

HOVNANIAN ENTERPRISES INC
Form 10-K
December 20, 2013

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

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

For the fiscal year ended OCTOBER 31, 2013

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

Commission file number: 1-8551

Hovnanian Enterprises, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or Other Jurisdiction of Incorporation or Organization)
110 West Front Street, P.O. Box 500, Red Bank, N.J.
(Address of Principal Executive Offices)

22-1851059
(I.R.S. Employer Identification No.)
07701
(Zip Code)

732-747-7800
(Registrant's Telephone Number, Including Area Code)
Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class

Class A Common Stock, \$0.01 par value per share
7.25% Tangible Equity Units
Preferred Stock Purchase Rights

Name of Each Exchange on Which
Registered

New York Stock Exchange
New York Stock Exchange
New York Stock Exchange
NASDAQ Global Market

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Depository Shares, each representing 1/1,000th of a share of 7.625% Series A Preferred Stock

Securities registered pursuant to Section 12(g) of the Act:
Class B Common Stock, \$0.01 par value per share
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act of 1933. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate “website”, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant’s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large Accelerated Filer Accelerated Filer Nonaccelerated Filer Smaller Reporting Company

(Do Not Check if a smaller reporting Company)

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

The aggregate market value of the voting and nonvoting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity as of April 30, 2013 (the last business day of the registrant's most recently completed second fiscal quarter) was \$614,817,623.

As of the close of business on December 16, 2013, there were outstanding 124,546,460 shares of the Registrant's Class A Common Stock and 14,654,867 shares of its Class B Common Stock.

HOVNANIAN ENTERPRISES, INC.

DOCUMENTS INCORPORATED BY REFERENCE:

Part III — Those portions of the registrant’s definitive proxy statement to be filed pursuant to Regulation 14A in connection with registrant’s annual meeting of stockholders to be held on March 11, 2014, which are responsive to those parts of Part III, Items 10, 11, 12, 13, and 14 as identified herein.

FORM 10-K

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Part I

ITEM 1

BUSINESS

Business Overview

We design, construct, market, and sell single-family detached homes, attached townhomes and condominiums, urban infill, and active adult homes in planned residential developments and are one of the nation's largest builders of residential homes. Founded in 1959 by Kevork Hovnanian, Hovnanian Enterprises, Inc. (the "Company", "we", "us" or "our") was incorporated in New Jersey in 1967 and reincorporated in Delaware in 1983. Since the incorporation of our predecessor company and including unconsolidated joint ventures, we have delivered in excess of 306,000 homes, including 5,930 homes in fiscal 2013. The Company consists of two distinct operations: homebuilding and financial services. Our homebuilding operations consist of six segments: Northeast, Mid-Atlantic, Midwest, Southeast, Southwest, and West. Our financial services operations provide mortgage loans and title services to the customers of our homebuilding operations.

We are currently, excluding unconsolidated joint ventures, offering homes for sale in 192 communities in 34 markets in 16 states throughout the United States. We market and build homes for first-time buyers, first-time and second-time move-up buyers, luxury buyers, active adult buyers, and empty nesters. We offer a variety of home styles at base prices ranging from \$68,652 (low-income housing) to \$1,524,990 with an average sales price, including options, of \$339,000 nationwide in fiscal 2013.

Our operations span all significant aspects of the home-buying process – from design, construction, and sale, to mortgage origination and title services.

The following is a summary of our growth history:

1959 - Founded by Kevork Hovnanian as a New Jersey homebuilder.

1983 - Completed initial public offering.

1986 - Entered the North Carolina market through the investment in New Fortis Homes.

1992 - Entered the greater Washington, D.C. market.

1994 - Entered the Coastal Southern California market.

1998 - Expanded in the greater Washington, D.C. market through the acquisition of P.C. Homes.

1999 - Entered the Dallas, Texas market through our acquisition of Goodman Homes. Further diversified and strengthened our position as New Jersey's largest homebuilder through the acquisition of Matzel & Mumford.

2001 - Continued expansion in the greater Washington D.C. and North Carolina markets through the acquisition of Washington Homes. This acquisition further strengthened our operations in each of these markets.

2002 - Entered the Central Valley market in Northern California and Inland Empire region of Southern California through the acquisition of Forecast Homes.

2003 - Expanded operations in Texas and entered the Houston market through the acquisition of Parkside Homes and Brighton Homes. Entered the greater Ohio market through our acquisition of Summit Homes and entered the greater metro Phoenix market through our acquisition of Great Western Homes.

2004 - Entered the greater Tampa, Florida market through the acquisition of Windward Homes and started operations in the Minneapolis/St. Paul, Minnesota market.

2005 - Entered the Orlando, Florida market through our acquisition of Cambridge Homes and entered the greater Chicago, Illinois market and expanded our position in Florida and Minnesota through the acquisition of the operations of Town & Country Homes, which occurred concurrently with our entering into a joint venture with affiliates of Blackstone Real Estate Advisors to own and develop Town & Country Homes' existing residential communities. We also entered the Fort Myers market through the acquisition of First Home Builders of Florida, and the Cleveland, Ohio

market through the acquisition of Oster Homes.

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2006 - Entered the coastal markets of South Carolina and Georgia through the acquisition of Craftbuilt Homes.

Geographic Breakdown of Markets by Segment

Hovnanian markets and builds homes that are constructed in 21 of the nation's top 50 housing markets. We segregate our homebuilding operations geographically into the following six segments:

Northeast: New Jersey and Pennsylvania

Mid-Atlantic: Delaware, Maryland, Virginia, Washington, D.C., and West Virginia

Midwest: Illinois, Minnesota, and Ohio

Southeast: Florida, Georgia, North Carolina, and South Carolina

Southwest: Arizona and Texas

West: California

For financial information about our segments, see Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations," and Note 11 to the Consolidated Financial Statements.

Employees

We employed approximately 1,749 full-time employees (whom we refer to as associates) as of October 31, 2013.

Corporate Offices and Available Information

Our corporate offices are located at 110 West Front Street, P.O. Box 500, Red Bank, New Jersey 07701, our telephone number is 732-747-7800, and our Internet web site address is www.khov.com. Information available on or through our web site is not a part of this Form 10-K. We make available through our web site our Annual Report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to these reports filed or furnished pursuant to Section 13(d) or 15(d) of the Exchange Act as soon as reasonably practicable after they are filed with, or furnished to, the Securities and Exchange Commission (SEC). Copies of the Company's Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to these reports are available free of charge upon request. Any materials we file with the SEC may be read and copied at the SEC's Public Reference Room at 100 F Street, NE, Washington, D.C., 20549. Information on the operation of the Public Reference Room may be obtained by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site (<http://www.sec.gov>) that contains reports, proxy, and information statements and other information regarding issuers that file electronically with the SEC.

Business Strategies

Although new home demand remains at historically low levels, during fiscal 2013 the overall homebuilding market improved. Improved conditions in our markets resulted in our higher revenues and gross margins, increased contracts and deliveries and profitability for the first time since fiscal 2006. From 2006 to 2012, the homebuilding industry had been in a prolonged downturn. During that time, our primary focus, while market conditions were extremely weak, had been to strengthen our financial condition by reducing inventories of homes and land, controlling and reducing construction and overhead costs, maximizing cash flows, reducing outstanding debt, and maintaining strong liquidity. In 2009, we began to see opportunities to purchase land at prices and terms that made economic sense in light of our sales prices and sales paces. As a result, since early 2009, we have been more active in purchasing or putting under option new properties that meet or exceed our internal rate of return investment requirements. Deliveries from these newly acquired communities helped us achieve profitability in fiscal 2013, and in order to continue to increase profitability in the future, we will need to continue purchasing new land that will generate good investment returns and drive greater operating efficiencies, as well as control expenses commensurate with our level of deliveries.

In addition to our current focus on maintaining strong liquidity and evaluating new investment opportunities, we intend to continue to focus on our historic key business strategies as enumerated below. We believe that these strategies separate us from our competitors in the residential homebuilding industry and the adoption, implementation, and adherence to these principles will continue to benefit our business.

Our goal is to become a significant builder in each of the selected markets in which we operate, which will enable us to achieve powers and economies of scale and differentiate ourselves from most of our competitors.

We offer a broad product array to provide housing to a wide range of customers. Our customers consist of first-time buyers, first-time and second-time move-up buyers, luxury buyers, active adult buyers, and empty nesters. Our diverse product array includes single-family detached homes, attached townhomes and condominiums, urban infill, and active adult homes.

We are committed to customer satisfaction and quality in the homes that we build. We recognize that our future success rests in the ability to deliver quality homes to satisfied customers. We seek to expand our commitment to customer service through a variety of quality initiatives. In addition, our focus remains on attracting and developing quality associates. We use several leadership development and mentoring programs to identify key individuals and prepare them for positions of greater responsibility within our Company.

We focus on achieving high return on invested capital. Each new community is evaluated based on its ability to meet or exceed internal rate of return requirements. Our belief is that the best way to create lasting value for our shareholders is through a strong focus on return on invested capital.

We prefer to use a risk-averse land strategy. We attempt to acquire land with a minimum cash investment and negotiate takedown options, thereby limiting the financial exposure to the amounts invested in property and predevelopment costs. This approach significantly reduces our risk and generally allows us to obtain necessary development approvals before acquisition of the land.

We enter into homebuilding and land development joint ventures from time to time as a means of controlling lot positions, expanding our market opportunities, establishing strategic alliances, reducing our risk profile, leveraging our capital base, and enhancing our returns on capital. Our homebuilding joint ventures are generally entered into with third-party investors to develop land and construct homes that are sold directly to home buyers. Our land development joint ventures include those with developers and other homebuilders, as well as financial investors to develop finished lots for sale to the joint venture's members or other third parties.

We manage our financial services operations to better serve all of our home buyers. Our current mortgage financing and title service operations enhance our contact with customers and allow us to coordinate the home-buying experience from beginning to end.

Operating Policies and Procedures

We attempt to reduce the effect of certain risks inherent in the housing industry through the following policies and procedures:

Training - Our training is designed to provide our associates with the knowledge, attitudes, skills, and habits necessary to succeed in their jobs. Our training department regularly conducts online or webinar training in sales, construction, administration, and managerial skills.

Land Acquisition, Planning, and Development - Before entering into a contract to acquire land, we complete extensive comparative studies and analyses which assist us in evaluating the economic feasibility of such land acquisition. We generally follow a policy of acquiring options to purchase land for future community developments.

Where possible, we acquire land for future development through the use of land options, which need not be exercised before the completion of the regulatory approval process. We attempt to structure these options with flexible takedown schedules rather than with an obligation to take down the entire parcel upon receiving regulatory approval. If we are unable to negotiate flexible takedown schedules, we will buy parcels in a single bulk purchase. Additionally, we purchase improved lots in certain markets by acquiring a small number of improved lots with an option on additional lots. This allows us to minimize the economic costs and risks of carrying a large land inventory, while maintaining our ability to commence new developments during favorable market periods.

Our option and purchase agreements are typically subject to numerous conditions, including, but not limited to, our ability to obtain necessary governmental approvals for the proposed community. Generally, the deposit on the agreement will be returned to us if all approvals are not obtained, although predevelopment costs may not be recoverable. By paying an additional nonrefundable deposit, we have the right to extend a significant number of our options for varying periods of time. In most instances, we have the right to cancel any of our land option agreements by forfeiture of our deposit on the agreement. In fiscal 2013, 2012, and 2011, rather than purchase additional lots in underperforming communities, we took advantage of this right and walked away from 1,611 lots, 2,134 lots, and 6,983 lots, respectively, out of 17,134 total lots, 13,552 total lots, and 16,896 total lots, respectively, under option, resulting in pretax charges of \$2.6 million, \$2.7 million, and \$24.3 million, respectively.

Design - Our residential communities are generally located in suburban areas easily accessible through public and personal transportation. Our communities are designed as neighborhoods that fit existing land characteristics. We strive to create diversity within the overall planned community by offering a mix of homes with differing architecture, textures, and colors. Recreational amenities, such as swimming pools, tennis courts, clubhouses, open areas, and tot lots, are frequently included.

