

MDC HOLDINGS INC
Form 10-Q
November 03, 2011
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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, 2011

OR

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

Commission File No. 1-8951

M.D.C. HOLDINGS, INC.

(Exact name of Registrant as specified in its charter)

Delaware
(State or other jurisdiction
of incorporation or organization)

84-0622967
(I.R.S. employer
identification no.)

4350 South Monaco Street, Suite 500

80237

Denver, Colorado
(Address of principal executive offices)

(Zip code)

(303) 773-1100

(Registrant's telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes 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, non-accelerated filer, or a smaller reporting company. See definition of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer Accelerated Filer
Non-Accelerated Filer (Do not check if a smaller reporting company) Smaller Reporting Company

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

As of September 30, 2011, 47,474,000 shares of M.D.C. Holdings, Inc. common stock were outstanding.

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M.D.C. HOLDINGS, INC. AND SUBSIDIARIES

FORM 10-Q

FOR THE QUARTER ENDED SEPTEMBER 30, 2011

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Table of Contents**ITEM 1. Unaudited Consolidated Financial Statements****M.D.C. HOLDINGS, INC.****Consolidated Balance Sheets****(In thousands, except share and per share amounts)****(Unaudited)**

| | September 30, 2011 | December 31, 2010 |
|---|-------------------------------|------------------------------|
| Assets | | |
| Cash and cash equivalents | \$ 567,501 | \$ 572,225 |
| Marketable securities | 535,494 | 968,729 |
| Restricted cash | 682 | 420 |
| Receivables | | |
| Home sales receivables | 11,160 | 8,530 |
| Income taxes receivable | - | 2,048 |
| Other receivables | 8,254 | 9,432 |
| Mortgage loans held-for-sale, net | 42,301 | 65,114 |
| Inventories, net | | |
| Housing completed or under construction | 333,350 | 372,422 |
| Land and land under development | 517,337 | 415,237 |
| Property and equipment, net | 37,400 | 40,826 |
| Deferred tax asset, net of valuation allowance of \$274,380 and \$231,379 at September 30, 2011 and December 31, 2010, respectively | - | - |
| Related party assets | 7,393 | 7,393 |
| Prepaid expenses and other assets, net | 54,097 | 85,393 |
| Total Assets | \$ 2,114,969 | \$ 2,547,769 |
| Liabilities | | |
| Accounts payable | \$ 27,295 | \$ 35,018 |
| Accrued liabilities | 189,161 | 260,729 |
| Income taxes payable | 869 | - |
| Related party liabilities | 70 | 90 |
| Mortgage repurchase facility | 10,708 | 25,434 |
| Senior notes, net | 1,006,656 | 1,242,815 |
| Total Liabilities | 1,234,759 | 1,564,086 |
| Commitments and Contingencies | | |
| Stockholders Equity | | |
| Preferred stock, \$0.01 par value; 25,000,000 shares authorized; none issued or outstanding | - | - |
| Common stock, \$0.01 par value; 250,000,000 shares authorized; 47,530,000 and 47,474,000 issued and outstanding, respectively, at September 30, 2011 and 47,198,000 and 47,142,000 issued and outstanding, respectively, at December 31, 2010 | 475 | 472 |
| Additional paid-in-capital | 850,795 | 820,237 |
| Retained earnings | 43,620 | 158,749 |
| Accumulated other comprehensive (loss) income | (14,021) | 4,884 |
| Treasury stock, at cost; 56,000 shares at September 30, 2011 and December 31, 2010 | (659) | (659) |
| Total Stockholders Equity | 880,210 | 983,683 |

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| | | | |
|------------------------------------|--------|--------------|--------------|
| Total Liabilities and Stockholders | Equity | \$ 2,114,969 | \$ 2,547,769 |
|------------------------------------|--------|--------------|--------------|

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

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Table of Contents**M.D.C. HOLDINGS, INC.****Consolidated Statements of Operations****(In thousands, except per share amounts)****(Unaudited)**

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|--------------------|--|--------------------|
| | 2011 | 2010 | 2011 | 2010 |
| Revenue | | | | |
| Home sales revenue | \$ 204,886 | \$ 216,501 | \$ 574,432 | \$ 668,720 |
| Land sales revenue | 730 | 904 | 3,499 | 6,618 |
| Other revenue | 5,744 | 8,276 | 18,861 | 23,751 |
| Total revenue | 211,360 | 225,681 | 596,792 | 699,089 |
| Costs and expenses | | | | |
| Home cost of sales | 170,443 | 171,199 | 490,521 | 535,651 |
| Land cost of sales | 724 | 818 | 2,482 | 5,983 |
| Asset impairments | 4,692 | 3,718 | 14,090 | 3,718 |
| Marketing expenses | 10,002 | 11,191 | 29,732 | 29,726 |
| Commission expenses | 7,476 | 8,078 | 20,699 | 24,818 |
| General and administrative expenses | 35,580 | 39,269 | 108,569 | 124,060 |
| Other operating expenses | 2,390 | 817 | 3,287 | 1,837 |
| Related party expenses | 24 | - | 56 | 9 |
| Total operating costs and expenses | 231,331 | 235,090 | 669,436 | 725,802 |
| Loss from operations | (19,971) | (9,409) | (72,644) | (26,713) |
| Other income (expense) | | | | |
| Interest income | 6,745 | 7,544 | 21,943 | 19,513 |
| Interest expense | (3,695) | (9,000) | (19,819) | (28,810) |
| Extinguishment of senior notes and other | (17,268) | 271 | (17,176) | 475 |
| Loss before income taxes | (34,189) | (10,594) | (87,696) | (35,535) |
| Benefit from income taxes, net | 2,479 | 355 | 8,127 | 739 |
| Net loss | \$ (31,710) | \$ (10,239) | \$ (79,569) | \$ (34,796) |
| Loss per share | | | | |
| Basic | \$ (0.68) | \$ (0.22) | \$ (1.72) | \$ (0.75) |
| Diluted | \$ (0.68) | \$ (0.22) | \$ (1.72) | \$ (0.75) |
| Dividends declared per share | \$ 0.25 | \$ 0.25 | \$ 0.75 | \$ 0.75 |

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

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

| | Nine Months Ended September 30, | |
|--|--|------------------|
| | 2011 | 2010 |
| Operating Activities | | |
| Net loss | \$ (79,569) | \$ (34,796) |
| Adjustments to reconcile net loss to net cash used in operating activities | | |
| Loss on extinguishment of senior notes | 18,559 | - |
| Asset impairments | 14,090 | 3,718 |
| Stock-based compensation expense | 12,092 | 12,421 |
| Amortization of deferred marketing costs | 7,385 | 7,922 |
| Write-offs of land option deposits and pre-acquisition costs | 5,201 | 1,794 |
| Depreciation and amortization of long-lived assets | 4,713 | 3,884 |
| Other non-cash expenses | 619 | 1,680 |
| Net changes in assets and liabilities: | | |
| Restricted cash | (262) | (28) |
| Home sales and other receivables | (1,452) | (9,356) |
| Income taxes receivable | 17,566 | 144,502 |
| Mortgage loans held-for-sale | 22,813 | 14,154 |
| Housing completed or under construction | 53,737 | (158,304) |
| Land and land under development | (104,201) | (103,029) |
| Prepaid expenses and other assets | (11,419) | (21,850) |
| Accounts payable | (7,723) | 14,683 |
| Accrued liabilities and related party liabilities | (32,892) | (14,986) |
| Net cash used in operating activities | (80,743) | (137,591) |
| Investing Activities | | |
| Purchase of marketable securities | (431,011) | (796,334) |
| Maturity of marketable securities | 553,071 | 129,519 |
| Sales of marketable securities | 290,819 | 77,340 |
| Purchase of property and equipment and other | (31,717) | (7,651) |
| Net cash provided by (used in) investing activities | 381,162 | (597,126) |
| Financing Activities | | |
| Extinguishment of senior notes | (254,903) | - |
| Payments on mortgage repurchase facility | (56,454) | (131,142) |
| Advances on mortgage repurchase facility | 41,728 | 113,182 |
| Dividend payments | (35,560) | (35,355) |
| Proceeds from issuance of senior notes | - | 242,288 |
| Proceeds from exercise of stock options | 46 | 53 |
| Net cash (used in) provided by financing activities | (305,143) | 189,026 |
| Net decrease in cash and cash equivalents | (4,724) | (545,691) |
| Cash and cash equivalents | | |
| Beginning of period | 572,225 | 1,234,252 |

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| | | |
|---------------|------------|------------|
| End of period | \$ 567,501 | \$ 688,561 |
|---------------|------------|------------|

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

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Table of Contents**M.D.C. HOLDINGS, INC.****Notes to Unaudited Consolidated Financial Statements (Continued)****1. Basis of Presentation**

The Unaudited Consolidated Financial Statements of M.D.C. Holdings, Inc. (MDC or the Company, which refers to M.D.C. Holdings, Inc. and its subsidiaries) have been prepared, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC). Accordingly, they do not include all information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. These statements reflect all normal and recurring adjustments which, in the opinion of management, are necessary to present fairly the financial position, results of operations and cash flows of MDC at September 30, 2011 and for all periods presented. These statements should be read in conjunction with MDC's Consolidated Financial Statements and Notes thereto included in MDC's Annual Report on Form 10-K for the year ended December 31, 2010, filed with the SEC on February 11, 2011.

The Consolidated Statements of Operations for the three and nine months ended September 30, 2011 and Consolidated Statements of Cash Flows for the nine months ended September 30, 2011 are not necessarily indicative of the results to be expected for the full year. Refer to the economic conditions described under the caption Risk Factors in Part II, Item 1A of this Quarterly Report on Form 10-Q and Risk Factors Relating to our Business in Item 1A of the Company's December 31, 2010 Annual Report on Form 10-K.

2. Fair Value Measurements

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

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

Cash and Cash Equivalents. For cash and cash equivalents, the fair value approximates carrying value.

Marketable Securities. The Company's marketable securities consist of fixed rate and floating rate interest earning securities, primarily: (1) debt securities, which may include, among others, United States government and government agency debt and corporate debt; (2) holdings in mutual fund equity securities and (3) deposit securities, which may include, among others, certificates of deposit and time deposits. As of September 30, 2011 all of the Company's marketable securities are treated as available-for-sale investments and, as such, the Company has recorded all of its marketable securities at fair value with changes in fair value recorded as a component of accumulated other comprehensive (loss) income.

As of December 31, 2010, the Company classified certain marketable securities as held-to-maturity as it had, at the time of purchase, the intent and ability to hold those securities until maturity. In July 2011, the Company sold \$100 million of held-to-maturity marketable securities prior to their maturity and, as a result, the Company now classifies its debt securities, which were previously accounted for as held-to-maturity, as available-for-sale.

The following table sets forth the Company's amortized cost and fair values of marketable securities which were re-classified from held-to-maturity to available-for-sale (in thousands) during 2011. The fair values of the Company's marketable securities are based upon Level 1 and Level 2 fair value inputs.

| | September 30, 2011 | | December 31, 2010 | |
|---|--------------------|----------------------|-------------------|----------------------|
| | Amortized Cost | Estimated Fair Value | Amortized Cost | Estimated Fair Value |
| Debt securities - maturity less than 1 year | \$ 65,690 | \$ 65,534 | \$ 469,318 | \$ 469,956 |
| Debt securities - maturity 1 to 5 years | 20,341 | 20,284 | 120,078 | 121,406 |

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| | | | | |
|-------|-----------|-----------|------------|------------|
| Total | \$ 86,031 | \$ 85,818 | \$ 589,396 | \$ 591,362 |
|-------|-----------|-----------|------------|------------|

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

The following table sets forth the amortized cost and estimated fair value of the Company's other available-for-sale marketable securities (in thousands).

| | September 30, 2011 | | December 31, 2010 | |
|-------------------|--------------------|----------------------|-------------------|----------------------|
| | Amortized Cost | Estimated Fair Value | Amortized Cost | Estimated Fair Value |
| Equity securities | \$ 166,460 | \$ 155,266 | \$ 103,189 | \$ 105,304 |
| Debt securities | 297,024 | 294,410 | 271,260 | 274,029 |
| Total | \$ 463,484 | \$ 449,676 | \$ 374,449 | \$ 379,333 |

As of September 30, 2011, the Company's marketable securities were in an unrealized loss position of \$14.0 million including three mutual fund securities that have a combined unrealized loss of \$11.2 million and various debt securities that are in an unrealized position of \$2.8 million as of September 30, 2011. These debt and equity securities have been in this unrealized loss position for less than 12 months. The Company has evaluated the decline in the market value in the debt and equity securities in order to determine if this decline is other than temporary. Based upon this evaluation, the Company does not believe the decline in value is permanent and, as such, an other-than-temporary impairment has not been recorded.

Mortgage Loans Held-for-Sale, Net. As of September 30, 2011, the primary components of the Company's mortgage loans held-for-sale that are measured at fair value on a recurring basis are: (1) mortgage loans held-for-sale under commitments to sell; and (2) mortgage loans held-for-sale not under commitments to sell. At September 30, 2011 and December 31, 2010, the Company had \$39.9 million and \$56.9 million, respectively, of mortgage loans held-for-sale under commitments to sell for which fair value was based upon a Level 2 input being the quoted market prices for those mortgage loans. At September 30, 2011 and December 31, 2010, the Company had \$2.4 million and \$8.2 million, respectively, of mortgage loans held-for-sale that were not under commitments to sell and, as such, their fair value was based upon Level 2 fair value inputs, primarily estimated market price received from an outside party.

Inventories. The Company records its homebuilding inventory (housing completed or under construction and land and land under development) at fair value only when the estimated fair value of a subdivision is less than its carrying value. The Company determines the estimated fair value of each impaired subdivision either by: (1) calculating the present value of the estimated future cash flows at discount rates that are commensurate with the risk of the subdivision under evaluation; or (2) assessing what the market value of the land is in its current condition by considering the estimated price a willing buyer would pay for the land (other than in a forced liquidation), and recent land purchase transactions that the Company believes are indicators of fair value. These estimates are dependent on specific market or sub-market conditions for each subdivision. Local market-specific conditions that may impact these estimates for a subdivision include, among other things: (1) forecasted base selling prices and home sales incentives; (2) estimated land development costs and home cost of construction; (3) the current sales pace for active subdivisions; (4) changes by management in the sales strategy of a given subdivision; and (5) the level of competition within a market or sub-market, including publicly available home sales prices and home sales incentives offered by our competitors. The estimated fair values of impaired subdivisions are based upon Level 3 inputs. The fair value of the Company's inventory that was impaired at September 30, 2011 is as follows (in thousands).

| | Land and Land Under Development | Housing Completed or Under Construction | Total Fair Value of Impaired Inventory |
|----------|---------------------------------|---|--|
| West | \$ 9,115 | \$ 4,437 | 13,552 |
| Mountain | 808 | 1,500 | 2,308 |
| East | - | - | - |

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| | | | |
|--------------------|-----------|----------|-----------|
| Other Homebuilding | 1,238 | 1,466 | 2,704 |
| Consolidated | \$ 11,161 | \$ 7,403 | \$ 18,564 |

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

Related Party Assets. The Company's related party assets are debt security bonds that it acquired from a quasi-municipal corporation in the state of Colorado. The Company has estimated the fair value of the related party assets based upon discounted cash flows as the Company does not believe there is a readily available market for such assets. The estimated cash flows from the bonds are ultimately based upon the Company's estimated cash flows associated with the building, selling and closing of homes in one of its Colorado subdivisions. The estimated fair values of these assets are based upon Level 3 cash flow inputs. Based upon this evaluation, the estimated fair value of the related party assets approximates its carrying value.

Mortgage Repurchase Facility. The Company's Mortgage Repurchase Facility (as defined below) is at floating rates or at fixed rates that approximate current market rates and have relatively short-term maturities. The fair value approximates carrying value.

Senior Notes. The following table states the estimated fair values of the Company's senior notes (in thousands).

| | September 30, 2011 | | December 31, 2010 | |
|--|--------------------|----------------------|-------------------|----------------------|
| | Recorded Amount | Estimated Fair Value | Recorded Amount | Estimated Fair Value |
| 7% Senior Notes due 2012 | \$ 86,110 | \$ 92,347 | \$ 149,650 | \$ 160,493 |
| 5 1/2% Senior Notes due 2013 | 176,615 | 189,782 | 349,748 | 362,198 |
| 5 3/8% Medium Term Senior Notes due 2014 | 249,394 | 265,000 | 249,266 | 255,683 |
| 5 3/8% Medium Term Senior Notes due 2015 | 249,848 | 261,675 | 249,821 | 251,450 |
| 5 5/8% Senior Notes due 2020 | 244,689 | 221,675 | 244,330 | 244,400 |
| Total | \$ 1,006,656 | \$ 1,030,479 | \$ 1,242,815 | \$ 1,274,224 |

On July 7, 2011, the Company completed a debt tender offer extinguishing \$63.7 million of its 7% Senior Notes due 2012 and \$173.3 million of its 5 1/2% Senior Notes due 2013. The Company paid \$254.9 million for the acquired notes.

As further described in Note 16, in October 2011, the Company redeemed the remaining \$86.1 million of its outstanding 7% Senior Notes due 2012 and announced that it will redeem the remaining \$176.6 million outstanding balance of its 5 1/2% Senior Notes due 2013 in November 2011.

The estimated fair value of the 7% Senior Notes due 2012 and 5 1/2% Senior Notes due 2013 are based upon the amounts paid and expected to be paid up redemption in October and November, respectively. The estimated fair value of the remaining senior notes is based on Level 2 fair value inputs, including market prices of bonds in the homebuilding sector.

3. Inventory Impairments

The following table sets forth, by reportable segment, the asset impairments recorded during the three and nine months ended September 30, 2011 (in thousands).

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

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|----------------------------------|-----------------|---------------------------------|-----------------|
| | 2011 | 2010 | 2011 | 2010 |
| Land and Land Under Development | | | | |
| West | \$ 1,193 | \$ 2,490 | \$ 7,112 | \$ 2,490 |
| Mountain | 550 | - | 1,786 | - |
| East | - | - | 285 | - |
| Other Homebuilding | 1,519 | - | 1,519 | - |
| Subtotal | 3,262 | 2,490 | 10,702 | 2,490 |
| Housing Completed or Under Construction | | | | |
| West | 484 | 1,143 | 1,438 | 1,143 |
| Mountain | 210 | - | 449 | - |
| East | - | - | - | - |
| Other Homebuilding | 93 | - | 93 | - |
| Subtotal | 787 | 1,143 | 1,980 | 1,143 |
| Other Assets | 643 | 85 | 1,408 | 85 |
| Consolidated Asset Impairments | \$ 4,692 | \$ 3,718 | \$ 14,090 | \$ 3,718 |

The Company recorded \$4.7 million and \$14.1 million of asset impairments during the three and nine months ended September 30, 2011, which resulted from a decline in the market value of land and homes in certain subdivisions of the West, Mountain and Other Homebuilding segments. The Company recorded \$3.7 million of asset impairments during the three and nine months ended September 30, 2010 which resulted from a decline in the market value of land and homes in several subdivisions of our West segment.

4. Derivative Financial Instruments

The Company utilizes certain derivative instruments in the normal course of business, which primarily include commitments to originate mortgage loans (interest rate lock commitments or locked pipeline) and forward sales of mortgage-backed securities commitments, both of which typically are short-term in nature. Forward sales securities commitments and private investor sales commitments are utilized to hedge changes in fair value of mortgage loan inventory and commitments to originate mortgage loans. At September 30, 2011, the Company had \$89.1 million in interest rate lock commitments and \$38.0 million in forward sales of mortgage-backed securities.

