is as follows:

	September 30, 2007	December 31, 2006
Assets		
Housing and land inventory	$ 530,674	$ 452,359
Other assets	34,415	38,063
	$ 565,089	$ 490,422

Liabilities and Equity				
Project specific financings	$	316,527	$	253,529
Accounts payable and other liabilities		29,967		32,319
Investment and advances				
Brookfield Homes		108,112		90,325
Others		110,483		114,249
	$	565,089	$	490,422

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BROOKFIELD HOMES CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands of U.S. dollars except per share amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	**2006**	**2007**	**2006**
Revenue and Expenses				
Revenue	$ 8,186	$ 86,326	$ 47,994	$ 116,549
Expenses	(6,906)	(46,973)	(87,628)	(73,496)
Net income / (loss)	$ 1,280	$ 39,353	$ (39,634)	$ 43,053
Company s share of net income / (loss)	$ (6,727)	$ 11,204	$ (6,347)	$ 12,874

In reporting the Company s share of net income, all inter-company profits or losses from housing and land joint ventures are eliminated on lots purchased by the Company.

The net loss for the nine months ended September 30, 2007, results from an impairment charge of $41.7 million recognized in one of the Company s joint ventures during the second quarter of 2007. In calculating the Company s share of the joint venture net loss at the end of the second quarter of 2007, the Company did not require an impairment charge as its carrying value in this joint venture was below its proportionate share of the underlying assets in that period. During the third quarter of 2007, in accordance with Accounting Principles Board Opinion No. 18 (APB 18), The Equity Method of Accounting for Investments in Common Stock , the Company recognized an impairment charge of $7.1 million related to this joint venture as a result of continued deterioration in this project which resulted in the carrying value of the Company s investment in the joint venture exceeding its estimated fair value.

Joint ventures in which the Company has a non-controlling interest are accounted for using the equity method. In addition, the Company has performed an evaluation of its existing joint venture relationships by applying the provisions of FIN 46R. The Company has determined that for those entities for which this interpretation applies, none of these joint ventures were considered to be a VIE requiring consolidation pursuant to the requirements of FIN 46R.

The Company and/or its joint venture partners have provided varying levels of guarantees of debt in its joint ventures. At September 30, 2007, the Company had recourse guarantees of $19.2 million (December 31, 2006 $12.7 million) and limited maintenance guarantees of $114.2 million (December 31, 2006 $89.4 million) with respect to debt in its joint ventures. As of September 30, 2007, the fair market value of the recourse guarantees was insignificant.

Note 4. Accounts Payable and Other Liabilities

The components of accounts payable and other liabilities included in the Company s balance sheet are summarized as follows:

	September 30, 2007	December 31, 2006
Trade payables and cost to complete accruals	$ 57,490	$ 70,187
Warranty costs	19,046	19,569
Customer deposits	4,007	4,030
Stock-based compensation	16,058	33,824
Due to minority interest	25,763	31,863
Accrued and deferred compensation	48,540	