Construction - We design and supervise the development and building of our communities. Our homes are constructed according to standardized prototypes, which are designed and engineered to provide innovative product design while attempting to minimize costs of construction. We generally employ subcontractors for the installation of site improvements and construction of homes. Agreements with subcontractors are generally short term and provide for a fixed price for labor and materials. We rigorously control costs through the use of computerized monitoring systems.

Because of the risks involved in speculative building, our general policy is to construct an attached condominium or townhouse building only after signing contracts for the sale of at least 50% of the homes in that building. A majority of our single family detached homes are constructed after the signing of a sales contract and mortgage approval has been obtained. This limits the buildup of inventory of unsold homes and the costs of maintaining and carrying that inventory.

Materials and Subcontractors - We attempt to maintain efficient operations by utilizing standardized materials available from a variety of sources. In addition, we generally contract with subcontractors to construct our homes. We have reduced construction and administrative costs by consolidating the number of vendors serving certain markets and by executing national purchasing contracts with select vendors. In recent years, we have experienced no significant construction delays due to shortage of materials or labor; however, we cannot predict the extent to which shortages in necessary materials or labor may occur in the future.

Marketing and Sales - Our residential communities are sold principally through on-site sales offices. In order to respond to our customers' needs and trends in housing design, we rely upon our internal market research group to analyze information gathered from, among other sources, buyer profiles, and exit interviews at model sites, focus groups, and demographic databases. We make use of newspaper, radio, television, Internet, magazine, our web site, billboard, video and direct mail advertising, special and promotional events, illustrated brochures, and full-sized and scale model homes in our comprehensive marketing program. In addition, we have home design galleries in our Florida, Illinois, New Jersey, North Carolina, and Virginia markets, which offer a wide range of customer options to satisfy individual customer tastes.

Customer Service and Quality Control - In many of our markets, associates are responsible for customer service and preclosing quality control inspections as well as responding to postclosing customer needs. Prior to closing, each home is inspected and any necessary completion work is undertaken by us. Our homes are enrolled in a standard limited warranty program which, in general, provides a homebuyer with a one-year warranty for the home's materials

and workmanship, a two-year warranty for the home's heating, cooling, ventilating, electrical, and plumbing systems, and a 10-year warranty for major structural defects. All of the warranties contain standard exceptions, including, but not limited to, damage caused by the customer.

Customer Financing - We sell our homes to customers who generally finance their purchases through mortgages. Our financial services segment provides our customers with competitive financing and coordinates and expedites the loan origination transaction through the steps of loan application, loan approval, and closing and title services. We originate loans in Arizona, California, Delaware, Florida, Georgia, Illinois, Maryland, Minnesota, New Jersey, North Carolina, Pennsylvania, South Carolina, Texas, Virginia, and Washington, D.C. We believe that our ability to offer financing to customers on competitive terms as a part of the sales process is an important factor in completing sales.

During the year ended October 31, 2013, for the markets in which our mortgage subsidiaries originated loans, 14.6% of our home buyers paid in cash and 71.5% of our noncash home buyers obtained mortgages from our mortgage banking subsidiary. The loans we originated in fiscal 2013 were 32.7% Federal Housing Administration/Veterans Affairs ("FHA/VA"), 65.7% prime, and 1.6% United States Department of Agriculture.

We customarily sell virtually all of the loans and loan-servicing rights that we originate within a short period of time. Loans are sold either individually or against forward commitments to institutional investors, including banks, mortgage banking firms, and savings and loan associations.

Residential Development Activities

Our residential development activities include site planning and engineering, obtaining environmental and other regulatory approvals and constructing roads, sewer, water, and drainage facilities, recreational facilities, and other amenities and marketing and selling homes. These activities are performed by our associates, together with independent architects, consultants, and contractors. Our associates also carry out long-term planning of communities. A residential development generally includes single-family detached homes and/or a number of residential buildings containing from two to 24 individual homes per building, together with amenities, such as club houses, swimming pools, tennis courts, tot lots, and open areas.

Current base prices for our homes in contract backlog at October 31, 2013, range from \$68,652 (low-income housing) to \$1,040,000 in the Northeast, from \$159,900 to \$1,524,990 in the Mid-Atlantic, from \$99,490 to \$701,808 in the Midwest, from \$173,490 to \$566,252 in the Southeast, from \$90,450 to \$878,990 in the Southwest, and from \$142,760 to \$1,130,000 in the West. Closings generally occur and are typically reflected in revenues within 12 months of when sales contracts are signed.

Information on homes delivered by segment for the year ended October 31, 2013, is set forth below:

(Housing revenue in thousands)	Housing Revenues	Homes Delivered	Average Price
Northeast	\$279,695	617	\$453,314
Mid-Atlantic	288,323	623	462,798
Midwest	162,758	657	247,730
Southeast	146,264	535	273,391
Southwest	684,258	2,331	293,547
West	223,029	503	443,398
Consolidated total	\$1,784,327	5,266	\$338,839
Unconsolidated joint ventures	306,174	664	461,105
Total including unconsolidated joint ventures	\$2,090,501	5,930	\$352,530

The value of our net sales contracts, excluding unconsolidated joint ventures, increased to \$1.9 billion from \$1.6 billion for the years ended October 31, 2013 and 2012, respectively. The number of homes contracted increased to 5,544 in 2013 from 5,137 in 2012. The increase in the number of homes contracted occurred along with an increase in the number of open-for-sale communities from 172 to 192. We contracted an average of 30.7 homes per average active selling community in 2013 compared to 28.1 homes per active selling community in 2012, demonstrating an increase in sales pace as the homebuilding market has improved.

Information on the value of net sales contracts by segment for the years ended October 31, 2013 and 2012, is set forth below.

(Value of net sales contracts in thousands)	2013	2012	Percentage of Change	
Northeast	\$269,284	\$225,168	19.6	%
Mid-Atlantic	310,718	250,350	24.1	%
Midwest	217,759	157,385	38.4	%
Southeast	182,225	145,963	24.8	%
Southwest	739,784	590,208	25.3	%
West	194,678	228,624	(14.8))%
Consolidated total	\$1,914,448	\$1,597,698	19.8	%
Unconsolidated joint ventures	282,205	318,409	(11.4))%
Total including unconsolidated joint ventures	\$2,196,653	\$1,916,107	14.6	%

The following table summarizes our active selling communities under development as of October 31, 2013. The contracted not delivered and remaining homes available in our active selling communities are included in the consolidated total homesites under the total residential real estate chart in Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

Active Selling Communities

	Communities	Approved Homes	Homes Delivered	Contracted Not Delivered(1)	Remaining Homes Available(2)
Northeast	12	3,181	2,039	220	922
Mid-Atlantic	29	4,393	1,748	271	2,374
Midwest	27	4,092	1,009	605	2,478
Southeast	24	2,229	972	308	949
Southwest	88	11,484	6,539	677	4,268
West	12	2,371	961	86	1,324
Total	192	27,750	13,268	2,167	12,315

(1) Includes 274 home sites under option.

(2) Of the total remaining homes available, 694 were under construction or completed (including 61 models and sales offices), and 6,490 were under option.

Backlog

At October 31, 2013 and 2012, including unconsolidated joint ventures, we had a backlog of signed contracts for 2,392 homes and 2,145 homes, respectively, with sales values aggregating \$848.4 million and \$742.2 million, respectively. The majority of our backlog at October 31, 2013, is expected to be completed and closed within the next 12 months. At November 30, 2013 and 2012, our backlog of signed contracts, including unconsolidated joint ventures, was 2,464 homes and 2,138 homes, respectively, with sales values aggregating \$892.8 million and \$745.8 million, respectively. For information on our backlog excluding unconsolidated joint ventures, see the table on page 42 under Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Results of Operations -Homebuilding.”

Sales of our homes typically are made pursuant to a standard sales contract that provides the customer with a statutorily mandated right of rescission for a period ranging up to 15 days after execution. This contract requires a nominal customer deposit at the time of signing. In addition, in the Northeast, and some sections of the Mid-Atlantic and Midwest, we typically obtain an additional 5% to 10% down payment due within 30 to 60 days after signing. The contract may include a financing contingency, which permits customers to cancel their obligation in the event mortgage financing at prevailing interest rates (including financing arranged or provided by us) is unobtainable within the period specified in the contract. This contingency period typically is four to eight weeks following the date of execution of the contract. When housing values decline in certain markets, some customers cancel their contracts and

forfeit their deposits. Cancellation rates are discussed further in Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations.” Sales contracts are included in backlog once the sales contract is signed by the customer, which in some cases includes contracts that are in the rescission or cancellation periods. However, revenues from sales of homes are recognized in the Consolidated Statement of Operations, when title to the home is conveyed to the buyer, adequate initial and continuing investments have been received, and there is no continued involvement.

Residential Land Inventory in Planning

It is our objective to control a supply of land, primarily through options, whenever possible, consistent with anticipated homebuilding requirements in each of our housing markets. Controlled land (land owned and under option) as of October 31, 2013, exclusive of communities under development described above under “Active Selling Communities” and excluding unconsolidated joint ventures, is summarized in the following table. The proposed developable home sites in communities in planning are included in the 32,097 consolidated total home sites under the total residential real estate table in Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations” on page 36.

Communities in Planning

	Number	Proposed	Total	
(Dollars in thousands)	of Proposed	Developable	Land	Book
	Communities	Home Sites	Option	Value
			Price	
Northeast:				
Under option(1)	22	2,486	\$204,117	\$11,720
Owned	14	1,140		108,120
Total	36	3,626		\$119,840
Mid-Atlantic:				
Under option(1)	13	1,212	\$135,258	\$2,596
Owned	15	1,741		29,412
Total	28	2,953		\$32,008
Midwest:				
Under option(1)	22	1,241	\$50,081	\$2,722
Owned	11	468		6,078
Total	33	1,709		\$8,800
Southeast:				
Under option(1)	22	2,010	\$92,020	\$5,381
Owned	15	568		5,484
Total	37	2,578		\$10,865
Southwest:				
Under option(1)	31	1,746	\$126,818	\$11,538
Owned	5	305		14,899
Total	36	2,051		\$26,437
West:				
Under option(1)	-	-	-	-
Owned	25	4,634		\$27,202
Total	25	4,634		\$27,202

Totals:				
Under option(1)	110	8,695	\$608,294	\$33,957
Owned	85	8,856		191,195
Combined total	195	17,551		\$225,152

Properties under option also include costs incurred on properties not under option but which are under evaluation.
 (1) *For properties under option, as of October 31, 2013, option fees and deposits aggregated approximately \$25.8 million. As of October 31, 2013, we spent an additional \$15.2 million in nonrefundable predevelopment costs on such properties.*

We either option or acquire improved or unimproved home sites from land developers or other sellers. Under a typical agreement with the land developer, we purchase a minimal number of home sites. The balance of the home sites to be purchased is covered under an option agreement or a nonrecourse purchase agreement. During the declining homebuilding market, we decided to mothball (or stop development on) certain communities where we determined that current market conditions did not justify further investment at that time. When we decide to mothball a community, the inventory is reclassified on our Consolidated Balance Sheet from Sold and unsold homes and lots under development to Land and land options held for future development or sale. See Note 3 to the Consolidated Financial Statements for further discussion on mothballed communities. For additional financial information regarding our homebuilding segments, see Note 11 to the Consolidated Financial Statements.

Raw Materials

The homebuilding industry has from time to time experienced raw material and labor shortages. In particular, shortages and fluctuations in the price of lumber or in other important raw materials could result in delays in the start or completion of or increase the cost of developing one or more of our residential communities. We attempt to maintain efficient operations by utilizing standardized materials available from a variety of sources. In addition, we generally contract with subcontractors to construct our homes. We have reduced construction and administrative costs by consolidating the number of vendors serving certain markets and by executing national purchasing contracts with select vendors.

Seasonality

Our business is seasonal in nature and, historically, weather-related problems, typically in the fall, late winter and early spring, can delay starts or closings and increase costs.

Competition

Our homebuilding operations are highly competitive. We are among the top 10 homebuilders in the United States in both homebuilding revenues and home deliveries. We compete with numerous real estate developers in each of the geographic areas in which we operate. Our competition ranges from small local builders to larger regional builders to publicly owned builders and developers, some of which have greater sales and financial resources than we do. Previously owned homes and the availability of rental housing provide additional competition. We compete primarily on the basis of reputation, price, location, design, quality, service, and amenities.