The Company records its mortgage loans held-for-sale at fair value to achieve matching of the changes in the fair value of its derivative instruments with the changes in fair values of the loans it is hedging, without having to designate its derivatives as hedging instruments. For forward sales commitments, as well as commitments to originate mortgage loans that are still outstanding at the end of a reporting period, the Company records the fair value of the derivatives in other revenue in the Consolidated Statements of Operations with an offset to either prepaid and other assets or accrued liabilities in the Consolidated Balance Sheets, depending on the nature of the change. The changes in fair value of the Company's derivatives were not material during the three and nine months ended September 30, 2011 and 2010.

Table of Contents**M.D.C. HOLDINGS, INC.****Notes to Unaudited Consolidated Financial Statements (Continued)****5. Balance Sheet Components**

The following table sets forth information relating to prepaid expenses and other assets, net (in thousands).

| | September 30, 2011 | December 31, 2010 |
|--------------------------------|-----------------------|----------------------|
| Deferred marketing costs | \$ 22,444 | \$ 22,736 |
| Land option deposits | 9,192 | 11,606 |
| Goodwill | 6,458 | - |
| Deferred debt issue costs, net | 3,850 | 5,021 |
| Prepaid expenses | 5,771 | 5,935 |
| IRS deposit (See Note 13) | - | 35,562 |
| Other | 6,382 | 4,533 |
| Total | \$ 54,097 | \$ 85,393 |

The following table sets forth information relating to accrued liabilities (in thousands).

| | September 30, 2011 | December 31, 2010 |
|---|-----------------------|----------------------|
| Accrued liabilities | | |
| Insurance reserves | \$ 51,575 | \$ 52,901 |
| Warranty reserves | 28,803 | 34,704 |
| Accrued executive deferred compensation | 23,301 | 20,956 |
| Accrued interest payable | 16,264 | 17,822 |
| Accrued compensation and related expenses | 13,966 | 22,659 |
| Legal accruals | 12,673 | 14,230 |
| Land development and home construction accruals | 8,376 | 12,450 |
| Mortgage loan loss reserves | 6,961 | 6,881 |
| Customer and escrow deposits | 6,678 | 4,523 |
| Liability for unrecognized tax benefits | 3,505 | 55,850 |
| Other accrued liabilities | 17,059 | 17,753 |
| Total accrued liabilities | \$ 189,161 | \$ 260,729 |

6. Loss Per Share

A company that has participating security holders (for example, unvested restricted stock that has nonforfeitable dividend rights) is required to utilize the two-class method for purposes of calculating earnings (loss) per share (EPS). The two-class method is an allocation of earnings/(loss) between the holders of common stock and a company's participating security holders. Under the two-class method, earnings/(loss) for the reporting period are allocated between common shareholders and other security holders, based on their respective rights to receive distributed earnings (i.e. dividends) and undistributed earnings (i.e. net income or loss). Currently, the Company has one class of security and has participating security holders consisting of shareholders of unvested restricted stock. The basic and diluted EPS calculations are shown below (in

thousands, except per share amounts).

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

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|----------------------------------|-------------|---------------------------------|-------------|
| | 2011 | 2010 | 2011 | 2010 |
| Basic and Diluted Loss Per Common Share | | | | |
| Net loss | \$ (31,710) | \$ (10,239) | \$ (79,569) | \$ (34,796) |
| Less: distributed and undistributed earnings allocated to participating securities | (215) | (135) | (580) | (394) |
| Net loss attributable to common stockholders | \$ (31,925) | \$ (10,374) | \$ (80,149) | \$ (35,190) |
| Basic and diluted weighted-average shares outstanding | 46,737 | 46,625 | 46,717 | 46,619 |
| Basic Loss Per Common Share | \$ (0.68) | \$ (0.22) | \$ (1.72) | \$ (0.75) |
| Dilutive Loss Per Common Share | \$ (0.68) | \$ (0.22) | \$ (1.72) | \$ (0.75) |

Diluted EPS includes the dilutive effect of common stock equivalents and is computed using the weighted-average number of common stock and common stock equivalents outstanding during the reporting period. Common stock equivalents include stock options and unvested restricted stock. Diluted EPS for the three and nine months ending September 30, 2011 and 2010 excluded common stock equivalents because the effect of their inclusion would be anti-dilutive, or would decrease the reported loss per share. Using the treasury stock method, the weighted-average common stock equivalents excluded from diluted EPS were 0.2 million and 0.4 million shares during the three and nine months ended September 30, 2011, respectively, and 0.4 million shares during the three and nine months ended September 30, 2010.

7. Interest Activity

The Company capitalizes interest on its senior notes associated with its qualifying assets, which includes land and land under development that is actively being developed and homes under construction through the completion of construction. When construction of a home is complete, such home is no longer considered to be a qualifying asset and interest is no longer capitalized on that home. The Company expensed \$3.7 million and \$9.0 million of interest primarily associated with interest incurred on its senior notes during the three months ended September 30, 2011 and 2010, respectively, and \$19.8 million and \$28.8 million during the nine months ended September 30, 2011 and 2010, respectively, that could not be capitalized.

Interest activity is shown below (in thousands).

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|----------------------------------|-----------|---------------------------------|-----------|
| | 2011 | 2010 | 2011 | 2010 |
| Total Interest Incurred | | | | |
| Corporate | \$ 14,474 | \$ 18,187 | \$ 50,744 | \$ 53,276 |
| Financial Services and Other | 54 | 183 | 177 | 389 |
| Total interest incurred | \$ 14,528 | \$ 18,370 | \$ 50,921 | \$ 53,665 |
| Total Interest Capitalized | | | | |
| Interest capitalized, beginning of period | \$ 49,058 | \$ 32,420 | \$ 38,446 | \$ 28,339 |
| Interest capitalized | 10,833 | 9,370 | 31,102 | 24,855 |

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| | | | | |
|--|-----------|-----------|-----------|-----------|
| Previously capitalized interest included in home cost of sales | (5,140) | (5,581) | (14,797) | (16,985) |
| Interest capitalized, end of period | \$ 54,751 | \$ 36,209 | \$ 54,751 | \$ 36,209 |

8. Warranty Reserves

The Company records expenses and warranty reserves for general and structural warranty claims, as well as reserves for known, unusual warranty-related expenditures. The establishment of warranty reserves is primarily

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

based on an actuarial based analysis that includes known facts and interpretations of circumstances, including, among other things, the Company's trends in historical warranty payment levels and warranty payments for claims not considered to be normal and recurring. Warranty payments incurred for an individual house may differ from the related reserve established for the home at the time it was closed. The actual disbursements for warranty claims are evaluated in the aggregate to determine if an adjustment to the historical warranty reserve should be recorded.

The following table summarizes the warranty reserve activity for the three and nine months ended September 30, 2011 and 2010 (in thousands).

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--------------------------------|----------------------------------|-----------|---------------------------------|-----------|
| | 2011 | 2010 | 2011 | 2010 |
| Balance at beginning of period | \$ 31,200 | \$ 51,986 | \$ 34,704 | \$ 59,022 |
| Expense provisions | 1,265 | 1,403 | 3,140 | 4,613 |
| Cash payments | (2,707) | (2,944) | (5,823) | (7,584) |
| Adjustments | (955) | (7,197) | (3,218) | (12,803) |
| Balance at end of period | \$ 28,803 | \$ 43,248 | \$ 28,803 | \$ 43,248 |

The favorable warranty adjustments that were recorded as a reduction to home cost of sales in the Consolidated Statements of Operations during the three and nine months ended September 30, 2011 and 2010 were primarily the result of favorable experience in the amount of warranty payments incurred on previously closed homes.

9. Insurance Reserves

The Company records expenses and liabilities for losses and loss adjustment expenses for claims associated with: (1) insurance policies with Allegiant Insurance Company, Inc., A Risk Retention Group (Allegiant) and re-insurance agreements issued by StarAmerican Insurance Ltd. (StarAmerican); (2) self-insurance, including workers compensation; and (3) deductible amounts under the Company's insurance policies. The establishment of the provisions for outstanding losses and loss adjustment expenses is based on actuarial studies that include known facts and interpretations of circumstances, including the Company's experience with similar cases and historical trends involving claim payment patterns, pending levels of unpaid claims, product mix or concentration, claim severity, frequency patterns such as those caused by natural disasters, fires, or accidents, depending on the business conducted, and changing regulatory and legal environments.

The following table summarizes the insurance reserve activity for the three and nine months ended September 30, 2011 and 2010 (in thousands).

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--------------------------------|----------------------------------|-----------|---------------------------------|-----------|
| | 2011 | 2010 | 2011 | 2010 |
| Balance at beginning of period | \$ 52,310 | \$ 48,312 | \$ 52,901 | \$ 51,606 |
| Expense provisions | 645 | 841 | 1,712 | 2,655 |
| Cash payments | (1,380) | (212) | (3,386) | (5,320) |
| Adjustments | - | - | 348 | - |
| Balance at end of period | \$ 51,575 | \$ 48,941 | \$ 51,575 | \$ 48,941 |

10. Information on Business Segments

The Company's operating segments are defined as a component of an enterprise for which discrete financial information is available and is reviewed regularly by the chief operating decision-maker, or decision-making group, to evaluate performance and make operating decisions. The Company has identified its chief operating decision-makers (CODMs) as two key executives the Chief Executive Officer and the Chief Operating Officer.

The Company has identified each homebuilding subdivision as an operating segment as each homebuilding subdivision engages in business activities from which it earns revenue, primarily from the sale of single-family

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

detached homes, generally to first-time and first-time move-up homebuyers. Subdivisions in the reportable segments noted below have been aggregated because they are similar in the following regards: (1) economic characteristics; (2) housing products; (3) class of homebuyer; (4) regulatory environments; and (5) methods used to construct and sell homes. The Company's homebuilding reportable segments are as follows:

- (1) West (Arizona, California, Nevada and Washington)
- (2) Mountain (Colorado and Utah)
- (3) East (Delaware Valley, Maryland and Virginia)
- (4) Other Homebuilding (Florida and Illinois)

The Company's Financial Services and Other reportable segment consists of the operations of the following operating segments: (1) HomeAmerican Mortgage Corporation (HomeAmerican); (2) Allegiant; (3) StarAmerican; (4) American Home Insurance Agency, Inc.; and (5) American Home Title and Escrow Company. These operating segments have been aggregated into one reportable segment because they do not individually exceed 10 percent of: (1) consolidated revenue; (2) the greater of (A) the combined reported profit of all operating segments that did not report a loss or (B) the positive value of the combined reported loss of all operating segments that reported losses; or (3) consolidated assets. The Company's Corporate reportable segment incurs general and administrative expenses that are not identifiable specifically to another operating segment, earns interest income on its cash, cash equivalents and marketable securities, and incurs interest expense on its senior notes.

The following table summarizes revenue for each of the Company's six reportable segments (in thousands). Inter-company adjustments noted in the revenue table below relate to mortgage loan origination fees paid by the Company's homebuilding subsidiaries to HomeAmerican on behalf of homebuyers.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|------------------------------|----------------------------------|-------------------|---------------------------------|-------------------|
| | 2011 | 2010 | 2011 | 2010 |
| Homebuilding | | | | |
| West | \$ 71,292 | \$ 66,233 | \$ 183,176 | \$ 246,563 |
| Mountain | 82,637 | 89,111 | 232,463 | 245,905 |
| East | 36,610 | 58,304 | 130,778 | 162,466 |
| Other Homebuilding | 16,678 | 7,344 | 37,486 | 33,137 |
| Total Homebuilding | 207,217 | 220,992 | 583,903 | 688,071 |
| Financial Services and Other | 5,540 | 7,932 | 17,974 | 22,696 |
| Corporate | - | - | - | - |
| Intercompany adjustments | (1,397) | (3,243) | (5,085) | (11,678) |
| Consolidated | \$ 211,360 | \$ 225,681 | \$ 596,792 | \$ 699,089 |

The following table summarizes (loss) income before income taxes for each of the Company's six reportable segments (in thousands). Inter-company supervisory fees (Supervisory Fees), which are included in (loss) income before income taxes for each reportable segment in the table below, are charged by the Company's Corporate segment to the homebuilding segments and the Financial Services and Other segment. Supervisory Fees represent costs incurred by the Company's Corporate segment associated with certain resources that support the Company's other reportable segments. Transfers, if any, between operating segments are recorded at cost.

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| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|------------------------------|----------------------------------|-------------|---------------------------------|-------------|
| | 2011 | 2010 | 2011 | 2010 |
| Homebuilding | | | | |
| West | \$ (2,584) | \$ 4,900 | \$ (18,981) | \$ 13,611 |
| Mountain | 2,988 | 520 | 552 | 6,652 |
| East | (2,518) | 2,021 | (6,819) | 1,957 |
| Other Homebuilding | (1,514) | (1,673) | (3,206) | (1,897) |
| Total Homebuilding | (3,628) | 5,768 | (28,454) | 20,323 |
| Financial Services and Other | (450) | 4,326 | 4,419 | 10,261 |
| Corporate | (30,111) | (20,688) | (63,661) | (66,119) |
| Consolidated | \$ (34,189) | \$ (10,594) | \$ (87,696) | \$ (35,535) |

The following table summarizes total assets for each of the Company's six reportable segments (in thousands). Inter-company adjustments noted in the table below relate to loans from the Company's Financial Services and Other segment to its Corporate segment. The assets in the Company's Corporate segment primarily include cash, cash equivalents and marketable securities.

| | September 30, 2011 | December 31, 2010 |
|------------------------------|-----------------------|----------------------|
| Homebuilding | | |
| West | \$ 365,759 | \$ 300,652 |
| Mountain | 289,828 | 311,833 |
| East | 224,497 | 188,693 |
| Other Homebuilding | 30,331 | 40,554 |
| Total Homebuilding | 910,415 | 841,732 |
| Financial Services and Other | 115,176 | 135,286 |
| Corporate | 1,093,523 | 1,573,408 |
| Intercompany adjustments | (4,145) | (2,657) |
| Consolidated | \$ 2,114,969 | \$ 2,547,769 |

The following table summarizes depreciation and amortization of long-lived assets and amortization of deferred marketing costs for each of the Company's six reportable segments (in thousands).

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--------------|----------------------------------|----------|---------------------------------|----------|
| | 2011 | 2010 | 2011 | 2010 |
| Homebuilding | | | | |
| West | \$ 1,102 | \$ 1,189 | \$ 3,223 | \$ 4,474 |
| Mountain | 857 | 941 | 2,618 | 2,495 |

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| | | | | |
|------------------------------|----------|----------|-----------|-----------|
| East | 393 | 454 | 1,439 | 1,405 |
| Other Homebuilding | 290 | 97 | 689 | 495 |
| Total Homebuilding | 2,642 | 2,681 | 7,969 | 8,869 |
| Financial Services and Other | 156 | 169 | 486 | 508 |
| Corporate | 1,233 | 855 | 3,643 | 2,429 |
| Consolidated | \$ 4,031 | \$ 3,705 | \$ 12,098 | \$ 11,806 |

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Table of Contents**M.D.C. HOLDINGS, INC.****Notes to Unaudited Consolidated Financial Statements (Continued)****11. Commitments and Contingencies**

The Company often is required to obtain bonds and letters of credit in support of its obligations for land development and subdivision improvements, homeowner association dues and start-up expenses, warranty work, contractor license fees and earnest money deposits. At September 30, 2011 the Company had issued and outstanding performance bonds and letters of credit totaling \$70.6 million and \$21.5 million, respectively, including \$7.8 million in letters of credit issued by HomeAmerican. In the event any such bonds or letters of credit issued by third parties are called, MDC could be obligated to reimburse the issuer of the bond or letter of credit.

Mortgage Loan Loss Reserves. In the normal course of business, the Company establishes reserves for potential losses associated with HomeAmerican's sale of mortgage loans to third-parties. These reserves are created to address repurchase and indemnity claims by third-party purchasers of the mortgage loans, which claims arise primarily out of allegations of homebuyer fraud at the time of origination of the loan. These reserves are based upon, among other matters: (1) pending claims received from third-party purchasers associated with previously sold mortgage loans; (2) a current assessment of the potential exposure associated with future claims of homebuyer fraud in mortgage loans originated in prior periods; and (3) historical loss experience. During 2011, HomeAmerican reached settlements associated with claims and potential claims to repurchase certain previously sold mortgage loans. Primarily as a result of these settlements, coupled with an increase in the volume of mortgage loans that may be subject to repurchase, the Company increased its estimated mortgage loan loss reserve by \$3.0 million and \$4.3 million during the three and nine months ended September 30, 2011, respectively. The Company's mortgage loan reserves are reflected as a component of accrued liabilities in the Consolidated Balance Sheets, and the associated expenses are included as a component of general and administrative expenses in the Consolidated Statements of Operations.

The following table summarizes the mortgage loan loss reserve activity for the three and nine months ended September 30, 2011 and 2010 (in thousands).

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--------------------------------|----------------------------------|----------|---------------------------------|----------|
| | 2011 | 2010 | 2011 | 2010 |
| Balance at beginning of period | \$ 4,100 | \$ 8,069 | \$ 6,881 | \$ 9,641 |
| Expense provisions | - | - | - | - |
| Cash payments | (174) | (563) | (4,252) | (2,135) |
| Adjustments | 3,035 | - | 4,332 | - |
| Balance at end of period | \$ 6,961 | \$ 7,506 | \$ 6,961 | \$ 7,506 |

Legal Accruals. Litigation has been filed by homeowners in West Virginia against MDC, its subsidiary Richmond American Homes of West Virginia, Inc. (RAH West Virginia) and various subcontractors alleging a failure to install functional passive radon mitigation systems in their homes. The plaintiffs seek compensatory and punitive damages and medical monitoring costs for alleged negligent construction, failure to warn, breach of warranty or contract, breach of implied warranty of habitability, fraud, and intentional and negligent infliction of emotional distress based upon alleged exposure to radon gas. The litigation includes the following actions:

Joy, et al. v. Richmond American Homes of West Virginia, Inc., et al., No. 08-C-204, Circuit Court of Jefferson County, West Virginia (Joy). This action was filed on May 16, 2008, by sixty-six plaintiffs from fifteen households. The Company and RAH West Virginia have answered and asserted cross-claims against the subcontractors for contractual and implied indemnity and contribution.

Bauer, et al. v. Richmond American Homes of West Virginia, Inc., et al., No. 08-C-431, Circuit Court of Jefferson County, West Virginia (Bauer). This action was filed on October 24, 2008, by eighty-six plaintiffs from twenty-one households. This action has been consolidated for discovery and pre-trial proceedings with the Joy action.

Saliba, et al. v. Richmond American Homes of West Virginia, Inc., et al., No. 08-C-447, Circuit Court, Jefferson County, West Virginia (Saliba). This action was filed on November 7, 2008, by thirty-five plaintiffs from nine households. This action has been consolidated for discovery and

pre-trial proceedings with the Joy action.

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M.D.C. HOLDINGS, INC.

Notes to Unaudited Consolidated Financial Statements (Continued)

By orders dated November 4 and 18, 2009, the trial court struck the answers filed by the Company and RAH West Virginia and entered judgment by default in favor of the plaintiffs on liability, with damages to be determined in a subsequent jury trial. On December 7, 2009, the Company and RAH West Virginia filed with the West Virginia Supreme Court of Appeals a motion seeking to stay the proceedings and a petition for writ of prohibition to vacate the default judgment. On June 16, 2010, the West Virginia Supreme Court of Appeals granted the Company and RAH West Virginia a writ of prohibition and vacated the trial court's sanctions orders.

On July 29, 2010, the plaintiffs filed a renewed motion for sanctions based on substantially the same alleged misconduct. On January 14, 2011 the trial court again entered an order striking the answers filed by the Company and RAH West Virginia and imposing judgment by default upon them on the claims asserted in plaintiffs' complaints (exclusive of the claim for punitive damages). As stated in the January 14, 2011 order, the cross-claims made by the Company and RAH West Virginia remain in effect.

