M I HOMES INC
Form 10-Q
October 25, 2013

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

FORM 10-Q

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

For the Quarterly Period Ended September 30, 2013

o	TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (D) OF THE SECURITIES ACT OF 1934

Commission File Number 1-12434

M/I HOMES, INC.
(Exact name of registrant as specified in it charter)

Ohio	31-1210837
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

3 Easton Oval, Suite 500, Columbus, Ohio 43219
(Address of principal executive offices) (Zip Code)
(614) 418-8000
(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 X 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 X No

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

Large accelerated filer		Accelerated filer	X
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 X

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.
Common shares, par value $.01 per share: 24,357,943 shares outstanding as of October 23, 2013.

M/I HOMES, INC.
FORM 10-Q

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M/I HOMES, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except par values)	September 30, 2013	December 31, 2012
ASSETS:		
Cash and cash equivalents	$142,475	$145,498
Restricted cash	15,806	8,680
Mortgage loans held for sale	60,388	71,121
Inventory	676,336	556,817
Property and equipment - net	10,346	10,439
Investment in unconsolidated joint ventures	34,088	11,732
Deferred income taxes, net of valuation allowance of $14.9 million and $135.7 million at September 30, 2013 and December 31, 2012, respectively	112,682	—
Other assets	30,946	27,013
TOTAL ASSETS	$1,083,067	$831,300
LIABILITIES AND SHAREHOLDERS' EQUITY		
LIABILITIES:		
Accounts payable	$85,804	$47,690
Customer deposits	14,918	10,239
Other liabilities	62,310	49,972
Community development district (“CDD”) obligations	3,419	4,634
Obligation for consolidated inventory not owned	1,576	19,105
Notes payable bank - financial services operations	55,614	67,957
Notes payable - other	8,126	11,105
Convertible senior subordinated notes due 2017	57,500	57,500
Convertible senior subordinated notes due 2018	86,250	—
Senior notes	227,970	227,670
TOTAL LIABILITIES	603,487	495,872
Commitments and contingencies	—	—
SHAREHOLDERS' EQUITY:		
Preferred shares - $.01 par value; authorized 2,000,000 shares; 2,000 and 4,000 shares issued at September 30, 2013 and December 31, 2012, respectively; 2,000 and 4,000 shares outstanding as of September 30, 2013 and December 31, 2012, respectively	48,163	96,325
Common shares - $.01 par value; authorized 38,000,000 shares; issued 27,092,723 and 24,631,723 shares at September 30, 2013 and December 31, 2012, respectively	271	246
Additional paid-in capital	235,880	180,289
Retained earnings	249,582	117,048
Treasury shares - at cost - 2,734,780 and 2,944,470 shares at September 30, 2013 and December 31, 2012, respectively	(54,316)	(58,480)
TOTAL SHAREHOLDERS' EQUITY	479,580	335,428
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$1,083,067	$831,300

See Notes to Unaudited Condensed Consolidated Financial Statements.

M/I HOMES, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands, except per share amounts)	2013	2012	2013	2012
Revenue	$275,195	$208,875	$700,475	$510,994
Costs and expenses:				
Land and housing	218,150	164,452	556,799	408,893
Impairment of inventory and investment in unconsolidated joint ventures	2,136	1,309	4,237	1,876
General and administrative	18,261	16,016	52,389	42,299
Selling	17,999	14,647	47,383	38,483
Equity in income of unconsolidated joint ventures	(278)	—	(278)	—
Interest	3,449	3,999	12,186	12,066
Loss on early extinguishment of debt	1,726	—	1,726	—
Total costs and expenses	261,443	200,423	674,442	503,617
Income before income taxes	13,752	8,452	26,033	7,377
(Benefit) provision for income taxes	(111,559)	138	(111,129)	(955)
Net income	$125,311	$8,314	$137,162	$8,332
Preferred dividends	1,219	—	2,438	—
Excess of fair value over book value of preferred shares redeemed	—	—	2,190	—
Net income to common shareholders	$124,092	$8,314	$132,534	$8,332
Earnings per common share:				
Basic	$5.09	$0.43	$5.61	$0.44
Diluted	$4.22	$0.42	$4.79	$0.43
Weighted average shares outstanding:				
Basic	24,358	19,434	23,642	19,014
Diluted	29,745	20,273	28,410	19,238

See Notes to Unaudited Condensed Consolidated Financial Statements.

M/I HOMES, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

	Nine Months Ended September 30, 2013							
	Preferred Shares		Common Shares					
(Dollars in thousands)	Shares Outstanding	Amount	Shares Outstanding	Amount	Additional Paid-in Capital	Retained Earnings	Treasury Shares	Total Shareholders' Equity
Balance at December 31, 2012	4,000	$96,325	21,687,253	$246	$180,289	$117,048	$(58,480)	$335,428
Net income	—	—	—	—	—	137,162	—	137,162
Fair value over carrying value of preferred shares redeemed	—	2,190	—	—	—	(2,190)	—	—
Dividends to shareholders, $609.375 per preferred share	—	—	—	—	—	(2,438)	—	(2,438)
Common share issuance	—	—	2,461,000	25	54,592	—	—	54,617
Preferred shares redeemed	(2,000)	(50,352)	—	—		—	—	(50,352)
Income tax effect of stock options and executive deferred compensation distributions	—	—	—	—	383	—	—	383
Stock options exercised	—	—	184,832	—	(1,031)	—	3,671	2,640
Stock-based compensation expense	—	—	—	—	1,835	—	—	1,835
Deferral of executive and director compensation	—	—	—	—	305	—	—	305
Executive and director deferred compensation distributions	—	—	24,858	—	(493)	—	493	—
Balance at September 30, 2013	2,000	$48,163	24,357,943	$271	$235,880	$249,582	$(54,316)	$479,580

See Notes to Unaudited Condensed Consolidated Financial Statements.

M/I HOMES, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine Months Ended September 30,	
(Dollars in thousands)	2013	2012
OPERATING ACTIVITIES:		
Net income	$137,162	$8,332
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Inventory valuation adjustments and abandoned land transaction write-offs	4,237	2,132
Equity in income of unconsolidated joint ventures	(278)	—
Bargain purchase gain	—	(1,219)
Mortgage loan originations	(426,636)	(355,075)
Proceeds from the sale of mortgage loans	439,151	354,443
Fair value adjustment of mortgage loans held for sale	(1,782)	(431)
Depreciation	3,777	4,940
Amortization of intangibles, debt discount and debt issue costs	2,555	1,822
Loss on early extinguishment of debt	1,726	—
Stock-based compensation expense	1,835	1,398
Deferred income tax expense	9,190	3,721
Deferred tax asset valuation allowances	(120,836)	(3,721)
Other	—	50
Change in assets and liabilities:		
Cash held in escrow	148	(37)
Inventory	(142,642)	(71,236)
Other assets	(2,443)	(4,030)
Accounts payable	38,114	23,016
Customer deposits	4,679	6,604
Accrued compensation	1,767	1,667
Other liabilities	9,840	11,303
Net cash used in operating activities	(40,436)	(16,321)
INVESTING ACTIVITIES:		
Change in restricted cash	(7,274)	32,391
Purchase of property and equipment	(1,654)	(858)
Return of capital from unconsolidated joint ventures	1,522	—
Acquisition, net of cash acquired	—	(4,707)
Investment in unconsolidated joint ventures	(25,496)	(949)
Net cash (used in) provided by investing activities	(32,902)	25,877
FINANCING ACTIVITIES:		
Repayment of senior notes, including transaction costs	—	(41,443)
Net proceeds from issuance of senior notes	—	29,700
Proceeds from issuance of convertible senior subordinated notes due 2018	86,250	—
Proceeds from issuance of convertible senior subordinated notes due 2017	—	57,500
Repayments of bank borrowings - net	(12,343)	2,234
	(2,979)	4,968

(Principal repayments of) proceeds from notes payable-other and CDD bond obligations		
Dividends paid on preferred shares	(2,438)	—
Net proceeds from issuance of common shares	54,617	42,085
Redemption of preferred shares	(50,352)	—
Debt issue costs	(5,463)	(5,843)
Proceeds from exercise of stock options	2,640	1,215
Excess tax deficiency from stock-based payment arrangements	383	—
Net cash provided by financing activities	70,315	90,416
Net (decrease) increase in cash and cash equivalents	(3,023)	99,972
Cash and cash equivalents balance at beginning of period	145,498	59,793
Cash and cash equivalents balance at end of period	$142,475	$159,765
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid during the year for:		
Interest — net of amount capitalized	$4,977	$5,442
Income taxes	$679	$280
NON-CASH TRANSACTIONS DURING THE PERIOD:		
Community development district infrastructure	$(1,215)	$(995)
Consolidated inventory not owned	$(17,529)	$3,608
Distribution of single-family lots from unconsolidated joint ventures	$1,912	$—

See Notes to Unaudited Condensed Consolidated Financial Statements.

M/I HOMES, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. Basis of Presentation

The accompanying Unaudited Condensed Consolidated Financial Statements (the "financial statements") of M/I Homes, Inc. and its subsidiaries (the "Company") and notes thereto have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission (the "SEC") for interim financial information. The financial statements include the accounts of M/I Homes, Inc. and its subsidiaries. All intercompany transactions have been eliminated. Results for the interim period are not necessarily indicative of results for a full year. In the opinion of management, the accompanying financial statements reflect all adjustments (all of which are normal and recurring in nature) necessary for a fair presentation of financial results for the interim periods presented. These financial statements should be read in conjunction with the Consolidated Financial Statements and Notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2012 (the "2012 Form 10-K").

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during that period. Actual results could differ from these estimates and have a significant impact on the financial condition and results of operations and cash flows. With regard to the Company, estimates and assumptions are inherent in calculations relating to valuation of inventory and investment in unconsolidated joint ventures, property and equipment depreciation, valuation of derivative financial instruments, accounts payable on inventory, accruals for costs to complete inventory, accruals for warranty claims, accruals for self-insured general liability claims, litigation, accruals for health care and workers' compensation, accruals for guaranteed or indemnified loans, stock-based compensation expense, income taxes, and contingencies. Items that could have a significant impact on these estimates and assumptions include the risks and uncertainties listed in "Item 1A. Risk Factors" in Part I of our 2012 Form 10-K, as the same may be updated from time to time in our subsequent filings with the SEC.

Reclassifications

The Company reclassified certain amounts presented in the Supplemental Condensed Consolidating Balance Sheet for the period ended December 31, 2012 and the Supplemental Condensed Consolidating Statement of Cash Flows for the nine months ended September 30, 2012 included in Note 13. The Company believes these reclassifications are immaterial to the supplemental condensed consolidating financial statements which are presented as supplemental information. These reclassifications do not affect the Company's consolidated financial statements for either period.

Impact of New Accounting Standards

In January 2013, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2013-01: Balance Sheet (Topic 210) - Disclosures about Offsetting Assets and Liabilities ("ASU 2013-01"). ASU 2013-01 amended ASU 2011-11 and will enhance disclosures required by the United States Generally Accepted Accounting Principles ("U.S. GAAP") by requiring additional information about financial and derivative instruments that are either (1) offset in accordance with Section 210-20-45 or Section 815-10-45 or (2) subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in accordance with Section 210-20-45 or Section 815-10-45. We are required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and for interim periods within those annual periods. The Company adopted this standard on January 1, 2013, and the adoption did not have a material impact on its Unaudited Condensed Consolidated Financial Statements.

In April 2013, the FASB issued ASU No. 2013-04: Liabilities (“ASU 2013-04”), which provides guidance for the recognition, measurement, and disclosure of obligations resulting from joint and several liability arrangements for which the total amount of the obligation is fixed at the reporting date. ASU 2013-04 is effective for us beginning January 1, 2014. The Company does not anticipate the adoption of this guidance will have a material impact on its Unaudited Condensed Consolidated Financial Statements or disclosures.

In July 2013, the FASB issued ASU No. 2013-11: Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists (“ASU 2013-11”). The amendments in ASU 2013-11 are intended to end inconsistent practices regarding the presentation of unrecognized tax benefits on the balance sheet. An entity will be required to present an unrecognized tax benefit as a reduction of a deferred tax asset for a net operating loss (“NOL”) or tax credit carryforward whenever the NOL or tax credit carryforward would be available to reduce the additional taxable income or tax due if the tax position is disallowed. An entity is required to apply the amendments prospectively for annual reporting periods

beginning after December 15, 2013, and for interim periods within those annual periods. Early adoption and retrospective application are permitted. The Company does not anticipate the adoption of this guidance will have a material impact on its Unaudited Condensed Consolidated Financial Statements or disclosures.

NOTE 2. Fair Value Measurements

There are three measurement input levels for determining fair value: Level 1, Level 2, and Level 3. Fair values determined by Level 1 inputs utilize quoted prices in active markets for identical assets or liabilities that the Company has the ability to access. Fair values determined by Level 2 inputs utilize inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals. Level 3 inputs are unobservable inputs for the asset or liability, and include situations where there is little, if any, market activity for the asset or liability.

Assets Measured on a Recurring Basis

The Company measures both mortgage loans held for sale and interest rate lock commitments (“IRLCs”) at fair value. In the normal course of business, our financial services segment enters into contractual commitments to extend credit to buyers of single-family homes with fixed expiration dates. The commitments become effective when the borrowers “lock-in” a specified interest rate within established time frames. Market risk arises if interest rates move adversely between the time of the “lock-in” of rates by the borrower and the sale date of the loan to an investor. To mitigate the effect of the interest rate risk inherent in providing rate lock commitments to borrowers, the Company enters into optional or mandatory delivery forward sale contracts to sell whole loans and mortgage-backed securities to broker/dealers. The forward sale contracts lock in an interest rate and price for the sale of loans similar to the specific rate lock commitments. The Company does not engage in speculative trading or derivative activities. Both the rate lock commitments to borrowers and the forward sale contracts to broker/dealers or investors are undesignated derivatives, and accordingly, are marked to fair value through earnings. Changes in fair value measurements are included in earnings in the accompanying statements of operations.