Regulation and Environmental Matters

We are subject to various local, state, and federal statutes, ordinances, rules, and regulations concerning zoning, building design, construction, and similar matters, including local regulations which impose restrictive zoning and density requirements in order to limit the number of homes that can eventually be built within the boundaries of a particular locality. In addition, we are subject to registration and filing requirements in connection with the construction, advertisement, and sale of our communities in certain states and localities in which we operate even if all necessary government approvals have been obtained. We may also be subject to periodic delays or may be precluded entirely from developing communities due to building moratoriums that could be implemented in the future in the states in which we operate. Generally, such moratoriums relate to insufficient water or sewerage facilities or

inadequate road capacity.

In addition, some state and local governments in markets where we operate have approved, and others may approve, slow-growth, or no-growth initiatives that could negatively affect the availability of land and building opportunities within those areas. Approval of these initiatives could adversely affect our ability to build and sell homes in the affected markets and/or could require the satisfaction of additional administrative and regulatory requirements, which could result in slowing the progress or increasing the costs of our homebuilding operations in these markets. Any such delays or costs could have a negative effect on our future revenues and earnings.

We are also subject to a variety of local, state, federal, and foreign laws and regulations concerning protection of health and the environment (“environmental laws”). The particular environmental laws which apply to any given community vary greatly according to the community site, the site’s environmental conditions, and the present and former uses of the site. These environmental laws may result in delays; may cause us to incur substantial compliance, remediation, and/or other costs; and prohibit or severely restrict development and homebuilding activity. See Item 3 “Legal Proceedings” and Note 19 to the Consolidated Financial Statements.

Despite our past ability to obtain necessary permits and approvals for our communities, we anticipate that increasingly stringent requirements will be imposed on developers and homebuilders in the future. Although we cannot predict the effect of these requirements, they could result in time-consuming and expensive compliance programs and in substantial expenditures, which could cause delays and increase our cost of operations. In addition our ability to obtain or renew permits or approvals and the continued effectiveness of permits already granted or approvals already obtained is dependent upon many factors, some of which are beyond our control, such as changes in policies, rules, and regulations and their interpretation and application.

ITEM 1A

RISK FACTORS

You should carefully consider the following risks in addition to the other information included in this Annual Report on Form 10-K, including the Consolidated Financial Statements and the notes thereto.

The homebuilding industry is significantly affected by changes in general and local economic conditions, real estate markets, and weather and other environmental conditions, which could affect our ability to build homes at prices our customers are willing or able to pay, could reduce profits that may not be recaptured, could result in cancellation of sales contracts, and could affect our liquidity.

The homebuilding industry is cyclical, has from time to time experienced significant difficulties, and is significantly affected by changes in general and local economic conditions such as:

- Employment levels and job growth;

- Availability of financing for home buyers;

- Interest rates;

- Foreclosure rates;

- Inflation;

- Adverse changes in tax laws;

- Consumer confidence;

- Housing demand;

- Population growth; and

- Availability of water supply in locations in which we operate.

Turmoil in the financial markets could affect our liquidity. In addition, our cash balances are primarily invested in short-term government-backed instruments. The remaining cash balances are held at numerous financial institutions and may, at times, exceed insurable amounts. We seek to mitigate this risk by depositing our cash in major financial institutions and diversifying our investments. In addition, our homebuilding operations often require us to obtain letters of credit. We recently entered into a new \$75 million unsecured revolving credit facility under which letters of credit may be issued. We also have certain stand-alone letter of credit facilities and agreements pursuant to which letters of credit are issued. However, we may need additional letters of credit above the amounts provided under these facilities and agreements. If we are unable to obtain such additional letters of credit as needed to operate our business, we may be adversely affected.

Weather conditions and man-made or natural disasters such as hurricanes, tornadoes, earthquakes, floods, droughts, fires, and other environmental conditions, can harm the local homebuilding business. For example, our business in Florida was adversely affected in late 2005 and into 2006 due to the effects of Hurricane Wilma on materials and labor availability and pricing. Conversely, Hurricane Ike, which hit Houston in September 2008, did not have an effect on materials and labor availability or pricing, but did affect the volume of home sales in subsequent weeks. In August 2011 and October 2012, Hurricane Irene and Hurricane Sandy, respectively, caused widespread flooding and disruptions on the Atlantic seaboard, which impacted our sales and construction activity in affected markets during those months.

The difficulties described above could cause us to take longer and incur more costs to build our homes. We may not be able to recapture increased costs by raising prices in many cases because we fix our prices up to 12 months in advance of delivery by signing home sales contracts. In addition, some home buyers may cancel or not honor their home sales contracts altogether.

The homebuilding industry has experienced a significant and sustained downturn which has, and could continue to, materially and adversely affect our business, liquidity, and results of operations.

The homebuilding industry experienced a significant and sustained downturn over the past several years. An industry-wide softening of demand for new homes resulted from a lack of consumer confidence, decreased availability of mortgage financing, and large supplies of resale and new home inventories, among other factors. In addition, an oversupply of alternatives to new homes, such as rental properties, resale homes, and foreclosures, depressed prices, and reduced margins for the sale of new homes. Industry conditions had a material adverse effect on our business and results of operations in fiscal years 2007 through 2011 and may continue to materially adversely affect our business and results of operations in future years. Further, we substantially increased our inventory through fiscal 2006, which required significant cash outlays and which increased our price and margin exposure as we worked through this inventory.

General economic conditions in the United States remain weak. Several challenges, such as persistently high unemployment levels, national and global economic weakness and uncertainty, the restrictive mortgage lending environment, and the potential for more foreclosures, continue to threaten the recovery in the housing market. In addition, both national new home sales and our home sales remain below historical levels. Until there is a more robust U.S. economic recovery, we expect national demand for new homes to remain at historically low levels, with uneven improvement across our operating markets. Looking forward, although we have begun to see improvements, given instability in the housing market, it may continue to be difficult to generate positive cash flow especially as we invest in land to fund future homebuilding. In addition, while our sales have increased, we saw lower sales in July through September 2013 in part due to increasing interest rates. Market volatility has been unprecedented and extraordinary in the last several years, and the resulting economic turmoil may continue to exacerbate industry conditions or have other unforeseen consequences, leading to uncertainty about future conditions in the homebuilding industry. Continuation or worsening of the downturn or general economic conditions would continue to have a material adverse effect on our business, liquidity, and results of operations.

In addition, an increase in the default rate on the mortgages we originate may adversely affect our ability to sell mortgages or the pricing we receive upon the sale of mortgages. Although substantially all of the mortgage loans we originate are sold in the secondary mortgage market on a servicing released, non-recourse basis, we remain liable for certain limited representations, such as fraud, and warranties related to loan sales. As default rates rise, this may increase our potential exposure regarding mortgage loan sales because investors may seek to have us buy back or make whole investors for mortgages we previously sold. To date, we have not made significant payments related to our mortgage loans, but because of the uncertainties inherent to these matters, actual future payments could differ significantly from our currently estimated amounts.

During the industry downturn, the housing market benefited from a number of government programs, including:

- Tax credits for home buyers provided by the federal government and certain state governments, including California; and

- Support of the mortgage market, including through purchases of mortgage-backed securities by The Federal Reserve Bank and the underwriting of a substantial amount of new mortgages by the Federal Housing Administration (“FHA”) and other governmental agencies.

These programs are expected to wind down over time; for example, the California tax credit ended in the fourth quarter of fiscal 2009 and the federal tax credit expired in April 2010. In addition, in fiscal 2010, the U.S. Department of Housing and Urban Development (“HUD”) tightened FHA underwriting standards. The maximum size of mortgage loans that are treated as conforming by Fannie Mae and Freddie Mac was reduced on October 1, 2011, which could further weaken home sales in general as mortgages may become more expensive and, if conforming loan limits are further reduced (as currently expected to occur on January 1, 2014), it could have a material adverse effect on the Company. Housing markets may further decline as these programs are modified or terminated.

Our leverage places burdens on our ability to comply with the terms of our indebtedness, may restrict our ability to operate, may prevent us from fulfilling our obligations, and may adversely affect our financial condition.

We have a significant amount of debt.

Our debt (excluding nonrecourse secured debt and debt of our financial subsidiaries), as of October 31, 2013, including the debt of the subsidiaries that guarantee our debt, was \$1,544.2 million (\$1,529.4 million net of discount); and

Our debt service payments for the 12-month period ended October 31, 2013, were \$121.2 million, substantially all of which represented interest incurred and the remainder of which represented payments on the principal of our amortizing notes, and do not include principal and interest on nonrecourse secured debt, debt of our financial subsidiaries and fees under our letter of credit and other credit facilities and agreements.

In addition, as of October 31, 2013, we had \$30.9 million in aggregate outstanding face amount of letters of credit issued under various letter of credit and other credit facilities and agreements, certain of which were collateralized by \$5.2 million of cash. Our fees for these letters of credit for the year ended October 31, 2013, which are based on both the used and unused portion of the facilities and agreements, were \$0.7 million. We also had substantial contractual commitments and contingent obligations, including approximately \$242.0 million of performance bonds as of October 31, 2013. See Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations - Contractual Obligations.”

Our significant amount of debt could have important consequences. For example, it could:

• Limit our ability to obtain future financing for working capital, capital expenditures, acquisitions, debt service requirements, or other requirements;

• Require us to dedicate a substantial portion of our cash flow from operations to the payment of our debt and reduce our ability to use our cash flow for other purposes;

• Limit our flexibility in planning for, or reacting to, changes in our business;

• Place us at a competitive disadvantage because we have more debt than some of our competitors; and

• Make us more vulnerable to downturns in our business and general economic conditions.

Our ability to meet our debt service and other obligations will depend upon our future performance. We are engaged in businesses that are substantially affected by changes in economic cycles. Our revenues and earnings vary with the level of general economic activity in the markets we serve. Our businesses are also affected by customer sentiment and financial, political, business, and other factors, many of which are beyond our control. The factors that affect our ability to generate cash can also affect our ability to raise additional funds for these purposes through the sale of equity securities, the refinancing of debt, or the sale of assets. Changes in prevailing interest rates may affect our ability to meet our debt service obligations to the extent we have any floating rate indebtedness. A higher interest rate on our debt service obligations could result in lower earnings or increased losses.

Our sources of liquidity are limited and may not be sufficient to meet our needs.

We are largely dependent on our current cash balance and future cash flows from operations (which may not be positive) to enable us to service our indebtedness, to cover our operating expenses, and/or to fund our other liquidity needs. Although we generated \$9.3 million of cash in operating activities in the fiscal year ended October 31, 2013, for the prior two years we generated negative cash flow, and currently expect to continue to generate slightly positive or negative cash flow, after taking into account land purchases. If the homebuilding industry does not experience improved conditions over the next several years, our cash flows could be insufficient to fund our obligations and support land purchases; if we cannot buy additional land we would ultimately be unable to generate future revenues from the sale of houses. In addition, we may need to further refinance all or a portion of our debt on or before maturity, which we may not be able to do on favorable terms or at all. If our cash flows and capital resources are insufficient to fund our debt service obligations or we are unable to refinance our indebtedness, we may be forced to reduce or delay investments and capital expenditures, sell assets, seek additional capital, or restructure our indebtedness. These alternative measures may not be successful or, if successful, made on desirable terms and may

not permit us to meet our debt service obligations. We have also entered into certain cash collateralized letters of credit agreements and facilities that require us to maintain specified amounts of cash in segregated accounts as collateral to support our letters of credit issued thereunder. If our available cash and capital resources are insufficient to meet our debt service and other obligations, we could face substantial liquidity problems and might be required to dispose of material assets or operations to meet our debt service and other obligations. We may not be able to consummate those dispositions or the proceeds from the dispositions may not be adequate to meet any debt service obligations then due. For additional information about capital resources and liquidity, see Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Capital Resources and Liquidity.”

Restrictive covenants in our debt instruments may restrict our and certain of our subsidiaries’ ability to operate and if our financial performance worsens, we may not be able to undertake transactions within the restrictions of our debt instruments.