On March 31, 2011 the West Virginia Supreme Court of Appeals declined to enter a writ of prohibition with respect to the trial court's re-entry of its judgment of default stating that the issues presented are more properly presented on appeal after full development of the record in the lower court.

Separately, additional claims have been filed by homeowners in West Virginia against the Company, RAH West Virginia and individual superintendants who had worked for RAH West Virginia. The new litigation consists of the following:

Thorin, et al. v. Richmond American Homes of West Virginia, Inc., et al., No. 10-C-154, Circuit Court of Jefferson County, West Virginia (*Thorin*). This litigation was filed on May 12, 2010, by forty plaintiffs from eleven households in Jefferson and Berkeley Counties. To date, this action has not been consolidated for any purposes with the prior three actions. The claims asserted and the relief sought in the Thorin case are substantially similar to the Joy, Bauer and Saliba cases.

MDC and RAH West Virginia believe that they have meritorious defenses to each of the lawsuits and intend to vigorously defend the actions.

Additionally, in the normal course of business, the Company is a defendant in claims primarily relating to construction defects, product liability and personal injury claims. These claims seek relief from the Company under various theories, including breach of implied and express warranty, negligence, strict liability, misrepresentation and violation of consumer protection statutes.

The Company has accrued for losses that may be incurred with respect to legal claims based upon information provided to it by its legal counsel, including counsels' on-going evaluation of the merits of the claims and defenses. Due to uncertainties in the estimation and legal process, actual results could significantly vary from those accruals. The Company had legal accruals of \$12.7 million and \$14.2 million at September 30, 2011 and December 31, 2010, respectively.

12. Line of Credit and Total Debt Obligations

Mortgage Lending. HomeAmerican has a Master Repurchase Agreement, which was amended in September 2011 and extended until September 27, 2012 (the Mortgage Repurchase Facility), with U.S. Bank National Association (USBNA). The Mortgage Repurchase Facility provides liquidity to HomeAmerican by providing for the sale of eligible mortgage loans to USBNA with an agreement by HomeAmerican to repurchase the mortgage loans at a future date. Until such mortgage loans are transferred back to HomeAmerican, the documents relating to such loans are held by USBNA, as custodian, pursuant to the Custody Agreement (Custody Agreement), dated as of November 12, 2008, by and between HomeAmerican and USBNA. As of September 30, 2011, the Mortgage Repurchase Facility has a maximum aggregate commitment of \$50 million, reduced from \$70 million through the fourth amendment in September 2011. At September 30, 2011 and December 31, 2010, the Company had \$10.7 million and \$25.4 million, respectively, of mortgage loans that the Company was obligated to repurchase under its Mortgage Repurchase Facility. Mortgage loans that the Company is obligated to repurchase under the Mortgage Repurchase Facility are accounted for as a

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

debt financing arrangement and are reported as mortgage repurchase facility on the Consolidated Balance Sheets. Advances under the Mortgage Repurchase Facility carry a Pricing Rate equal to the greater of (i) the LIBOR Rate (as defined in the Mortgage Repurchase Facility) plus 2.5%, or (ii) 3.75%. At HomeAmerican's option the Balance Funded Rate (equal to 3.75%) may be applied to advances under the Mortgage Repurchase Facility provided the applicable Buyer is holding sufficient Qualifying Balances. The foregoing terms are defined in the Mortgage Repurchase Facility.

The Company's senior notes are not secured and, while the senior note indentures contain some restrictions on secured debt and other transactions, they do not contain financial covenants. The Company's senior notes are fully and unconditionally guaranteed on an unsecured basis, jointly and severally, by most of its homebuilding segment subsidiaries.

The Company's debt obligations at September 30, 2011 and December 31, 2010 are as follows (in thousands):

| | September 30, 2011 | December 31, 2010 |
|--|-----------------------|----------------------|
| 7% Senior Notes due 2012 | \$ 86,110 | \$ 149,650 |
| 5 1/2% Senior Notes due 2013 | 176,615 | 349,748 |
| 5 3/8% Medium-Term Senior Notes due 2014 | 249,394 | 249,266 |
| 5 3/8% Medium-Term Senior Notes due 2015 | 249,848 | 249,821 |
| 5 5/8% Senior Notes due 2020 | 244,689 | 244,330 |
| Total Senior Notes, net | 1,006,656 | 1,242,815 |
| Mortgage repurchase facility | 10,708 | 25,434 |
| Total Debt | \$ 1,017,364 | \$ 1,268,249 |

On July 7, 2011, the Company completed a debt tender offer extinguishing \$63.7 million of its 7% Senior Notes due 2012 and \$173.3 million of its 5 1/2% Senior Notes due 2013. The Company paid \$254.9 million for the acquired notes and, as a result of the tender, the Company recorded an \$18.6 million charge during the 2011 third quarter.

As further described in Note 16, in October 2011, the Company redeemed the remaining \$86.1 million of its outstanding 7% Senior Notes due 2012 and announced that it will redeem the remaining \$176.6 million outstanding balance of its 5 1/2% Senior Notes due 2013 in November 2011.

13. Income Taxes

The Company is required, at the end of each interim period, to estimate its annual effective tax rate for the fiscal year and use that rate to provide for income taxes for the current year-to-date reporting period. Due to the effects of the deferred tax valuation allowance and changes in unrecognized tax benefits, the Company's effective tax rates in 2011 and 2010 are not meaningful as the income tax benefit is not directly correlated to the amount of pretax loss. The income tax benefits of \$2.5 million and \$8.1 million during the three and nine months ended September 30, 2011, respectively, resulted primarily from our 2011 second and third quarter settlement of various state income tax matters and our 2011 first quarter settlement with the IRS on its audit of the 2004 and 2005 federal income tax returns. The Company's income tax benefits during the three and nine months ended September 30, 2010 were not material to our results of operations.

The Company is required to recognize the financial statement effects of a tax position when it is more likely than not (defined as a likelihood of more than 50%), based on the technical merits, that the position will be sustained upon examination. Any difference between the income tax return position and the benefit recognized in the financial statements results in a liability for unrecognized tax benefits. The Company's liability

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for unrecognized tax benefits was \$3.5 million and \$55.9 million at September 30, 2011 and December 31, 2010, respectively. This decrease resulted primarily from the Company's settlement with the IRS on the audit of its 2004 and 2005 federal income tax returns and settlement of various state income tax matters.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of the assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The increase in the Company's total deferred tax asset at September 30, 2011 (per the table below) resulted primarily from an increase in the Company's net operating loss carry forwards.

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A valuation allowance is recorded against a deferred tax asset if, based on the weight of available evidence, it is more-likely-than-not (a likelihood of more than 50%) that some portion, or all, of the deferred tax asset will not be realized. At September 30, 2011 and December 31, 2010, the Company had a full valuation allowance recorded against its net deferred tax assets. The Company's future realization of its deferred tax assets ultimately depends upon the existence of sufficient taxable income in the carryback or carryforward periods under the tax laws. The Company will continue analyzing, in subsequent reporting periods, the positive and negative evidence in determining the expected realization of its deferred tax assets.

The tax effects of significant temporary differences that give rise to the net deferred tax asset are as follows (in thousands).

| | September 30, 2011 | December 31, 2010 |
|--|-----------------------|----------------------|
| Deferred tax assets | | |
| Federal net operating loss carryforward | \$ 118,716 | \$ 73,189 |
| State net operating loss carryforward | 51,286 | 47,041 |
| Asset impairment charges | 35,794 | 46,118 |
| Stock-based compensation expense | 26,041 | 22,777 |
| Warranty, litigation and other reserves | 23,304 | 27,635 |
| Accrued liabilities | 10,450 | 9,789 |
| Alternative minimum tax and other tax credit carryforwards | 10,296 | 10,296 |
| Unrealized loss on marketable securities | 5,398 | - |
| Inventory, additional costs capitalized for tax purposes | 3,264 | 5,368 |
| Other | 1,228 | 3,037 |
| Total deferred tax assets | 285,777 | 245,250 |
| Valuation allowance | (274,380) | (231,379) |
| Total deferred tax assets, net of valuation allowance | 11,397 | 13,871 |
| Deferred tax liabilities | | |
| Deferred revenue | 5,591 | 6,401 |
| Unrealized gain | - | 1,880 |
| Inventory, additional costs capitalized for financial statement purposes | 546 | 604 |
| Accrued liabilities | 383 | 713 |
| Other, net | 4,877 | 4,273 |
| Total deferred tax liabilities | 11,397 | 13,871 |
| Net deferred tax asset | \$ - | \$ - |

14. Variable Interest Entities

In the normal course of business, the Company enters into lot option purchase contracts (Option Contracts), generally through a deposit of cash or letter of credit, for the right to purchase land or lots at a future point in time with predetermined terms. The use of such land option and other contracts generally allows the Company to reduce the risks associated with direct land ownership and development, reduces the Company's capital and financial commitments, including interest and other carrying costs, and minimizes the amount of the Company's land inventories on its consolidated balance sheets. The Company's obligation with respect to Option Contracts generally is limited to forfeiture of the related cash

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deposits and/or letters of credit. At September 30, 2011 the Company had cash deposits and letters of credit of \$8.9 million and \$5.1 million, respectively, at risk associated with 2,385 lots under Option Contracts.

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Table of Contents**M.D.C. HOLDINGS, INC.****Notes to Unaudited Consolidated Financial Statements (Continued)****15. Other Comprehensive Loss**

Total other comprehensive loss includes net loss and unrealized holding gains or losses on the Company's available-for-sale marketable securities. The following table sets forth the Company's other comprehensive loss during the three and nine months ended September 30, 2011 and 2010 (in thousands).

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--------------------------------|----------------------------------|-------------|---------------------------------|-------------|
| | 2011 | 2010 | 2011 | 2010 |
| Net loss | \$ (31,710) | \$ (10,239) | \$ (79,569) | \$ (34,796) |
| Unrealized holding (loss) gain | (20,237) | 5,917 | (18,905) | 4,623 |
| Total other comprehensive loss | \$ (51,947) | \$ (4,322) | \$ (98,474) | \$ (30,173) |

16. Subsequent Events

On October 19, 2011, the Company redeemed the remaining \$86.1 million of its outstanding 7% Senior Notes due 2012. The Company paid \$94.6 million as a result of this redemption pursuant to the terms of the 7% Senior Notes and will record a loss on redemption of \$8.6 million during the 2011 fourth quarter. Additionally, the Company announced its intent to redeem the remaining \$176.7 million outstanding balance of its 5 1/2% Senior Notes due 2013 in November 2011. The Company anticipates recording a loss on redemption of these 5 1/2% Senior Notes of approximately \$13.2 million pursuant to the terms of the 5 1/2% Senior Notes during the 2011 fourth quarter.

17. Supplemental Guarantor Information

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

M.D.C. Land Corporation
 RAH of Florida, Inc.
 Richmond American Construction, Inc.
 Richmond American Homes of Arizona, Inc.
 Richmond American Homes of Colorado, Inc.
 Richmond American Homes of Delaware, Inc.
 Richmond American Homes of Florida, LP
 Richmond American Homes of Illinois, Inc.
 Richmond American Homes of Maryland, Inc.
 Richmond American Homes of Nevada, Inc.
 Richmond American Homes of New Jersey, Inc.
 Richmond American Homes of Pennsylvania, Inc.
 Richmond American Homes of Utah, Inc.
 Richmond American Homes of Virginia, Inc.

Subsidiaries that do not guarantee the Company's senior notes (collectively, the "Non-Guarantor Subsidiaries") primarily include:

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American Home Insurance
American Home Title
HomeAmerican
StarAmerican
Allegiant
Richmond American Homes of West Virginia, Inc.
Richmond American Homes of Washington, Inc.

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M.D.C. HOLDINGS, INC.

Notes to Unaudited Consolidated Financial Statements (Continued)

The Company has determined that separate, full financial statements of the Guarantor Subsidiaries would not be material to investors and, accordingly, supplemental financial information for the Guarantor Subsidiaries is presented.

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Table of Contents**M.D.C. HOLDINGS, INC.****Notes to Unaudited Consolidated Financial Statements (Continued)****Supplemental Condensed Combining Balance Sheet****September 30, 2011****(In thousands)**

| | MDC | Guarantor Subsidiaries | Non- Guarantor Subsidiaries | Eliminating Entries | Consolidated MDC |
|---|---------------------|-----------------------------------|--|--------------------------------|-----------------------------|
| Assets | | | | | |
| Cash and cash equivalents | \$ 532,302 | \$ 2,845 | \$ 32,354 | \$ - | \$ 567,501 |
| Marketable securities | 503,828 | - | 31,666 | - | 535,494 |
| Restricted cash | - | 682 | - | - | 682 |
| Receivables | 4,645 | 12,499 | 4,709 | (2,439) | 19,414 |
| Mortgage loans held-for-sale, net | - | - | 42,301 | - | 42,301 |
| Inventories, net | | | | | |
| Housing completed or under construction | - | 318,737 | 14,613 | - | 333,350 |
| Land and land under development | - | 498,830 | 18,507 | - | 517,337 |
| Investment in subsidiaries | 123,615 | - | - | (123,615) | - |
| Other assets, net | 48,619 | 38,722 | 12,390 | (841) | 98,890 |
| Total Assets | \$ 1,213,009 | \$ 872,315 | \$ 156,540 | \$ (126,895) | \$ 2,114,969 |
| Liabilities | | | | | |
| Accounts payable and related party liabilities | \$ 2,804 | \$ 24,731 | \$ 2,492 | \$ (2,662) | \$ 27,365 |
| Accrued liabilities | 69,904 | 54,611 | 66,133 | (618) | 190,030 |
| Advances and notes payable to parent and subsidiaries | (746,565) | 732,473 | 14,092 | - | - |
| Mortgage repurchase facility | - | - | 10,708 | - | 10,708 |
| Senior notes, net | 1,006,656 | - | - | - | 1,006,656 |
| Total Liabilities | 332,799 | 811,815 | 93,425 | (3,280) | 1,234,759 |
| Stockholders Equity | 880,210 | 60,500 | 63,115 | (123,615) | 880,210 |
| Total Liabilities and Stockholders Equity | \$ 1,213,009 | \$ 872,315 | \$ 156,540 | \$ (126,895) | \$ 2,114,969 |

Table of Contents**M.D.C. HOLDINGS, INC.****Notes to Unaudited Consolidated Financial Statements (Continued)****Supplemental Condensed Combining Balance Sheet****December 31, 2010****(In thousands)**

| | MDC | Guarantor Subsidiaries | Non- Guarantor Subsidiaries | Eliminating Entries | Consolidated MDC |
|---|---------------------|-----------------------------------|--|--------------------------------|-----------------------------|
| Assets | | | | | |
| Cash and cash equivalents | \$ 535,035 | \$ 4,287 | \$ 32,903 | \$ - | \$ 572,225 |
| Marketable securities | 938,471 | - | 30,258 | - | 968,729 |
| Restricted cash | - | 420 | - | - | 420 |
| Receivables | 14,402 | 8,071 | 194 | (2,657) | 20,010 |
| Mortgage loans held-for-sale, net | - | - | 65,114 | - | 65,114 |
| Inventories, net | | | | | |
| Housing completed or under construction | - | 372,422 | - | - | 372,422 |
| Land and land under development | - | 415,237 | - | - | 415,237 |
| Investment in subsidiaries | 110,065 | - | - | (110,065) | - |
| Other assets, net | 88,267 | 42,288 | 3,057 | - | 133,612 |
| Total Assets | \$ 1,686,240 | \$ 842,725 | \$ 131,526 | \$ (112,722) | \$ 2,547,769 |
| Liabilities | | | | | |
| Accounts payable and related party liabilities | \$ 2,747 | \$ 34,553 | \$ 465 | \$ (2,657) | \$ 35,108 |
| Accrued liabilities | 130,960 | 65,622 | 64,147 | - | 260,729 |
| Advances and notes payable to parent and subsidiaries | (673,965) | 671,190 | 2,775 | - | - |
| Mortgage repurchase facility | - | - | 25,434 | - | 25,434 |
| Senior notes, net | 1,242,815 | - | - | - | 1,242,815 |
| Total Liabilities | 702,557 | 771,365 | 92,821 | (2,657) | 1,564,086 |
| Stockholders Equity | 983,683 | 71,360 | 38,705 | (110,065) | 983,683 |
| Total Liabilities and Stockholders Equity | \$ 1,686,240 | \$ 842,725 | \$ 131,526 | \$ (112,722) | \$ 2,547,769 |

Table of Contents**M.D.C. HOLDINGS, INC.****Notes to Unaudited Consolidated Financial Statements (Continued)****Supplemental Condensed Combining Statements of Operations****Three Months Ended September 30, 2011****(In thousands)**

| | MDC | Guarantor Subsidiaries | Non- Guarantor Subsidiaries | Eliminating Entries | Consolidated MDC |
|---|--------------------|-----------------------------------|--|--------------------------------|-----------------------------|
| Revenue | | | | | |
| Home sales revenue | \$ - | \$ 193,128 | \$ 13,154 | \$ (1,396) | \$ 204,886 |
| Land sales and other revenue | - | 923 | 5,551 | - | 6,474 |
| Equity in (loss) income of subsidiaries | (4,022) | - | - | 4,022 | - |
| Total revenue | (4,022) | 194,051 | 18,705 | 2,626 | 211,360 |
| Costs and Expenses | | | | | |
| Home cost of sales | - | 161,027 | 10,812 | (1,396) | 170,443 |
| Asset impairments | - | 4,692 | - | - | 4,692 |
| Marketing and commission expenses | - | 16,559 | 919 | - | 17,478 |
| General and administrative and other expenses | 15,120 | 15,191 | 8,407 | - | 38,718 |
| Total operating costs and expenses | 15,120 | 197,469 | 20,138 | (1,396) | 231,331 |
| Loss from operations | (19,142) | (3,418) | (1,433) | 4,022 | (19,971) |
| Other (expense) income | (14,987) | 35 | 734 | - | (14,218) |
| Loss before income taxes | (34,129) | (3,383) | (699) | 4,022 | (34,189) |
| Benefit from (provision for) income taxes | 2,419 | (1) | 61 | - | 2,479 |
| Net loss | \$ (31,710) | \$ (3,384) | \$ (638) | \$ 4,022 | \$ (31,710) |

Table of Contents**M.D.C. HOLDINGS, INC.****Notes to Unaudited Consolidated Financial Statements (Continued)****Supplemental Condensed Combining Statements of Operations****Three Months Ended September 30, 2010****(In thousands)**

| | MDC | Guarantor Subsidiaries | Non- Guarantor Subsidiaries | Eliminating Entries | Consolidated MDC |
|---|--------------------|-----------------------------------|--|--------------------------------|-----------------------------|
| Revenue | | | | | |
| Home sales revenue | \$ - | \$ 219,743 | \$ - | \$ (3,242) | \$ 216,501 |
| Land sales and other revenue | - | 1,249 | 7,931 | - | 9,180 |
| Equity in (loss) income of subsidiaries | 9,066 | - | - | (9,066) | - |
| Total revenue | 9,066 | 220,992 | 7,931 | (12,308) | 225,681 |
| Costs and Expenses | | | | | |
| Home cost of sales | - | 173,963 | 478 | (3,242) | 171,199 |
| Asset impairments | - | 3,718 | - | - | 3,718 |
| Marketing and commission expenses | - | 19,269 | - | - | 19,269 |
| General and administrative and other expenses | 18,530 | 13,078 | 9,296 | - | 40,904 |
| Total operating costs and expenses | 18,530 | 210,028 | 9,774 | (3,242) | 235,090 |
| (Loss) income from operations | (9,464) | 10,964 | (1,843) | (9,066) | (9,409) |
| Other (expense) income | (2,169) | 50 | 934 | - | (1,185) |
| (Loss) income before income taxes | (11,633) | 11,014 | (909) | (9,066) | (10,594) |
| Benefit from (provision for) income taxes | 1,394 | 753 | (1,792) | - | 355 |
| Net (loss) income | \$ (10,239) | \$ 11,767 | \$ (2,701) | \$ (9,066) | \$ (10,239) |