The fair value of mortgage loans held for sale is estimated based primarily on published prices for mortgage-backed securities with similar characteristics. To calculate the effects of interest rate movements, the Company utilizes applicable published mortgage-backed security prices, and multiplies the price movement between the rate lock date and the balance sheet date by the notional loan commitment amount. The Company generally sells loans on a servicing released basis, and receives a servicing release premium upon sale. Thus, the value of the servicing rights included in the fair value measurement is based upon contractual terms with investors and depends on the loan type. The Company applies a fallout rate to IRLCs when measuring the fair value of rate lock commitments. Fallout is defined as locked loan commitments for which the Company does not close a mortgage loan and is based on management’s judgment and company experience.

The fair value of the Company’s forward sales contracts to broker/dealers solely considers the market price movement of the same type of security between the trade date and the balance sheet date. The market price changes are multiplied by the notional amount of the forward sales contracts to measure the fair value.

Interest Rate Lock Commitments. IRLCs are extended to certain home-buying customers who have applied for a mortgage loan and meet certain defined credit and underwriting criteria. Typically, the IRLCs will have a duration of less than six months; however, in certain markets, the duration could extend to twelve months.

Some IRLCs are committed to a specific third party investor through the use of best-efforts whole loan delivery commitments matching the exact terms of the IRLC loan. Uncommitted IRLCs are considered derivative instruments and are fair value adjusted, with the resulting gain or loss recorded in current earnings.

Forward Sales of Mortgage-Backed Securities. Forward sales of mortgage-backed securities ("FMBSs") are used to protect uncommitted IRLC loans against the risk of changes in interest rates between the lock date and the funding date. FMBSs related to uncommitted IRLCs are classified and accounted for as non-designated derivative instruments and are recorded at fair value, with gains and losses recorded in current earnings.

Mortgage Loans Held for Sale. Mortgage loans held for sale consists primarily of single-family residential loans collateralized by the underlying property. Generally, all of the mortgage loans and related servicing rights are sold to third-party investors shortly after origination. During the intervening period between when a loan is closed and when it is sold to an investor, the interest rate risk is covered through the use of a best-efforts contract or by FMBSs. The FMBSs are classified and accounted for as non-designated derivative instruments, with gains and losses recorded in current earnings.

The table below shows the notional amounts of our financial instruments at September 30, 2013 and December 31, 2012:

Description of financial instrument (in thousands)	September 30, 2013	December 31, 2012
Best efforts contracts and related committed IRLCs	$4,417	$1,184
Uncommitted IRLCs	79,594	25,854
FMBSs related to uncommitted IRLCs	80,000	26,000
Best efforts contracts and related mortgage loans held for sale	3,025	25,441
FMBSs related to mortgage loans held for sale	55,000	44,000
Mortgage loans held for sale covered by FMBSs	54,720	44,524

The table below shows the level and measurement of assets and liabilities measured on a recurring basis at September 30, 2013 and December 31, 2012:

Description of Financial Instrument (in thousands)	Fair Value Measurements September 30, 2013	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Mortgage loans held for sale	$60,388	$—	$60,388	$—
Forward sales of mortgage-backed securities	(1,971)	—	(1,971)	—
Interest rate lock commitments	942	—	942	—
Best-efforts contracts	(179)	—	(179)	—
Total	$59,180	$—	$59,180	$—

Description of Financial Instrument (in thousands)	Fair Value Measurements December 31, 2012	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Mortgage loans held for sale	$71,121	$—	$71,121	$—
Forward sales of mortgage-backed securities	253	—	253	—
Interest rate lock commitments	1	—	1	—
Best-efforts contracts	(3)	—	(3)	—
Total	$71,372	$—	$71,372	$—

The following table sets forth the amount of (loss) gain recognized, within our revenue in the Unaudited Condensed Consolidated Statements of Operations, on assets and liabilities measured on a recurring basis for the three and nine months ended September 30, 2013 and 2012:

	Three Months Ended September 30,		Nine Months Ended September 30,	
Description (in thousands)	2013	2012	2013	2012
Mortgage loans held for sale	$3,365	$328	$1,782	$431
Forward sales of mortgage-backed securities	(5,262)	(838)	(2,224)	(925)
Interest rate lock commitments	1,677	341	941	328
Best-efforts contracts	(193)	(84)	(176)	(77)
Total (loss) gain recognized	$(413)	$(253)	$323	$(243)

The following tables set forth the fair value of the Company's derivative instruments and their location within the Unaudited Condensed Consolidated Balance Sheets for the periods indicated (except for mortgage loans held for sale which is disclosed as a separate line item):

	Asset Derivatives September 30, 2013		Liability Derivatives September 30, 2013	
Description of Derivatives	Balance Sheet Location	Fair Value (in thousands)	Balance Sheet Location	Fair Value (in thousands)
Forward sales of mortgage-backed securities	Other assets	$—	Other liabilities	$1,971
Interest rate lock commitments	Other assets	942	Other liabilities	—
Best-efforts contracts	Other assets	—	Other liabilities	179
Total fair value measurements		$942		$2,150

	Asset Derivatives December 31, 2012		Liability Derivatives December 31, 2012	
Description of Derivatives	Balance Sheet Location	Fair Value (in thousands)	Balance Sheet Location	Fair Value (in thousands)
Forward sales of mortgage-backed securities	Other assets	$253	Other liabilities	$—
Interest rate lock commitments	Other assets	1	Other liabilities	—
Best-efforts contracts	Other assets	—	Other liabilities	3
Total fair value measurements		$254		$3

Assets Measured on a Non-Recurring Basis

The Company assesses inventory for recoverability on a quarterly basis if events or changes in local or national economic conditions indicate that the carrying amount of an asset may not be recoverable. In conducting our quarterly review for indicators of impairment on a community level, we evaluate, among other things, margins on sales contracts in backlog, the margins on homes that have been delivered, expected changes in margins with regard to future home sales over the life of the community, expected changes in margins with regard to future land sales, the value of the land itself as well as any results from third party appraisals. We pay particular attention to communities in which inventory is moving at a slower than anticipated absorption pace, and communities whose average sales price and/or margins are trending downward and are anticipated to continue to trend downward. We also evaluate communities where management intends to lower the sales price or offer incentives in order to improve absorptions even if the community's historical results do not indicate a potential for impairment. From the review of all of these factors, we identify communities whose carrying values may exceed their estimated undiscounted future cash flows and run a test for recoverability. For those communities whose carrying values exceed the estimated undiscounted future cash flows and which are deemed to be impaired, the impairment recognized is measured by the amount by which the carrying amount of the communities exceeds the estimated fair value. Due to the fact that the Company's cash flow models and estimates of fair values are based upon management estimates and assumptions, unexpected changes in market conditions and/or changes in management's intentions with respect to the inventory may lead the Company to incur additional impairment charges in the future.

Our determination of fair value is based on projections and estimates, which are Level 3 measurement inputs. Our analysis is completed at a phase level within each community; therefore, changes in local conditions may affect one or several of our communities. For all of the categories listed below, the key assumptions relating to the valuations are dependent on project-specific local market and/or community conditions and are inherently uncertain. Because each inventory asset is unique, there are numerous inputs and assumptions used in our valuation techniques. Market factors that may impact these assumptions include:

- historical project results such as average sales price and sales pace, if closings have occurred in the project;
- competitors' market and/or community presence and their competitive actions;
- project specific attributes such as location desirability and uniqueness of product offering;
- potential for alternative product offerings to respond to local market conditions; and
- current economic and demographic conditions and related trends and forecasts.

These and other market factors that may impact project assumptions are considered by personnel in our homebuilding divisions as they prepare or update the forecasts for each community. Quantitative and qualitative factors other than home sales prices could significantly impact the potential for future impairments. The sales objectives can differ between communities, even within a given sub-market. For example, facts and circumstances in a given community may lead us to price our homes with the objective of yielding a higher sales absorption pace, while facts and circumstances in another community may lead us to price our homes to minimize deterioration in our gross margins, although it may result in a slower sales absorption pace. Furthermore, the key assumptions included in our estimated future undiscounted cash flows may be interrelated. For example, a decrease in estimated

base sales price or an increase in home sales incentives may result in a corresponding increase in sales absorption pace or a reduction in base house costs. Changes in our key assumptions, including estimated average selling price, construction and development costs, absorption pace, selling strategies, or discount rates, could materially impact future cash flow and fair value estimates.

As of September 30, 2013, our projections generally assume a gradual improvement in market conditions over time. If communities are not recoverable based on estimated future undiscounted cash flows, the impairment to be recognized is measured as the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets. The fair value of a community is estimated by discounting management's cash flow projections using an appropriate risk-adjusted interest rate. As of September 30, 2013, we utilized discount rates ranging from 13% to 16% in our valuations. The discount rate used in determining each asset's estimated fair value reflects the inherent risks associated with the related estimated cash flow stream, as well as current risk-free rates available in the market and estimated market risk premiums. For example, construction in progress inventory, which is closer to completion, will generally require a lower discount rate than land under development in communities consisting of multiple phases spanning several years of development.

Operating Communities. If an indicator for impairment exists for existing operating communities, the recoverability of assets is evaluated by comparing the carrying amount of the assets to estimated future undiscounted net cash flows expected to be generated by the assets based on home sales. These estimated cash flows are developed based primarily on management's assumptions relating to the specific community. The significant assumptions used to evaluate the recoverability of assets include: the timing of development and/or marketing phases; projected sales price and sales pace of each existing or planned community; the estimated land development, home construction, and selling costs of the community; overall market supply and demand; the local market; and competitive conditions. Management reviews these assumptions on a quarterly basis. While we consider available information to determine what we believe to be our best estimates as of the end of a reporting period, these estimates are subject to change in future reporting periods as facts and circumstances change. We believe the most critical assumptions in the Company's cash flow models are projected absorption pace for home sales, sales prices, and costs to build and deliver homes on a community by community basis.

In order to estimate the assumed absorption pace for home sales included in the Company's cash flow models, the Company analyzes the historical absorption pace in the community as well as other communities in the geographic area. In addition, the Company considers internal and external market studies and trends, which may include, but are not limited to, statistics on population demographics, unemployment rates, foreclosure sales, and availability of competing products in the geographic area where a community is located. When analyzing the Company's historical absorption pace for home sales and corresponding internal and external market studies, the Company places greater emphasis on more current metrics and trends such as the absorption pace realized in its most recent quarters and management's most current assessment of sales pace.

In order to estimate the sales prices included in its cash flow models, the Company considers the historical sales prices realized on homes it delivered in the community and other communities in the geographic area, as well as the sales prices included in its current backlog for such communities. In addition, the Company considers internal and external market studies and trends, which may include, but are not limited to, statistics on sales prices in neighboring communities, which include the impact of short sales, if any, and sales prices on similar products in non-neighboring communities in the geographic area where the community is located. When analyzing its historical sales prices and corresponding market studies, the Company places greater emphasis on more current metrics and trends such as the sales prices realized in its most recent quarters and the sales prices in current backlog. Based upon this analysis, the Company sets a sales price for each house type in the community which it believes will achieve an acceptable gross margin and sales pace in the community. This price becomes the price published to the sales force for use in its sales efforts. The Company then considers the average of these published sales prices when estimating the future sales

prices in its cash flow models, assuming no increase in weighted average sales price in 2013, a 4% increase in 2014 and 2015, and a 2% increase in 2016 and beyond.

In order to arrive at the Company's assumed costs to build and deliver homes, the Company generally assumes a cost structure reflecting contracts currently in place with its vendors and subcontractors, adjusted for any anticipated cost reduction initiatives or increases in cost structure. With respect to overhead included in the cash flow models, the Company uses forecasted rates included in the Company's annual budget adjusted for actual experience that is materially different than budgeted rates. The Company anticipates no increase in assumed weighted average costs in 2013, a 4% increase in 2014 and 2015, and a 2% increase in 2016 and beyond.

Future communities. If an indicator of impairment exists for raw land, land under development, or lots that management anticipates will be utilized for future homebuilding activities, the recoverability of assets is evaluated by comparing the carrying amount of the assets to the estimated future undiscounted cash flows expected to be generated by the assets based on home sales, consistent with the evaluations performed for operating communities discussed above.

For raw land, land under development, or lots that management intends to market for sale to a third party, but that do not meet all of the criteria to be classified as land held for sale as discussed below, the estimated fair value of the assets is determined based on either the estimated net sales proceeds expected to be realized on the sale of the assets or the estimated fair value determined using cash flow valuation techniques.

If the Company has not yet determined whether raw land, land under development, or lots will be utilized for future homebuilding activities or marketed for sale to a third party, the Company assesses the recoverability of the inventory using a probability-weighted approach.

Land held for sale. Land held for sale includes land that meets all of the following six criteria: (1) management, having the authority to approve the action, commits to a plan to sell the asset; (2) the asset is available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets; (3) an active program to locate a buyer and other actions required to complete the plan to sell the asset have been initiated; (4) the sale of the asset is probable, and transfer of the asset is expected to qualify for recognition as a completed sale, within one year; (5) the asset is being actively marketed for sale at a price that is reasonable in relation to its current fair value; and (6) actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn. The Company records land held for sale at the lower of its carrying value or estimated fair value less costs to sell. In performing the impairment evaluation for land held for sale, management considers, among other things, prices for land in recent comparable sales transactions, market analysis and recent bona fide offers received from outside third parties, as well as actual contracts. If the estimated fair value less the costs to sell an asset is less than the asset's current carrying value, the asset is written down to its estimated fair value less costs to sell.