The indentures governing our outstanding debt securities and our revolving credit facility impose certain restrictions on our and certain of our subsidiaries’ operations and activities. The most significant restrictions relate to debt incurrence, creating liens, sales of assets, cash distributions, including paying dividends on common and preferred stock, capital stock and debt repurchases, and investments by us and certain of our subsidiaries. Because of these restrictions, we are currently prohibited from paying dividends on our common and preferred stock and anticipate that we will remain prohibited for the foreseeable future.

The restrictions in our debt instruments could prohibit or restrict our and certain of our subsidiaries’ activities, such as undertaking capital raising or restructuring activities or entering into other transactions. In such a situation, we may be unable to amend the instrument or obtain a waiver. In addition, if we fail to make timely payments on this debt and other material indebtedness, our debt under these debt instruments could become due and payable prior to maturity. In such a situation, there can be no assurance that we would be able to obtain alternative financing. Either situation could have a material adverse effect on the solvency of the Company.

The terms of our debt instruments allow us to incur additional indebtedness.

Under the terms of our indebtedness under our indentures and under our revolving credit facility, we have the ability, subject to our debt covenants, to incur additional amounts of debt. The incurrence of additional indebtedness could magnify the risks described above. In addition, certain obligations, such as standby letters of credit and performance bonds issued in the ordinary course of business, including those issued under our stand-alone letter of credit agreements and facilities, are not considered indebtedness under our debt instruments (and may be secured), and therefore, are not subject to limits in our debt covenants.

We could be adversely affected by a negative change in our credit rating.

Our ability to access capital on favorable terms is a key factor in our ability to service our indebtedness to cover our operating expenses and to fund our other liquidity needs. For example, during fiscal 2011 and thereafter, credit agencies took a series of negative actions, including downgrades, with respect to their credit ratings of us and our debt. Downgrades may make it more difficult and costly for us to access capital. Therefore, any further downgrade by any of the principal credit agencies may exacerbate these difficulties. Although certain of our credit ratings have recently been upgraded, there can be no assurances that our credit ratings will not be further downgraded in the future, whether as a result of deteriorating general economic conditions, a more protracted downturn in the housing industry, failure to successfully implement our operating strategy, the adverse impact on our results of operations or liquidity position of any of the above, or otherwise.

Our business is seasonal in nature and our quarterly operating results can fluctuate.

Our quarterly operating results generally fluctuate by season. The construction of a customer's home typically begins after signing the agreement of sale and can take 12 months or more to complete. Weather-related problems, typically in the fall, winter and early spring, can delay starts or closings and increase costs and thus reduce profitability. In addition, delays in opening communities could have an adverse effect on our sales and revenues. Due to these factors, our quarterly operating results will likely continue to fluctuate.

Our success depends on the availability of suitable undeveloped land and improved lots at acceptable prices and our having sufficient liquidity to fund such investments.

Our success in developing land and in building and selling homes depends in part upon the continued availability of suitable undeveloped land and improved lots at acceptable prices. The availability of undeveloped land and improved

lots for purchase at favorable prices depends on a number of factors outside of our control, including the risk of competitive over bidding on land and lots and restrictive governmental regulation. Should suitable land opportunities become less available, the number of homes we may be able to build and sell would be reduced, which would reduce revenue and profits. In addition, our ability to make land purchases will depend upon us having sufficient liquidity to fund such purchases. We may be at a disadvantage in competing for land due to our significant debt obligations, which require substantial cash resources.

Raw material and labor shortages and price fluctuations could delay or increase the cost of home construction and adversely affect our operating results.

The homebuilding industry has from time to time experienced raw material and labor shortages. In particular, shortages and fluctuations in the price of lumber or in other important raw materials could result in delays in the start or completion of, or increase the cost of, developing one or more of our residential communities. For example, manufacturers have increased the price of drywall in 2013 by approximately 20% as compared to the prior year, and there is a potential for significant future price increases. In addition, we contract with subcontractors to construct our homes. Therefore, the timing and quality of our construction depends on the availability, skill, and cost of our subcontractors. Delays or cost increases caused by shortages and price fluctuations could harm our operating results, the impact of which may be further affected depending on our ability to raise sales prices to offset increased costs. We have experienced some labor shortages and increased labor costs in recent months.

Changes in economic and market conditions could result in the sale of homes at a loss or holding land in inventory longer than planned, the cost of which can be significant.

Land inventory risk can be substantial for homebuilders. We must continuously seek and make acquisitions of land for expansion into new markets and for replacement and expansion of land inventory within our current markets. The market value of undeveloped land, buildable lots, and housing inventories can fluctuate significantly as a result of changing economic and market conditions. In the event of significant changes in economic or market conditions, we may have to sell homes at a loss or hold land in inventory longer than planned. In the case of land options, we could choose not to exercise them, in which case we would write off the value of these options. Inventory carrying costs can be significant and can result in losses in a poorly performing project or market. The assessment of communities for indication of impairment is performed quarterly. While we consider available information to determine what we believe to be our best estimates as of the reporting period, these estimates are subject to change in future reporting periods as facts and circumstances change. See Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operation - Critical Accounting Policies." For example, while in fiscal 2013 and 2012, we did not have significant land option write-offs or impairments, during fiscal 2011, 2010, and 2009, we decided not to exercise many option contracts and walked away from land option deposits and predevelopment costs, which resulted in land option write-offs of \$24.3 million, \$13.2 million, and \$45.4 million, respectively. Also, in fiscal 2011, 2010, and 2009, as a result of the difficult market conditions, we recorded inventory impairment losses on owned property of \$77.5 million, \$122.5 million, and \$614.1 million, respectively. If market conditions worsen, additional inventory impairment losses and land option write-offs will likely be necessary.

Home prices and sales activities in the Arizona, California, New Jersey, and Texas, markets have a large impact on our results of operations because we conduct a significant portion of our business in these markets.

We presently conduct a significant portion of our business in the Arizona, California, New Jersey, and Texas, markets. Home prices and sales activities in these markets and in most of the other markets in which we operate have declined from time to time, particularly as a result of slow economic growth. Furthermore, precarious economic and budget situations at the state government level may adversely affect the market for our homes in those affected areas. If home prices and sales activity decline in one or more of the markets in which we operate, our costs may not decline at all or at the same rate and may negatively impact our results of operations.

Because almost all of our customers require mortgage financing, increases in interest rates or the decreased availability of mortgage financing could impair the affordability of our homes, lower demand for our products, limit our marketing effectiveness, and limit our ability to fully realize our backlog.

Virtually all of our customers finance their acquisitions through lenders providing mortgage financing. Increases in interest rates (or the perception that interest rates will rise, including as a result of government actions) or decreases in availability of mortgage financing could lower demand for new homes because of the increased monthly mortgage costs to potential home buyers. Even if potential customers do not need financing, changes in interest rates and mortgage availability could make it harder for them to sell their existing homes to potential buyers who need financing. This could prevent or limit our ability to attract new customers as well as our ability to fully realize our backlog because our sales contracts generally include a financing contingency. Financing contingencies permit the customer to cancel its obligation in the event mortgage financing at prevailing interest rates, including financing arranged or provided by us, is unobtainable within the period specified in the contract. This contingency period is typically four to eight weeks following the date of execution of the sales contract.

Starting in 2007, many lenders have been significantly tightening their underwriting standards, and subprime and other alternative mortgage products are no longer being made available in the marketplace. If these trends continue and mortgage loans continue to be difficult to obtain, the ability and willingness of prospective buyers to finance home purchases or to sell their existing homes will be adversely affected, which will adversely affect our operating results. In addition, we believe that the availability of mortgage financing, including Federal National Mortgage Association, Federal Home Loan Mortgage Corp, and FHA/VA financing, is an important factor in marketing many of our homes. The maximum size of mortgage loans that are treated as conforming by Fannie Mae and Freddie Mac was reduced on October 1, 2011, which could further weaken home sales in general as mortgages may become more expensive and, if conforming loan limits are further reduced (as currently expected to occur on January 1, 2014), it could have a material adverse effect on the Company. In addition, HUD continues to tighten FHA underwriting standards. Any limitations or restrictions on the availability of those types of financing could reduce our sales.

Increases in the after-tax costs of owning a home could prevent potential customers from buying our homes and adversely affect our business or financial results.

Significant expenses of owning a home, including mortgage interest expenses and real estate taxes, generally are deductible expenses for an individual's federal, and in some cases state, income taxes, subject to limitations under current tax law and policy. If the federal government or a state government were to change its income tax laws to eliminate or substantially limit these income tax deductions, as has been discussed from time to time, the after-tax cost of owning a new home would increase for many of our potential customers. The loss or reduction of these homeowner tax deductions, if such tax law changes were enacted without any offsetting legislation, would adversely impact demand for and sales prices of new homes, including ours. In addition, increases in property tax rates or fees on developers by local governmental authorities, as experienced in response to reduced federal and state funding or to fund local initiatives, such as funding schools or road improvements, can adversely affect the ability of potential customers to obtain financing or their desire to purchase new homes, and can have an adverse impact on our business and financial results.

We conduct certain of our operations through unconsolidated joint ventures with independent third parties in which we do not have a controlling interest. These investments involve risks and are highly illiquid.

We currently operate through a number of unconsolidated homebuilding and land development joint ventures with independent third parties in which we do not have a controlling interest. At October 31, 2013, we had invested an aggregate of \$51.4 million in these joint ventures, including advances to these joint ventures of approximately \$4.6 million. In addition, as part of our strategy, we intend to continue to evaluate additional joint venture opportunities.

These investments involve risks and are highly illiquid. There are a limited number of sources willing to provide acquisition, development, and construction financing to land development and homebuilding joint ventures, and if market conditions become more challenging, it may be difficult or impossible to obtain financing for our joint ventures on commercially reasonable terms. Over the past few years, we have been unable to obtain financing for newly created joint ventures. In addition, we lack a controlling interest in these joint ventures and, therefore, are usually unable to require that our joint ventures sell assets or return invested capital, make additional capital contributions, or take any other action without the vote of at least one of our venture partners. Therefore, absent partner agreement, we will be unable to liquidate our joint venture investments to generate cash.

Homebuilders are subject to a number of federal, local, state, and foreign laws and regulations concerning the development of land, the homebuilding, sales, and customer financing processes and the protection of the environment, which can cause us to incur delays and costs associated with compliance and which can prohibit or restrict our activity in some regions or areas.

We are subject to extensive and complex laws and regulations that affect the development of land and homebuilding, sales and customer financing processes, including zoning, density, building standards and mortgage financing. These laws and regulations often provide broad discretion to the administering governmental authorities. This can delay or increase the cost of development or homebuilding. In light of recent developments in the home building industry and the financial markets, federal, state, or local governments may seek to adopt regulations that limit or prohibit homebuilders from providing mortgage financing to their customers. If adopted, any such regulations could adversely affect future revenues and earnings. In addition, some state and local governments in markets where we operate have approved, and others may approve, slow-growth or no-growth initiatives that could negatively impact the availability of land and building opportunities within those areas. Approval of these initiatives could adversely affect our ability to build and sell homes in the affected markets and/or could require the satisfaction of additional administrative and regulatory requirements, which could result in slowing the progress or increasing the costs of our homebuilding operations in these markets. Any such delays or costs could have a negative effect on our future revenues and earnings.

We also are subject to a variety of local, state, federal, and foreign laws and regulations concerning protection of health and the environment. The particular environmental laws and regulations that apply to any given community vary greatly according to the community site, the site's environmental conditions, and the present and former uses of the site. These environmental laws and regulations may result in delays, may cause us to incur substantial compliance, remediation, and/or other costs, and can prohibit or severely restrict development and homebuilding activity.

For example, we engaged in discussions with the U.S. Environmental Protection Agency ("EPA") and the U.S. Department of Justice ("DOJ") regarding alleged violations of storm water discharge requirements. In resolution of this matter, in April 2010, we agreed to the terms of a consent decree with the EPA, DOJ and the states of Virginia, Maryland, West Virginia and the District of Columbia (collectively, the "States"). The consent decree was approved by the federal district court in August 2010. Under the terms of the consent decree, we paid a fine of \$1.0 million collectively to the United States and the States named above and have agreed to perform under the terms of the consent decree for a minimum of three years, which includes implementing certain operational and training measures nationwide to facilitate ongoing compliance with storm water regulations. We received in October 2012 a notice from Region III of the EPA concerning stipulated penalties, totaling approximately \$120,000, based on the extent to which we reportedly did not meet certain compliance performance specified in the previously reported consent decree entered into in August 2010; we have since paid the stipulated penalties as assessed, and more recently have paid approximately \$8,000 in response to an EPA demand received in June 2013 for stipulated penalties based on information about our performance under the consent decree for 2012. The consent decree was terminated by court order without objection in December 2013.