Table of Contents**M.D.C. HOLDINGS, INC.****Notes to Unaudited Consolidated Financial Statements (Continued)****Supplemental Condensed Combining Statements of Operations****Nine Months Ended September 30, 2011****(In thousands)**

| | MDC | Guarantor Subsidiaries | Non- Guarantor Subsidiaries | Eliminating Entries | Consolidated MDC |
|---|--------------------|-----------------------------------|--|--------------------------------|-----------------------------|
| Revenue | | | | | |
| Home sales revenue | \$ - | \$ 552,579 | \$ 26,937 | \$ (5,084) | \$ 574,432 |
| Land sales and other revenue | - | 4,314 | 18,046 | - | 22,360 |
| Equity in (loss) income of subsidiaries | (23,295) | - | - | 23,295 | - |
| Total revenue | (23,295) | 556,893 | 44,983 | 18,211 | 596,792 |
| Costs and Expenses | | | | | |
| Home cost of sales | - | 472,522 | 23,083 | (5,084) | 490,521 |
| Asset impairments | - | 14,090 | - | - | 14,090 |
| Marketing and commission expenses | - | 48,646 | 1,785 | - | 50,431 |
| General and administrative and other expenses | 46,139 | 49,620 | 18,635 | - | 114,394 |
| Total operating costs and expenses | 46,139 | 584,878 | 43,503 | (5,084) | 669,436 |
| (Loss) income from operations | (69,434) | (27,985) | 1,480 | 23,295 | (72,644) |
| Other (expense) income | (17,515) | 118 | 2,345 | - | (15,052) |
| (Loss) income before income taxes | (86,949) | (27,867) | 3,825 | 23,295 | (87,696) |
| Benefit from (provision for) income taxes | 7,380 | 2,583 | (1,836) | - | 8,127 |
| Net (loss) income | \$ (79,569) | \$ (25,284) | \$ 1,989 | \$ 23,295 | \$ (79,569) |

Table of Contents**M.D.C. HOLDINGS, INC.****Notes to Unaudited Consolidated Financial Statements (Continued)****Supplemental Condensed Combining Statements of Operations****Nine Months Ended September 30, 2010****(In thousands)**

| | MDC | Guarantor Subsidiaries | Non- Guarantor Subsidiaries | Eliminating Entries | Consolidated MDC |
|---|--------------------|-----------------------------------|--|--------------------------------|-----------------------------|
| Revenue | | | | | |
| Home sales revenue | \$ - | \$ 680,398 | \$ - | \$ (11,678) | \$ 668,720 |
| Land sales and other revenue | - | 7,673 | 22,696 | - | 30,369 |
| Equity in (loss) income of subsidiaries | 26,727 | - | - | (26,727) | - |
| Total revenue | 26,727 | 688,071 | 22,696 | (38,405) | 699,089 |
| Costs and Expenses | | | | | |
| Home cost of sales | - | 546,888 | 441 | (11,678) | 535,651 |
| Asset impairments | - | 3,718 | - | - | 3,718 |
| Marketing and commission expenses | - | 54,544 | - | - | 54,544 |
| General and administrative and other expenses | 55,319 | 57,529 | 19,041 | - | 131,889 |
| Total operating costs and expenses | 55,319 | 662,679 | 19,482 | (11,678) | 725,802 |
| (Loss) income from operations | (28,592) | 25,392 | 3,214 | (26,727) | (26,713) |
| Other (expense) income | (10,799) | 126 | 1,851 | - | (8,822) |
| (Loss) income before income taxes | (39,391) | 25,518 | 5,065 | (26,727) | (35,535) |
| Benefit from (provision for) income taxes | 4,595 | 530 | (4,386) | - | 739 |
| Net (loss) income | \$ (34,796) | \$ 26,048 | \$ 679 | \$ (26,727) | \$ (34,796) |

Table of Contents**M.D.C. HOLDINGS, INC.****Notes to Unaudited Consolidated Financial Statements (Continued)****Supplemental Condensed Combining Statements of Cash Flows****Nine Months Ended September 30, 2011****(In thousands)**

| | MDC | Guarantor Subsidiaries | Non- Guarantor Subsidiaries | Eliminating Entries | Consolidated MDC |
|---|-------------|-----------------------------------|--|--------------------------------|-----------------------------|
| Net cash (used in) provided by operating activities | \$ (39,482) | \$ (77,129) | \$ 12,567 | \$ 23,301 | \$ (80,743) |
| Net cash provided by (used in) investing activities | 413,999 | (20) | (32,817) | - | 381,162 |
| Financing activities | | | | | |
| (Advances to) payments from subsidiaries | (86,833) | 75,707 | 34,427 | (23,301) | - |
| Extinguishment of senior notes | (254,903) | - | - | - | (254,903) |
| Mortgage repurchase facility, net | - | - | (14,726) | - | (14,726) |
| Dividend payments | (35,560) | - | - | - | (35,560) |
| Proceeds from exercise of stock options | 46 | - | - | - | 46 |
| Net cash (used in) provided by financing activities | (377,250) | 75,707 | 19,701 | (23,301) | (305,143) |
| Net decrease in cash and cash equivalents | (2,733) | (1,442) | (549) | - | (4,724) |
| Cash and cash equivalents | | | | | |
| Beginning of period | 535,035 | 4,287 | 32,903 | - | 572,225 |
| End of period | \$ 532,302 | \$ 2,845 | \$ 32,354 | \$ - | \$ 567,501 |

Table of Contents**M.D.C. HOLDINGS, INC.****Notes to Unaudited Consolidated Financial Statements (Continued)****Supplemental Condensed Combining Statements of Cash Flows****Nine Months Ended September 30, 2010****(In thousands)**

| | MDC | Guarantor Subsidiaries | Non- Guarantor Subsidiaries | Eliminating Entries | Consolidated MDC |
|--|------------|-----------------------------------|--|--------------------------------|-----------------------------|
| Net cash provided by (used in) operating activities | \$ 70,017 | \$ (235,638) | \$ 11,456 | \$ 16,574 | \$ (137,591) |
| Net cash used in investing activities | (566,995) | (1,029) | (29,102) | - | (597,126) |
| Financing activities | | | | | |
| (Advances to) payments from subsidiaries | (269,877) | 238,312 | 48,139 | (16,574) | - |
| Proceeds from issuance of senior notes, net | 242,288 | - | - | - | 242,288 |
| Mortgage repurchase facility, net | - | - | (17,960) | - | (17,960) |
| Dividend payments | (35,355) | - | - | - | (35,355) |
| Proceeds from exercise of stock options | 53 | - | - | - | 53 |
| Net cash (used in) provided by financing activities | (62,891) | 238,312 | 30,179 | (16,574) | 189,026 |
| Net (decrease) increase in cash and cash equivalents | (559,869) | 1,645 | 12,533 | - | (545,691) |
| Cash and cash equivalents | | | | | |
| Beginning of period | 1,210,123 | 3,258 | 20,871 | - | 1,234,252 |
| End of period | \$ 650,254 | \$ 4,903 | \$ 33,404 | \$ - | \$ 688,561 |

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ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with, and is qualified in its entirety by, the Unaudited Consolidated Financial Statements and Notes thereto included elsewhere in this Quarterly Report on Form 10-Q. This item contains forward-looking statements that involve risks and uncertainties. Actual results may differ materially from those indicated in such forward-looking statements. Factors that may cause such a difference include, but are not limited to, those discussed in Item 1A: Risk Factors Relating to our Business of our Annual Report on Form 10-K for the year ended December 31, 2010 and this Quarterly Report on Form 10-Q.

INTRODUCTION

M.D.C. Holdings, Inc. is a Delaware corporation. We refer to M.D.C. Holdings, Inc. as the Company, MDC, we or our in this Quarterly Report on Form 10-Q, and these designations include our subsidiaries unless we state otherwise. We have two primary operations, homebuilding and financial services. Our homebuilding operations consist of wholly-owned subsidiary companies that generally purchase finished lots for the construction and sale of single-family detached homes to first-time and first-time move-up homebuyers under the name Richmond American Homes. Our homebuilding operations are comprised of many homebuilding subdivisions that we consider to be our operating segments. Homebuilding subdivisions in a given market are aggregated into reportable segments as follows: (1) West (Arizona, California, Nevada and Washington); (2) Mountain (Colorado and Utah); (3) East (Maryland, which includes Maryland, Pennsylvania, Delaware and New Jersey, and Virginia, which includes Virginia and West Virginia); and (4) Other Homebuilding (Florida and Illinois).

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

EXECUTIVE SUMMARY

Overview and Outlook:

The Company's goal is to return to profitability, even if overall market conditions do not improve. Through the second quarter of 2011, our main strategy to accomplish the goal of profitability was to increase our community count, which we expected would give us the opportunity to capture additional market share and drive higher revenues. This effort resulted in a 23% increase in our active subdivisions at September 30, 2011 from December 31, 2010, through (1) growth in existing markets and (2) our expansion into the Seattle market through an asset acquisition in April 2011. However, as our economy continues to display considerable weakness, including continued low consumer confidence and high unemployment, it has become difficult to justify a significant number of additional land acquisitions in the near-term. Therefore, while our existing subdivision count provides us with an opportunity for revenue growth, we do not believe it is enough to achieve our goal and, as such, we are now focusing on other strategies to drive profitability. In particular, we are focused on: (1) reducing our general and administrative expenses; (2) evaluating and improving our sales process; and (3) aligning our debt structure with our operating needs. See **Forward-Looking Statements** below.

Since 2009, we have maintained a general and administrative structure designed to open new communities, implement a new enterprise resource planning system, and position ourselves for expected market improvement. However, given that market conditions have remained depressed, we have taken additional steps to reduce general and administrative expenses. Since the beginning of 2011, we have reduced our general and administrative headcount by approximately 33% from September 30, 2010, the most significant reductions coming during the 2011 second and third quarters.

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As we look at the communities we already own, we have closely analyzed our sales process. Over the past eighteen months, we have relied on large promotions as a critical component of our sales strategy. While these promotions were successful in producing a high level of urgency for our sales personnel and customers, we have also experienced increased volatility in sales absorptions and Cancellation Rates (as defined below), which created inefficiencies on the operational and back-office side of our business. As a result, we are modifying our sales and marketing strategies to rely less on these large promotions in the future, and have made management changes in these departments, with the goal of increasing absorptions and home gross margins. Furthermore, during the 2011 third quarter, we changed our approach to the production of spec homes, which historically have yielded margins significantly below margins on homes that are started with a buyer under contract. In most of our markets, we intend to start very few spec homes and anticipate that our spec inventory should continue to decrease in these markets. See **Forward-Looking Statements** below.

In light of our subdivision count and current demand for new homes, we are in the process of better aligning our debt structure with our operating needs. Accordingly, we completed a debt tender offer in July 2011 that extinguished \$63.7 million of our 7% Senior Notes due 2012 and \$173.3 million of our 5 ½% Senior Notes due 2013. On October 19, 2011, we redeemed the remaining \$86.3 million of our outstanding 7% Senior Notes due 2012 and, in November 2011, we anticipate redeeming the remaining \$176.7 million of our 5 ½% Senior Notes due 2013.

Summary Company Results

Our net orders for homes have been negatively impacted by: (1) strong competition for prospective homebuyers; (2) homebuyer anxiety about the housing market; (3) our prospective homebuyers having difficulty qualifying for mortgage loans; (4) home sales promotions during the 2011 second quarter that captured many potential home buyers who subsequently cancelled their purchase during the 2011 third quarter; and (5) selling efforts during the 2010 third quarter that resulted in the sale of a significant number of aged specs. The decline in net orders during the nine months ended September 30, 2011 was also impacted by the expiration of the federal homebuyer tax credit (which required the sale of homes to be completed by April 30, 2010), which significantly influenced the period to period comparisons. We believe our ability to execute a revised sales and marketing strategy to help capture more market share in the current homebuilding environment is a key factor to improve our net orders for homes. See **Forward-Looking Statements** below.

Our closed homes were down 2% and 17%, respectively, during the three and nine months ended September 30, 2011 compared with the same periods in 2010. This decline partially reflects our decision to limit the number of speculative homes. Our Home Gross Margins were 16.8% and 14.6% during the three and nine months ended September 30, 2011, respectively, and 20.9% and 19.9% during the three and nine months ended September 30, 2010, respectively. These items contributed significantly to our loss from operations for the three and nine months ended September 30, 2011.

On the expense side of our business, we incurred asset impairments of \$4.7 million and \$14.1 million during the three and nine months ended September 30, 2011 compared with \$3.7 million during the same periods in 2010. We saw a combined decrease of \$1.8 million and \$4.1 million, respectively, in marketing and commission expenses during the three and nine months ended September 30, 2011, compared with the same periods in 2010, generally attributable to closing fewer homes during the 2011 periods. Additionally, we experienced a \$3.7 million and a \$15.5 million decrease, respectively, in our general and administrative expenses during the three and nine months ended September 30, 2011, compared with the same periods in 2010, primarily due to lower costs associated with legal-related matters and employee compensation.

Because we closed fewer homes (which had lower Home Gross Margins) our losses from operations during the three and nine months ended September 30, 2011 were \$20.1 million and \$72.6 million, respectively, compared with \$9.4 million and \$26.7 million during the same periods in 2010.

During the three months ended September 30, 2011, we had net interest income of \$3.1 million compared to net interest expense of \$1.5 million during the same period in 2010. We had net interest income of \$2.1 million during the nine months ended September 30, 2011, compared to net interest expense of \$9.3 million during the same period in 2010. The improvement during the 2011 periods primarily related to capitalizing interest incurred to our inventory during the first nine months of 2011 compared with the same period in 2010. The debt tender offer we completed in July 2011, which extinguished \$237 million of certain of our Senior Notes, resulted in a loss on extinguishment of debt of \$18.6 million.

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CRITICAL ACCOUNTING ESTIMATES AND POLICIES

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

Our critical accounting estimates and policies have not changed from those reported in Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2010.

Results of Operations

The following discussion compares results for the three and nine months ended September 30, 2011 with the three and nine months ended September 30, 2010.

Home Sales Revenue. Home sales revenue from a home closing includes the base sales price and any purchased options and upgrades and is reduced for any Sales Price Incentives (defined as discounts on the sales price of a home) or paid Mortgage Loan Origination Fees (defined as mortgage loan origination fees paid by Richmond American Homes to HomeAmerican) and interest rate buydowns by HomeAmerican in mortgage loan financing offered to our homebuyers. The combination of base sales price and any purchased options and upgrades, less any of the foregoing incentives, for each closed home constitutes the selling price of our closed homes.

Our home sales revenue can be impacted by changes in our home closing levels and changes in the average selling prices of closed homes. The combination of home sales incentives offered to prospective homebuyers may vary from subdivision-to-subdivision and from home-to-home, and may be revised during the home closing process based upon homebuyer preferences or upon changes in market conditions, such as changes in our competitors' pricing.

The table below summarizes home sales revenue by reportable segment (dollars in thousands).

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| | Three Months Ended September 30, | | Change | |
|---------------------------|----------------------------------|-------------------|--------------------|------------|
| | 2011 | 2010 | Amount | % |
| West | \$ 71,241 | \$ 66,076 | \$ 5,165 | 8% |
| Mountain | 82,537 | 88,080 | (5,543) | -6% |
| East | 36,566 | 58,243 | (21,677) | -37% |
| Other Homebuilding | 15,939 | 7,345 | 8,594 | 117% |
| Total Homebuilding | 206,283 | 219,744 | (13,461) | -6% |
| Intercompany | (1,397) | (3,243) | 1,846 | 57% |
| Consolidated | \$ 204,886 | \$ 216,501 | \$ (11,615) | -5% |

| | Nine Months Ended September 30, | | Change | |
|---------------------------|---------------------------------|-------------------|--------------------|-------------|
| | 2011 | 2010 | Amount | % |
| West | \$ 180,585 | \$ 240,555 | \$ (59,970) | -25% |
| Mountain | 231,700 | 244,751 | (13,051) | -5% |
| East | 130,525 | 162,351 | (31,826) | -20% |
| Other Homebuilding | 36,707 | 32,741 | 3,966 | 12% |
| Total Homebuilding | 579,517 | 680,398 | (100,881) | -15% |
| Intercompany | (5,085) | (11,678) | 6,593 | 56% |
| Consolidated | \$ 574,432 | \$ 668,720 | \$ (94,288) | -14% |

West Segment The increase in home sales revenue during the three months ended September 30, 2011 primarily was driven by closing 49 homes in our new Washington market, which generated \$13.2 million in home sales revenue. Additionally, we closed 15 more homes in the Arizona market, which resulted in home sales revenue increasing by \$3.0 million. This was partially offset by the impact of closing 35 fewer homes in our California and Nevada markets, which resulted in a \$7.4 million decrease in home sales revenue. Additionally, a decrease of \$64,600 in the average selling price of closed homes in the California market resulted in a \$3.7 million decline in home sales revenue.

The decline in home sales revenue during the nine months ended September 30, 2011 primarily resulted from (1) closing 372 fewer homes in the Arizona, California and Nevada markets of this segment as this caused home sales revenue to decrease by \$73.0 million and (2) a decline of \$14.7 million associated with reductions in the average selling prices of homes in our Arizona and California markets. This was partially offset by the impact of closing 100 homes in our new Washington market, which generated \$26.9 million of home sales revenue.

Mountain Segment The decline in home sales revenue during the three months ended September 30, 2011 primarily resulted from closing 39 fewer homes. This decrease in an \$11.5 million decline in home sales revenue. Partially offsetting this decline was the impact of increases in the average selling prices of closed homes in both markets of this segment, which resulted in a \$6.0 million increase in home sales revenue.

During the nine months ended September 30, 2011, the impact of closing 108 fewer homes resulted in a \$29.8 million reduction in home sales revenue. This was partially offset by a \$29,200 increase in the average selling price of closed homes in the Colorado market.

East Segment The decline in home sales revenue during the three months ended September 30, 2011 primarily was driven by: (1) closing 43 fewer homes as this resulted in home sales revenue decreasing by \$20.2 million; and (2) a decrease of \$1.9 million associated with reductions in the average selling prices of homes in the Virginia market.

The decline in home sales revenue during the nine months ended September 30, 2011 was the result of closing 47 fewer homes as this caused home sales revenue to decrease by \$21.5 million and a decline of \$10.3 million associated with reductions in the average selling prices of homes in the markets of this segment.

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Other Homebuilding Segment During the three months ended September 30, 2011, the impact of closing 38 more homes resulted in an \$8.6 million increase in home sales revenue.

During the nine months ended September 30, 2011, the impact of closing 17 more homes resulted in a \$4.3 million increase in home sales revenue.

Home Gross Margins. We define Home Gross Margins to mean home sales revenue less home cost of sales as a percent of home sales revenue.

The following table sets forth our Home Gross Margins by reportable segment.

| | Three Months Ended September 30, | | Change |
|--------------------|----------------------------------|-------|--------|
| | 2011 | 2010 | |
| Homebuilding | | | |
| West | 20.6% | 35.3% | -14.7% |
| Mountain | 16.1% | 12.0% | 4.1% |
| East | 10.3% | 18.5% | -8.2% |
| Other Homebuilding | 17.0% | 9.2% | 7.8% |
| Consolidated | 16.8% | 20.9% | -4.1% |

| | Nine Months Ended September 30, | | Change |
|--------------------|---------------------------------|-------|--------|
| | 2011 | 2010 | |
| Homebuilding | | | |
| West | 18.2% | 25.7% | -7.5% |
| Mountain | 13.7% | 14.9% | -1.2% |
| East | 10.5% | 17.7% | -7.2% |
| Other Homebuilding | 15.0% | 18.7% | -3.7% |
| Consolidated | 14.6% | 19.9% | -5.3% |

Home Gross Margins can be impacted positively or negatively in a reporting period by adjustments to our warranty reserves. During the three and nine months ended September 30, 2011 and 2010, we continued to experience lower warranty payments on previously closed homes. As a result of favorable warranty payment experience relative to our estimates at the time of home closing, we recorded adjustments to reduce our warranty reserve of \$1.0 million and \$3.2 million during the three and nine months ended September 30, 2011, respectively, and \$7.2 million and \$12.8 million during the three and nine months ended September 30, 2010, respectively.