Our quarterly assessments reflect management's best estimates. Due to the inherent uncertainties in management's estimates and uncertainties related to our operations and our industry as a whole, we are unable to determine at this time if and to what extent continuing future impairments will occur. Additionally, due to the volume of possible outcomes that can be generated from changes in the various model inputs for each community, we do not believe it is possible to create a sensitivity analysis that can provide meaningful information for the users of our financial statements.

Variable Interest Entities. In order to minimize our investment and risk of land exposure in a single location, we have periodically partnered with other land developers or homebuilders to share in the land investment and development of a property through joint ownership and development agreements, joint ventures, and other similar arrangements. During the nine month period ended September 30, 2013, we increased our total investment in such joint venture arrangements from December 31, 2012 by $22.4 million primarily due to a joint investment with another builder in a land development in our Southern region.

For joint venture arrangements where a special purpose entity is established to own the property, we generally enter into limited liability company or similar arrangements (“LLCs”) with the other partners. The Company's ownership in these LLCs as of September 30, 2013 ranged from 25% to 61%. These entities typically engage in land development activities for the purpose of distributing or selling developed lots to the Company and its partners in the LLC. With respect to our investments in these LLCs, we are required, under ASC 810-10, Consolidation (“ASC 810-10”), to evaluate whether or not such entities should be consolidated into our financial statements. We initially perform these evaluations when each new entity is created and upon any events that require reconsideration of the entity. In order to determine if we should consolidate an LLC, we determine (1) if the LLC is a Variable Interest Entity (“VIE”) and (2) if we are the primary beneficiary of the entity. To determine whether we are the primary beneficiary of an entity, we consider whether we have the ability to control the activities of the VIE that most significantly impact its economic performance. This analysis considers, among other things, whether we have the ability to determine the budget and

scope of land development work, if any; the ability to control financing decisions for the VIE; the ability to acquire additional land into the VIE or dispose of land in the VIE not under contract with M/I Homes; and the ability to change or amend the existing option contract with the VIE. If it is determined we are not able to control such activities, we are not considered the primary beneficiary of the VIE.

As of September 30, 2013, we have determined that one of the LLCs in which we have an interest meets the requirements of a VIE due to a lack of equity at risk in the entity. However, we have determined that we do not have substantive control over any of these entities, including our VIE, as we do not have the ability to control the activities that most significantly impact their economic performance. As a result, none of these LLCs are required to be consolidated into our financial statements and the entities are instead recorded in Investment in Unconsolidated Joint Ventures on our Unaudited Condensed Consolidated Balance Sheets.

We enter into option or purchase agreements to acquire land or lots, for which we generally pay non-refundable deposits. We also analyze these agreements under ASC 810-10 to determine whether we are the primary beneficiary of the VIE, if applicable, using

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an analysis similar to that described above. If we are deemed to be the primary beneficiary of the VIE, we will consolidate the VIE in our consolidated financial statements. In cases where we are the primary beneficiary, even though we do not have title to such land, we are required to consolidate these purchase/option agreements and reflect such assets and liabilities as Consolidated Inventory not Owned in our Unaudited Condensed Consolidated Balance Sheets.

Investment In Unconsolidated Joint Ventures. We use the equity method of accounting for investments in unconsolidated joint ventures over which we exercise significant influence but do not have a controlling interest. Under the equity method, our share of the unconsolidated joint ventures' earnings or loss, if any, is included in our statement of operations. We evaluate our investments in unconsolidated joint ventures for impairment at least quarterly as described below.

If the fair value of the investment is less than the investment's carrying value and the Company has determined that the decline in value is other than temporary, the Company would write down the value of the investment to fair value. The determination of whether an investment's fair value is less than the carrying value requires management to make certain assumptions regarding the amount and timing of future contributions to the unconsolidated joint venture, the timing of distribution of lots to the Company from the unconsolidated joint venture, the projected fair value of the lots at the time of distribution to the Company, and the estimated proceeds from, and timing of, the sale of land or lots to third parties. In determining the fair value of investments in unconsolidated joint ventures, the Company evaluates the projected cash flows associated with each unconsolidated joint venture. As of September 30, 2013, the Company used a discount rate of 16% in determining the fair value of investments in unconsolidated joint ventures. In addition to the assumptions management must make to determine if the investment's fair value is less than the carrying value, management must also use judgment in determining whether the impairment is other than temporary. The factors management considers are: (1) the length of time and the extent to which the market value has been less than cost; (2) the financial condition and near-term prospects of the company; and (3) the intent and ability of the Company to retain its investment in the unconsolidated joint venture for a period of time sufficient to allow for any anticipated recovery in market value. We believe that the Company's maximum exposure related to its investment in these unconsolidated joint ventures as of September 30, 2013 is the amount invested of $34.1 million (in addition to a $2.5 million note due to the Company from one of the unconsolidated joint ventures), although we expect to invest further amounts in these unconsolidated joint ventures as development of the properties progresses. Included in the Company's investment in unconsolidated joint ventures at September 30, 2013 and December 31, 2012 were $0.7 million and $0.8 million of capitalized interest and other costs, respectively.

Because of the high degree of judgment involved in developing these assumptions, it is possible that the Company may determine the investment is not impaired in the current period; however, due to the passage of time, change in market conditions, and/or changes in management's intentions with respect to the inventory, a change in assumptions could result and impairment could occur.

The table below summarizes the Company's assets measured on a non-recurring basis as of and for the three and nine months ended September 30, 2013 and 2012:

		Three Months Ended September 30,		Nine Months Ended September 30,	
Description (in thousands)	Hierarchy	2013	2012 (2)	2013	2012 (2)
Adjusted basis of inventory (1)	Level 3	$1,975	$2,108	$3,876	$2,350
Impairments		2,136	1,309	4,237	1,876
Initial basis of inventory (1)		$4,111	$3,417	$8,113	$4,226

The fair values in the table above represent only assets whose carrying values were adjusted in the respective period.

(2) The carrying values for these assets may have subsequently increased or decreased from the fair value reported due to activities that have occurred since the measurement date.

Financial Instruments

Counterparty Credit Risk. To reduce the risk associated with losses that would be recognized if counterparties failed to perform as contracted, the Company limits the entities with whom management can enter into commitments. This risk of accounting loss is the difference between the market rate at the time of non-performance by the counterparty and the rate to which the Company committed.

The following table presents the carrying amounts and fair values of the Company's financial instruments at September 30, 2013 and December 31, 2012. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (an exit price).

	September 30, 2013		December 31, 2012	
(In thousands)	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Assets:				
Cash, cash equivalents and restricted cash	$158,281	$158,281	$154,178	$154,178
Mortgage loans held for sale	60,388	60,388	71,121	71,121
Split dollar life insurance policies	176	174	710	678
Notes receivable	3,312	3,180	8,787	7,460
Commitments to extend real estate loans	942	942	1	1
Forward sales of mortgage-backed securities	—	—	253	253
Liabilities:				
Notes payable - banks	55,614	55,614	67,957	67,957
Notes payable - other	8,126	8,137	11,105	11,148
Convertible senior subordinated notes due 2017	57,500	65,406	57,500	74,175
Convertible senior subordinated notes due 2018	86,250	87,328	—	—
Senior notes due 2018	227,970	246,675	227,670	250,700
Best-efforts contracts for committed IRLCs and mortgage loans held for sale	179	179	3	3
Forward sales of mortgage-backed securities	1,971	1,971	—	—
Off-Balance Sheet Financial Instruments:				
Letters of credit	—	659	—	493

The following methods and assumptions were used by the Company in estimating its fair value disclosures of financial instruments at September 30, 2013 and December 31, 2012:

Cash, Cash Equivalents and Restricted Cash. The carrying amounts of these items approximate fair value because they are short-term by nature.

Mortgage Loans Held for Sale, Forward Sales of Mortgage-Backed Securities, Commitments to Extend Real Estate Loans, Best-Efforts Contracts for Committed IRLCs and Mortgage Loans Held for Sale, 2017 Convertible Senior Subordinated Notes, 2018 Convertible Senior Subordinated Notes and 2018 Senior Notes. The fair value of these financial instruments was determined based upon market quotes at September 30, 2013 and December 31, 2012. The market quotes used were quoted prices for similar assets or liabilities along with inputs taken from observable market data by correlation. The inputs were adjusted to account for the condition of the asset or liability.

Split Dollar Life Insurance Policies and Notes Receivable. The estimated fair value was determined by calculating the present value of the amounts based on the estimated timing of receipts using discount rates that incorporate management's estimate of risk associated with the corresponding note receivable. During the third quarter of 2013, the balance of our split dollar life insurance policies decreased by $0.5 million due to the surrender of a policy (and termination of the related split-dollar agreement) by an officer.

Notes Payable - Banks. The interest rate available to the Company in the third quarter of 2013 fluctuated with the Alternate Base Rate or the Eurodollar Rate (for the Company's new $200 million unsecured revolving credit facility (the “Credit Facility”) or LIBOR (for M/I Financial Corp.'s $100 million secured mortgage warehousing agreement as amended and restated on March 29, 2013 (the “MIF Mortgage Warehousing Agreement”) and for M/I Financial's $15

million mortgage repurchase agreement dated November 13, 2012, as amended (the “MIF Mortgage Repurchase Facility”)), and thus their carrying value is a reasonable estimate of fair value. During the second quarter of 2013, M/I Financial exercised the accordion feature under the MIF Mortgage Warehousing Agreement to increase the maximum borrowing availability amount thereunder by $20.0 million to $100.0 million.

Notes Payable - Other. The estimated fair value was determined by calculating the present value of the future cash flows using the Company's current incremental borrowing rate.

Letters of Credit. Letters of credit of $29.4 million and $25.7 million represent potential commitments at September 30, 2013 and December 31, 2012, respectively. The letters of credit generally expire within one or two years. The estimated fair value of letters of credit was determined using fees currently charged for similar agreements.

NOTE 3. Inventory

A summary of the Company's inventory as of September 30, 2013 and December 31, 2012 is as follows:

(In thousands)	September 30, 2013	December 31, 2012
Single-family lots, land and land development costs	$283,455	$257,397
Land held for sale	6,899	8,442
Homes under construction	331,969	221,432
Model homes and furnishings - at cost (less accumulated depreciation: September 30, 2013 - $5,242; December 31, 2012 - $4,883)	35,664	37,080
Community development district infrastructure	3,418	4,634
Land purchase deposits	13,355	8,727
Consolidated inventory not owned	1,576	19,105
Total inventory	$676,336	$556,817

Single-family lots, land and land development costs include raw land that the Company has purchased to develop into lots, costs incurred to develop the raw land into lots, and lots for which development has been completed, but which have not yet been used to start construction of a home.

Homes under construction include homes that are in various stages of construction. As of September 30, 2013 and December 31, 2012, we had 822 homes (with a carrying value of $110.0 million) and 649 homes (with a carrying value of $89.8 million), respectively, included in homes under construction that were not subject to a sales contract.

Model homes and furnishings include homes that are under construction or have been completed and are being used as sales models. The amount also includes the net book value of furnishings included in our model homes. Depreciation on model home furnishings is recorded using an accelerated method over the estimated useful life of the assets, typically three years.

The Company assesses inventory for recoverability on a quarterly basis. Refer to Note 2 of our Unaudited Condensed Consolidated Financial Statements for additional details relating to our procedures for evaluating our inventories for impairment.

Land purchase deposits include both refundable and non-refundable amounts paid to third party sellers relating to the purchase of land. On an ongoing basis, the Company evaluates the land option agreements relating to the land purchase deposits. In the period during which the Company makes the decision not to proceed with the purchase of land under an agreement, the Company writes off any deposits and accumulated pre-acquisition costs relating to such agreement.

NOTE 4. Valuation Adjustments and Write-offs

The Company assesses inventory for recoverability on a quarterly basis, by reviewing for impairment whenever events or changes in local or national economic conditions indicate that the carrying amount of an asset may not be recoverable.

A summary of the Company's valuation adjustments and write-offs for the three and nine months ended September 30, 2013 and 2012 is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	2013	2012	2013	2012
Impairment of operating communities:				
Midwest	$481	$—	$481	$10
Southern	—	—	—	—
Mid-Atlantic	—	—	—	—
Total impairment of operating communities (a)	$481	$—	$481	$10
Impairment of future communities:				
Midwest	$1,655	$1,309	$2,465	$1,771
Southern	—	—	—	—
Mid-Atlantic	—	—	—	—
Total impairment of future communities (a)	$1,655	$1,309	$2,465	$1,771
Impairment of land held for sale:				
Midwest	$—	$—	$1,291	$95
Southern	—	—	—	—
Mid-Atlantic	—	—	—	—
Total impairment of land held for sale (a)	$—	$—	$1,291	$95
Option deposits and pre-acquisition costs write-offs:				
Midwest	$—	$—	$—	$36
Southern	—	—	—	110
Mid-Atlantic	—	—	—	110
Total option deposits and pre-acquisition costs write-offs (b)	$—	$—	$—	$256
Impairment of investments in unconsolidated joint ventures:				
Midwest	$—	$—	$—	$—
Southern	—	—	—	—
Mid-Atlantic	—	—	—	—
Total impairment of investments in unconsolidated joint ventures (a)	$—	$—	$—	$—
Total impairments and write-offs of option deposits and pre-acquisition costs	$2,136	$1,309	$4,237	$2,132

(a) Amounts are recorded within Impairment of inventory and investment in unconsolidated joint ventures in the Company's Unaudited Condensed Consolidated Statements of Operations.