In March 2013, we received a letter from the EPA requesting information about our involvement in a housing redevelopment project in Newark, New Jersey that a Company entity undertook during the 1990s. We understand that the development is in the vicinity of a former lead smelter and that recent tests on soil samples from properties within the development conducted by the EPA show elevated levels of lead. We also understand that the smelter operated before the City of Newark acquired properties, demolished structures existing on them, and sold the properties to the Company entity in connection with the redevelopment project. We responded to the EPA's request. In August 2013, we were notified that the EPA considers us a potentially responsible party (or "PRP") with respect to the site, that the EPA believes the site requires cleanup, and that the EPA is proposing that we address contamination at the site. We have begun preliminary discussions with the EPA concerning a possible resolution but do not know the scope or extent of the Company's obligations, if any, that may arise from the site and, therefore cannot provide any assurance that this matter will not have a material impact on the Company.

We anticipate that increasingly stringent requirements will be imposed on developers and homebuilders in the future. Although we cannot predict the effect of these requirements, they could result in time-consuming and expensive compliance programs and in substantial expenditures, which could cause delays and increase our cost of operations. In addition our ability to obtain or renew permits or approvals and the continued effectiveness of permits already granted or approvals already obtained is dependent upon many factors, some of which are beyond our control, such as changes in policies, rules, and regulations and their interpretations and application.

Several other homebuilders have received inquiries from regulatory agencies regarding the potential for homebuilders using contractors to be deemed employers of the employees of their contractors under certain circumstances. Contractors are independent of the homebuilders that contract with them under normal management practices and the terms of trade contracts and subcontracts within the industry; however, if regulatory agencies reclassify the employees of contractors as employees of homebuilders, homebuilders using contractors could be responsible for wage, hour, and other employment-related liabilities of their contractors.

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

As a homebuilder, we are subject to construction defect and home warranty claims arising in the ordinary course of business. Such claims are common in the homebuilding industry and can be costly. For example, in the past we have received construction defect and home warranty claims associated with, and we were involved in a multidistrict litigation concerning, allegedly defective drywall manufactured in China (“Chinese Drywall”) that may have been responsible for noxious smells and accelerated corrosion of certain metals in certain homes we have constructed. We remediated certain homes in response to such claims and settled the litigation. In addition, the amount and scope of coverage offered by insurance companies is currently limited, and this coverage may be further restricted and become more costly. If we are not able to obtain adequate insurance against such claims, if the costs associated with such claims significantly exceed the amount of our insurance coverage, or if our insurers do not pay on claims under our policies (whether because of dispute, inability, or otherwise), we may experience losses that could hurt our financial results. Our financial results could also be adversely affected if we were to experience an unusually high number of claims or unusually severe claims. Our insurance companies have the right to review our claims and claims history, and do so from time to time, and could decline to pay on such claims if such reviews determine the claims did not meet the terms for coverage. Additionally, we may need to significantly increase our construction defect and home warranty reserves as a result of insurance not being available for any of the reasons discussed above, such claims or the results of our annual actuarial study.

Mortgage investors could seek to have us buy back loans or compensate them for losses incurred on mortgages we have sold based on claims that we breached our limited representations or warranties.

Our financial services segment originates mortgages, primarily for our homebuilding customers. Substantially all of the mortgage loans originated are sold within a short period of time in the secondary mortgage market on a servicing released, nonrecourse basis, although we remain liable for certain limited representations, such as fraud, and warranties related to loan sales. Accordingly, mortgage investors have in the past and could in the future seek to have us buy back loans or compensate them for losses incurred on mortgages we have sold based on claims that we breached our limited representations or warranties. We believe there continues to be an industry-wide issue with the number of purchaser claims in which purchasers purport to have found inaccuracies related to sellers' representations and warranties in particular loan sale agreements. We have established reserves for potential losses; however, there can be no assurance that we will not have significant liabilities in respect of such claims in the future, which could exceed our reserves, or that the impact of such claims on our results of operations will not be material.

We compete on several levels with homebuilders that may have greater sales and financial resources, which could hurt future earnings.

We compete not only for home buyers but also for desirable properties, financing, raw materials, and skilled labor often within larger subdivisions designed, planned, and developed by other homebuilders. Our competitors include other local, regional, and national homebuilders, some of which have greater sales and financial resources.

The competitive conditions in the homebuilding industry together with current market conditions have, and could continue to, result in:

- difficulty in acquiring suitable land at acceptable prices;

- increased selling incentives;

- lower sales; or

- delays in construction.

Any of these problems could increase costs and/or lower profit margins.

We may have difficulty in obtaining the additional financing required to operate and develop our business.

Our operations require significant amounts of cash, and we may be required to seek additional capital, whether from sales of debt or equity securities or borrowing additional money, for the future growth and development of our business. The terms or availability of additional capital is uncertain. Moreover, the agreements governing our outstanding debt instruments contain provisions that restrict the debt we may incur in the future and our ability to pay dividends on equity. If we are not successful in obtaining sufficient capital, it could reduce our sales and may hinder our future growth and results of operations. In addition, pledging substantially all of our assets to support our senior secured notes may make it more difficult to raise additional financing in the future.

Our future growth may include additional acquisitions of companies that may not be successfully integrated and may not achieve expected benefits.

Acquisitions of companies have contributed to our historical growth and may again be a component of our growth strategy in the future. In the future, we may acquire businesses, some of which may be significant. As a result of acquisitions of companies, we may need to seek additional financing and integrate product lines, dispersed operations, and distinct corporate cultures. These integration efforts may not succeed or may distract our management from operating our existing business. Additionally, we may not be able to enhance our earnings as a result of acquisitions. Our failure to successfully identify and manage future acquisitions could harm our operating results.

Our controlling stockholders are able to exercise significant influence over us.

Members of the Hovnanian family, including Ara K. Hovnanian, our chairman of the board, president, and chief executive officer, have voting control, through personal holdings, the limited partnership and the limited liability company established for members of Mr. Hovnanian's family, family trusts and shares held by the estate of our former chairman, Kevork S. Hovnanian, of Class A and Class B common stock that enables them to cast approximately 56% of the votes that may be cast by the holders of our outstanding Class A and Class B common stock combined. Their combined stock ownership enables them to exert significant control over us, including power to control the election of the Board of Directors and to approve matters presented to our stockholders. This concentration of ownership may also make some transactions, including mergers or other changes in control, more difficult or impossible without their support. Also, because of their combined voting power, circumstances may occur in which their interests could be in conflict with the interests of other stakeholders.

Our net operating loss carryforwards could be substantially limited if we experience an ownership change as defined in the Internal Revenue Code.

Based on recent impairments and our current financial performance, we generated a federal net operating loss carryforward of \$1.5 billion through the fiscal year ended October 31, 2013, and we may generate net operating loss carryforwards in future years.

Section 382 of the Internal Revenue Code (the "Code") contains rules that limit the ability of a company that undergoes an ownership change, which is generally any change in ownership of more than 50% of its stock over a three-year period, to utilize its net operating loss carryforwards and certain built-in losses recognized in years after the ownership change. These rules generally operate by focusing on ownership shifts among stockholders owning directly or indirectly 5% or more of the stock of a company and any change in ownership arising from a new issuance of stock by the company.

If we undergo an ownership change for purposes of Section 382 as a result of future transactions involving our stock, including purchases or sales of stock between 5% shareholders, our ability to use our net operating loss carryforwards and to recognize certain built-in losses would be subject to the limitations of Section 382. Depending on the resulting limitation, a significant portion of our net operating loss carryforwards could expire before we would be able to use them. A limitation imposed under Section 382 on our ability to utilize our net operating loss carryforwards could have a negative impact on our financial position and results of operations.

In August 2008, we announced that the Board of Directors adopted a shareholder rights plan (the “Rights Plan”) designed to preserve shareholder value and the value of certain tax assets primarily associated with net loss carryforwards and built-in losses under Section 382 of the Code, and on December 5, 2008, our stockholders approved the Board’s decision to adopt the Rights Plan. The Rights Plan is intended to act as a deterrent to any person or group acquiring 4.9% or more of our outstanding Class A common stock (any such person an “Acquiring Person”), without the approval of the Company’s Board of Directors. Subject to the terms, provisions and conditions of the Rights Plan, if and when they become exercisable, each right would entitle its holder to purchase from the Company one ten-thousandth of a share of the Company’s Series B Junior Preferred Stock for a purchase price of \$35.00 per share (the “purchase price”). The rights will not be exercisable until the earlier of (i) 10 business days after a public announcement by us that a person or group has become an Acquiring Person and (ii) 10 business days after the commencement of a tender or exchange offer by a person or group for 4.9% of the Class A common stock (the “distribution date”). If issued, each fractional share of Series B Junior Preferred Stock would give the stockholder approximately the same dividend, voting and liquidation rights as does one share of the Company’s Class A common stock. However, prior to exercise, a right does not give its holder any rights as a stockholder of the Company, including without limitation any dividend, voting, or liquidation rights. After the distribution date, each holder of a right, other than rights beneficially owned by the Acquiring Person (which will thereupon become void), will thereafter have the right to receive upon exercise of a right and payment of the purchase price, that number of shares of Class A Common Stock or Class B Common Stock, as the case may be, having a market value of two times the purchase price. After the distribution date, our Board of Directors may exchange the rights (other than rights owned by an Acquiring Person which will have become void), in whole or in part, at an exchange ratio of one share of common stock, or a fractional share of Series B Junior Preferred Stock (or of a share of a similar class or series of Hovnanian’s preferred stock having similar rights, preferences, and privileges) of equivalent value, per right (subject to adjustment).

In addition, on December 5, 2008, our stockholders approved an amendment to our Certificate of Incorporation to restrict certain transfers of our common stock in order to preserve the tax treatment of our net operating loss carryforwards and built-in losses under Section 382 of the Code. Subject to certain exceptions pertaining to pre-existing 5% stockholders and Class B stockholders, the transfer restrictions in the amended Certificate of Incorporation generally restrict any direct or indirect transfer (such as transfers of the Company’s stock that result from the transfer of interests in other entities that own the Company’s stock) if the effect would be to: (i) increase the direct or indirect ownership of the Company’s stock by any person (or public group) from less than 5% to 5% or more of the Company’s stock; (ii) increase the percentage of the Company’s stock owned directly or indirectly by a person (or public group) owning or deemed to own 5% or more of the Company’s stock; or (iii) create a new “public group” (as defined in the applicable United States Treasury regulations).

Utility shortages and outages or rate fluctuations could have an adverse effect on our operations.

In prior years, the areas in which we operate in California have experienced power shortages, including periods without electrical power, as well as significant fluctuations in utility costs. We may incur additional costs and may not be able to complete construction on a timely basis if such power shortages and outages and utility rate fluctuations

continue. Furthermore, power shortages and outages and rate fluctuations may adversely affect the regional economies in which we operate, which may reduce demand for our homes. Our operations may be adversely affected if further rate fluctuations and/or power shortages and outages occur in California, the Northeast, or in our other markets.

Geopolitical risks and market disruption could adversely affect our operating results and financial condition.

Geopolitical events, such as the aftermath of the war with Iraq and the continuing involvement in Afghanistan, may have a substantial impact on the economy and the housing market. The terrorist attacks on the World Trade Center and the Pentagon on September 11, 2001 had an impact on our business and the occurrence of similar events in the future cannot be ruled out. The war and the continuing involvement in Afghanistan, terrorism, and related geopolitical risks have created many economic and political uncertainties, some of which may have additional material adverse effects on the U.S. economy, our customers and, in turn, our results of operations and financial condition.

ITEM 1B

UNRESOLVED STAFF COMMENTS

None.

ITEM 2

PROPERTIES

We own a 69,000 square-foot office complex located in the Northeast that serves as our corporate headquarters. We own 215,000 square feet of office and warehouse space throughout the Midwest. We lease approximately 488,000 square feet of space for our segments located in the Northeast, Mid-Atlantic, Midwest, Southeast, Southwest, and West. Included in this amount is 88,000 square feet of abandoned lease space.