Interest in home cost of sales as a percent of home sale revenue was 2.5% and 2.6% during the three and nine months ended September 30, 2011, respectively, compared with 2.6% and 2.5% during the same periods of 2010.

The following table sets forth our Home Gross Margins excluding warranty adjustments and interest in home cost of sales during the three and nine months ended September 30, 2011 and 2010.

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| | Three Months Ended September 30, | | |
|--------------------|----------------------------------|-------|--------|
| | 2011 | 2010 | Change |
| West | 22.4% | 24.0% | -1.6% |
| Mountain | 18.3% | 17.5% | 0.8% |
| East | 14.3% | 18.8% | -4.5% |
| Other Homebuilding | 14.6% | 21.0% | -6.4% |
| Consolidated | 18.8% | 20.2% | -1.4% |

| | Nine Months Ended September 30, | | |
|--------------------|------------------------------------|-------|--------|
| | 2011 | 2010 | Change |
| West | 19.9% | 23.0% | -3.1% |
| Mountain | 15.6% | 18.0% | -2.4% |
| East | 13.8% | 19.1% | -5.3% |
| Other Homebuilding | 14.4% | 21.1% | -6.7% |
| Consolidated | 16.6% | 20.5% | -3.9% |

West Segment Home Gross Margins excluding warranty and interest decreased during the three and nine months ended September 30, 2011 primarily due declines of \$64,600 and \$79,900 in the average selling price of closed home in our California market without corresponding declines in the cost of home construction or cost of land. These items partially were offset by the impact of recording adjustments associated with unused land budget commitments of \$4.1 million and \$5.2 million during the three and nine months ended September 30, 2011, respectively, compared with \$1.9 million and \$3.7 million during the same periods in 2010.

Mountain Segment Home Gross Margins excluding warranty and interest increased slightly during the three months ended September 30, 2011. Contributing to this increase was the impact of settling a construction defect claim the Company had against certain of its vendors in Colorado, the results of which had a \$2.3 million benefit to Home Gross Margins in this segment.

East Segment Home Gross Margins decreased during the three and nine months ended September 30, 2011 primarily resulting from declines of \$54,000 and \$50,900 in the average selling price of closed home in our Virginia market without corresponding decreases in land and home construction costs.

Other Homebuilding Segment Home Gross Margins excluding warranty and interest decreased during the three and nine months ended September 30, 2011 primarily resulting from closing, in our Florida market, a higher percentage of speculative homes that had been in the final stage of completion. These specific homes that were closed during the 2011 periods yielded significantly lower Home Gross Margins from those sold as dirt starts.

Future Home Gross Margins may be impacted negatively by, among other things: (1) selling and closing more spec homes than homes that are sold as dirt starts; (2) increases in the costs of subcontracted labor, building materials, and other resources, to the extent that market conditions prevent the recovery of increased costs through higher selling prices; (3) negative changes in our warranty payment experiences, increases in warranty expenses or litigation expenses associated with construction defect claims, and/or fewer adjustments to decrease warranty reserves based upon our actuary analysis of warranty payments; (4) increases in the costs of finished lots; (5) a weaker economic environment as well as homebuyers' reluctance to purchase new homes based on concerns about employment conditions; (6) increased competition and increases in the level of home order cancellations, which could affect our ability to maintain existing home prices and/or home sales incentive levels; (7) continued and/or increases in home foreclosure levels; (8) further tightening of mortgage loan origination requirements; (9) deterioration in the demand for new homes in our markets; (10) fluctuating energy costs, including oil and gasoline; (11) increases in interest expense included in home cost of sales; and (12) other general risk factors. See **Forward-Looking Statements** above.

The following table sets forth by reportable segment a reconciliation of our home cost of sales, as reported, to home cost of sales excluding warranty adjustments and interest in home cost of sales, which is used in the calculation of Home Gross Margins, excluding warranty adjustments and interest in home cost of sales (dollars in thousands).

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| Three Months Ended | Home Sales Revenue - As reported | Home Cost of Sales - As reported | Warranty Adjustments | Interest in Cost of Sales | Home Cost of Sales - Excluding Warranty Adjustments and Interest | Home Gross Margins - Excluding Warranty Adjustments and Interest |
|---------------------------|----------------------------------|----------------------------------|----------------------|---------------------------|--|--|
| September 30, 2011 | | | | | | |
| West | \$ 71,241 | \$ 56,565 | \$ (564) | \$ 1,845 | \$ 55,284 | 22.4% |
| Mountain | 82,537 | 69,225 | (169) | 1,951 | 67,443 | 18.3% |
| East | 36,566 | 32,817 | 431 | 1,067 | 31,319 | 14.3% |
| Other | 15,939 | 13,233 | (653) | 277 | 13,609 | 14.6% |
| Intercompany | (1,397) | (1,397) | - | - | (1,397) | N/A |
| Consolidated | \$ 204,886 | \$ 170,443 | \$ (955) | \$ 5,140 | \$ 166,258 | 18.9% |

Three Months Ended**September 30, 2010**

| | | | | | | |
|--------------------|------------|------------|------------|----------|------------|-------|
| West | \$ 66,076 | \$ 42,775 | \$ (9,287) | \$ 1,825 | \$ 50,237 | 24.0% |
| Mountain | 88,080 | 77,505 | 2,550 | 2,254 | 72,701 | 17.5% |
| East | 58,243 | 47,494 | (1,197) | 1,370 | 47,321 | 18.8% |
| Other Homebuilding | 7,345 | 6,668 | 737 | 132 | 5,799 | 21.0% |
| Intercompany | (3,243) | (3,243) | - | - | (3,243) | N/A |
| Consolidated | \$ 216,501 | \$ 171,199 | \$ (7,197) | \$ 5,581 | \$ 172,815 | 20.2% |

| Nine Months Ended | Home Sales Revenue - As reported | Home Cost of Sales - As reported | Warranty Adjustments | Interest in Cost of Sales | Home Cost of Sales - Excluding Warranty Adjustments and Interest | Home Gross Margins - Excluding Warranty Adjustments and Interest |
|---------------------------|----------------------------------|----------------------------------|----------------------|---------------------------|--|--|
| September 30, 2011 | | | | | | |
| West | \$ 180,585 | \$ 147,678 | \$ (1,782) | \$ 4,845 | \$ 144,615 | 19.9% |
| Mountain | 231,700 | 199,877 | (1,268) | 5,677 | 195,468 | 15.6% |
| East | 130,525 | 116,853 | 674 | 3,657 | 112,522 | 13.8% |
| Other | 36,707 | 31,198 | (842) | 618 | 31,422 | 14.4% |
| Intercompany | (5,085) | (5,085) | - | - | (5,085) | N/A |
| Consolidated | \$ 574,432 | \$ 490,521 | \$ (3,218) | \$ 14,797 | \$ 478,942 | 16.6% |

Nine Months Ended**September 30, 2010**

| | | | | | | |
|--------------------|------------|------------|-------------|-----------|------------|-------|
| West | \$ 240,555 | \$ 178,738 | \$ (13,114) | \$ 6,540 | \$ 185,312 | 23.0% |
| Mountain | 244,751 | 208,310 | 1,869 | 5,820 | 200,621 | 18.0% |
| East | 162,351 | 133,650 | (1,767) | 4,031 | 131,386 | 19.1% |
| Other Homebuilding | 32,741 | 26,631 | 209 | 594 | 25,828 | 21.1% |
| Intercompany | (11,678) | (11,678) | - | - | (11,678) | N/A |
| Consolidated | \$ 668,720 | \$ 535,651 | \$ (12,803) | \$ 16,985 | \$ 531,469 | 20.5% |

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Home Gross Margins excluding the impact of warranty adjustments and interest in home cost of sales is a non-GAAP financial measure. We believe this information is meaningful as it isolates the impact that warranty adjustments and interest have on our Home Gross Margins.

Land Sales Revenue. Land sale transactions were not material during the three and nine months ended September 30, 2011. Land sales revenue during the three and nine months ended September 30, 2010 was \$0.9 million and \$6.6 million, respectively, primarily in our West segment.

Other Revenue. Gains on the sale of mortgage loans primarily represent revenue earned by HomeAmerican from the sale of HomeAmerican's originated mortgage loans to third-parties. Insurance revenue primarily represents premiums collected by StarAmerican and Allegiant from our homebuilding subcontractors in connection with the construction of homes. Title and other revenue primarily consist of forfeitures of homebuyer deposits on home sales contracts and revenue associated with our American Home Title operations.

The table below sets forth the components of other revenue (dollars in thousands).

| | Three Months Ended September 30, | | Change | |
|----------------------------------|----------------------------------|----------|------------|------|
| | 2011 | 2010 | Amount | % |
| Gains on sales of mortgage loans | \$ 3,575 | \$ 5,920 | \$ (2,345) | -40% |
| Insurance revenue | 1,629 | 1,525 | 104 | 7% |
| Title and other revenue | 540 | 831 | (291) | -35% |
| Total other revenue | \$ 5,744 | \$ 8,276 | \$ (2,532) | -31% |

| | Nine Months Ended September 30, | | Change | |
|----------------------------------|---------------------------------|-----------|------------|------|
| | 2011 | 2010 | Amount | % |
| Gains on sales of mortgage loans | \$ 12,190 | \$ 16,523 | \$ (4,333) | -26% |
| Insurance revenue | 4,609 | 4,702 | (93) | -2% |
| Title and other revenue | 2,062 | 2,526 | (464) | -18% |
| Total other revenue | \$ 18,861 | \$ 23,751 | \$ (4,890) | -21% |

Gains on sales of mortgage loans decreased during the three and nine months ended September 30, 2011 primarily due to declines of 1,300 and 900 basis points in the Capture Rates (as defined below) during the 2011 periods, respectively, and due to the Company closing 15 and 410 fewer homes.

Home Cost of Sales. Home cost of sales primarily includes land acquisition, land development and related costs (both incurred and estimated to be incurred), specific construction costs of each home, warranty costs and finance and closing costs, including Closing Cost Incentives (defined as homebuyer closing costs assistance paid by Richmond American Homes to a third-party).

Our home cost of sales can be impacted primarily by changes in our home closing levels and changes in the cost of land acquisition, land development incurred and estimated to be incurred, construction cost of homes and changes in our estimated costs for warranty repairs.

The table below sets forth the home cost of sales by reportable segment (dollars in thousands).

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| | Three Months Ended September 30, | | Change | |
|--------------------------|----------------------------------|------------|-----------|------|
| | 2011 | 2010 | Amount | % |
| Homebuilding | | | | |
| West | \$ 56,565 | \$ 42,775 | \$ 13,790 | 32% |
| Mountain | 69,225 | 77,505 | (8,280) | -11% |
| East | 32,817 | 47,494 | (14,677) | -31% |
| Other Homebuilding | 13,233 | 6,668 | 6,565 | 98% |
| Total Homebuilding | 171,840 | 174,442 | (2,602) | -1% |
| Intercompany adjustments | (1,397) | (3,243) | 1,846 | 57% |
| Consolidated | \$ 170,443 | \$ 171,199 | \$ (756) | 0% |

| | Nine Months Ended September 30, | | Change | |
|--------------------------|---------------------------------|------------|-------------|------|
| | 2011 | 2010 | Amount | % |
| Homebuilding | | | | |
| West | \$ 147,678 | \$ 178,738 | \$ (31,060) | -17% |
| Mountain | 199,877 | 208,310 | (8,433) | -4% |
| East | 116,853 | 133,650 | (16,797) | -13% |
| Other Homebuilding | 31,198 | 26,631 | 4,567 | 17% |
| Total Homebuilding | 495,606 | 547,329 | (51,723) | -9% |
| Intercompany adjustments | (5,085) | (11,678) | 6,593 | 56% |
| Consolidated | \$ 490,521 | \$ 535,651 | \$ (45,130) | -8% |

West Segment Home cost of sales increased during the three months ended September 30, 2011 due to a \$4.4 million increase associated with closing 29 more homes and \$8.7 million from adjustments to decrease warranty reserves during 2010 that we did not experience during 2011.

Home cost of sales decreased during the nine months ended September 30, 2011 primarily resulting from a \$45.7 million decline associated with closing 272 fewer homes, partially offset by an increase of \$11.3 million associated with adjustments to decrease warranty reserves incurred in 2010 which we did not experience during 2011.

Mountain Segment Home cost of sales decreased during the three months ended September 30, 2011 as we closed 39 fewer homes, which caused a \$10.6 million decline and \$2.7 million associated with adjustments to increase warranty reserves incurred in 2010 that were not incurred during 2011. These items partially were offset by a \$4.3 million increase in home cost of construction associated with a change in the mix of homes that were closed during the 2011 period compared with the 2010 period.

Home cost of sales decreased during the nine months ended September 30, 2011 as we closed 108 fewer homes, which caused a \$27.3 million decline and \$3.1 million associated with adjustments to increase warranty reserves incurred in 2010 that were not incurred during 2011. These items partially were offset by a \$16.2 million increase in home cost of construction associated with a change in the mix of homes that were closed during the 2011 period compared with the 2010 period.

East Segment During the three months ended September 30, 2011, home cost of sales decreased \$16.2 million associated with closing 43 fewer homes and \$8.7 million associated with adjustments to warranty reserves incurred in 2010 that were not incurred during 2011.

Home cost of sales decreased during the nine months ended September 30, 2011 resulting from closing 47 fewer homes, which caused a \$17.9 million decline, partially offset by an increase of \$2.4 million associated with adjustments to decrease warranty reserves incurred in 2010 that were not incurred during 2011.

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Other Homebuilding Segment Home cost of sales during the 2011 third quarter increased primarily resulting from an \$8.7 million increase associated with closing 38 more homes, partially offset by a \$1.4 million decrease associated with warranty adjustments.

Home cost of sales the nine months ended September 30, 2011 increased primarily resulting from a \$3.2 million increase associated with closing 17 more homes.

Land Cost of Sales. Land sale transactions were not material during the three and nine months ended September 30, 2011. Land cost of sales during the three and nine months ended September 30, 2010 was \$0.8 million and \$6.0 million, respectively, and related to the sale of lots, primarily in our West segment.

Asset Impairments. We recorded \$4.7 million and \$14.1 million of asset impairments during the three and nine months ended September 30, 2011, respectively, resulting from a decline in the market value of land and homes in certain subdivisions of our West, Mountain and Other Homebuilding segments. We recorded \$3.7 million of asset impairments during the three and nine months ended September 30, 2010 resulting from a decline in the market value of land and homes in several subdivisions of our West segment.

The following table sets forth the asset impairments by reportable segment (dollars in thousands).

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|----------------------------------|----------|---------------------------------|----------|
| | 2011 | 2010 | 2011 | 2010 |
| Land and Land Under Development | | | | |
| West | \$ 1,193 | \$ 2,490 | \$ 7,112 | \$ 2,490 |
| Mountain | 550 | - | 1,786 | - |
| East | - | - | 285 | - |
| Other Homebuilding | 1,519 | - | 1,519 | - |
| Subtotal | 3,262 | 2,490 | 10,702 | 2,490 |
| Housing Completed or Under Construction | | | | |
| West | 484 | 1,143 | 1,438 | 1,143 |
| Mountain | 210 | - | 449 | - |
| East | - | - | - | - |
| Other Homebuilding | 93 | - | 93 | - |
| Subtotal | 787 | 1,143 | 1,980 | 1,143 |
| Other Assets | 643 | 85 | 1,408 | 85 |
| Consolidated Asset Impairments | \$ 4,692 | \$ 3,718 | \$ 14,090 | \$ 3,718 |

Marketing Expenses. Marketing expenses primarily include advertising, amortization of deferred marketing costs, model home expenses, compensation related expenses and other selling costs. The following table summarizes our marketing expenses by reportable segment (in thousands).

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| | Three Months Ended September 30, | | Amount | Change | |
|--------------------|----------------------------------|-----------|------------|--------|------|
| | 2011 | 2010 | | | % |
| Homebuilding | | | | | |
| West | \$ 4,400 | \$ 4,940 | \$ (540) | | -11% |
| Mountain | 3,155 | 3,491 | (336) | | -10% |
| East | 1,549 | 1,902 | (353) | | -19% |
| Other Homebuilding | 898 | 858 | 40 | | 5% |
| Consolidated | \$ 10,002 | \$ 11,191 | \$ (1,189) | | -11% |

| | Nine Months Ended September 30, | | Amount | Change | |
|--------------------|---------------------------------|-----------|----------|--------|-----|
| | 2011 | 2010 | | | % |
| Homebuilding | | | | | |
| West | \$ 12,925 | \$ 13,188 | \$ (263) | | -2% |
| Mountain | 9,445 | 9,137 | 308 | | 3% |
| East | 4,998 | 5,196 | (198) | | -4% |
| Other Homebuilding | 2,364 | 2,205 | 159 | | 7% |
| Consolidated | \$ 29,732 | \$ 29,726 | \$ 6 | | 0% |

Marketing expense during the three months ended September 30, 2011 decreased in our West, Mountain and East segments primarily resulting from a decline in sales office and product advertising expenses. Marketing expenses increased slightly during the three months ended September 30, 2011 in our Other Homebuilding segment primarily resulting from an increase in amortization of deferred marketing costs associated with closing more homes during the 2011 third quarter.

Marketing expenses during the nine months ended September 30, 2011 increased in our Mountain and Other Homebuilding segments primarily from increase in the amortization of deferred marketing costs associated with closed homes and increases in compensation related expenses. The declines in marketing expenses in our West and East segments during the nine months ended September 30, 2011 primarily resulted from lower compensation related costs, partially offset by increases in the amortization of deferred marketing costs.

Commission Expenses. Commission expenses include direct incremental commissions paid for closed homes. The following table summarizes our commission expenses by reportable segment (in thousands).

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| | Three Months Ended September 30, | | Change | |
|--------------------|----------------------------------|----------|----------|------|
| | 2011 | 2010 | Amount | % |
| Homebuilding | | | | |
| West | \$ 2,495 | \$ 2,655 | \$ (160) | -6% |
| Mountain | 2,991 | 3,176 | (185) | -6% |
| East | 1,369 | 1,903 | (534) | -28% |
| Other Homebuilding | 621 | 344 | 277 | 81% |
| Consolidated | \$ 7,476 | \$ 8,078 | \$ (602) | -7% |

| | Nine Months Ended September 30, | | Change | |
|--------------------|---------------------------------|-----------|------------|------|
| | 2011 | 2010 | Amount | % |
| Homebuilding | | | | |
| West | \$ 6,442 | \$ 9,320 | \$ (2,878) | -31% |
| Mountain | 8,166 | 8,649 | (483) | -6% |
| East | 4,516 | 5,428 | (912) | -17% |
| Other Homebuilding | 1,575 | 1,421 | 154 | 11% |
| Consolidated | \$ 20,699 | \$ 24,818 | \$ (4,119) | -17% |

Commission expense in our West segment decreased during the three months ended September 30, 2011 primarily due to closing fewer homes in our Nevada and California markets. This decline was partially offset by incurring \$0.4 million in commission expense in our new Washington market. The decline in commission expense during the three months ended September 30, 2011 in our Mountain and East segments resulted from closing 39 and 43 fewer homes, respectively. Commission expense increased during the three months ended September 30, 2011 in our Other Homebuilding segment due to closing 38 more homes.