(b) Amounts are recorded within General and administrative expenses in the Company's Unaudited Condensed Consolidated Statements of Operations.

NOTE 5. Capitalized Interest

The Company capitalizes interest during land development and home construction. Capitalized interest is charged to cost of sales as the related inventory is delivered to a third party. The summary of capitalized interest for the three and nine months ended September 30, 2013 and 2012 is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	2013	2012	2013	2012
Capitalized interest, beginning of period	$14,260	$17,967	$15,376	$18,869
Interest capitalized to inventory	3,940	2,574	10,045	7,128
Capitalized interest charged to cost of sales	(4,074)	(3,755)	(11,295)	(9,211)
Capitalized interest, end of period	$14,126	$16,786	$14,126	$16,786
Interest incurred	$7,389	$6,573	$22,231	$19,194

NOTE 6. Guarantees and Indemnifications

Warranty

Warranty reserves are recorded for warranties under our Home Builder's Limited Warranty ("HBLW") and our 10-year (Texas markets only) and 30-year (all markets excluding Texas) transferable structural warranty in Other liabilities on the Company's Unaudited Condensed Consolidated Balance Sheets.

The warranty reserves for the HBLW are established as a percentage of average sales price and adjusted based on historical payment patterns determined, generally, by geographic area and recent trends. Factors that are given consideration in determining the HBLW reserves include: (1) the historical range of amounts paid per average sales price on a home; (2) type and mix of amenity packages added to the home; (3) any warranty expenditures not considered to be normal and recurring; (4) timing of payments; (5) improvements in quality of construction expected to impact future warranty expenditures; and (6) conditions that may affect certain projects and require a different percentage of average sales price for those specific projects. Changes in estimates for warranties occur due to changes in the historical payment experience and differences between the actual payment pattern experienced during the period and the historical payment pattern used in our evaluation of the warranty reserve balance at the end of each quarter. Actual future warranty costs could differ from our current estimated amount.

Our warranty reserves for our transferable structural warranty programs are established on a per-unit basis. While the structural warranty reserve is recorded as each house closes, the sufficiency of the structural warranty per unit charge and total reserve is re-evaluated on an annual basis, with the assistance of an actuary, using our own historical data and trends, industry-wide historical data and trends, and other project specific factors. The reserves are also evaluated quarterly and adjusted if we encounter activity that is inconsistent with the historical experience used in the annual analysis. These reserves are subject to variability due to uncertainties regarding structural defect claims for products we build, the markets in which we build, claim settlement history, insurance and legal interpretations, among other factors.

While we believe that our warranty reserves are sufficient to cover our projected costs, there can be no assurances that historical data and trends will accurately predict our actual warranty costs.

A summary of warranty activity for the three and nine months ended September 30, 2013 and 2012 is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	2013	2012	2013	2012
Warranty reserves, beginning of period	$10,388	$8,733	$10,438	$9,025
Warranty expense on homes delivered during the period	1,999	1,646	5,004	4,021
Changes in estimates for pre-existing warranties	321	141	422	231
Settlements made during the period	(1,952)	(1,524)	(5,108)	(4,281)
Warranty reserves, end of period	$10,756	$8,996	$10,756	$8,996

Guarantees

In the ordinary course of business, M/I Financial Corp. ("M/I Financial"), a 100%-owned subsidiary of M/I Homes, Inc., enters into agreements that guarantee certain purchasers of its mortgage loans that M/I Financial will repurchase a loan if certain conditions occur, primarily if the mortgagor does not meet those conditions of the loan within the first six months after the sale of the loan. Loans totaling approximately $6.1 million and $3.1 million were covered under the above guarantees as of September 30, 2013 and December 31, 2012, respectively. A portion of the revenue paid to M/I Financial for providing the guarantees on the above loans was deferred at September 30, 2013, and will be

recognized in income as M/I Financial is released from its obligation under the guarantees. M/I Financial did not repurchase any loans under the above agreements during the nine months ended September 30, 2013. The risk associated with the guarantees above is offset by the value of the underlying assets.

M/I Financial has received inquiries concerning underwriting matters from purchasers of its loans regarding certain loans totaling approximately $8.4 million and $7.9 million at September 30, 2013 and December 31, 2012, respectively. The risk associated with the guarantees above is offset by the value of the underlying assets.

M/I Financial has also guaranteed the collectability of certain loans to third party insurers (U.S. Department of Housing and Urban Development and U.S. Veterans Administration) of those loans for periods ranging from five to thirty years. As of both September 30, 2013 and December 31, 2012, the total of all loans indemnified to third party insurers relating to the above agreements was $1.0 million. The maximum potential amount of future payments is equal to the outstanding loan value less the value of the underlying asset plus administrative costs incurred related to foreclosure on the loans, should this event occur.

The Company has recorded a liability relating to the guarantees described above totaling $2.9 million and $2.6 million at September 30, 2013 and December 31, 2012, respectively, which is management's best estimate of the Company's liability.

At September 30, 2013, the Company had outstanding $230.0 million aggregate principal amount of 8.625% Senior Notes due 2018 (the “2018 Senior Notes”), $57.5 million aggregate principal amount of 3.25% Convertible Senior Subordinated Notes due 2017 (the “2017 Convertible Senior Subordinated Notes”) and $86.3 million aggregate principal amount of 3.0% Convertible Senior Subordinated Notes due 2018 (the “2018 Convertible Senior Subordinated Notes”). The Company's obligations under the 2018 Senior Notes and the Credit Facility are guaranteed jointly and severally on a senior unsecured basis by all of the Company's subsidiaries, with the exception of subsidiaries that are primarily engaged in the business of mortgage financing, title insurance or similar financial businesses relating to the homebuilding and home sales business, certain subsidiaries that are not 100%-owned by the Company or another subsidiary, and other subsidiaries designated by the Company as Unrestricted Subsidiaries (as defined in Note 13), subject to limitations on the aggregate amount invested in such Unrestricted Subsidiaries in accordance with the terms of the Credit Facility and the Indenture for the 2018 Senior Notes. The Company's obligations under the 2017 Convertible Senior Subordinated Notes and the 2018 Convertible Senior Subordinated Notes are guaranteed jointly and severally on a senior subordinated unsecured basis by the same subsidiaries of the Company that are guarantors for the 2018 Senior Notes and the Credit Facility (the “Guarantor Subsidiaries”). Refer to Note 9 for a description of the guarantees of the Credit Facility.

NOTE 7. Commitments and Contingencies

At September 30, 2013, the Company had outstanding approximately $91.8 million of completion bonds and standby letters of credit, some of which were issued to various local governmental entities that expire at various times through October 2018. Included in this total are: (1) $59.2 million of performance and maintenance bonds and $13.6 million of performance letters of credit that serve as completion bonds for land development work in progress; (2) $15.8 million of financial letters of credit, of which $8.4 million represent deposits on land and lot purchase agreements; and (3) $3.2 million of financial bonds.

At September 30, 2013, the Company also had options and contingent purchase agreements to acquire land and developed lots with an aggregate purchase price of approximately $340.1 million. Purchase of properties under these agreements is contingent upon satisfaction of certain requirements by the Company and the sellers.

NOTE 8. Legal Liabilities

The Company and certain of its subsidiaries have been named as defendants in certain claims, complaints and legal actions which are incidental to our business. Certain of the liabilities resulting from these matters are covered by insurance. While management currently believes that the ultimate resolution of these matters, individually and in the aggregate, will not have a material effect on the Company's financial position, results of operations and cash flows, such matters are subject to inherent uncertainties. The Company has recorded a liability to provide for the anticipated costs, including legal defense costs, associated with the resolution of these matters. However, it is possible that the costs to resolve these matters could differ from the recorded estimates and, therefore, have a material effect on the Company's net income for the periods in which the matters are resolved. At both September 30, 2013 and December 31, 2012, we had $0.3 million reserved for legal expenses.

NOTE 9. Debt

Notes Payable - Homebuilding

On July 18, 2013, the Company entered into the Credit Facility, which has a maximum borrowing availability of $200 million. The Credit Facility matures on July 18, 2016. The Credit Facility contains an uncommitted $25 million accordion feature under which its aggregate principal amount can be increased to up to $225 million, subject to certain conditions, including obtaining additional commitments from existing or new lenders, as well as a sub-limit of $100 million for the issuance of letters of credit. Interest on amounts borrowed under the Credit Facility is payable at a rate based on either the Alternate Base Rate plus 2.25% or at the Eurodollar Rate plus 3.25%. Borrowings under the Credit Facility are unsecured and availability is subject to, among other things, a borrowing base. The Credit Facility also contains certain financial covenants, including a minimum tangible net worth requirement and a maximum leverage covenant that prohibits the leverage ratio (as defined therein) from exceeding 60%. In addition, we are restricted from allowing the amount of unsold owned land to exceed exceed 125% of the sum of tangible net worth and subordinated debt, we are prohibited from making investments in Unrestricted Subsidiaries and Joint Ventures in excess of 30% of tangible net worth, and we are required to maintain either (i) an interest coverage ratio (as defined therein) of at least 1.50 to 1.00 or (ii) liquidity (as defined therein) of an amount not less than our consolidated interest incurred during the trailing 12 months. At September 30, 2013, the Company was in compliance with all financial covenants of the Credit Facility.

The Credit Facility replaced the $140 million secured revolving credit facility (the “Prior Credit Facility”) that was scheduled to mature on December 31, 2014. The guarantors of the Credit Facility are the same subsidiaries that guarantee the 2018 Senior Notes, the 2017 Convertible Senior Subordinated Notes and the 2018 Convertible Senior Subordinated Notes. The Company incurred no prepayment penalties in connection with the termination and replacement of the Prior Credit Facility; however, the Company recorded a $1.7 million loss on early extinguishment of debt related to unamortized issuance fees on the Prior Credit Facility.

At September 30, 2013, borrowing availability under the Credit Facility in accordance with the borrowing base calculation was $352.9 million, so the full amount of the $200 million facility was available, and there were no borrowings outstanding and $13.9 million of letters of credit outstanding under the Credit Facility, leaving net remaining borrowing availability of $186.1 million as of September 30, 2013.

The Company is party to three secured credit agreements for the issuance of letters of credit outside of the Credit Facility (collectively, the “Letter of Credit Facilities”). During the three months ended September 30, 2013, the Company extended the maturity dates on two of the Letter of Credit Facilities for an additional year to August 31, 2014 and September 30, 2014, respectively, while also increasing the maximum available amount under the facility maturing on September 30, 2014 from $8.0 million to $10.0 million. At September 30, 2013, there was $15.5 million of outstanding letters of credit in aggregate under the Company's three Letter of Credit Facilities, which were collateralized with $15.8 million of the Company's cash.

Notes Payable — Financial Services

In March 2013, M/I Financial amended and restated the MIF Mortgage Warehousing Agreement, which, among other things, increased the maximum borrowing availability to $80.0 million and included an accordion feature which allowed for an increase of the maximum borrowing availability of up to an additional $20.0 million (subject to certain conditions, including obtaining additional commitments from existing or new lenders), extended the expiration date to March 28, 2014, and increased the maximum principal amount permitted to be outstanding at any one time in aggregate under all warehouse credit lines to $125.0 million. The interest rate was also adjusted to a per annum rate equal to the greater of (1) the floating LIBOR rate plus 275 basis points and (2) 3.50%. On June 3, 2013, M/I Financial exercised the accordion feature described above to increase the amount of our maximum borrowing availability under the MIF Mortgage Warehousing Agreement to $100.0 million by obtaining additional bank commitments totaling $20.0 million.

On November 13, 2012, M/I Financial entered into the MIF Mortgage Repurchase Facility with a maximum borrowing availability of $15.0 million and an expiration date of November 12, 2013. As is typical for similar credit facilities in the mortgage origination industry, at closing, the expiration of the MIF Mortgage Repurchase Facility was set at approximately one year and is under consideration for extension annually by the participating lenders. We expect to extend the MIF Mortgage Repurchase Facility on or prior to the current expiration date of November 12, 2013, but we cannot provide any assurance that we will be able to obtain such an extension.

At September 30, 2013, M/I Financial's total combined maximum borrowing availability under the two credit facilities was $115.0 million. At September 30, 2013, M/I Financial had $55.6 million outstanding on a combined basis under its credit facilities and was in compliance with all financial covenants of those agreements.

Convertible Senior Subordinated Notes

In March 2013, the Company issued $86.3 million aggregate principal amount of 2018 Convertible Senior Subordinated Notes. The 2018 Convertible Senior Subordinated Notes bear interest at a rate of 3.0% per year, payable semiannually in arrears on March 1 and September 1 of each year. The 2018 Convertible Senior Subordinated Notes

mature on March 1, 2018. At any time prior to the close of business on the second scheduled trading day immediately preceding the maturity date, holders may convert their 2018 Convertible Senior Subordinated Notes into the Company's common shares. The conversion rate initially equals 30.9478 shares per $1,000 of principal amount. This corresponds to an initial conversion price of approximately $32.31 per common share, which equates to approximately 2.7 million common shares. The conversion rate is subject to adjustment upon the occurrence of certain events. The 2018 Convertible Senior Subordinated Notes are fully and unconditionally guaranteed on a senior subordinated unsecured basis by those subsidiaries of the Company that are guarantors under the Company's 2018 Senior Notes and 2017 Convertible Senior Subordinated Notes. The 2018 Convertible Senior Subordinated Notes are senior subordinated unsecured obligations of the Company and the subsidiary guarantors and are subordinated in right of payment to our existing and future senior indebtedness and are also effectively subordinated to our existing and future secured indebtedness with respect to any assets comprising security or collateral for such indebtedness. The indenture governing the 2018 Convertible Senior Subordinated Notes provides that the Company may not redeem the 2018 Convertible Senior Subordinated Notes prior to March 6, 2016, but also

contains provisions requiring the Company to repurchase the notes (subject to certain exceptions), at a holder's option, upon the occurrence of a fundamental change (as defined in the indenture).