ITEM 3

LEGAL PROCEEDINGS

We are involved in litigation arising in the ordinary course of business, none of which is expected to have a material adverse effect on our financial position or results of operations, and we are subject to extensive and complex regulations that affect the development and home building, sales, and customer financing processes, including zoning, density, building standards, and mortgage financing. These regulations often provide broad discretion to the administering governmental authorities. This can delay or increase the cost of development or homebuilding.

We also are subject to a variety of local, state, federal, and foreign laws and regulations concerning protection of health and the environment. The particular environmental laws that apply to any given community vary greatly according to the community site, the site's environmental conditions and the present and former uses of the site. These environmental laws may result in delays, may cause us to incur substantial compliance, remediation and/or other costs, and can prohibit or severely restrict development and homebuilding activity.

We received in October 2012 a notice from Region III of the U. S. Environmental Protection Agency ("EPA") concerning stipulated penalties, totaling approximately \$120,000, based on the extent to which we reportedly did not meet certain compliance performance specified in the previously reported consent decree entered into in August 2010; we have since paid the stipulated penalties as assessed, and more recently have paid approximately \$8,000 in response to an EPA demand received in June 2013 for stipulated penalties based on information about our performance under the consent decree for 2012. The consent decree was terminated by court order without objection in December 2013.

In March 2013, we received a letter from the EPA requesting information about our involvement in a housing redevelopment project in Newark, New Jersey that a Company entity undertook during the 1990s. We understand that the development is in the vicinity of a former lead smelter and that recent tests on soil samples from properties within the development conducted by the EPA show elevated levels of lead. We also understand that the smelter operated before the City of Newark acquired properties, demolished structures existing on them, and sold the properties to the Company entity in connection with the redevelopment project. We responded to the EPA's request. In August 2013, we were notified that the EPA considers us a potentially responsible party (or "PRP") with respect to the site, that the EPA believes the site requires cleanup, and that the EPA is proposing that we address contamination at the site. We have begun preliminary discussions with the EPA concerning a possible resolution but do not know the scope or extent of the Company's obligations, if any, that may arise from the site and therefore cannot provide any assurance that this matter will not have a material impact on the Company.

We anticipate that increasingly stringent requirements will be imposed on developers and homebuilders in the future. Although we cannot predict the effect of these requirements, they could result in time-consuming and expensive compliance programs and in substantial expenditures, which could cause delays and increase our cost of operations. In

addition our ability to obtain or renew permits or approvals and the continued effectiveness of permits already granted or approvals already obtained is dependent upon many factors, some of which are beyond our control, such as changes in policies, rules, and regulations and their interpretations and application.

The Company is also involved in the following litigation:

Hovnanian Enterprises, Inc. and K. Hovnanian Venture I, L.L.C. (collectively, the “Company Defendants”) have been named as defendants in a class action suit. The action was filed by Mike D’Andrea and Tracy D’Andrea, on behalf of themselves and all others similarly situated in the Superior Court of New Jersey, Gloucester County. The action was initially filed on May 8, 2006 alleging that the HVAC systems installed in certain of the Company’s homes are in violation of applicable New Jersey building codes and are a potential safety issue. On December 14, 2011, the Superior Court granted class certification; the potential class is 1,065 homes. The Company Defendants filed a request to take an interlocutory appeal regarding the class certification decision. The Appellate Division denied the request, and the Company Defendants filed a request for interlocutory review by the New Jersey Supreme Court, which remanded the case back to the Appellate Division for a review on the merits of the appeal on May 8, 2012. The Appellate Division, on remand, heard oral arguments on December 4, 2012, reviewing the Superior Court’s original finding of class certification. On June 18, 2013, the Appellate Division affirmed class certification. On July 3, 2013, the Company Defendants appealed the June 2013 Appellate Division’s decision to the New Jersey Supreme Court, which elected not to hear the appeal on October 22, 2013. Accordingly, the matter is proceeding in the Superior Court and discovery is ongoing. The Company Defendants have pending a motion to consolidate an indemnity action they filed against various manufacturer and sub-contractor defendants so that these parties will be required to participate directly in the class action. The plaintiff class seeks unspecified damages as well as treble damages pursuant to the NJ Consumer Fraud Act. The Company Defendants believe there is insurance coverage available for this action. It is not possible to estimate a loss or range of loss related to this matter at this time.

ITEM 4

MINE SAFETY DISCLOSURES

Not applicable

EXECUTIVE OFFICERS OF THE REGISTRANT

Information on executive officers of the registrant is incorporated herein from Part III, Item 10.

Part II**ITEM 5****MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS, AND ISSUER PURCHASES OF EQUITY SECURITIES**

Our Class A Common Stock is traded on the New York Stock Exchange under the symbol "HOV" and was held by 503 stockholders of record at December 16, 2013. There is no established public trading market for our Class B Common Stock, which was held by 241 stockholders of record at December 16, 2013. In order to trade Class B Common Stock, the shares must be converted into Class A Common Stock on a one-for-one basis. The high and low closing sales prices for our Class A Common Stock were as follows for each fiscal quarter during the years ended October 31, 2013 and 2012:

Quarter	October 31, 2013		October 31, 2012	
	High	Low	High	Low
First	\$7.00	\$4.42	\$2.67	\$1.23
Second	\$6.32	\$4.76	\$3.24	\$1.88
Third	\$6.43	\$5.20	\$2.94	\$1.61
Fourth	\$5.53	\$4.93	\$4.44	\$2.25

Certain debt instruments to which we are a party contain restrictions on the payment of cash dividends. As a result of the most restrictive of these provisions, we are not currently able to pay any cash dividends. We have never paid a cash dividend to common stockholders.

Recent Sales of Unregistered Equity Securities

None.

Issuer Purchases of Equity Securities

No shares of our Class A Common Stock or Class B Common Stock were purchased by or on behalf of the Company or any affiliated purchaser during the fiscal fourth quarter of 2013. The maximum number of shares that may yet be purchased under the Company's repurchase plans or programs is 0.5 million.

ITEM 6

SELECTED FINANCIAL DATA

The following table sets forth our selected consolidated financial data and should be read in conjunction with Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our Consolidated Financial Statements and Notes thereto included elsewhere in this Annual Report on Form 10-K.

Summary Consolidated Statements of Operations Data	Year Ended				
	October 31,	October 31,	October 31,	October 31,	October 31,
	2013	2012	2011	2010	2009
(In thousands, Except Per Share Data)					
Revenues	\$1,851,253	\$1,485,353	\$1,134,907	\$1,371,842	\$1,596,290
Expenses excluding inventory impairment loss and land option write-offs	1,835,633	1,550,406	1,323,316	1,557,428	1,972,978
Inventory impairment loss and land option write-offs	4,965	12,530	101,749	135,699	659,475
Total Expenses	1,840,598	1,562,936	1,425,065	1,693,127	2,632,453
(Loss) gain on extinguishment of debt	(760)	(29,066)	7,528	25,047	410,185
Income (loss) from unconsolidated joint ventures	12,040	5,401	(8,958)	956	(46,041)
Income (loss) before income taxes	21,935	(101,248)	(291,588)	(295,282)	(672,019)
State and federal income tax (benefit) provision	(9,360)	(35,051)	(5,501)	(297,870)	44,693
Net income (loss)	\$31,295	\$(66,197)	\$(286,087)	\$2,588	\$(716,712)
Per share data:					
Basic:					
Income (loss) per common share	\$0.22	\$(0.52)	\$(2.85)	\$0.03	\$(9.16)
Weighted-average number of common shares outstanding	145,087	126,350	100,444	78,691	78,238
Assuming dilution:					
Income (loss) per common share	\$0.22	\$(0.52)	\$(2.85)	\$0.03	\$(9.16)
Weighted-average number of common shares outstanding	162,329	126,350	100,444	79,683	78,238

Summary Consolidated Balance Sheet Data

(In thousands)	October 31,	October 31,	October 31,	October 31,	October 31,
	2013	2012	2011	2010	2009
	Total assets	\$1,759,130	\$1,684,250	\$1,602,180	\$1,817,560
Mortgages and lines of credit	\$172,299	\$164,562	\$95,598	\$98,613	\$77,364
Senior secured notes, senior notes, senior amortizing notes, senior exchangeable notes and TEU senior subordinated amortizing notes (net of discount)	\$1,529,445	\$1,542,196	\$1,602,770	\$1,616,347	\$1,751,701
Total equity deficit	\$(432,799)	\$(485,345)	\$(496,602)	\$(337,938)	\$(348,868)

Ratios of Earnings to Fixed Charges and Earnings to Combined Fixed Charges and Preferred Stock Dividends

For purposes of computing the ratio of earnings to fixed charges and the ratio of earnings to combined fixed charges and preferred stock dividends, earnings consist of earnings from continuing operations before income taxes and income or loss from equity investees, plus fixed charges and distributed income of equity investees, less interest capitalized. Fixed charges consist of all interest incurred, plus that portion of operating lease rental expense (33%) deemed to be representative of interest, plus the amortization of debt issuance costs and bond discounts. Combined fixed charges and preferred stock dividends consist of fixed charges and preferred stock dividends declared. Due to covenant restrictions, we have been prohibited from paying preferred stock dividends beginning with the first quarter of fiscal 2008. The following table sets forth the ratios of earnings to fixed charges and the ratios of earnings to combined fixed charges and preferred stock dividends for each of the periods indicated:

	Years Ended October				
	31,				
	2013	2012	2011	2010	2009
Ratio of earnings to fixed charges	1.2	(a)	(a)	(a)	(a)
Ratio of earnings to combined fixed charges and preferred stock dividends	1.2	(b)	(b)	(b)	(b)

(a) *Earnings for the years ended October 31, 2012, 2011, 2010 and 2009 were insufficient to cover fixed charges for such period by \$105.1 million, \$272.9 million, \$273.8 million, and \$628.3 million, respectively.*

Earnings for the years ended October 31, 2012, 2011, 2010 and 2009 were insufficient to cover fixed charges and preferred stock dividends for such period by \$105.1 million, \$272.9 million, \$273.8 million and \$628.3 million, (b) respectively. Due to restrictions in our indentures for our senior and senior secured notes, we are currently prohibited from paying dividends on our preferred stock and did not make any dividend payments in fiscal 2013, 2012, 2011, 2010, and 2009.

ITEM 7

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

During fiscal 2013, the housing market continued to strengthen, and, as a result, we experienced further positive operating trends, including improvements in several metrics for the year ended October 31, 2013 compared to the year ended October 31, 2012, such as: net contract growth of 7.9%, an increase in gross margin percentage, before cost of sales interest expense and land charges, from 17.8% to 20.1% and a decrease in selling, general and administrative costs (including corporate general and administrative expenses) as a percentage of total revenue from 12.8% to 11.9%. In addition, our contract cancellation rate was 18% for fiscal 2013, which is below what we believe to be a normalized level of approximately 20%. Active selling communities were 192 and 172 at October 31, 2013 and 2012, respectively. Net contracts per average active selling community increased to 30.7 for the year ended October 31, 2013, compared to 28.1 in the same period in the prior year. Net contracts for the fourth quarter of fiscal 2013 were 6.4% below the same period of the prior year as a result of the slowdown in the housing market due to the adverse impacts of higher mortgage rates, the sequester and the government shutdown. However, this negative trend reversed in October and November of 2013, where net contracts increased slightly over the same periods of the prior year.

Our gross margin percentage, before cost of sales interest expense and land charges, and selling, general and administrative costs (including corporate general and administrative expenses) as a percentage of total revenues also had favorable variances when comparing sequentially from the third quarter of fiscal 2013 to the fourth quarter of fiscal 2013. Gross margin percentage increased from 20.3% to 22.6% and selling, general and administrative costs (including corporate general and administrative expenses) as a percentage of revenues decreased from 11.8% to 10.6%, as compared to the third quarter of fiscal 2013. Cost of sales and selling, general and administrative costs include some fixed costs that are not impacted by delivery volume. Therefore, as deliveries increased from the third quarter of fiscal 2013 to the fourth quarter of fiscal 2013, selling, general and administrative costs as a percentage of revenues improved. The increase in gross margin percentage partially resulted from the delivery volume increase, but also was the result of higher home prices that exceeded increased construction costs in certain markets and an increase in the percentage of deliveries from newly identified communities (which we define as communities that were controlled subsequent to January 31, 2009), which generally have higher gross margins than our older communities.