Commission expense in our West segment decreased during the nine months ended September 30, 2011 primarily due to closing a combined 372 fewer homes in the Arizona, Nevada and California markets of this segment. This decline was partially offset by incurring \$0.9 million in commission expense in our new Washington market. The decline in commission expense during the nine months ended September 30, 2011 in our Mountain and East segments resulted from closing 108 and 47 fewer homes, respectively. Commission expense increased during the three months ended September 30, 2011 in our Other Homebuilding segment due to closing 17 more homes.

General and Administrative Expenses. The following table summarizes our general and administrative expenses by reportable segment (in thousands).

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| | Three Months Ended September 30, | | Change | |
|------------------------------|----------------------------------|-----------|------------|------|
| | 2011 | 2010 | Amount | % |
| Homebuilding | | | | |
| West | \$ 7,052 | \$ 6,717 | \$ 335 | 5% |
| Mountain | 2,782 | 3,532 | (750) | -21% |
| East | 3,194 | 4,805 | (1,611) | -34% |
| Other Homebuilding | 738 | 1,057 | (319) | -30% |
| Total Homebuilding | 13,766 | 16,111 | (2,345) | -15% |
| Financial Services and Other | 6,701 | 4,521 | 2,180 | 48% |
| Corporate | 15,113 | 18,637 | (3,524) | -19% |
| Consolidated | \$ 35,580 | \$ 39,269 | \$ (3,689) | -9% |

| | Nine Months Ended September 30, | | Change | |
|------------------------------|---------------------------------|------------|-------------|------|
| | 2011 | 2010 | Amount | % |
| Homebuilding | | | | |
| West | \$ 20,872 | \$ 22,037 | \$ (1,165) | -5% |
| Mountain | 10,790 | 12,004 | (1,214) | -10% |
| East | 10,182 | 16,043 | (5,861) | -37% |
| Other Homebuilding | 2,703 | 4,242 | (1,539) | -36% |
| Total Homebuilding | 44,547 | 54,326 | (9,779) | -18% |
| Financial Services and Other | 15,832 | 14,267 | 1,565 | 11% |
| Corporate | 48,190 | 55,467 | (7,277) | -13% |
| Consolidated | \$ 108,569 | \$ 124,060 | \$ (15,491) | -12% |

West Segment The increase during the three months ended September 30, 2011 was primarily due to legal related expenses and supervisory fees that increased by a combined \$1.0 million, partially offset by a \$0.7 million decline in salary and compensation related expenses. The decrease during the nine months ended September 30, 2011 primarily resulted from a \$0.8 million decrease in salary and compensation related expenses.

Mountain Segment The decrease during the three and nine months ended September 30, 2011 primarily resulted from a \$0.7 million and \$1.2 million decrease, respectively, in salary and compensation related expenses.

East Segment The decrease during the three months ended September 30, 2011 primarily resulted from a \$0.9 million decline in salary and compensation related expenses and legal related expenses, which were lower by \$0.6 million. The decrease during the nine months ended September 30, 2011 primarily resulted from incurring \$4.3 million less in legal related matters and a \$1.7 million reduction in salary and compensation related expenses.

Other Homebuilding Segment The decrease during the 2011 third quarter was attributable to lower salary and compensation related expenses. The decrease during the nine months ended September 30, 2011 primarily resulted from incurring \$1.0 million less in legal related matters and a \$0.4 million reduction in salary and compensation related expenses.

Financial Services and Other Segment General and administrative expense increased during the three months ended September 30, 2011 resulting from a \$3.0 million increase in the estimated mortgage loan loss reserve, partially offset by decreases in salary and compensation related expenses.

The increase during the nine months ended September 30, 2011, primarily resulted from a \$4.2 million increase in expenses associated with our mortgage loan loss reserve, partially offset by a \$1.2 million reduction in salary and compensation related expenses and a \$1.0 million reduction in insurance expense associated with closing fewer homes.

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Corporate Segment During the three months ended September 30, 2011, general and administrative expenses were down due to the following decreases: (1) \$1.9 million associated with executive bonuses; (2) \$2.5 million in salary and compensation related expenses; and (3) \$0.3 million primarily associated with office related costs. These items partially were offset by the impact of a \$1.0 million expense during the 2011 third quarter associated with stock options granted to our Board of Directors, which in prior years were recorded during the fourth quarter. With the new Board of Directors stock option plan, the stock option grant to our Board of Directors now takes place during the third quarter.

During the nine months ended September 30, 2011 general and administrative expenses were down \$7.3 million due to the following decreases: (1) \$5.4 million associated with salary and compensation related expenses; (2) \$1.9 million associated with executive bonuses; and (3) \$0.9 million associated with office related expenses. These items partially were offset by the impact of a \$1.0 million expense during the 2011 third quarter associated with stock options granted to our Board of Directors.

Other Operating Expense. Other operating expenses increased by \$1.6 million and \$1.5 million, respectively, during the three and nine months ended September 30, 2011 primarily due to \$2.4 million and \$5.3 million in write-offs of land option deposits and pre-acquisition costs associated with lot option contracts that we elected not to exercise. Other operating expenses during the nine months ended September 30, 2011 also included \$0.6 million in due diligence costs associated with an asset acquisition in April 2011. These items partially were offset by the release of a \$2.7 million employment tax contingency reserve as a result of the finalization of an IRS examination.

Other Income (Expense). Other income (expense) primarily includes interest and dividend income on our cash, cash equivalents and marketable securities, interest expense primarily on our senior notes, loss on extinguishment of senior notes and gain or loss on the sale of other assets. Interest income was \$6.7 million and \$21.9 million during the three and nine months ended September 30, 2011, respectively, compared with \$7.5 million and \$19.5 million, respectively, during the three and nine months ended September 30, 2010. Our available-for-sale marketable securities include certain debt securities, primarily corporate debt and holdings in equity security mutual funds.

Interest expense during the three and nine months ended September 30, 2011 decreased \$5.3 million and \$9.0 million, respectively. We capitalize interest on our senior notes associated with our qualifying assets. We have determined that inventory is a qualifying asset during the period of active development of our land and through the completion of construction of a home. When construction of a home is complete, the home is no longer considered to be a qualifying asset and interest is no longer capitalized on that home. As a result of the increase in our inventory levels from the first nine months of 2010, we capitalized \$10.8 million and \$31.1 million of interest incurred during the three and nine months ended September 30, 2011, respectively, compared with \$9.4 million and \$24.9 million from the same periods during 2010, respectively.

During the 2011 third quarter, we completed a debt tender offer purchasing \$63.7 million of our 7% Senior Notes due 2012 and \$173.3 million of our 5 1/2% Senior Notes due 2013. We paid \$254.9 million, including interest and fees, for the acquired notes and, as a result of the tender, we recorded an \$18.6 million charge associated with the extinguishment of senior notes.

(Loss)/Income Before Income Taxes. The table below summarizes our (loss)/income before income taxes by reportable segment (dollars in thousands).

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| | Three Months Ended September 30, | | Change Amount | % |
|------------------------------|----------------------------------|-------------|------------------|-------|
| | 2011 | 2010 | | |
| Homebuilding | | | | |
| West | \$ (2,584) | \$ 4,900 | \$ (7,484) | 153% |
| Mountain | 2,988 | 520 | 2,468 | -475% |
| East | (2,518) | 2,021 | (4,539) | 225% |
| Other Homebuilding | (1,514) | (1,673) | 159 | 10% |
| Total Homebuilding | (3,628) | 5,768 | (9,396) | 163% |
| Financial Services and Other | (450) | 4,326 | (4,776) | -110% |
| Corporate | (30,111) | (20,688) | (9,423) | -46% |
| Consolidated | \$ (34,189) | \$ (10,594) | \$ (23,595) | -223% |

| | Nine Months Ended September 30, | | Change Amount | % |
|------------------------------|---------------------------------|-------------|------------------|-------|
| | 2011 | 2010 | | |
| Homebuilding | | | | |
| West | \$ (18,981) | \$ 13,611 | \$ (32,592) | 239% |
| Mountain | 552 | 6,652 | (6,100) | 92% |
| East | (6,819) | 1,957 | (8,776) | 448% |
| Other Homebuilding | (3,206) | (1,897) | (1,309) | -69% |
| Total Homebuilding | (28,454) | 20,323 | (48,777) | 240% |
| Financial Services and Other | 4,419 | 10,261 | (5,842) | -57% |
| Corporate | (63,661) | (66,119) | 2,458 | 4% |
| Consolidated | \$ (87,696) | \$ (35,535) | \$ (52,161) | -147% |

West Segment We had a loss before income taxes of \$2.6 million during the three months ended September 30, 2011 compared with income before income taxes of \$4.9 million during the same period in 2010. This decline primarily resulted from a 1,470 basis point reduction in Home Gross Margins and a \$0.3 million increase in general and administrative expenses. Also contributing to this decline was an increase in expenses associated with the write-offs of land option deposits and pre-acquisition costs associated with lot option contracts that we elected not to exercise. Partially offsetting these items was a combined decrease of \$0.7 million in marketing and commission expense and \$2.0 million decrease in inventory impairments.

We had a loss before income taxes of \$19.0 million during the nine months ended September 30, 2011 compared with income before income taxes of \$13.6 million during the same period in 2010. This decline primarily resulted from: (1) a \$4.9 million increase in inventory impairments; (2) a 750 basis point decline in Home Gross Margins; and (3) closing 372 fewer homes in the Arizona, California and Nevada markets. These items were partially offset by a combined decrease of \$4.0 million in commission and general and administrative expenses.

Mountain Segment Income before income taxes increased \$2.5 million during the three months ended September 30, 2011 primarily from a combined decrease of \$1.3 million in general and administrative, marketing and commission expenses and a 410 basis point increase in Home Gross Margins, partially offset by closing 39 fewer homes and a \$0.8 million increase in inventory impairments.

Income before income taxes decreased \$6.1 million during the nine months ended September 30, 2011 primarily resulting from closing 108 fewer homes, a 120 basis point decline in Home Gross Margins and an increase of \$2.3 million in inventory impairments. These items were partially offset by a combined decrease of \$1.7 million in commission and general and administrative expenses.

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East Segment We had a loss before income taxes of \$2.5 million during the three months ended September 30, 2011 compared with income before income taxes of \$2.0 million during the same period in 2010. This decline primarily resulted from an 820 basis point decline in Home Gross Margins and closing 43 fewer homes. These items were partially offset by a combined decrease of \$2.5 million in marketing, commission and general and administrative expenses.

We had a loss before income taxes of \$6.8 million during the nine months ended September 30, 2011 compared with income before income taxes of \$2.0 million during the same period in 2010. This decline primarily resulted from a 720 basis point decline in Home Gross Margins and closing 47 fewer homes. These items were partially offset by a combined decrease of \$7.0 million in marketing, commission and general and administrative expenses.

Other Homebuilding Segment Our loss before income taxes was \$0.2 million lower during the three months ended September 30, 2011, primarily resulting from a 780 basis point increase in Home Gross Margins and closing 38 more homes in this segment. These items partially were offset by a \$1.6 million increase in inventory impairments.

Our loss before income taxes during the nine months ended September 30, 2011 increased by \$1.3 million primarily resulting from a \$1.6 million increase in inventory impairments and a 370 basis reduction in Home Gross Margins. These items partially were offset by a \$1.5 million decrease in general and administrative expenses and the impact of closing 17 more homes.

Financial Services and Other Segment We had a loss before income taxes during the three months ended September 30, 2011 of \$0.5 million compared with income before income taxes of \$4.3 million in the prior 2010 period. This decline primarily resulted from a \$2.2 million increase in general and administrative expenses and a \$2.3 million decline in gains on the sale of mortgage loans.

Income before income taxes during the nine months ended September 30, 2011 decreased \$5.8 million due to a \$4.3 million decrease in gains on sale of mortgage loans and a \$1.6 million increase in general and administrative expenses.

Corporate Segment Loss before income taxes during the three months ended September 30, 2011 increased \$9.4 million as we incurred an \$18.6 million charge associated with the extinguishment of senior notes during the 2011 third quarter. This item was partially offset by a \$3.6 million decline in interest expense and a \$3.5 million decrease in general and administrative expenses.

Loss before income taxes during the nine months ended September 30, 2011 decreased by \$2.5 million primarily resulting from a \$7.3 million decrease in general and administrative expenses, a \$1.8 million increase in interest income and an \$8.8 million decrease in interest expense. These items partially were offset by the \$18.6 million charge we incurred associated with the extinguishment of debt during the 2011 third quarter.

Income Taxes. We are required, at the end of each interim period, to estimate our annual effective tax rate for the fiscal year and use that rate to provide for income taxes for the current year-to-date reporting period. Due to the effects of the deferred tax valuation allowance and changes in unrecognized tax benefits, our effective tax rates in 2011 and 2010 are not meaningful as the income tax benefit is not directly correlated to the amount of pretax loss. The income tax benefits of \$2.5 million and \$8.1 million during the three and nine months ended September 30, 2011, respectively, resulted primarily from our 2011 second and third quarter settlement of various state income tax matters and our 2011 first quarter settlement with the IRS on its audit of the 2004 and 2005 federal income tax returns. Our income tax benefits during the three and nine months ended September 30, 2010 were not material to our results of operations.

Homebuilding Operating Activities

Orders for Homes, net. The table below sets forth information relating to orders for homes (dollars in thousands).

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| | Three Months Ended September 30, | | Change | | Nine Months Ended September 30, | | Change | |
|---|----------------------------------|-------------------|--------------------|-------------|---------------------------------|-------------------|--------------------|-------------|
| | 2011 | 2010 | Amount | % | 2011 | 2010 | Amount | % |
| Orders For Homes, net (units) | | | | | | | | |
| Arizona | 104 | 119 | (15) | -13% | 390 | 471 | (81) | -17% |
| California | 53 | 101 | (48) | -48% | 247 | 236 | 11 | 5% |
| Nevada | 107 | 106 | 1 | 1% | 349 | 471 | (122) | -26% |
| Washington | 42 | - | 42 | N/M | 68 | - | 68 | N/M |
| West | 306 | 326 | (20) | -6% | 1,054 | 1,178 | (124) | -11% |
| Colorado | 147 | 220 | (73) | -33% | 560 | 722 | (162) | -22% |
| Utah | 38 | 73 | (35) | -48% | 214 | 308 | (94) | -31% |
| Mountain | 185 | 293 | (108) | -37% | 774 | 1,030 | (256) | -25% |
| Maryland | 48 | 67 | (19) | -28% | 168 | 176 | (8) | -5% |
| Virginia | 42 | 60 | (18) | -30% | 205 | 202 | 3 | 1% |
| East | 90 | 127 | (37) | -29% | 373 | 378 | (5) | -1% |
| Florida | 16 | 50 | (34) | -68% | 158 | 156 | 2 | 1% |
| Illinois | (2) | - | (2) | N/M | 5 | - | 5 | N/M |
| Other Homebuilding | 14 | 50 | (36) | -72% | 163 | 156 | 7 | 4% |
| Total | 595 | 796 | (201) | -25% | 2,364 | 2,742 | (378) | -14% |
| Estimated Value of Orders for Homes, net | \$ 175,000 | \$ 231,000 | \$ (56,000) | -24% | \$ 682,000 | \$ 770,000 | \$ (88,000) | -11% |
| Estimated Average Selling Price of Orders for Homes, net | \$ 294.1 | \$ 290.2 | \$ 3.9 | 1% | \$ 288.5 | \$ 280.8 | \$ 7.7 | 3% |
| N/M | Not meaningful | | | | | | | |

Net order for homes during the three months ended September 30, 2011 decreased in each of our homebuilding segments driven primarily by: (1) previously discussed volatility in our Cancellation Rates; (2) the impact of severe competition for home orders with other homebuilders; and (3) the continued uncertainty in the housing market.

During the nine months ended September 30, 2011, our net orders for homes decreased, which was driven by a 256 unit decline in the markets of our Mountain segment and 203 unit decline in the Arizona and Nevada markets of our West segment. The decline in these markets was driven primarily by the impact of the expiration of the 2010 federal homebuyer tax credit and increased volatility in our Cancellation Rates. These declines partially were offset by the 68 net orders for homes we received in our new Washington market. In certain markets, we did see some increases in net orders for homes, which were primarily the result of higher active subdivision counts.

Homes Closed. The following table sets forth homes closed for each market within our homebuilding segments (in units).

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| | Three Months Ended September 30, | | Change | | Nine Months Ended September 30, | | Change | |
|--------------------|----------------------------------|------------|-------------|-------------|---------------------------------|--------------|--------------|-------------|
| | 2011 | 2010 | Amount | % | 2011 | 2010 | Amount | % |
| Arizona | 126 | 111 | 15 | 14% | 301 | 461 | (160) | -35% |
| California | 58 | 62 | (4) | -6% | 168 | 176 | (8) | -5% |
| Nevada | 77 | 108 | (31) | -29% | 223 | 427 | (204) | -48% |
| Washington | 49 | - | 49 | N/M | 100 | - | 100 | N/M |
| West | 310 | 281 | 29 | 10% | 792 | 1,064 | (272) | -26% |
| Colorado | 189 | 208 | (19) | -9% | 537 | 546 | (9) | -2% |
| Utah | 58 | 78 | (20) | -26% | 178 | 277 | (99) | -36% |
| Mountain | 247 | 286 | (39) | -14% | 715 | 823 | (108) | -13% |
| Maryland | 47 | 68 | (21) | -31% | 153 | 185 | (32) | -17% |
| Virginia | 36 | 58 | (22) | -38% | 151 | 166 | (15) | -9% |
| East | 83 | 126 | (43) | -34% | 304 | 351 | (47) | -13% |
| Florida | 63 | 29 | 34 | 117% | 154 | 142 | 12 | 8% |
| Illinois | 4 | - | 4 | 0% | 5 | - | 5 | 0% |
| Other Homebuilding | 67 | 29 | 38 | 131% | 159 | 142 | 17 | 12% |
| Total | 707 | 722 | (15) | -2% | 1,970 | 2,380 | (410) | -17% |

Homes closed in our West and Other Homebuilding segments were up during the three months ended September 30, 2011. In our West segment, the increase of 29 units resulted from closing 49 homes in our new Washington market. Homes closed in our Florida market increased during the three months ended September 30, 2011. During 2010, due to the Federal Homebuyer Tax Credit, we closed more homes during the 2010 second quarter, thus resulting in an increase in closing during the 2011 third quarter when compared with the 2010 third quarter.

Homes closed during the nine months ended September 30, 2011 were down in our West, Mountain and East segments each of our homebuilding segments. Contributing to the decline in home closings was the negative impact from the federal homebuyer tax credit, which expired during 2010. In our West segment, this item was partially offset by closing 100 homes in our new Washington market.

Backlog. The following table below sets forth information relating to Backlog for each market within our homebuilding segments (dollars in thousands).

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| | September 30, 2011 | December 31, 2010 | September 30, 2010 |
|---|-----------------------|----------------------|-----------------------|
| Backlog (units) | | | |
| Arizona | 173 | 84 | 113 |
| California | 158 | 79 | 136 |
| Nevada | 202 | 76 | 132 |
| Washington | 44 | - | - |
| West | 577 | 239 | 381 |
| Colorado | 296 | 273 | 383 |
| Utah | 105 | 69 | 125 |
| Mountain | 401 | 342 | 508 |
| Maryland | 141 | 126 | 117 |
| Virginia | 124 | 70 | 109 |
| East | 265 | 196 | 226 |
| Florida | 68 | 64 | 73 |
| Illinois | 1 | 1 | - |
| Other Homebuilding | 69 | 65 | 73 |
| Total | 1,312 | 842 | 1,188 |
| Backlog Estimated Sales Value | \$ 405,000 | \$ 269,000 | \$ 368,000 |
| Estimated Average Selling Price of Homes in Backlog | \$ 308.7 | \$ 319.5 | \$ 309.8 |

We define Backlog as homes under contract but not yet delivered. Our Backlog at a point in time is impacted by net orders for homes and closed homes during a reporting period. The increase in our Backlog at September 30, 2011 compared with September 30, 2010 can be attributed to the ratio of closings to beginning Backlog which decreased to 50% for the 2011 third quarter, compared with 65% in the 2010 third quarter. This decline primarily resulted from the year-over-year decrease in the percentage of our Backlog under construction at the beginning of the quarter.