On or after March 6, 2016, the Company may redeem for cash any or all of the 2018 Convertible Senior Subordinated Notes (except for any 2018 Convertible Senior Subordinated Notes that the Company is required to repurchase in connection with a fundamental change), but only if the last reported sale price of the Company's common shares exceeds 130% of the applicable conversion price for the notes on each of at least 20 applicable trading days. The 20 trading days do not need to be consecutive, but must occur during a period of 30 consecutive trading days that ends within 10 trading days immediately prior to the date the Company provides the notice of redemption. The redemption price for the 2018 Convertible Senior Subordinated Notes to be redeemed will equal 100% of the principal amount, plus accrued and unpaid interest, if any.

In September 2012, the Company issued $57.5 million aggregate principal amount of 2017 Convertible Senior Subordinated Notes. The 2017 Convertible Senior Subordinated Notes bear interest at a rate of 3.25% per year, payable semiannually in arrears on March 15 and September 15 of each year. The 2017 Convertible Senior Subordinated Notes mature on September 15, 2017. At any time prior to the close of business on the second scheduled trading day immediately preceding the maturity date, holders may convert their 2017 Convertible Senior Subordinated Notes into the Company's common shares. The conversion rate initially equals 42.0159 shares per $1,000 of principal amount. This corresponds to an initial conversion price of approximately $23.80 per common share, which equates to approximately 2.4 million common shares. The conversion rate is subject to adjustment upon the occurrence of certain events. The 2017 Convertible Senior Subordinated Notes are fully and unconditionally guaranteed on a senior subordinated unsecured basis by those subsidiaries of the Company that are guarantors under the Company's 2018 Senior Notes and 2018 Convertible Senior Subordinated Notes. The 2017 Convertible Senior Subordinated Notes are senior subordinated unsecured obligations of the Company and the subsidiary guarantors and are subordinated in right of payment to our existing and future senior indebtedness and are also effectively subordinated to our existing and future secured indebtedness with respect to any assets comprising security or collateral for such indebtedness. The indenture governing the 2017 Convertible Senior Subordinated Notes provides that we may not redeem the notes prior to their stated maturity date, but also contains provisions requiring the Company to repurchase the 2017 Convertible Senior Subordinated Notes (subject to certain exceptions), at a holder's option, upon the occurrence of a fundamental change (as defined in the indenture).

Senior Notes

As of September 30, 2013, we had $230.0 million of our 2018 Senior Notes outstanding. The 2018 Senior Notes bear interest at a rate of 8.625% per year, payable semiannually in arrears on May 15 and November 15 of each year, and mature on November 15, 2018. The 2018 Senior Notes are general, unsecured senior obligations of the Company and the subsidiary guarantors and rank equally in right of payment with all our existing and future unsecured senior indebtedness. The 2018 Senior Notes are fully and unconditionally guaranteed on a senior unsecured basis by all of our subsidiaries, with the exception of subsidiaries that are primarily engaged in the business of mortgage financing, title insurance or similar financial businesses relating to the homebuilding and home sales business, certain subsidiaries that are not 100%-owned by the Company or another subsidiary, and other subsidiaries designated by the Company as Unrestricted Subsidiaries in accordance with the terms of the indenture.

The indenture governing our 2018 Senior Notes limits our ability to pay dividends on, and repurchase, our common shares and our 9.75% Series A Preferred Shares (the “Series A Preferred Shares”) to the amount of the positive balance in our “restricted payments basket,” as defined in the indenture. The restricted payments basket was $127.5 million at September 30, 2013. The increase in the balance of our restricted payments basket from the second quarter of 2013 was primarily due to the net income of our Restricted Subsidiaries in the third quarter of 2013, offset partially by a $1.2 million dividend payment made on our Series A Preferred Shares on September 16, 2013. We are permitted to

pay dividends on, and repurchase, our common shares and Series A Preferred Shares to the extent of the positive balance in our restricted payments basket. The determination to pay future dividends on, or make future repurchases of, our common shares or Series A Preferred Shares will be at the discretion of our board of directors and will depend upon our results of operations, financial condition, capital requirements and compliance with debt covenants and the terms of our Series A Preferred Shares, and other factors deemed relevant by our board of directors.

NOTE 10. Earnings Per Share

The table below presents a reconciliation between basic and diluted weighted average shares outstanding, net income available to common shareholders and basic and diluted income per share for the three and nine months ended September 30, 2013 and 2012:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands, except per share amounts)	2013	2012	2013	2012
NUMERATOR				
Net income	$125,311	$8,314	$137,162	$8,332
Preferred stock dividends	(1,219)	—	(2,438)	—
Excess of fair value over book value of preferred shares redeemed	—	—	(2,190)	—
Interest on 3.25% convertible senior subordinated notes due 2017	611	128	1,833	—
Interest on 3.00% convertible senior subordinated notes due 2018	824	—	1,851	—
Net income to common shareholders	125,527	8,442	136,218	8,332
DENOMINATOR				
Basic weighted average shares outstanding	24,358	19,434	23,642	19,014
Effect of dilutive securities:				
Stock option awards	183	187	246	92
Deferred compensation awards	119	127	111	132
3.25% convertible senior subordinated notes due 2017	2,416	525	2,416	—
3.00% convertible senior subordinated notes due 2018	2,669	—	1,995	—
Diluted weighted average shares outstanding - adjusted for assumed conversions	29,745	20,273	28,410	19,238
Earnings per common share				
Basic	$5.09	$0.43	$5.61	$0.44
Diluted	$4.22	$0.42	$4.79	$0.43
Anti-dilutive equity awards not included in the calculation of diluted earnings per common share	998	695	951	1,003

During both the second and third quarters of 2013, the Company declared a cash dividend of $609.375 per preferred share on its 2,000 outstanding Series A Preferred Shares. The dividend was paid on June 17, 2013 and September 16, 2013 to holders of record as of June 1, 2013 and September 1, 2013 for $1.2 million in cash, respectively.

In March 2013, the Company announced its intention to redeem 2,000 of its outstanding Series A Preferred Shares and recognized a $2.2 million non-cash equity charge in the first quarter of 2013 related to the excess of fair value over carrying value relating primarily to the original issuance costs that were paid in 2007. This charge reduced net income to common shareholders in the earnings per share calculation above for the nine month period ended September 30, 2013. On April 10, 2013, the Company redeemed the 2,000 Series A Preferred Shares for $50.4 million in cash.

In March 2013, the Company also issued 2.461 million common shares in a public offering at a price of $23.50 per share (for net proceeds of $54.6 million), which shares are included above in our total basic weighted average shares outstanding for the nine month period ended September 30, 2013.

For the three months ended September 30, 2013 and 2012 and for the nine months ended September 30, 2013, the effect of convertible debt was included in the diluted earnings per share calculations. For the nine months ended September 30, 2012, the effect of convertible debt was not included in the diluted earnings per share calculations as it would have been anti-dilutive.

NOTE 11. Income Taxes

The Company records income taxes under the asset and liability method, whereby deferred tax assets and liabilities are recognized based on future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and attributable to operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply in the years in which the temporary differences are expected to be recovered or paid. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in earnings in the period when the changes are enacted. At September 30, 2013, the Company's net gross deferred tax asset balance was $126.6 million, of which $127.6 million were gross deferred tax assets (reported as such on the Company's consolidated balance

sheets, net of a $14.9 million valuation allowance), and $1.0 million were gross deferred tax liabilities (included in other liabilities on the Company's consolidated balance sheets).
In accordance with ASC 740-10, Income Taxes, we evaluate our deferred tax assets, including the benefit from net operating losses (“NOLs”) and tax credit carryforwards, to determine if a valuation allowance is required. Companies must assess, using significant judgments, whether a valuation allowance should be established based on the consideration of all available evidence using a “more likely than not” standard with significant weight being given to evidence that can be objectively verified. This assessment gives appropriate consideration to all positive and negative evidence related to the realization of the deferred tax assets and considers, among other matters, the nature, frequency and severity of current and cumulative losses, forecasts of future profitability, the length of statutory carryforward periods, our experience with operating losses and our experience of utilizing tax credit carryforwards and tax planning alternatives. Based upon a review of all available evidence, we recorded a full valuation allowance against our deferred tax assets during 2008 due to economic conditions and the weight of negative evidence at the time.

During the quarter ended September 30, 2013, the Company concluded that it was more likely than not that the majority of its deferred tax assets would be utilized. This conclusion was based on a detailed evaluation of all relevant evidence, both positive and negative. The Company is required to use judgment in considering the relative impact of negative and positive evidence when determining the need for a valuation allowance for its deferred tax asset. The weight given to the potential effect of negative and positive evidence shall be commensurate with the extent to which it can be objectively verified. The more negative evidence that exists, the more positive evidence is needed.

The positive evidence considered by the Company in its evaluation for each of our taxing jurisdictions was the objective evidence related to our past and current financial results, including a period of sustained profitability comprising six consecutive quarters of pre-tax net income totaling $43.2 million, and the projected utilization of a majority of our current NOL carryforwards and temporary differences as they reverse in the carryforward periods, generally 20 years. Other positive evidence considered, among other things, was our expectation of continued earnings, and continued indications of a sustained recovery in the housing markets in which the Company operates, as evidenced by the significant increases experienced by the Company in several key financial indicators compared to the prior year, including new contracts, revenues, backlog sales value, new home deliveries and declining overhead leverage as a percent of revenue. We believe that economic data, such as recent and forecasted increases in housing starts, homebuilding volume and average sales prices, also affirm the recovery in the housing industry. We believe historically low mortgage rates, affordable home prices, reduced foreclosures, and a favorable home ownership to rental comparison continue to drive the recovery in the housing industry.
The most significant direct negative evidence that currently exists is that the Company is currently in a four-year cumulative loss position, which period represents our estimated business cycle. However, at September 30, 2013, the Company's cumulative four-year loss has declined significantly as a result of six consecutive quarters of profitability and, based on the Company's current earnings level, the Company will realize a majority of its deferred tax assets. Other negative evidence considered was the recent rise in mortgage interest rates and the potential impact of such rise on our business. While we believe it has caused a temporary slow down in the pace of the housing recovery and related trends compared to previous quarters in 2013, we believe the demand for housing continues to increase new contracts, as evidenced by the 15% increase in new contracts that we experienced during the three months ended September 30, 2013 when compared to the same period in 2012 as well as other factors.
Based on its analysis of positive and negative evidence, the Company concluded that the objective positive evidence outweighed the negative evidence, and that the Company will more likely than not realize a majority of its deferred tax assets. In accordance with GAAP, when a change in valuation allowance is recognized as a result of a change in judgment in an interim period, a portion of the valuation allowance to be reversed must be spread over the remaining interim periods. Accordingly, the Company reversed $111.6 million of its deferred tax asset valuation allowance during the third quarter of 2013 and retained a $4.7 million valuation allowance for estimated utilization pertaining to estimated earnings in the fourth quarter of 2013. In addition to the retained $4.7 million valuation allowance, the Company retained an additional $10.2 million valuation allowance for certain state jurisdictions which have a shorter

NOL carryforward utilization period or a large NOL carryforward relative to their current earnings. In future periods, the remaining valuation allowance for these state jurisdictions will be evaluated to determine if sufficient positive evidence indicates that it is more likely than not that an additional portion of the underlying state NOL carryforwards will be realized. The Company's net gross deferred tax assets were $126.6 million at September 30, 2013, which, inclusive of our valuation allowance, results in a net deferred tax asset of $111.6 million.

The tax effects of the significant temporary differences that comprise the deferred tax assets and liabilities are as follows:

(In thousands)	September 30, 2013	December 31, 2012
Deferred tax assets:		
Warranty, insurance and other accruals	$11,487	11,378
Inventory	17,417	22,612
State taxes	71	(64)
Net operating loss carryforward	98,007	102,475
Deferred charges	613	336
Total deferred tax assets	127,595	136,737
Deferred tax liabilities:		
Depreciation	397	804
Prepaid expenses	639	184
Total deferred tax liabilities	1,036	988
Net total deferred tax assets	126,559	135,749
Less valuation allowance	(14,913)	(135,749)
Total deferred tax assets, net of valuation allowance	111,646	—

The benefit from income taxes consists of the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	2013	2012	2013	2012
Current:				
Federal	$2	$—	$2	$—
State	$85	$138	$515	$(955)
	$87	$138	$517	$(955)
(In thousands)				
Deferred:				
Federal	$(104,751)	$—	$(104,751)	$—
State	$(6,895)	$—	$(6,895)	$—
	(111,646)	—	(111,646)	—
Total	$(111,559)	$138	$(111,129)	$(955)

At September 30, 2013, the Company had federal NOL carryforwards of approximately $77.8 million and federal credit carryforwards of $4.3 million. Federal NOL carryforwards may be carried forward up to 20 years to offset future taxable income. Our federal carryforward benefits begin to expire in 2028. The Company had $15.9 million of state NOL carryforwards at September 30, 2013. State NOLs may be carried forward from 5 to 20 years, depending on the tax jurisdiction, with $8.9 million expiring between 2013 and 2027 and $7.0 million expiring between 2028 and 2032, absent sufficient state taxable income. As of September 30, 2013, we have recorded a $10.2 million valuation allowance against these state NOLs.