While we are encouraged by the positive operating trends that began in fiscal 2012 and continued into fiscal 2013, several challenges, such as persistently high unemployment levels, national and global economic weakness and uncertainty, the restrictive mortgage lending environment, higher mortgage interest rates and the potential for more foreclosures, continue to threaten a recovery in the housing market. Our recent operating results and other national data indicate that the overall demand for new homes has continued to improve. However, both national new home sales and our home sales remain below historical levels. Until there is a more robust U.S. economic recovery, we expect national demand for new homes to remain at below normal levels, with uneven improvement across our operating markets.

During the prolonged downturn of the housing market, we adjusted our approach to land acquisition and construction practices and shortened our land pipeline, reduced production volumes, and balanced home price and profitability with sales pace. We delayed and cancelled planned land purchases, renegotiated land prices, and significantly reduced our total number of controlled lots owned and under option. Additionally, we significantly reduced our total number of speculative homes put into production. Since January 2009, however, we began to see more opportunities to purchase land at prices that made economic sense in light of our then current sales prices and sales paces and plan to continue pursuing such land acquisitions. New land purchases at pricing that we believe will generate appropriate investment returns and drive greater operating efficiencies are needed to return to sustained profitability. During fiscal 2013, we opened for sale 91 new communities, purchased approximately 6,200 lots within 236 newly identified communities (which we define as communities that were controlled subsequent to January 31, 2009), and optioned approximately 12,100 lots in 230 newly identified communities. As we have experienced increased sales pace over the past year, causing communities to sell out more rapidly, we continue to consider and make new land acquisitions to replenish or grow our community count. As a result, our active community count increased by 20 communities from October 31, 2012 to 192 communities at October 31, 2013. We have also continued to closely evaluate and control selling, general and administrative expenses, including corporate general and administrative expenses. While homebuilding selling, general and administrative expenses increased \$23.7 million from \$142.1 million in fiscal 2012 to \$165.8 million for fiscal 2013, in connection with our increased revenues, these expenses as a percentage of total homebuilding revenues decreased from 9.8% to 9.2% due to the revenue growth across our operating segments. Corporate general and administrative expenses as a percentage of total revenue decreased from 3.2% in fiscal 2012 to 2.9% in fiscal 2013. Given the persistence of difficult market conditions, improving the efficiency of our selling, general and administrative expenses will continue to be a significant area of focus.

Critical Accounting Policies

Management believes that the following critical accounting policies require its most significant judgments and estimates used in the preparation of the consolidated financial statements:

Income Recognition from Home and Land Sales - We are primarily engaged in the development, construction, marketing and sale of residential single-family and multi-family homes where the planned construction cycle is less than 12 months. For these homes, in accordance with Accounting Standards Certification (ASC) 360-20, "Property, Plant and Equipment - Real Estate Sales" ("ASC 360-20"), revenue is recognized when title is conveyed to the buyer, adequate initial and continuing investments have been received, and there is no continued involvement. In situations where the buyer's financing is originated by our mortgage subsidiary and the buyer has not made an adequate initial investment or continuing investment as prescribed by ASC 360-20, the profit on such sales is deferred until the sale of the related mortgage loan to a third-party investor has been completed.

Income Recognition from Mortgage Loans - Our Financial Services segment originates mortgages, primarily for our homebuilding customers. We use mandatory investor commitments and forward sales of mortgage-backed securities to hedge our mortgage-related interest rate exposure on agency and government loans.

We elected the fair value option for our mortgage loans held for sale in accordance with ASC 825, "Financial Instruments," which permits us to measure our loans held for sale at fair value. Management believes that the election of the fair value option for loans held for sale improves financial reporting by mitigating volatility in reported earnings caused by measuring the fair value of the loans and the derivative instruments used to economically hedge them without having to apply complex hedge accounting provisions.

Substantially all of the mortgage loans originated are sold within a short period of time in the secondary mortgage market on a servicing released, nonrecourse basis, although the Company remains liable for certain limited representations, such as fraud, and warranties related to loan sales. Mortgage investors could seek to have us buy back loans or compensate them for losses incurred on mortgages we have sold based on claims that we breached our limited representations and warranties. We believe there continues to be an industry-wide issue with the number of purchaser claims in which purchasers purport to have found inaccuracies related to the sellers' representations and warranties in particular loan sale agreements. We have established reserves for probable losses.

Inventories - Inventories consist of land, land development, home construction costs, capitalized interest, and construction overhead and property taxes. Construction costs are accumulated during the period of construction and charged to cost of sales under specific identification methods. Land, land development, and common facility costs are allocated based on buildable acres to product types within each community, then charged to cost of sales equally

based upon the number of homes to be constructed in each product type.

We record inventories in our consolidated balance sheets at cost unless the inventory is determined to be impaired, in which case the inventory is written down to its fair value. Our inventories consist of the following three components: (1) sold and unsold homes and lots under development, which includes all construction, land, capitalized interest, and land development costs related to started homes and land under development in our active communities; (2) land and land options held for future development or sale, which includes all costs related to land in our communities in planning or mothballed communities; and (3) consolidated inventory not owned, which includes all costs related to specific performance options, variable interest entities, and other options, which consists primarily of model homes financed with an investor and inventory related to land banking arrangements.

We decide to mothball (or stop development on) certain communities when we determine that current market conditions do not justify further investment at that time. When we decide to mothball a community, the inventory is reclassified on our consolidated balance sheets from "Sold and unsold homes and lots under development" to "Land and land options held for future development or sale." As of October 31, 2013, the net book value associated with our 50 mothballed communities was \$115.9 million, net of impairment charges recorded in prior periods of \$431.6 million. We regularly review communities to determine if mothballing is appropriate. During fiscal 2013, we mothballed one community, re-activated three previously mothballed communities, and sold one mothballed community.

From time to time we enter into option agreements that include specific performance requirements, whereby we are required to purchase a minimum number of lots. Because of our obligation to purchase these lots, for accounting purposes in accordance with ASC 360-20-40-38, we are required to record this inventory on our Consolidated Balance Sheets. As of October 31, 2013, we had \$0.8 million of specific performance options recorded on our Consolidated Balance Sheets to “Consolidated inventory not owned – specific performance options,” with a corresponding amount recorded to “Liabilities from inventory not owned.”

“Consolidated inventory not owned – other options” consists of certain model sale leasebacks and land banking arrangements, and other options that were included on our balance sheet in accordance with GAAP. During fiscal 2013, we sold and leased back certain of our model homes with the right to participate in the potential profit when each home is sold to a third party at the end of the respective lease. As a result of our continued involvement, for accounting purposes in accordance with ASC 360-20-40-38, these sale and leaseback transactions are considered a financing rather than a sale. Therefore, for purposes of our Consolidated Balance Sheet, at October 31, 2013, inventory of \$47.6 million was recorded to “Consolidated inventory not owned – other options”, with a corresponding amount of \$45.7 million recorded to “Liabilities from inventory not owned.”

In addition, we entered into a land banking arrangement in fiscal 2012 with GSO Capital Partners LP ("GSO"), that continued in fiscal 2013, whereby we sold a portfolio of our land parcels to GSO, and GSO provided us an option to purchase back finished lots on a quarterly basis. Because of our option to repurchase these parcels, for accounting purposes, in accordance with ASC 360-20-40-38, this transaction is considered a financing rather than a sale. For purposes of our Consolidated Balance Sheet, at October 31, 2013, inventory of \$52.4 million was recorded as “Consolidated inventory not owned – other options”, with a corresponding amount of \$41.4 million recorded to “Liabilities from inventory not owned” for the amount of net cash received from the transactions.

The recoverability of inventories and other long-lived assets is assessed in accordance with the provisions of ASC 360-10, “Property, Plant and Equipment - Overall” (“ASC 360-10”). ASC 360-10 requires long-lived assets, including inventories, held for development to be evaluated for impairment based on undiscounted future cash flows of the assets at the lowest level for which there are identifiable cash flows. As such, we evaluate inventories for impairment at the individual community level, the lowest level of discrete cash flows that we measure.

We evaluate inventories of communities under development and held for future development for impairment when indicators of potential impairment are present. Indicators of impairment include, but are not limited to, decreases in local housing market values, decreases in gross margins or sales absorption rates, decreases in net sales prices (base sales price net of sales incentives), or actual or projected operating or cash flow losses. The assessment of communities for indication of impairment is performed quarterly. As part of this process, we prepare detailed budgets for all of our communities at least semi-annually and identify those communities with a projected operating loss. For those communities with projected losses, we estimate the remaining undiscounted future cash flows and compare those to the carrying value of the community, to determine if the carrying value of the asset is recoverable.

The projected operating profits, losses, or cash flows of each community can be significantly impacted by our estimates of the following:

future base selling prices;

future home sales incentives;

future home construction and land development costs; and

future sales absorption pace and cancellation rates.

These estimates are dependent upon specific market conditions for each community. While we consider available information to determine what we believe to be our best estimates as of the end of a quarterly reporting period, these estimates are subject to change in future reporting periods as facts and circumstances change. Local market-specific conditions that may impact our estimates for a community include:

the intensity of competition within a market, including available home sales prices and home sales incentives offered by our competitors;

the current sales absorption pace for both our communities and competitor communities;

community specific attributes, such as location, availability of lots in the market, desirability and uniqueness of our community, and the size and style of homes currently being offered;

potential for alternative product offerings to respond to local market conditions;

changes by management in the sales strategy of the community;

current local market economic and demographic conditions and related trends of forecasts; and

existing home inventory supplies, including foreclosures and short sales.

These and other local market-specific conditions that may be present are considered by management in preparing projection assumptions for each community. The sales objectives can differ between our communities, even within a given 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. In addition, the key assumptions included in our estimate of future undiscounted cash flows may be interrelated. For example, a decrease in estimated base sales price or an increase in homes sales incentives may result in a corresponding increase in sales absorption pace. Additionally, a decrease in the average sales price of homes to be sold and closed in future reporting periods for one community that has not been generating what management believes to be an adequate sales absorption pace may impact the estimated cash flow assumptions of a nearby community. Changes in our key assumptions, including estimated construction and development costs, absorption pace and selling strategies, could materially impact future cash flow and fair-value estimates. Due to the number of possible scenarios that would result from various changes in these factors, we do not believe it is possible to develop a sensitivity analysis with a level of precision that would be meaningful.

If the undiscounted cash flows are more than the carrying value of the community, then the carrying amount is recoverable, and no impairment adjustment is required. However, if the undiscounted cash flows are less than the carrying amount, then the community is deemed impaired and is written-down to its fair value. We determine the estimated fair value of each community by determining the present value of its estimated future cash flows at a discount rate commensurate with the risk of the respective community, or in limited circumstances, prices for land in recent comparable sale transactions, market analysis studies, which include the estimated price a willing buyer would pay for the land (other than in a forced liquidation sale), and recent bona fide offers received from outside third parties. Our discount rates used for all impairments recorded from October 31, 2011 to October 31, 2013 ranged from 16.8% to 19.8%. The estimated future cash flow assumptions are virtually the same for both our recoverability and fair value assessments. Should the estimates or expectations used in determining estimated cash flows or fair value, including discount rates, decrease or differ from current estimates in the future, we may be required to recognize additional impairments related to current and future communities. The impairment of a community is allocated to each lot on a relative fair value basis.

From time to time, we write off deposits and approval, engineering and capitalized interest costs when we determine that it is no longer probable that we will exercise options to buy land in specific locations or when we redesign communities and/or abandon certain engineering costs. In deciding not to exercise a land option, we take into

consideration changes in market conditions, the timing of required land takedowns, the willingness of land sellers to modify terms of the land option contract (including timing of land takedowns), and the availability and best use of our capital, among other factors. The write-off is recorded in the period it is deemed not probable that the optioned property will be acquired. In certain instances, we have been able to recover deposits and other pre-acquisition costs that were previously written off. These recoveries have not been significant in comparison to the total costs written off.