Cancellation Rate. We define our home order Cancellation Rate as the approximate number of cancelled home order contracts during a reporting period as a percentage of total home order contracts received during such reporting period. The following tables set forth our Cancellation Rate by segment.

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| | Three Months Ended September 30, | | Increase |
|--------------------|----------------------------------|------|----------|
| | 2011 | 2010 | |
| Homebuilding | | | |
| West | 42% | 27% | 15% |
| Mountain | 42% | 34% | 8% |
| East | 42% | 30% | 12% |
| Other Homebuilding | 79% | 30% | 49% |
| Consolidated | 44% | 30% | 14% |

| | Nine Months Ended September 30, | | Increase |
|--------------------|---------------------------------|------|----------|
| | 2011 | 2010 | |
| Homebuilding | | | |
| West | 33% | 22% | 11% |
| Mountain | 36% | 29% | 7% |
| East | 33% | 28% | 5% |
| Other Homebuilding | 41% | 31% | 10% |
| Consolidated | 35% | 26% | 9% |

Our consolidated Cancellation Rates during the three and nine months ended September 30, 2011 increased in each of our homebuilding segments. During both 2011 periods, we experienced a significant increase in the number of home orders that were cancelled. As a result of our gross number of home orders remaining constant between the 2011 periods and the 2010 periods, coupled with the higher volume of cancellations in 2011, we experienced a higher cancellation rate during the three and nine months ended September 30, 2011.

The cancellations that we experienced during the 2011 periods primarily resulted from: (1) our homebuyers having difficulties qualifying for mortgage loans; (2) low consumer confidence in the housing market; and (3) home orders that were contingent upon our prospective homebuyers being able to sell their existing home, which has been difficult given the challenging housing market.

Active Subdivisions. The following table displays the number of our active subdivisions for each market within our homebuilding segments.

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| | September 30, 2011 | December 31, 2010 | September 30, 2010 |
|--------------------|-----------------------|----------------------|-----------------------|
| Arizona | 26 | 26 | 28 |
| California | 16 | 13 | 10 |
| Nevada | 20 | 18 | 19 |
| Washington | 10 | - | - |
| West | 72 | 57 | 57 |
| Colorado | 47 | 39 | 39 |
| Utah | 21 | 19 | 19 |
| Mountain | 68 | 58 | 58 |
| Maryland | 14 | 14 | 9 |
| Virginia | 13 | 8 | 7 |
| East | 27 | 22 | 16 |
| Florida | 15 | 11 | 11 |
| Illinois | - | - | - |
| Other Homebuilding | 15 | 11 | 11 |
| Total | 182 | 148 | 142 |

Our active subdivisions at September 30, 2011 have increased in each of our homebuilding segments compared with both September 30, 2010 and December 31, 2010. These increases are the result of our efforts primarily in the first half of 2011 to expand operations and generate more home closings in existing markets. However, as a result of continued uncertainty regarding the homebuilding industry, we have slowed our pace of new asset purchases and opening of new subdivisions during the 2011 third quarter, compared with recent quarters. As of September 30, 2011, we currently have more than 30 subdivisions we expect to become active in the near term and, assuming similar sales paces, we have nearly 25 subdivisions that we expect to become inactive in the near term.

Average Selling Prices Per Home Closed. The average selling price for our closed homes includes the base sales price, any purchased options and upgrades, reduced by any Sales Price Incentives (defined as discounts on the sales price of a home) or paid Mortgage Loan Origination Fees (defined as mortgage loan origination fees paid by Richmond American Homes to HomeAmerican). The following tables set forth our average selling prices per home closed, by market (dollars in thousands).

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| | Three Months Ended September 30, | | Change | |
|------------|----------------------------------|----------|-----------|------|
| | 2011 | 2010 | Amount | % |
| Arizona | \$ 202.2 | \$ 200.7 | \$ 1.5 | 1% |
| California | 310.6 | 375.2 | (64.6) | -17% |
| Colorado | 347.7 | 322.6 | 25.1 | 8% |
| Florida | 232.7 | 253.2 | (20.5) | -8% |
| Illinois | 320.2 | N/A | N/M | N/M |
| Maryland | 448.2 | 443.3 | 4.9 | 1% |
| Nevada | 189.5 | 190.2 | (0.7) | 0% |
| Utah | 289.9 | 268.9 | 21.0 | 8% |
| Virginia | 430.5 | 484.5 | (54.0) | -11% |
| Washington | 268.5 | N/A | N/M | N/M |
| Average | \$ 289.8 | \$ 299.9 | \$ (10.1) | -3% |

| | Nine Months Ended September 30, | | Change | |
|------------|---------------------------------|----------|----------|------|
| | 2011 | 2010 | Amount | % |
| Arizona | \$ 192.0 | \$ 196.1 | \$ (4.1) | -2% |
| California | 316.1 | 396.0 | (79.9) | -20% |
| Colorado | 339.0 | 309.8 | 29.2 | 9% |
| Florida | 228.1 | 230.6 | (2.5) | -1% |
| Illinois | 314.7 | N/A | N/M | N/M |
| Maryland | 430.2 | 447.3 | (17.1) | -4% |
| Nevada | 191.7 | 188.4 | 3.3 | 2% |
| Utah | 278.9 | 272.8 | 6.1 | 2% |
| Virginia | 428.6 | 479.5 | (50.9) | -11% |
| Washington | 269.4 | N/A | N/M | N/M |
| Average | \$ 291.6 | \$ 281.0 | \$ 10.6 | 4% |

N/M Not Meaningful

The average selling price of closed homes during the three months ended September 30, 2011 decreased by 4%. This decline resulted from closing a higher percentage of our homes in our lower priced markets such as Arizona and Washington, compared to higher priced markets such as Colorado and Virginia. During the nine months ended September 30, 2011, the average selling price of closed homes increased by 4% as we closed a greater percentage of our homes in higher priced markets of Colorado and Virginia and closing fewer homes in our lower priced markets of Arizona and Nevada.

We did experience declines in the average selling price of closed homes in our California market during the three and nine months ended September 30, 2011, primarily resulting from closing homes in subdivisions with lower price points and declines in the market value of homes in certain subdivisions of this market. The declines in the average selling prices of closed homes in our Virginia market during the three and nine months ended September 30, 2011 primarily resulted from mix. In our Colorado market, the average selling price of closed homes increased during the three and nine months ended September 30, 2011 primarily driven from closing homes in higher priced subdivisions.

Inventory. Our inventory consists of housing completed or under construction and land and land under development. Housing completed or under construction in our Consolidated Balance Sheets primarily includes: (1) land costs transferred from land and land under development; (2) hard costs associated with the construction of a house; (3) overhead costs, which include real property taxes, engineering and permit fees; (4) capitalized interest; and (5) certain indirect fees. Land and land under development on our Consolidated Balance Sheets primarily includes land acquisition costs, land development costs associated with subdivisions for which we have the intent to construct and sell homes and capitalized interest.

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The following table shows the carrying value of housing completed or under construction for each market within our homebuilding segments (dollars in thousands).

| | September 30, 2011 | December 31, 2010 | September 30, 2010 |
|--------------------|-----------------------|----------------------|-----------------------|
| Arizona | \$ 23,049 | \$ 31,923 | \$ 40,075 |
| California | 58,568 | 49,516 | 57,533 |
| Nevada | 29,187 | 33,377 | 35,706 |
| Washington | 14,613 | - | - |
| West | 125,417 | 114,816 | 133,314 |
| Colorado | 84,744 | 111,397 | 122,830 |
| Utah | 16,973 | 26,372 | 35,034 |
| Mountain | 101,717 | 137,769 | 157,864 |
| Maryland | 41,760 | 48,740 | 46,014 |
| Virginia | 47,749 | 45,836 | 52,613 |
| East | 89,509 | 94,576 | 98,627 |
| Florida | 15,318 | 24,262 | 27,060 |
| Illinois | 1,389 | 999 | 620 |
| Other Homebuilding | 16,707 | 25,261 | 27,680 |
| Total | \$ 333,350 | \$ 372,422 | \$ 417,485 |

The table below shows the stage of construction for our homes completed or under construction, number of sold homes under construction and model homes (in units).

| | September 30, 2011 | December 31, 2010 | September 30, 2010 |
|--|-----------------------|----------------------|-----------------------|
| Unsold Homes Under Construction - Final | 85 | 119 | 56 |
| Unsold Homes Under Construction - Frame | 314 | 722 | 725 |
| Unsold Homes Under Construction - Foundation | 85 | 103 | 104 |
| Total Unsold Homes Under Construction | 484 | 944 | 885 |
| Sold Homes Under Construction | 871 | 609 | 955 |
| Model Homes | 220 | 242 | 246 |
| Homes Completed or Under Construction | 1,575 | 1,795 | 2,086 |

Our housing completed and under construction decreased by \$39.1 million, as we decreased the total unsold homes under construction to 484 at September 30, 2011 from 944 at December 31, 2010. This decrease primarily resulted from our efforts to sell and close our spec inventory that had increased during 2010. The increase during 2010 primarily resulted from the following: (1) building more spec homes as we anticipated increased net orders for homes prior to the expiration of the federal homebuyer tax credit, which required the sale of a home to be completed by April 30, 2010 with a closing date by September 30, 2010; and (2) increased spec levels as a result of our practice of building specs homes and stopping construction at drywall (we moved away from this practice beginning in the 2011 third quarter). However, as a result of low levels of net orders for homes during the year ended December 31, 2010, our total unsold homes under construction remained high at December 31, 2010.

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The following table shows the carrying value of land and land under development for each market within our homebuilding segments (dollars in thousands).

| | September 30, 2011 | December 31, 2010 | September 30, 2010 |
|---------------------------|-----------------------|----------------------|-----------------------|
| Arizona | \$ 35,761 | \$ 41,892 | \$ 52,509 |
| California | 108,313 | 93,194 | 82,104 |
| Nevada | 51,475 | 32,605 | 20,306 |
| Washington | 18,506 | - | - |
| West | 214,055 | 167,691 | 154,919 |
| Colorado | 142,656 | 128,727 | 117,987 |
| Utah | 28,841 | 30,457 | 26,983 |
| Mountain | 171,497 | 159,184 | 144,970 |
| Maryland | 51,012 | 31,782 | 17,570 |
| Virginia | 69,007 | 44,083 | 36,261 |
| East | 120,019 | 75,865 | 53,831 |
| Florida | 10,509 | 9,274 | 8,958 |
| Illinois | 1,257 | 3,223 | 2,629 |
| Other Homebuilding | 11,766 | 12,497 | 11,587 |
| Total | \$ 517,337 | \$ 415,237 | \$ 365,307 |

The tables below show the total number of lots owned (excluding homes completed or under construction) and lots controlled under option agreements for each market within our homebuilding segments (in units).

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| | September 30, 2011 | December 31, 2010 | September 30, 2010 |
|--|-----------------------|----------------------|-----------------------|
| Lots Owned | | | |
| Arizona | 981 | 1,257 | 1,290 |
| California | 1,306 | 1,201 | 1,095 |
| Nevada | 1,091 | 991 | 632 |
| Washington | 312 | - | - |
| West | 3,690 | 3,449 | 3,017 |
| Colorado | 3,103 | 2,919 | 2,762 |
| Utah | 545 | 594 | 494 |
| Mountain | 3,648 | 3,513 | 3,256 |
| Maryland | 446 | 319 | 207 |
| Virginia | 566 | 414 | 380 |
| East | 1,012 | 733 | 587 |
| Florida | 233 | 210 | 204 |
| Illinois | 123 | 130 | 130 |
| Other Homebuilding | 356 | 340 | 334 |
| Total | 8,706 | 8,035 | 7,194 |
| Lots Controlled Under Option | | | |
| Arizona | 96 | 408 | 453 |
| California | - | 222 | 45 |
| Nevada | 75 | 838 | 1,018 |
| Washington | 182 | - | - |
| West | 353 | 1,468 | 1,516 |
| Colorado | 464 | 688 | 616 |
| Utah | 273 | 393 | 581 |
| Mountain | 737 | 1,081 | 1,197 |
| Maryland | 730 | 745 | 906 |
| Virginia | 192 | 132 | 220 |
| East | 922 | 877 | 1,126 |
| Florida | 373 | 733 | 906 |
| Illinois | - | - | - |
| Other Homebuilding | 373 | 733 | 906 |
| Total | 2,385 | 4,159 | 4,745 |
| Total Lots Owned and Controlled | 11,091 | 12,194 | 11,939 |

The table below shows the amount of at risk option deposits (in thousands).

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| | September 30, 2011 | December 31, 2010 | September 30, 2010 |
|--------------------------------------|-----------------------|----------------------|-----------------------|
| Cash | \$ 8,932 | \$ 9,019 | \$ 9,314 |
| Letters of Credit | 5,139 | 4,467 | 3,086 |
| Total At Risk Option Deposits | \$ 14,071 | \$ 13,486 | \$ 12,400 |

Our total lots owned (excluding homes completed or under construction) increased by 569 units from December 31, 2010 resulting from the purchase of lots, primarily during the first six months of 2011 that had been controlled under option contracts as of December 31, 2010. Also contributing to the increase in lots owned was an asset acquisition in Washington in April 2011 where we have 312 owned lots as of September 30, 2011. However, our total lots owned has decreased by 432 units from our June 30, 2011 levels primarily due to our election to limit additional land purchases given the on-going uncertainty in the market value of homes and continued depressed demand for new homes.

The decline in total lots under option primarily resulted from purchasing a limited number of lots during the 2011 third quarter and electing not to purchase lots that were under option. As a result of not purchasing lots that were under option, we recorded \$2.4 million and \$5.3 million of expenses of project write-off costs during the three and nine months ended September 30, 2011. We did, however, see an increase in the amount of option deposits at risk primarily attributable to new lot option contracts in the markets of our East segment, where greater option deposits were required by land sellers.

HomeAmerican Operating Activities

The following table sets forth information relating to mortgage loans originated by our HomeAmerican operations, mortgage loans brokered and our Capture Rate (dollars in thousands). The Capture Rate is defined as the number of mortgage loans originated by HomeAmerican for our homebuyers as a percent of total Company home closings.

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| | Three Months Ended September 30, | | Change | |
|--|----------------------------------|------------|-------------|------|
| | 2011 | 2010 | Amount | % |
| Principal amount of mortgage loans originated | \$ 129,005 | \$ 158,337 | \$ (29,332) | -19% |
| Principal amount of mortgage loans brokered | \$ 1,622 | \$ 370 | \$ 1,252 | 338% |
| Capture Rate | 66% | 79% | -13% | |
| Including brokered loans | 67% | 79% | -12% | |
| Mortgage products (% of mortgage loans originated) | | | | |
| Fixed rate | 96% | 97% | -1% | |
| Adjustable rate - other | 4% | 3% | 1% | |
| Prime loans ⁽¹⁾ | 38% | 32% | 6% | |
| Government loans ⁽²⁾ | 62% | 68% | -6% | |

| | Nine Months Ended September 30, | | Change | |
|--|---------------------------------|------------|--------------|------|
| | 2011 | 2010 | Amount | % |
| Principal amount of mortgage loans originated | \$ 390,660 | \$ 507,120 | \$ (116,460) | -23% |
| Principal amount of mortgage loans brokered | \$ 4,518 | \$ 5,883 | \$ (1,365) | -23% |
| Capture Rate | 72% | 81% | -9% | |
| Including brokered loans | 73% | 82% | -9% | |
| Mortgage products (% of mortgage loans originated) | | | | |
| Fixed rate | 96% | 96% | 0% | |
| Adjustable rate - other | 4% | 4% | 0% | |
| Prime loans | 33% | 27% | 6% | |
| Government loans | 67% | 73% | -6% | |

(1) Prime loans are defined as loans with Fair, Isaac & Company (FICO) scores greater than 620 and which comply with the documentation standards of the government sponsored enterprise guidelines.

(2) Government loans are loans either insured by the FHA or guaranteed by the VA.

The principal amount of mortgage loans originated decreased during the three and nine months ended September 30, 2011, primarily due to the Company closing 15 and 410 fewer homes, respectively, and declines in the Capture Rates during the 2011 periods.

LIQUIDITY AND CAPITAL RESOURCES

We use our liquidity and capital resources to (1) support our operations, including the purchase of land, land development and construction of homes; (2) provide working capital; and (3) provide mortgage loans for our homebuyers. Our liquidity includes our balances of cash and cash equivalents, marketable securities and capital resources, our senior notes and Mortgage Repurchase Facility (as defined below). Additionally, as of November 3, 2011, we have an existing effective shelf registration statement that allows us to issue equity, debt or hybrid securities up to \$1.0 billion.

On July 7, 2011, the Company completed a debt tender offer extinguishing \$63.7 million of its 7% Senior Notes due 2012 and \$173.3 million of its 5 1/2% Senior Notes due 2013. The Company paid \$254.9 million for the acquired notes.

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On October 19, 2011, the Company paid \$94.7 million to redeem the remaining \$86.3 million of its outstanding 7% Senior Notes due 2012. Additionally, the Company announced its intent to redeem the remaining \$176.7 million outstanding balance of its 5 1/2% Senior Notes due 2013.

The Company's marketable securities consist of fixed rate and floating rate interest earning securities, primarily: (1) debt securities, which may include, among others, United States government and government agency debt and corporate debt; (2) holdings in mutual fund equity securities and (3) deposit securities, which may include, among others, certificates of deposit and time deposits.

Capital Resources

Our capital structure is primarily a combination of (1) permanent financing, represented by stockholders' equity; (2) long-term financing, represented by our publicly traded 5 3/8% medium-term senior notes due 2014 and 2015 and 5 5/8% senior notes due 2020; and (3) our Mortgage Repurchase Facility. Because of our current balance of cash, cash equivalents, marketable securities and available capacity under our Mortgage Repurchase Facility, we believe that our capital resources are adequate to satisfy our short and long-term capital requirements, including meeting future payments on our senior notes as they become due. See **Forward-Looking Statements** above.

Senior Notes and Mortgage Repurchase Facility

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

Mortgage Lending. HomeAmerican has a Master Repurchase Agreement, which was amended in September 2011 and extended until September 27, 2012 (the Mortgage Repurchase Facility), with U.S. Bank National Association (USBNA). The Mortgage Repurchase Facility provides liquidity to HomeAmerican by providing for the sale of eligible mortgage loans to USBNA with an agreement by HomeAmerican to repurchase the mortgage loans at a future date. Until such mortgage loans are transferred back to HomeAmerican, the documents relating to such loans are held by USBNA, as custodian, pursuant to the Custody Agreement (Custody Agreement), dated as of November 12, 2008, by and between HomeAmerican and USBNA. As of September 30, 2011, the Mortgage Repurchase Facility has a maximum aggregate commitment of \$50 million, reduced from \$70 million through the fourth amendment in September 2011. At September 30, 2011 and December 31, 2010, we had \$10.7 million and \$25.4 million, respectively, of mortgage loans that we are obligated to repurchase under our Mortgage Repurchase Facility. Mortgage loans that we are obligated to repurchase under the Mortgage Repurchase Facility are accounted for as a debt financing arrangement and are reported as mortgage repurchase facility on the Consolidated Balance Sheets. Advances under the Mortgage Repurchase Facility carry a Pricing Rate equal to the greater of (i) the LIBOR Rate (as defined in the Mortgage Repurchase Facility) plus 2.5%, or (ii) 3.75%. At HomeAmerican's option the Balance Funded Rate (equal to 3.75%) may be applied to advances under the Mortgage Repurchase Facility provided the applicable Buyer is holding sufficient Qualifying Balances. The foregoing terms are defined in the Mortgage Repurchase Facility.