NOTE 12. Business Segments

The Company’s segment information is presented on the basis that the chief operating decision makers use in evaluating segment performance. The Company’s chief operating decision makers evaluate the Company’s performance in various ways, including: (1) the results of our 13 individual homebuilding operating segments and the results of our financial services operations; (2) the results of our three homebuilding regions; and (3) our consolidated financial results. We have determined our reportable segments as follows: Midwest homebuilding, Southern homebuilding, Mid-Atlantic homebuilding and financial services operations. The homebuilding operating segments that are included within each reportable segment have similar operations and exhibit similar long-term economic characteristics. Our homebuilding operations include the acquisition and development of land, the sale and construction of single-family attached and detached homes, and the occasional sale of lots to third parties. The homebuilding operating segments that comprise each of our reportable segments are as follows:

Midwest	Southern	Mid-Atlantic
Columbus, Ohio	Tampa, Florida	Washington, D.C.
Cincinnati, Ohio	Orlando, Florida	Charlotte, North Carolina
Indianapolis, Indiana	Houston, Texas	Raleigh, North Carolina
Chicago, Illinois	San Antonio, Texas	
	Austin, Texas	
	Dallas/Fort Worth, Texas	

Our financial services operations include the origination, sale and servicing of mortgage loans and title services primarily for purchasers of the Company's homes.

The following table shows, by segment, revenue, operating income and interest expense for the three and nine months ended September 30, 2013 and 2012, as well as the Company’s income before income taxes for such periods:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	2013	2012	2013	2012
Revenue:				
Midwest homebuilding	$82,689	$79,015	$222,890	$198,994
Southern homebuilding	96,275	50,828	216,181	123,400
Mid-Atlantic homebuilding	89,550	72,649	239,061	172,977
Financial services (a)	6,681	6,383	22,343	15,623
Total revenue	$275,195	$208,875	$700,475	$510,994
Operating income:				
Midwest homebuilding (b)	$5,114	$3,940	$11,696	$9,012
Southern homebuilding (b)	8,271	6,144	15,222	9,837
Mid-Atlantic homebuilding (b)	8,433	5,787	18,961	9,496
Financial services (a)	3,827	3,960	13,451	8,606
Less: Corporate selling, general and administrative expense	(6,996)	(7,380)	(19,663)	(17,508)
Total operating income	$18,649	$12,451	$39,667	$19,443
Interest expense:				
Midwest homebuilding	$1,023	$1,243	$3,852	$4,181
Southern homebuilding	1,405	999	4,510	2,543
Mid-Atlantic homebuilding	659	1,342	2,809	4,248
Financial services (a)	362	415	1,015	1,094

Total interest expense	$3,449	$3,999	$12,186	$12,066
Equity in income of unconsolidated joint ventures	(278)	—	(278)	—
Loss on early extinguishment of debt	1,726	—	1,726	—
Income before income taxes	$13,752	$8,452	$26,033	$7,377

(a) Our financial services operational results should be viewed in connection with our homebuilding business as its operations originate loans and provide title services primarily for our homebuying customers, with the exception of a small amount of mortgage re-financing.

(b) For the three months ended September 30, 2013 and 2012, the impact of charges relating to the impairment of inventory and investment in unconsolidated joint ventures and the write-off of abandoned land transaction costs was $2.1 million and $1.3 million, respectively. These charges reduced operating income by $2.1 million and $1.3 million in the Midwest region for the three months ended September 30, 2013 and 2012, respectively. There were no charges in the Mid-Atlantic or Southern regions for the three months ended September 30, 2013 and 2012.

For the nine months ended September 30, 2013 and 2012, the impact of charges relating to the impairment of inventory and investment in unconsolidated joint ventures and the write-off of abandoned land transaction costs was $4.2 million and $2.1 million, respectively. These charges reduced operating income by $4.2 million and $1.9 million in the Midwest region for the nine months ended September 30, 2013 and 2012, respectively, and $0.1 million in each of the Southern and Mid-Atlantic regions for the nine months ended September 30, 2012. There were no charges in the Mid-Atlantic or Southern regions for the nine months ended September 30, 2013.

The following tables show total assets by segment at September 30, 2013 and December 31, 2012:

	September 30, 2013				
(In thousands)	Midwest	Southern	Mid-Atlantic	Corporate, Financial Services and Unallocated	Total
Deposits on real estate under option or contract	$2,141	$7,737	$3,477	$—	$13,355
Inventory (a)	241,233	212,665	209,083	—	662,981
Investments in unconsolidated joint ventures	5,200	28,888	—	—	34,088
Other assets	7,699	14,186	9,146	341,612	372,643
Total assets	$256,273	$263,476	$221,706	$341,612	$1,083,067

	December 31, 2012				
(In thousands)	Midwest	Southern	Mid-Atlantic	Corporate, Financial Services and Unallocated	Total
Deposits on real estate under option or contract	$1,462	$4,612	$2,653	$—	$8,727
Inventory (a)	196,554	157,302	194,234	—	548,090
Investments in unconsolidated joint ventures	5,121	6,611	—	—	11,732
Other assets	4,421	8,436	7,759	242,135	262,751
Total assets	$207,558	$176,961	$204,646	$242,135	$831,300

(a) Inventory includes single-family lots, land and land development costs; land held for sale; homes under construction; model homes and furnishings; community development district infrastructure; and consolidated inventory not owned.

NOTE 13. Supplemental Guarantor Information

The Company's obligations under the 2018 Senior Notes, the 2017 Convertible Senior Subordinated Notes and the 2018 Convertible Senior Subordinated Notes are not guaranteed by all of the Company's subsidiaries and therefore, the Company has disclosed condensed consolidating financial information in accordance with SEC Regulation S-X Rule 3-10, Financial Statements of Guarantors and Issuers of Guaranteed Securities Registered or Being Registered. The subsidiary guarantors of the 2018 Senior Notes, the 2017 Convertible Senior Subordinated Notes and the 2018 Convertible Senior Subordinated Notes are the same.

The following condensed consolidating financial information includes balance sheets, statements of operations and cash flow information for the parent company, the Guarantor Subsidiaries, collectively, and for all other subsidiaries and joint ventures of the Company (the "Unrestricted Subsidiaries"), collectively. Each Guarantor Subsidiary is a direct or indirect 100%-owned subsidiary of M/I Homes, Inc. and has fully and unconditionally guaranteed the (a) 2018

Senior Notes, on a joint and several senior unsecured basis, (b) the 2017 Convertible Senior Subordinated Notes on a joint and several senior subordinated unsecured basis and (c) the 2018 Convertible Senior Subordinated Notes on a joint and several senior subordinated unsecured basis.

There are no significant restrictions on the parent company's ability to obtain funds from its Guarantor Subsidiaries in the form of a dividend, loan, or other means.

As of September 30, 2013, each of the Company's subsidiaries is a Guarantor Subsidiary, with the exception of subsidiaries that are primarily engaged in the business of mortgage financing, title insurance or similar financial businesses relating to the homebuilding and home sales business, certain subsidiaries that are not 100%-owned by the Company or another subsidiary, and other subsidiaries designated by the Company as Unrestricted Subsidiaries, subject to limitations on the aggregate amount invested in such Unrestricted Subsidiaries in accordance with the terms of the Credit Facility and the Indenture for the 2018 Senior Notes.

In the condensed financial tables presented below, the parent company presents all of its 100%-owned subsidiaries as if they were accounted for under the equity method. All applicable corporate expenses have been allocated appropriately among the Guarantor Subsidiaries and Unrestricted Subsidiaries.

CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS

	Three Months Ended September 30, 2013				
(In thousands)	M/I Homes, Inc.	Guarantor Subsidiaries	Unrestricted Subsidiaries	Eliminations	Consolidated
Revenue	$—	$268,514	$6,681	$—	$275,195
Costs and expenses:					
Land and housing	—	218,150	—	—	218,150
Impairment of inventory and investment in unconsolidated joint ventures	—	2,136		—	2,136
General and administrative	—	15,309	2,952	—	18,261
Selling	—	17,979	20	—	17,999
Equity in income of unconsolidated joint ventures	—	—	(278)	—	(278)
Interest	—	3,087	362	—	3,449
Loss on early extinguishment of debt	—	1,726	—	—	1,726
Total costs and expenses	—	258,387	3,056	—	261,443
Income before income taxes	—	10,127	3,625	—	13,752
(Benefit) provision for income taxes	—	(112,694)	1,135	—	(111,559)
Equity in subsidiaries	125,311	—	—	(125,311)	—
Net income (loss)	125,311	122,821	2,490	(125,311)	125,311
Preferred dividends	1,219	—	—	—	1,219
Net income (loss) to common shareholders	$124,092	$122,821	$2,490	$(125,311)	$124,092

	Three Months Ended September 30, 2012				
(In thousands)	M/I Homes, Inc.	Guarantor Subsidiaries	Unrestricted Subsidiaries	Eliminations	Consolidated
Revenue	$—	$202,492	$6,383	$—	$208,875
Costs and expenses:					
Land and housing	—	164,452	—	—	164,452
Impairment of inventory and investment in unconsolidated joint ventures	—	1,309	—	—	1,309
General and administrative	—	13,425	2,591	—	16,016
Selling	—	14,647	—	—	14,647
Interest	—	3,584	415	—	3,999
Total costs and expenses	—	197,417	3,006	—	200,423
Income before income taxes	—	5,075	3,377	—	8,452
(Benefit) provision for income taxes	—	(1,003)	1,141	—	138

Equity in subsidiaries	8,314	—	—	(8,314	) —
Net income (loss)	$ 8,314	$ 6,078	$ 2,236	$ (8,314	) $ 8,314

CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS

	Nine Months Ended September 30, 2013				
(In thousands)	M/I Homes, Inc.	Guarantor Subsidiaries	Unrestricted Subsidiaries	Eliminations	Consolidated
Revenue	$—	$678,132	$22,343	$—	$700,475
Costs and expenses:					
Land and housing	—	556,799	—	—	556,799
Impairment of inventory and investment in unconsolidated joint ventures	—	4,237	—	—	4,237
General and administrative	—	43,104	9,285	—	52,389
Selling	—	47,317	66	—	47,383
Equity in income of unconsolidated joint ventures	—	—	(278)	—	(278)
Interest	—	11,171	1,015	—	12,186
Loss on early extinguishment of debt	—	1,726	—	—	1,726
Total costs and expenses	—	664,354	10,088	—	674,442
Income before income taxes	—	13,778	12,255	—	26,033
(Benefit) provision for income taxes	—	(115,308)	4,179	—	(111,129)
Equity in subsidiaries	137,162	—	—	(137,162)	—
Net income (loss)	137,162	129,086	8,076	(137,162)	137,162
Preferred dividends	2,438	—	—	—	2,438
Excess of fair value over book value of preferred shares redeemed	2,190	—	—	—	2,190
Net income (loss) to common shareholders	$132,534	$129,086	$8,076	$(137,162)	$132,534

	Nine Months Ended September 30, 2012				
(In thousands)	M/I Homes, Inc.	Guarantor Subsidiaries	Unrestricted Subsidiaries	Eliminations	Consolidated
Revenue	$—	$495,371	$15,623	$—	$510,994
Costs and expenses:					
Land and housing	—	408,893	—	—	408,893
Impairment of inventory and investment in unconsolidated joint ventures	—	1,876	—	—	1,876
General and administrative	—	34,938	7,361	—	42,299
Selling	—	38,482	1	—	38,483
Interest	—	10,972	1,094	—	12,066
Total costs and expenses	—	495,161	8,456	—	503,617
Income before income taxes	—	210	7,167	—	7,377

(Benefit) provision for income taxes	—	(3,403)	2,448	—	(955)
Equity in subsidiaries	8,332	—	—	(8,332)	—
Net income (loss)	$8,332	$3,613	$4,719	$(8,332)	$8,332

CONDENSED CONSOLIDATING BALANCE SHEET

(In thousands)	September 30, 2013 M/I Homes, Inc.	Guarantor Subsidiaries	Unrestricted Subsidiaries	Eliminations	Consolidated
ASSETS:					
Cash and cash equivalents	$—	$126,254	$16,221	$—	$142,475
Restricted cash	—	15,806	—	—	15,806
Mortgage loans held for sale	—	—	60,388	—	60,388
Inventory	—	676,336	—	—	676,336
Property and equipment - net	—	10,139	207	—	10,346
Investment in unconsolidated joint ventures	—	14,656	19,432	—	34,088
Investment in subsidiaries	521,617	—	—	(521,617)	—
Deferred income taxes, net of valuation allowances	—	112,164	518	—	112,682
Intercompany assets	319,136	—	—	(319,136)	—
Other assets	10,547	12,389	8,010	—	30,946
TOTAL ASSETS	$851,300	$967,744	$104,776	$ (840,753)	$1,083,067
LIABILITIES AND SHAREHOLDERS' EQUITY					
LIABILITIES:					
Accounts payable	$—	$85,383	$421	$—	$85,804
Customer deposits	—	14,918	—	—	14,918
Intercompany liabilities	—	298,130	21,006	(319,136)	—
Other liabilities	—	54,669	7,641	—	62,310
Community development district obligations	—	3,419	—	—	3,419
Obligation for consolidated inventory not owned	—	1,576	—	—	1,576
Notes payable bank - financial services operations	—	—	55,614	—	55,614
Notes payable - other	—	8,126	—	—	8,126
Convertible senior subordinated notes due 2017	57,500	—	—	—	57,500
Convertible senior subordinated notes due 2018	86,250	—	—	—	86,250
Senior notes	227,970	—	—	—	227,970
TOTAL LIABILITIES	371,720	466,221	84,682	(319,136)	603,487
SHAREHOLDERS' EQUITY	479,580	501,523	20,094	(521,617)	479,580
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$851,300	$967,744	$104,776	$ (840,753)	$1,083,067

CONDENSED CONSOLIDATING BALANCE SHEET

	December 31, 2012				
(In thousands)	M/I Homes, Inc.	Guarantor Subsidiaries	Unrestricted Subsidiaries	Eliminations	Consolidated
ASSETS:					
Cash and cash equivalents	$—	$126,334	$19,164	$—	$145,498
Restricted cash	—	8,680	—	—	8,680
Mortgage loans held for sale	—	—	71,121	—	71,121
Inventory	—	540,761	16,056	—	556,817
Property and equipment - net	—	10,314	125	—	10,439
Investment in unconsolidated joint ventures	—	—	11,732	—	11,732
Investment in subsidiaries	391,555	—	—	(391,555)	—
Intercompany assets	219,962	—	—	(219,962)	—
Other assets	9,081	12,375	5,557	—	27,013
TOTAL ASSETS	$620,598	$698,464	$123,755	$(611,517)	$831,300
LIABILITIES AND SHAREHOLDERS' EQUITY					
LIABILITIES:					
Accounts payable	$—	$46,882	$808	$—	$47,690
Customer deposits	—	10,239	—	—	10,239
Intercompany liabilities	—	205,389	14,573	(219,962)	—
Other liabilities	—	44,230	5,742	—	49,972
Community development district obligations	—	4,634	—	—	4,634
Obligation for consolidated inventory not owned	—	3,549	15,556	—	19,105
Notes payable bank - financial services operations	—	—	67,957	—	67,957
Notes payable - other	—	11,105	—	—	11,105
Convertible senior subordinated notes due 2017	57,500	—	—	—	57,500
Senior notes	227,670	—	—	—	227,670
TOTAL LIABILITIES	285,170	326,028	104,636	(219,962)	495,872
SHAREHOLDERS' EQUITY	335,428	372,436	19,119	(391,555)	335,428
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$620,598	$698,464	$123,755	$(611,517)	$831,300

(a) Certain amounts above have been reclassified from intercompany assets to intercompany liabilities as of December 31, 2012. These reclassifications relate solely to transactions between M/I Homes, Inc. and its subsidiaries and are immaterial to the Supplemental Condensed Consolidated Financial Statements. These reclassifications do not impact the Company's consolidated financial statements.

CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS

	Nine Months Ended September 30, 2013				
(In thousands)	M/I Homes, Inc.	Guarantor Subsidiaries	Unrestricted Subsidiaries	Eliminations	Consolidated
CASH FLOWS FROM OPERATING ACTIVITIES:					
Net cash provided by (used in) operating activities	$7,100	$ (60,703)	$ 20,267	$ (7,100)	$ (40,436)
CASH FLOWS FROM INVESTING ACTIVITIES:					
Restricted cash	—	(7,274)	—		(7,274)
Purchase of property and equipment	—	(1,528)	(126)		(1,654)
Investments in and advances to unconsolidated joint ventures	—	(14,657)	(10,839)	—	(25,496)
Return of capital from unconsolidated joint ventures	—	—	1,522	—	1,522
Net cash used in investing activities	—	(23,459)	(9,443)	—	(32,902)
CASH FLOWS FROM FINANCING ACTIVITIES:					
Repayments of bank borrowings - net	—	—	(12,343)	—	(12,343)
Principal repayments of note payable - other and community development district bond obligations	—	(2,979)	—	—	(2,979)
Proceeds from issuance of convertible senior subordinated notes due 2018	86,250	—	—	—	86,250
Redemption of preferred shares	(50,352)	—	—	—	(50,352)
Proceeds from issuance of common shares	54,617	—	—	—	54,617
Proceeds from exercise of stock options	2,640	—	—	—	2,640
Excess tax benefits from stock-based payment arrangements	383	—	—	—	383
Intercompany financing	(98,200)	92,463	5,737	—	—
Dividends paid	(2,438)	—	(7,100)	7,100	(2,438)
Debt issue costs	—	(5,402)	(61)	—	(5,463)
Net cash (used in) provided by financing activities	(7,100)	84,082	(13,767)	7,100	70,315
Net (decrease) increase in cash and cash equivalents	—	(80)	(2,943)	—	(3,023)
Cash and cash equivalents balance at beginning of period	—	126,334	19,164	—	145,498
Cash and cash equivalents balance at end of period	$—	$ 126,254	$ 16,221	$ —	$ 142,475

	Nine Months Ended September 30, 2012				
(In thousands)	M/I Homes, Inc.	Guarantor Subsidiaries	Unrestricted Subsidiaries	Eliminations	Consolidated
CASH FLOWS FROM OPERATING ACTIVITIES:					
Net cash (used in) provided by operating activities	$2,000	$ (20,546)	$ 4,225	$ (2,000)	$ (16,321)
CASH FLOWS FROM INVESTING ACTIVITIES:					
Restricted cash	—	32,391	—	—	32,391

Purchase of property and equipment	—	(786)	(72)	—	(858)
Acquisition, net of cash acquired	—	(4,707)	—	—	(4,707)
Investments in and advances to unconsolidated joint ventures	—	—	(949)	—	(949)
Net cash provided by (used in) investing activities	—	26,898	(1,021)	—	25,877
CASH FLOWS FROM FINANCING ACTIVITIES:					
Proceeds from bank borrowings - net	—	—	2,234	—	2,234
Repayment of Senior Notes	(41,443)	—	—	—	(41,443)
Principal proceeds from note payable - other and community development district bond obligations	—	4,968	—	—	4,968
Proceeds from issuance of convertible senior subordinated notes due 2017	57,500	—	—	—	57,500
Proceeds from issuance of common shares	42,085	—	—	—	42,085
Intercompany financing	(91,057)	91,852	(795)	—	—
Proceeds from issuance of senior notes	29,700	—	—	—	29,700
Dividends paid	—	—	(2,000)	2,000	—
Debt issue costs	—	(5,812)	(31)	—	(5,843)
Proceeds from exercise of stock options	1,215	—	—	—	1,215
Net cash provided by (used in) financing activities	(2,000)	91,008	(592)	2,000	90,416
Net increase in cash and cash equivalents	—	97,360	2,612	—	99,972
Cash and cash equivalents balance at beginning of period	—	43,539	16,254	—	59,793
Cash and cash equivalents balance at end of period	$—	$ 140,899	$ 18,866	$ —	$ 159,765

(a) Certain amounts above have been reclassified from intercompany financing to dividends paid and cash flows from operating activities for the nine months ended September 30, 2012. These reclassifications relate solely to transactions between M/I Homes, Inc. and its subsidiaries and are immaterial to the Supplemental Condensed Consolidated Financial Statements. These reclassifications do not impact the Company's consolidated financial statements.

ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

OVERVIEW

M/I Homes, Inc. (the “Company” or “we”) is one of the nation’s leading builders of single-family homes, having delivered approximately 86,000 homes since we commenced homebuilding activities in 1976. The Company's homes are marketed and sold under the M/I Homes, Showcase Collection and Triumph Homes trade names. The Company has homebuilding operations in Columbus and Cincinnati, Ohio; Indianapolis, Indiana; Chicago, Illinois; Tampa and Orlando, Florida; Austin, Dallas/Fort Worth, Houston and San Antonio, Texas; Charlotte and Raleigh, North Carolina; and the Virginia and Maryland suburbs of Washington, D.C.

Included in this Management's Discussion and Analysis of Financial Condition and Results of Operations are the following topics relevant to the Company's performance and financial condition:

- Information Relating to Forward-Looking Statements;
- Our Application of Critical Accounting Estimates and Policies;
- Our Results of Operations;
- Discussion of Our Liquidity and Capital Resources;
- Summary of Our Contractual Obligations;
- Discussion of Our Utilization of Off-Balance Sheet Arrangements; and
- Impact of Interest Rates and Inflation.

FORWARD-LOOKING STATEMENTS

Certain information included in this report or in other materials we have filed or will file with the Securities and Exchange Commission (the “SEC”) (as well as information included in oral statements or other written statements made or to be made by us) contains or may contain forward-looking statements, including, but not limited to, statements regarding our future financial performance and financial condition. Words such as “expects,” “anticipates,” “targets,” “goals,” “projects,” “intends,” “plans,” “believes,” “seeks,” and “estimates,” variations of such words and similar expressions are intend to identify such forward-looking statements. These statements involve a number of risks and uncertainties. Any forward-looking statements that we make herein and in future reports and statements are not guarantees of future performance, and actual results may differ materially from those in such forward-looking statements as a result of various risk factors. Please see “Item 1A. Risk Factors” in Part I of our Annual Report on Form 10-K for the year ended December 31, 2012 and “Item 1A. Risk Factors” of Part II of our Quarterly Reports on Form 10-Q for the quarters ended March 31, 2013 and June 30, 2013.

Any forward-looking statement speaks only as of the date made. Except as required by applicable law, 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 our subsequent reports on Forms 10-K, 10-Q and 8-K should be consulted. This discussion is provided as permitted by the Private Securities Litigation Reform Act of 1995, and all of our forward-looking statements are expressly qualified in their entirety by the cautionary statements contained or referenced in this section.

APPLICATION OF CRITICAL ACCOUNTING ESTIMATES AND POLICIES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (“GAAP”) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial

statements and the reported amounts of revenue and expenses during the reporting period. 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. On an ongoing basis, management evaluates such estimates and judgments and makes adjustments as deemed necessary. Actual results could differ from these estimates using different estimates and assumptions, or if conditions are significantly different in the future. See Note 1 (Summary of Significant Accounting Policies) to our consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2012 for additional information about our accounting policies.

We believe that there have been no significant changes to our critical accounting policies during the quarter ended September 30, 2013 as compared to those disclosed in Management's Discussion and Analysis of Financial Condition and Results of Operations included in our Annual Report on Form 10-K for the year ended December 31, 2012.

RESULTS OF OPERATIONS

The Company's segment information is presented on the basis that the chief operating decision makers use in evaluating segment performance. The Company's chief operating decision makers evaluate the Company's performance in various ways, including: (1) the results of our 13 individual homebuilding operating segments and the results of our financial services operations; (2) the results of our three homebuilding regions; and (3) our consolidated financial results. We have determined our reportable segments as follows: Midwest homebuilding, Southern homebuilding, Mid-Atlantic homebuilding and financial services operations. The homebuilding operating segments that are included within each reportable segment have similar operations and exhibit similar long-term economic characteristics. Our homebuilding operations include the acquisition and development of land, the sale and construction of single-family attached and detached homes, and the occasional sale of lots and land to third parties. The homebuilding operating segments that comprise each of our reportable segments are as follows:

Midwest	Southern	Mid-Atlantic
Columbus, Ohio	Tampa, Florida	Washington, D.C.
Cincinnati, Ohio	Orlando, Florida	Charlotte, North Carolina
Indianapolis, Indiana	Houston, Texas	Raleigh, North Carolina
Chicago, Illinois	San Antonio, Texas	
	Austin, Texas	
	Dallas/Fort Worth, Texas	

In July 2013, we announced our entry into the Dallas/Fort Worth, Texas market.

Our financial services operations include the origination, sale and servicing of mortgage loans and title services primarily for purchasers of the Company's homes.

Overview

During the nine months ended September 30, 2013, we continued to experience improving results as the recovery in the housing market continued. We believe that the recovery in the housing industry is being driven by the demand for housing created by growing population and re-accelerating household formations, favorable own-versus-rent dynamics, record low inventory levels for both new homes and resales, historically attractive affordability levels, and a slow but steady improvement in job growth. We continue to experience broad based improvements across all of our markets, albeit at a slower pace than the first half of 2013.

We experienced significant improvement in traffic quantity and quality, as well as our number of new contracts, during the nine months ended September 30, 2013, as buyer confidence in the housing market strengthened, and we achieved our highest operating margin in any quarter since 2007 during the third quarter of 2013. We believe that our improved results of operations are due to improving market conditions coupled with a strategic shift in our mix of communities towards better performing locations, our continued focus on shifting our investment to stronger housing markets, and the performance of our mortgage operations.

During the third quarter of 2013, we achieved net income of $125.3 million, of which $13.8 million ($0.47 per diluted share) related to our core profitability while $111.6 million ($3.75 per diluted share) related to the accounting benefit associated with a reversal of a majority of our deferred tax asset valuation allowance as more fully described in Note 11 of our Unaudited Condensed Consolidated Financial Statements.

In response to the continuing recovery in new home sales, we have increased our land positions to meet our strategic growth targets in each market, based on the availability of well-located land opportunities which meet our financial return targets and other requirements. To sustain our improved profitability, we believe that we need to purchase new

land at prices that we have underwritten to generate appropriate investment returns and drive greater operating efficiencies. Accordingly, we purchased $156.7 million of new land during the nine months ended September 30, 2013 and spent $67.5 million on land development.

On July 18, 2013, we entered into a new three-year unsecured revolving credit facility (the “Credit Facility”) with an aggregate commitment amount of $200 million, as more fully described below in our “Liquidity and Capital Resources” section, which replaced the $140 million secured revolving credit facility (the “Prior Credit Facility”) that was scheduled to mature on December 31, 2014. During the three and nine months ended September 30, 2013, we recognized a loss on early extinguishment of debt of $1.7 million which represented the write-off of unamortized debt issuance costs related to the termination of the Prior Credit Facility.

During the three and nine months ended September 30, 2013, we paid cash dividends of $609.375 per preferred share on our 2,000 outstanding Series A Preferred Shares for $1.2 million and $2.4 million , respectively.