The Mortgage Repurchase Facility contains various representations, warranties and affirmative and negative covenants customary for agreements of this type. The negative covenants include, among others, (i) an Adjusted Tangible Net Worth requirement, (ii) a minimum Adjusted Tangible Net Worth Ratio, (iii) an Adjusted Net Income requirement, (iv) a minimum Liquidity requirement; and (v) a requirement that HomeAmerican's HUD Compare Ratio may be no more than 1.50 to 1.00. Adjusted Tangible Net Worth means the sum of (a) all assets of HomeAmerican less (b) the sum of (i) all Debt and all Contingent Indebtedness of HomeAmerican, (ii) all assets of HomeAmerican that would be classified as intangible assets under generally accepted accounting principles, and (iii) receivables from Affiliates. HomeAmerican's Adjusted Tangible Net Worth Ratio is the ratio of HomeAmerican's total liabilities (excluding Permitted Letters of Credit) to the Adjusted Tangible Net Worth. HomeAmerican's Adjusted Net Income is a rolling twelve consecutive months of net income for HomeAmerican. HomeAmerican's Liquidity is defined as its unencumbered and unrestricted cash and Cash Equivalents plus the amount by which the aggregate Purchase Value of all Purchased Loans at such time exceeds the aggregate Purchase Price outstanding for all Open Transactions at such time. HomeAmerican's HUD Compare Ratio is the ratio of (a) the percentage of HomeAmerican's FHA Mortgage Loan originations that were seriously delinquent or claim terminated in the first two years to (b) the percentage of all such Mortgage Loan originations. The foregoing terms are defined in the Mortgage Repurchase Facility.

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Failure to meet the foregoing negative covenants would constitute an event of default. In the event of default, USBNA may, at its option, declare the Repurchase Date for any or all Transactions to be deemed immediately to occur. Upon such event of default, and if USBNA exercises its right to terminate any Transactions, then (a) HomeAmerican's obligation to repurchase all Purchased Loans in such Transactions will become immediately due and payable; (b) the Repurchase Price for each such Transaction shall be increased by the aggregate amount obtained by daily multiplication of (i) the greater of the Pricing Rate for such Transaction and the Default Pricing Rate by (ii) the Purchase Price for the Transaction as of the Repurchase Date, (c) all Income paid after the event of default will be payable to and retained by USBNA and applied to the aggregate unpaid Repurchase Prices owed by HomeAmerican and (d) HomeAmerican shall deliver any documents relating to Purchased Loans subject to such Transactions to USBNA. Upon the occurrence of an event of default, USBNA may (a) sell any or all Purchased Loans subject to such Transactions on a servicing released or servicing retained basis and apply the proceeds to the unpaid amounts owed by HomeAmerican, (b) give HomeAmerican credit for such Purchased Loans in an amount equal to the Market Value and apply such credit to the unpaid amounts owed by HomeAmerican, (c) replace HomeAmerican as Servicer, (d) exercise its right under the Mortgage Repurchase Facility with respect to the Income Account and Escrow Account, and (e) with notice to HomeAmerican, declare the Termination Date to have occurred. The foregoing terms are defined in the Mortgage Repurchase Facility.

The table below sets forth the actual results of the covenant calculations and covenant requirements under the Mortgage Repurchase Facility at September 30, 2011.

| | Covenant Test | Covenant Results |
|---|---------------|------------------|
| Adjusted Tangible Net Worth (minimum) | \$ 18,000,000 | \$ 25,341,000 |
| Adjusted Tangible Net Worth Ratio (maximum) | 8.0 : 1.0 | 0.9: 1.0 |
| Adjusted Net Income (minimum) | \$ 1 | \$ 2,351,000 |
| Liquidity Test (minimum) | \$ 8,000,000 | \$ 29,307,000 |

We believe we are in compliance with the representations, warranties and covenants included in the Mortgage Repurchase Facility and we are not aware of any covenant violations.

MDC Common Stock Repurchase Program

At September 30, 2011, we were authorized to repurchase up to 4,000,000 shares of our common stock. We did not repurchase any shares of our common stock during the three or nine months ended September 30, 2011 and 2010.

Consolidated Cash Flow

During the nine months ended September 30, 2011, we used \$80.7 million of cash in operating activities; \$50.4 million was used to increase our inventory levels through the purchase of lots during the first nine months of 2011, partially offset by the sale and closing of homes. Also contributing to the use of cash during the first nine months of 2011 was \$32.9 million of cash used to reduce our accrued liabilities and net loss before non cash items of \$16.9 million. This use of cash was partially offset by generating \$40.4 million in cash associated with our income tax receivable and sale of mortgage loan inventory.

During the nine months ended September 30, 2010, we used \$137.6 million of cash from operating activities; we increased our homebuilding inventory, which resulted in the use of \$261.3 million of cash during the first nine months of 2010 as we purchased approximately 3,900 lots and increased the total homes under construction from 1,321 at December 31, 2009 to 2,086 at September 30, 2010. These items partially were offset by the reduction of \$144.5 million in our income tax receivable.

We generated \$381.2 million in cash from investing activities during the nine months ended September 30, 2011, primarily attributable to the maturity and sale of marketable securities that increased our cash by \$843.9 million, partially offset by the purchase of \$431.0 million of marketable securities. We used \$31.7 million in cash for the purchase of property, equipment and other.

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We used \$597.1 million in cash from investing activities during the nine months ended September 30, 2010, primarily attributable to purchasing \$796.3 million of marketable securities and \$7.7 million of property and equipment relating to our new enterprise resource planning system. These items partially were offset by the \$206.9 million of marketable securities that matured or were sold during the nine months ended September 30, 2010.

During the nine months ended September 30, 2011, we used \$305.1 million in cash for financing activities primarily attributable to \$254.9 million used to extinguish certain of our senior notes due 2012 and 2013, \$35.6 million associated with cash dividends that were paid during the first nine months of 2011 and net payments on our mortgage repurchase facility, which resulted in use of \$14.7 million of cash during the period. During the first nine months of 2010, we generated \$189.0 million in cash from financing activities, primarily due to the issuance of senior notes that raised \$242.3 million. The proceeds from the issuance of the senior notes are being used for general corporate purposes. This was partially offset as we had net payments under our Mortgage Repurchase Facility of \$18.0 million and \$35.4 million in dividend payments.

Off-Balance Sheet Arrangements

In the ordinary course of business, we enter into lot option purchase contracts in order to procure lots for the construction of homes. Lot option contracts enable us to control lot positions with a minimal capital investment, which substantially reduces the risks associated with land ownership and development. At September 30, 2011, we had deposits of \$8.9 million in the form of cash and \$5.1 million in the form of letters of credit that were at risk to secure option contracts to purchase lots.

At September 30, 2011, we had outstanding performance bonds and letters of credit totaling approximately \$70.6 million and \$21.5 million, respectively, including \$7.8 million in letters of credit issued by HomeAmerican, with the remaining bonds and letters of credit issued by third-parties, to secure our performance under various contracts. We expect that the obligations secured by these performance bonds and letters of credit generally will be performed in the ordinary course of business and in accordance with the applicable contractual terms. To the extent that the obligations are performed, the related performance bonds and letters of credit should be released and we should not have any continuing obligations. However, in the event any such performance bonds or letters of credit are called, our indemnity obligations could require us to reimburse the issuer of the performance bond or letter of credit.

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

Contractual Obligations

Due to completing the tender offer of certain of our senior notes in July 2011, and the recent announcement of our intent to redeem additional senior notes, our contractual obligations have changed materially from those reported in Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2010. The following table sets forth the contractual obligations of our senior notes as of September 30, 2011 after the July tender offer and the shift in timing of payments in light of the October redemption and the anticipated November redemption. There have been no other significant changes other than those set forth below from those reported in the Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2010.

| | Less than 1 year | 1 - 3 years | 4 - 5 years | After 5 years | Total |
|--------------|---------------------|-------------|-------------|------------------|-----------|
| Interest | 69,865 | 81,875 | 48,281 | 49,219 | 249,240 |
| Senior Notes | 262,947 | - | 500,000 | 250,000 | 1,012,947 |

IMPACT OF INFLATION, CHANGING PRICES AND ECONOMIC CONDITIONS

The impact of inflation and changing prices have not changed materially from the disclosure in our December 31, 2010 Annual Report on Form 10-K.

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OTHER

Forward-Looking Statements

Certain statements in this Quarterly Report on Form 10-Q, as well as statements made by us in periodic press releases, oral statements made by our officials in the course of presentations about the Company and conference calls in connection with quarterly earnings releases, constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include statements regarding our business, financial condition, results of operation, cash flows, strategies and prospects. These forward-looking statements may be identified by terminology such as likely, may, will, should, expects, plans, anticipates, believes, estimates, or continue, or the negative of such terms and other comparable terminology. Although we believe that the expectations reflected in the forward-looking statements contained in this Report are reasonable, we cannot guarantee future results. These statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company to be materially different from those expressed or implied by the forward-looking statements. We undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future events or otherwise. However, any further disclosures made on related subjects in subsequent reports on Forms 10-K, 10-Q and 8-K should be consulted. Additionally, information about issues that could lead to material changes in performance and risk factors that have the potential to affect us is contained under the caption Risk Factors Relating to our Business in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2010 and Item 1A of Part II of this Quarterly Report on Form 10-Q.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

During 2011, we have increased the amount of marketable securities that are invested in equity securities from \$105.3 million at December 31, 2010 to \$155.3 million at September 30, 2011. Because these are equity securities and are accounted for as available-for-sale, changes in the market value are reported as a component of accumulated other comprehensive (loss) income each quarter. During the 2011 third quarter, we experienced declines of \$12.2 million in the market value of these securities. While we believe that the ultimate cost basis of these investments will be recovered in the future, there can be no assurances to that effect. In the event we elect to sell, or are otherwise required to sell these securities, we may be required to record significant losses in the event the market value does not increase prior to any sale. Such losses, if any, would be recorded as a component of our results of operations.

Item 4. Controls and Procedures

(a) *Conclusion regarding the effectiveness of disclosure controls and procedures* - An evaluation of the effectiveness of the design and operation of our disclosure controls and procedures was performed under the supervision, and with the participation, of our management, including the Chief Executive Officer and the Chief Accounting Officer. Based on that evaluation, the Company's management, including the Chief Executive Officer and Chief Accounting Officer, concluded that our disclosure controls and procedures were effective at September 30, 2011.

(b) *Changes in internal control over financial reporting* - In our Maryland and Virginia homebuilding divisions, we began operating under our new enterprise resource planning (ERP) system during the 2011 third quarter. As a result, our financial and operating transactions in these divisions are now utilizing the functionality provided by the new ERP system with oversight as to the completeness and accuracy of the information being performed through the ERP system. The full implementation of the ERP system in the other homebuilding divisions not currently operating under our new ERP system is scheduled to take place over the course of the next several quarters. There was no other change in our internal control over financial reporting that occurred during the 2011 third quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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M.D.C. HOLDINGS, INC.

FORM 10-Q

PART II

Item 1. Legal Proceedings

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

Shareholder Derivative Litigation

On September 28, 2011, a shareholder derivative lawsuit captioned Martha Woodford v. Larry A. Mizel, et al. was filed in the United States District Court for the District of Delaware. In the lawsuit, the plaintiff makes claims against our board of directors and our executive officers for alleged breaches of fiduciary duty, violation of Section 14(a) of the Securities Exchange Act, corporate waste and unjust enrichment relating to the company's executive officer compensation practices. The plaintiff seeks monetary damages and injunctive relief on behalf of the Company, and attorneys' and other professional fees and costs. The officer and director defendants believe the suit is without merit and that they have meritorious defenses to all of the plaintiff's claims.

We cannot currently predict or determine the timing or final outcome of the lawsuit or whether it would have a material adverse effect on our financial condition, results of operations or cash flows.

West Virginia Litigation

Additionally, litigation has been filed by homeowners in West Virginia against MDC, its subsidiary Richmond American Homes of West Virginia, Inc. (RAH West Virginia) and various subcontractors alleging a failure to install functional passive radon mitigation systems in their homes. The plaintiffs seek compensatory and punitive damages and medical monitoring costs for alleged negligent construction, failure to warn, breach of warranty or contract, breach of implied warranty of habitability, fraud, and intentional and negligent infliction of emotional distress based upon alleged exposure to radon gas. The litigation includes the following actions:

Joy, et al. v. Richmond American Homes of West Virginia, Inc., et al., No. 08-C-204, Circuit Court of Jefferson County, West Virginia (*Joy*). This action was filed on May 16, 2008, by sixty-six plaintiffs from fifteen households. The Company and RAH West Virginia have answered and asserted cross-claims against the subcontractors for contractual and implied indemnity and contribution.

Bauer, et al. v. Richmond American Homes of West Virginia, Inc., et al., No. 08-C-431, Circuit Court of Jefferson County, West Virginia (*Bauer*). This action was filed on October 24, 2008, by eighty-six plaintiffs from twenty-one households. This action has been consolidated for discovery and pre-trial proceedings with the Joy action.

Saliba, et al. v. Richmond American Homes of West Virginia, Inc., et al., No. 08-C-447, Circuit Court, Jefferson County, West Virginia (*Saliba*). This action was filed on November 7, 2008, by thirty-five plaintiffs from nine households. This action has been consolidated for discovery and pre-trial proceedings with the Joy action.

By orders dated November 4 and 18, 2009, the trial court struck the answers filed by the Company and RAH West Virginia and entered judgment by default in favor of the plaintiffs on liability, with damages to be determined in a subsequent jury trial. On December 7, 2009, the Company and RAH West Virginia filed with the West Virginia Supreme Court of Appeals a motion seeking to stay the proceedings and a petition for writ of prohibition to vacate the default judgment. On June 16, 2010, the West Virginia Supreme Court of Appeals granted the Company and RAH West Virginia a writ of prohibition and vacated the trial court's sanctions orders.

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On July 29, 2010, the plaintiffs filed a renewed motion for sanctions based on substantially the same alleged misconduct. On January 14, 2011 the trial court again entered an order striking the answers filed by the Company and RAH West Virginia and imposing judgment by default upon them on the claims asserted in plaintiffs' complaints (exclusive of the claim for punitive damages). As stated in the January 14, 2011 order, the cross-claims made by the Company and RAH West Virginia remain in effect.

On March 31, 2011 the West Virginia Supreme Court of Appeals declined to enter a writ of prohibition with respect to the trial court's re-entry of its judgment of default stating that the issues presented are more properly presented on appeal after full development of the record in the lower court.

Separately, additional claims have been filed by homeowners in West Virginia against the Company, RAH West Virginia and individual superintendants who had worked for RAH West Virginia. The new litigation consists of the following:

Thorin, et al. v. Richmond American Homes of West Virginia, Inc., et al., No. 10-C-154, Circuit Court of Jefferson County, West Virginia (*Thorin*). This litigation was filed on May 12, 2010, by forty plaintiffs from eleven households in Jefferson and Berkeley Counties. To date, this action has not been consolidated for any purposes with the prior three actions. The claims asserted and the relief sought in the Thorin case are substantially similar to the Joy, Bauer and Saliba cases.

MDC and RAH West Virginia believe that they have meritorious defenses to each of the lawsuits and intend to vigorously defend the actions.

We can give no assurance as to the final outcomes of these cases, or whether they would have a material adverse effect on our financial condition, results of operations or cash flows.

Item 1A. Risk Factors

There have been no significant changes in the risk factors previously identified as being attendant to our business in our Annual Report on Form 10-K for the year ended December 31, 2010. For a more complete discussion of other risk factors that affect our business, see "Risk Factors Relating to our Business" in our Form 10-K for the year ended December 31, 2010, which include the following:

The homebuilding industry is undergoing a significant downturn, and its duration and ultimate severity are uncertain. A continuation or further deterioration in industry conditions or in the broader economic conditions could have additional adverse effects on our business and financial results.

Increased competition levels in the homebuilding and mortgage lending industries could result in lower net home orders, closings and decreases in the average selling prices of sold and closed homes, which would have a negative impact on our home sales revenue and results of operations.

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

Our strategies in responding to the adverse conditions in the homebuilding industry and in the U.S. economy have had limited success, and the continued implementation of these and other strategies may not be successful.

Increases in our Cancellation Rate could have a negative impact on our Home Gross Margins and home sales revenue.

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

If mortgage interest rates rise or if mortgage financing otherwise becomes less affordable, it could adversely affect our sales and business, and the duration and ultimate severity of the effects are uncertain.

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

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

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

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

We are utilizing a new enterprise resource planning (ERP) system in eight of our homebuilding divisions, our Corporate office and our non-homebuilding subsidiaries and, if we encounter significant problems with this implementation or implementation throughout our remaining homebuilding divisions, it could have an adverse impact on our operating activities and/or financial reporting capabilities.

Our financial services operations have concentration risks that could impact our results of operations.

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

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

Our income tax provision or benefit and other tax liabilities may be insufficient if taxing authorities are successful in asserting tax positions that are contrary to our position.

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

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

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

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

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

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

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The Company did not repurchase any shares during the third quarter of 2011. In conjunction with the acquisition of substantially all of the assets of SDC Homes, LLC and certain affiliated entities as of April 28, 2011, the Company issued 176,716 shares of its common stock, valued at \$5 million, to Robert Trent, the principal owner of the seller entities. The shares issued to Mr. Trent were unregistered, having been issued in a private placement under Section 4(2) of the Securities Act of 1933, and are subject to the terms of a restricted stock agreement. The agreement provides for 25%, 25% and 10% of the shares, respectively, to vest after each of the first three anniversaries of the

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effective date of the agreement, conditioned on Mr. Trent remaining employed. The final 40% of the stock will vest on December 31, 2015, conditioned on Mr. Trent remaining employed. The Company may use any unvested shares to apply against guaranty obligations that Mr. Trent has undertaken.

Item 3. Defaults Upon Senior Securities

None.

Item 4. (Removed and Reserved)

None.

Item 5. Other Information

On October 24, 2011, MDC's Board of Directors declared a quarterly cash dividend of twenty five cents (\$0.25) per share. The dividend will be paid on November 22, 2011 to shareowners of record on November 8, 2011.

Item 6. Exhibits

- 10.1 Third Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of September 14, 2011.
- 10.2 Fourth Amendment to Master Repurchase Agreement between HomeAmerican Mortgage Corporation, as Seller, and U.S. Bank National Association, as Agent and Buyer, dated as of September 29, 2011 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed September 30, 2011).*
- 10.3 Waiver Agreement among M.D.C. Holdings, Inc., Larry A. Mizel and David D. Mandarich, dated as of October 13, 2011 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed October 13, 2011).*
- 12 Ratio of Earnings to Fixed Charges Schedule.
- 31.1 Certification of Chief Executive Officer required by 17 CFR 240.13a-14(a), pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
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- 101 The following financial statements, formatted in XBRL: (i) Consolidated Balance Sheets as of September 30, 2011 and December 31, 2010, (ii) Consolidated Statements of Operations for the three and nine months ended September 30, 2011 and 2010, (iii) Consolidated Statements of Cash Flows for the nine months ended September 30, 2011 and 2010; and (iv) Notes to the Unaudited Consolidated Financial Statements, tagged as blocks of text. The information in Exhibit 101 is furnished and not filed, as provided in Rule 402 of Regulation S-T.

* Incorporated by reference

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SIGNATURE

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.

Date: November 3, 2011

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

By: /s/ Vilia Valentine
Vilia Valentine,
Vice President Finance, Corporate Controller and Chief
Accounting Officer
(principal financial officer and principal accounting officer)

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EXHIBIT INDEX

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