Summary of Company Results

Summary of Financial Results

For the quarter ended September 30, 2013, we achieved net income to common shareholders of $124.1 million, or $4.22 per diluted share, which included a $111.6 million accounting benefit from income taxes due to the reversal of a majority of the valuation allowance against our deferred tax assets, offset partially by $2.1 million of pre-tax impairment charges, a $1.7 million charge related to the early termination of our Prior Credit Facility and $1.2 million of dividend payments made to holders of our Series A Preferred Shares. This compares to net income to common shareholders of $8.3 million, or $0.42 per diluted share, for the quarter ended September 30, 2012, which included income of $3.0 million related to a drywall settlement and $1.3 million of pre-tax impairment charges. For the nine months ended September 30, 2013, we achieved net income to common shareholders of $132.5 million, or $4.79 per diluted share, which included a $111.6 million accounting benefit from income taxes due to the reversal of a majority of the valuation allowance against our deferred tax assets, $4.2 million of pre-tax impairment charges, a $2.2 million non-cash equity adjustment resulting from the excess of fair value over carrying value of our Series A Preferred Shares that were called for redemption in the first quarter of 2013 and $2.4 million of dividend payments made to holders of our Series A Preferred Shares. This compares to net income to common shareholders of $8.3 million, or $0.43 per diluted share, for the nine months ended September 30, 2012, which included income of $3.0 million related to a drywall settlement and $1.9 million of pre-tax impairment charges.

For the third quarter of 2013, we recorded $265.9 million in revenue from homes delivered, $2.6 million in revenue from land sales and $6.7 million in revenue from our financial services operations. Revenue from homes delivered increased 34% driven primarily by the 191 additional homes delivered in 2013's third quarter compared to the same period in 2012 and a 7% increase in the average sales price of homes delivered ($18,000 per home delivered). Offsetting the increase in revenue from homes delivered above was a decrease in revenue from land sales of $1.5 million from the third quarter of 2012 due primarily to land sales in our Mid-Atlantic region in prior year. Revenue in our financial services segment increased 5% to $6.7 million in the third quarter of 2013 primarily due to the factors discussed below in our “Year Over Year Comparisons” section. For the nine months ended September 30, 2013, we recorded $665.4 million in revenue from homes delivered, $12.8 million in revenue from land sales and $22.3 million in revenue from our financial services operations. Revenue from homes delivered increased 37% driven primarily by the 474 additional homes delivered in the nine months ended September 30, 2013 compared to the same period in 2012 and a 9% increase in the average sales price of homes delivered ($24,000 per home delivered). Revenue from land sales increased $3.8 million from the nine months ended September 30, 2012. Revenue in our financial services segment increased 43% to $22.3 million in the nine months ended September 30, 2013 primarily due to the factors discussed below in our “Year Over Year Comparisons” section.

Total gross margin increased $11.8 million in the third quarter of 2013 compared to the corresponding period in 2012, which was largely the result of an $11.5 million improvement in our homebuilding operations, with the remainder due to our financial services operations. The improvement in our homebuilding operations for the third quarter of 2013 was primarily due to a $15.3 million increase in homebuilding gross margin when compared to the third quarter of 2012, offset, in part, by an increase of $0.8 million in land impairments taken during the third quarter of 2013. For the nine months ended September 30, 2013, total gross margin increased $39.2 million when compared to the nine months ended September 30, 2012, which was largely the result of a $32.5 million improvement in our homebuilding operations, with the remainder due to our financial services operations. The improvement in our homebuilding operations for the nine months ended September 30, 2013 was primarily due to a $34.9 million increase in homebuilding gross margin when compared to the nine months ended September 30, 2012, offset in part by an

increase of $2.4 million in land impairments taken during the nine month period ended September 30, 2013.

The increase in homebuilding gross margin for both the three and nine months ended September 30, 2013 resulted from the increase in the average sales price of homes delivered and the increase in the number of homes delivered offset, in part, by an increase in construction costs. The increased sales prices for both the three and nine months ended September 30, 2013 were driven primarily by the performance of our newer communities, the strategic shift in our geographic footprint, which resulted in more homes delivered in our better performing markets, a shift in the mix of homes delivered to higher priced and larger homes and improving market conditions. This allowed for more pricing leverage in select locations and submarkets. The pricing and unit improvements were partially offset by higher construction costs related to both the mix of homes delivered as well as cost increases associated with improving homebuilding industry conditions and normal supply and demand dynamics. In both the third quarter and the nine month period ended September 30, 2013, we were able to pass a majority of the higher construction costs to our homebuyers in the form of higher sales prices and lower incentives. However, recent moderation in the stronger sales price appreciation trends

we experienced earlier in 2013 may make it more difficult to continue to fully offset any further increase in material, labor and land cost that we may experience going forward.

Selling, general and administrative expense increased $5.6 million and $19.0 million for the three and nine months ended September 30, 2013, respectively, which offset, in part, the increase in our gross margins discussed above. For the third quarter of 2013, selling expense increased $3.4 million from the prior year's third quarter but declined as a percentage of revenue to 6.6% compared to 7.0% in the third quarter of 2012. Variable selling expense for sales commissions contributed $2.9 million to the increase due to the increase in the number of homes delivered and the increase in our average sales price. During the third quarter of 2013, general and administrative expense increased $2.2 million but declined as a percentage of revenue to 6.6% compared to 7.7% for the third quarter of 2012. For the nine months ended September 30, 2013, selling expense increased $8.9 million from the nine months ended September 30, 2012 but declined as a percentage of revenue to 6.8% compared to 7.5% in the nine months ended September 30, 2012. Variable selling expense for sales commissions contributed $7.7 million to the increase due to the increase in the number of homes delivered and the higher average sales price. General and administrative expense increased $10.1 million compared to the nine months ended September 30, 2012 but declined as a percentage of revenue from 8.3% in the nine months ended September 30, 2012 to 7.5% in the nine months ended September 30, 2013. Overall, our selling, general and administrative expense was 13.2% and 14.2% of revenue in the third quarter and nine months ended September 30, 2013, respectively, compared to 14.7% and 15.8% for the same periods in 2012, respectively.

Summary of Operational Results

In addition to the improving financial results noted above, our operational metrics also improved. For the quarter ended September 30, 2013, we achieved a 15% increase in our new contracts and a 26% increase in homes delivered. For the nine months ended September 30, 2013, we achieved a 28% increase in our new contracts and a 25% increase in homes delivered. We also experienced a 36% increase in the number of homes in our backlog and a 46% increase in the overall sales value of our backlog as of September 30, 2013 compared to September 30, 2012. Furthermore, we continue to invest in communities and markets that we believe are helping us attain improved profitability as housing markets improve and enhance our ability to establish market share and create a platform for future growth in our current markets. During the nine month period ended September 30, 2013, we opened 47 new communities and closed 31 older communities. We have continued to make progress selling the remaining homes in our older communities, which have lower margins. For the nine months ended September 30, 2013, we reduced the number of homes delivered in older communities to 22% of our total homes delivered during the period, compared to 31% of the total homes delivered during the nine months ended September 30, 2012. Additionally, our absorption rates per community improved from 2.1 for the nine months ended September 30, 2012 to 2.4 for the nine months ended September 30, 2013.

Outlook

Looking ahead, although the rate of improvement in the overall housing industry may moderate due to the upward movement in interest rates which occurred during the second quarter of 2013 as well as a decline in consumer confidence resulting from recent political and economic uncertainty, we believe that the fundamentals supporting a sustained multi-year housing recovery remain strong. Despite a moderation in the pace of improvement in new home sales activity during the third quarter and concerns reflected in recent sales volatility, we believe that longer-term demand for new homes will continue to improve as consumers continue to perceive good values amidst limited supply and generally low interest rates. We believe that we will continue to benefit from the recovery in housing sales, though maybe not at the same rate of improvement that we experienced during the first six months of 2013. Specifically, the pace and increase in our new contracts and average sales price when compared to our prior year results may be less than what we have experienced to date in 2013, and this slower pace of improvement may lead to

related impacts on the level of year-over-year improvements in our financial results.

Given our expectations with respect to homebuilding market conditions, and consistent with our focus on improving long-term returns, we will continue to emphasize the following strategic business objectives during the remainder of 2013:

- profitably growing our presence in our existing markets;
- strategically investing in new markets;
- maintaining a strong balance sheet; and
- emphasizing customer service, product design, and premier locations.

With these objectives and improving market conditions in mind, we took a number of steps during the nine months ended September 30, 2013 to position the Company for continued improvement throughout 2013 and beyond, including investing $156.7 million in land acquisition and $67.5 million in land development in the nine month period ended September 30, 2013 to help grow our

presence in our existing markets. We currently estimate that for fiscal 2013, we will spend approximately $300 million to $350 million on land purchases and land development.

We ended the third quarter of 2013 with $158.3 million of cash, no outstanding borrowings under our $200 million Credit Facility.

The following table shows, by segment, revenue; homebuilding gross margin; selling, general and administrative expense; operating income; and interest expense for the three and nine months ended September 30, 2013 and 2012, as well as the Company's income before income taxes for such periods:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	2013	2012	2013	2012
Revenue:				
Midwest homebuilding	$82,689	$79,015	$222,890	$198,994
Southern homebuilding	96,275	50,828	216,181	123,400
Mid-Atlantic homebuilding	89,550	72,649	239,061	172,977
Financial services (a)	6,681	6,383	22,343	15,623
Total revenue	$275,195	$208,875	$700,475	$510,994
Gross margin:				
Midwest homebuilding (b)	$13,406	$12,118	$35,156	$30,727
Southern homebuilding (b)	17,992	11,962	40,077	25,410
Mid-Atlantic homebuilding (b)	16,830	12,651	41,863	28,465
Financial services (a)	6,681	6,383	22,343	15,623
Total gross margin	$54,909	$43,114	$139,439	$100,225
Selling, general and administrative expense:				
Midwest homebuilding	$8,292	$8,178	$23,460	$21,715
Southern homebuilding	9,721	5,818	24,855	15,573
Mid-Atlantic homebuilding	8,397	6,864	22,902	18,969
Financial services (a)	2,854	2,423	8,892	7,017
Corporate	6,996	7,380	19,663	17,508
Total selling, general and administrative expense	$36,260	$30,663	$99,772	$80,782
Operating income (loss):				
Midwest homebuilding (b)	$5,114	$3,940	$11,696	$9,012
Southern homebuilding (b)	8,271	6,144	15,222	9,837
Mid-Atlantic homebuilding (b)	8,433	5,787	18,961	9,496
Financial services (a)	3,827	3,960	13,451	8,606
Corporate	(6,996)	(7,380)	(19,663)	(17,508)
Total operating income	$18,649	$12,451	$39,667	$19,443
Interest expense:				
Midwest homebuilding	$1,023	$1,243	$3,852	$4,181
Southern homebuilding	1,405	999	4,510	2,543
Mid-Atlantic homebuilding	659	1,342	2,809	4,248
Financial services (a)	362	415	1,015	1,094
Total interest expense	$3,449	$3,999	$12,186	$12,066

Equity in income of unconsolidated joint ventures	(278)	—	(278)	—
Loss on early extinguishment of debt	1,726	—	1,726	—
Income before income taxes	$13,752	$8,452	$26,033	$7,377

(a) Our financial services operational results should be viewed in connection with our homebuilding business as its operations originate loans and provide title services primarily for our homebuying customers, with the exception of a small amount of mortgage re-financing.

(b) For the three months ended September 30, 2013 and 2012, the impact of charges relating to the impairment of inventory and investment in unconsolidated joint ventures and the write-off of abandoned land transaction costs was $2.1 million and $1.3 million, respectively. These charges reduced gross margin and operating income by $2.1 million and $1.3 million in the Midwest region for the three months ended September 30, 2013 and 2012, respectively. There were no charges in the Mid-Atlantic or Southern regions for the three months ended September 30, 2013 and 2012.

For the nine months ended September 30, 2013 and 2012, the impact of charges relating to the impairment of inventory and investment in unconsolidated joint ventures and the write-off of abandoned land transaction costs was $4.2 million and $2.1 million, respectively. These charges reduced operating income by $4.2 million and $1.9 million in the Midwest region for the nine months ended September 30, 2013 and 2012, respectively, and $0.1 million in each of

the Southern and Mid-Atlantic regions for the nine months ended September 30, 2012. There were no charges in the Mid-Atlantic or Southern regions for the nine months ended September 30, 2013.

The following tables show total assets by segment at September 30, 2013 and December 31, 2012:

	At September 30, 2013				
(In thousands)	Midwest	Southern	Mid-Atlantic	Corporate, Financial Services and Unallocated	Total
Deposits on real estate under option or contract	$2,141	$7,737	$ 3,477	$—	$13,355
Inventory (a)	241,233	212,665	209,083	—	662,981
Investments in unconsolidated joint ventures	5,200	28,888	—	—	34,088
Other assets	7,699	14,186	9,146	341,612	372,643
Total assets	$256,273	$263,476	$ 221,706	$341,612	$1,083,067

	At December 31, 2012				
(In thousands)	Midwest	Southern	Mid-Atlantic	Corporate, Financial Services and Unallocated	Total
Deposits on real estate under option or contract	$1,462	$4,612	$ 2,653	$—	$8,727
Inventory (a)	196,554	157,302	194,234	—	548,090
Investments in unconsolidated joint ventures	5,121	6,611	—	—	11,732
Other assets	4,421	8,436	7,759	242,135	262,751
Total assets	$207,558	$176,961	$ 204,646	$242,135	$831,300

(a) Inventory includes single-family lots, land and land development costs; land held for sale; homes under construction; model homes and furnishings; community development district infrastructure; and consolidated inventory not owned.

Reportable Segments

The following table presents, by reportable segment, selected financial information for the three and nine months ended September 30, 2013 and 2012:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in thousands)	2013	2012	2013	2012
Midwest Region				
Homes delivered	307	307	837	795
New contracts, net	318	274	1,062	913
Backlog at end of period	643	505	643	505
Average sales price per home delivered	$269	$257	$263	$250
Average sales price of homes in backlog	$297	$		