Inventories held for sale are land parcels ready for sale in their current condition, where we have decided not to build homes but are instead actively marketing for sale. These land parcels represented \$2.7 million of our total inventories at October 31, 2013, and are reported at the lower of carrying amount or fair value less costs to sell. In determining fair value for land held for sale, management considers, among other things, prices for land in recent comparable sale transactions, market analysis studies, which include the estimated price a willing buyer would pay for the land (other than in a forced liquidation sale) and recent bona fide offers received from outside third parties.

Insurance Deductible Reserves - For homes delivered in fiscal 2013 and 2012, our deductible under our general liability insurance is \$20 million per occurrence for construction defect and warranty claims. For bodily injury claims, our deductible per occurrence in fiscal 2013 and 2012 is \$0.25 million and \$0.1 million, respectively, up to a \$5 million limit. Our aggregate retention in 2013 and 2012 is \$21 million for construction defect, warranty and bodily injury claims. We do not have a deductible on our worker's compensation insurance. Reserves for estimated losses for construction defects, warranty, bodily injury and workers' compensation claims have been established using the assistance of a third-party actuary. We engage a third-party actuary that uses our historical warranty and construction defect data and worker's compensation data to assist our management in estimating our unpaid claims, claim adjustment expenses and incurred but not reported claims reserves for the risks that we are assuming under the general liability and worker's compensation programs. The estimates include provisions for inflation, claims handling and legal fees. These estimates are subject to a high degree of variability due to uncertainties such as trends in construction defect claims relative to our markets and the types of products we build, claim settlement patterns, insurance industry practices, and legal interpretations, among others. Because of the high degree of judgment required in determining these estimated liability amounts, actual future costs could differ significantly from our currently estimated amounts.

Land Options – Deposits on options to acquire improved or unimproved home sites and pre-development costs incurred on this land under option are capitalized. Such amounts are either included as part of the purchase price if the land is acquired or charged to operations if we determine we will not exercise the option. If the options are with variable interest entities and we are the primary beneficiary, we record the land under option on the Consolidated Balance Sheets under “Consolidated inventory not owned” with an offset under “Liabilities from inventory not owned.” The evaluation of whether or not we are the primary beneficiary can require significant judgment. Similarly, if the option obligation is to purchase under specific performance or has terms that require us to record it as financing, then we record the option on the Consolidated Balance Sheets under “Consolidated inventory not owned” with an offset under “Liabilities from inventory not owned.” We record costs associated with other options on the Consolidated Balance Sheets under “Land and land options held for future development or sale.”

Unconsolidated Homebuilding and Land Development Joint Ventures - Investments in unconsolidated homebuilding and land development joint ventures are accounted for under the equity method of accounting. Under the equity method, we recognize our proportionate share of earnings and losses earned by the joint venture upon the delivery of lots or homes to third parties. Our ownership interest in joint ventures varies but our voting interests are generally less than or equal to 50%. In determining whether or not we must consolidate joint ventures where we are the managing member of the joint venture, we assess whether the other partners have specific rights to overcome the presumption of control by us as the manager of the joint venture. In most cases, the presumption is overcome because the joint venture agreements require that both partners agree on establishing the significant operating and capital decisions of the partnership, including budgets, in the ordinary course of business. The evaluation of whether or not we control a venture can require significant judgment. In accordance with ASC 323-10, “Investments - Equity Method and Joint Ventures - Overall” (“ASC 323-10”), we assess our investments in unconsolidated joint ventures for recoverability, and if it is determined that a loss in value of the investment below its carrying amount is other than temporary, we write down the investment to its fair value. We evaluate our equity investments for impairment based on the joint venture’s projected cash flows. This process requires significant management judgment and estimates. During fiscal 2012 and fiscal 2013, there were no write-downs of our joint venture investments.

Post-Development Completion and Warranty Costs - In those instances where a development is substantially completed and sold and we have additional construction work to be incurred, an estimated liability is provided to cover the cost of such work. We accrue for warranty costs that are covered under our existing general liability and construction defect policy as part of our general liability insurance deductible. This accrual is expensed as selling, general, and administrative costs. For homes delivered in fiscal 2013 and 2012, our deductible under our general liability insurance is \$20 million per occurrence for construction defect and warranty claims. For bodily injury claims, our deductible per occurrence in fiscal 2013 and 2012 is \$0.25 million and \$0.1 million, respectively, up to a \$5 million limit. Our aggregate retention in fiscal 2013 and 2012 is \$21 million for construction defect, warranty and bodily injury claims. In addition, we establish a warranty accrual for lower cost-related issues to cover home repairs, community amenities, and land development infrastructure that are not covered under our general liability and construction defect policy. We accrue an estimate for these warranty costs as part of cost of sales at the time each home is closed and title and possession have been transferred to the homebuyer. See Note 17 to the Consolidated Financial Statements for additional information on the amount of warranty costs recognized in cost of goods sold and administrative expenses.

Income Taxes - Deferred income taxes are provided for temporary differences between amounts recorded for financial reporting and for income tax purposes. If the combination of future years' income (or loss) combined with the reversal of the timing differences results in a loss, such losses can be carried back to prior years or carried forward to future years to recover the deferred tax assets. In accordance with ASC 740-10, "Income Taxes - Overall" ("ASC 740-10"), we evaluate our deferred tax assets quarterly to determine if valuation allowances are required. ASC 740-10 requires that companies assess whether valuation allowances should be established based on the consideration of all available evidence using a "more-likely-than-not" standard. See "Total Taxes" below under "Results of Operations" for further discussion of the valuation allowances.

In evaluating the exposures associated with our various tax filing positions, we recognize tax liabilities in accordance with ASC 740-10, for more likely than not exposures. We re-evaluate the exposures associated with our tax positions on a quarterly basis. This evaluation is based on factors such as changes in facts or circumstances, changes in tax law, new audit activity, and effectively settled issues. Determining whether an uncertain tax position is effectively settled requires judgment. Such a change in recognition or measurement would result in the recognition of a tax benefit or an additional charge to the tax provision. A number of years may elapse before a particular matter for which we have established a liability is audited and fully resolved or clarified. We adjust our liability for unrecognized tax benefits and income tax provision in the period in which an uncertain tax position is effectively settled, or the statute of limitations expires for the relevant taxing authority to examine the tax position or when more information becomes available. Due to the complexity of some of these uncertainties, the ultimate resolution may result in a liability that is materially different from our current estimate. Any such changes will be reflected as increases or decreases to income tax expense in the period in which they are determined.

Recent Accounting Pronouncements

There have been no accounting pronouncements that have been issued but not yet implemented that we believe will materially impact our financial statements.

Capital Resources and Liquidity

Our operations consist primarily of residential housing development and sales in the Northeast (New Jersey, Pennsylvania), the Mid-Atlantic (Delaware, Maryland, Virginia, Washington D.C., West Virginia), the Midwest (Illinois, Minnesota, Ohio), the Southeast (Florida, Georgia, North Carolina, South Carolina), the Southwest (Arizona, Texas), and the West (California). In addition, we provide certain financial services to our homebuilding customers.

We have historically funded our homebuilding and financial services operations with cash flows from operating activities, borrowings under our bank credit facilities (when we have had such facilities for our homebuilding operations) and the issuance of new debt and equity securities. During the prolonged housing market downturn that began in late 2006, we had been operating with a primary focus to generate cash flows from operations through reductions in assets during fiscal 2007 through fiscal 2009. The generation of cash flow, together with debt repurchases and exchanges at prices below par, allowed us to reduce debt (notes payable, excluding accrued interest) during fiscal 2009 by approximately \$754 million. Since the latter half of fiscal 2009, we have seen more opportunities to purchase land at prices that make economic sense given the then-current home sales prices and sales paces. As such, since that time, despite acquiring new land at higher levels than in the previous few years, we have been able to further reduce our debt by approximately \$222 million.

Our homebuilding cash balance at October 31, 2013 increased by \$60.8 million from October 31, 2012. The significant uses of cash during fiscal 2013 were primarily due to spending \$503.0 million on land and land development. The remaining change in cash came from normal operations, as well a \$31.4 million reduction of homebuilding restricted cash. Most of this restricted cash became unrestricted as the letters of credit the cash collateralized were released during fiscal 2013.

Our cash uses during fiscal 2013 and 2012 were for operating expenses, land purchases, land deposits, land development, construction spending, financing transactions, debt payments and repurchases, state income taxes, interest payments and investments in joint ventures. During these periods, we provided for our cash requirements from available cash on hand, financing transactions, debt and equity issuances, housing and land sales, model sale leasebacks, land banking deals, financial service revenues and other revenues. We believe that these sources of cash will be sufficient through fiscal 2014 to finance our working capital requirements and other needs. In June 2013, we enhanced our liquidity by entering into a \$75 million unsecured revolving credit facility, discussed below.

Our net income (loss) historically does not approximate cash flow from operating activities. The difference between net income (loss) and cash flow from operating activities is primarily caused by changes in inventory levels together with changes in receivables, prepaid and other assets, mortgage loans held for sale, interest and other accrued liabilities, deferred income taxes, accounts payable and other liabilities, and noncash charges relating to depreciation, amortization of computer software costs, stock compensation awards and impairment losses for inventory. When we are expanding our operations, inventory levels, prepaids, and other assets increase causing cash flow from operating activities to decrease. Certain liabilities also increase as operations expand and partially offset the negative effect on cash flow from operations caused by the increase in inventory levels, prepaids and other assets. Similarly, as our mortgage operations expand, net income from these operations increases, but for cash flow purposes net income is offset by the net change in mortgage assets and liabilities. The opposite is true as our investment in new land purchases and development of new communities decrease, which is what happened during the last half of fiscal 2007 through fiscal 2009, allowing us to generate positive cash flow from operations during this period. Since the latter part of fiscal 2009 cumulative through the first three quarters of fiscal 2013, as a result of the new land purchases and land development we have used cash in operations as we add new communities. In the fourth quarter of fiscal 2013, we generated a positive cash flow from operations, which was the result of a high volume of home deliveries. Looking forward, given the unstable housing market, it will continue to be difficult to generate positive cash flow from operations until we return to sustained profitability. However, we will continue to make adjustments to our structure and our business plans in order to maximize our liquidity while also taking steps to return to sustained profitability, including through land acquisitions.

On July 3, 2001, our Board of Directors authorized a stock repurchase program to purchase up to 4 million shares of Class A Common Stock. We did not repurchase any shares under this program during fiscal 2013 or 2011. During fiscal 2012, we repurchased 0.1 million shares under this program. As of October 31, 2013, the maximum number of shares of Class A Common Stock that may yet be purchased under this program is 0.5 million. (See Part II, Item 5 for information on equity purchases).

On July 12, 2005, we issued 5,600 shares of 7.625% Series A Preferred Stock, with a liquidation preference of \$25,000 per share. Dividends on the Series A Preferred Stock are not cumulative and are payable at an annual rate of 7.625%. The Series A Preferred Stock is not convertible into the Company's common stock and is redeemable in whole or in part at our option at the liquidation preference of the shares. The Series A Preferred Stock is traded as depositary shares, with each depositary share representing 1/1000th of a share of Series A Preferred Stock. The depositary shares are listed on the NASDAQ Global Market under the symbol "HOVNP". In fiscal 2013, 2012, and 2011, we did not make any dividend payments on the Series A Preferred Stock as a result of covenant restrictions in our debt instruments. We anticipate that we will continue to be restricted from paying dividends, which are not cumulative, for the foreseeable future.

On October 20, 2009, K. Hovnanian Enterprises, Inc. ("K. Hovnanian") issued \$785.0 million (\$770.9 million net of discount) of 10.625% Senior Secured Notes due October 15, 2016. The notes were secured, subject to permitted liens and other exceptions, by a first-priority lien on substantially all of the assets owned by us, K. Hovnanian and the guarantors. The net proceeds from this issuance, together with cash on hand, were used to fund certain cash tender offers for our then outstanding 11.5% Senior Secured Notes due 2013 and 18.0% Senior Secured Notes due 2017 and certain series of our unsecured notes. In May 2011, we issued \$12.0 million of additional 10.625% Senior Secured Notes as discussed below. The 10.625% Senior Secured Notes due 2016 were the subject of a tender offer in October 2012, and the notes that were not tendered in the tender offer were redeemed, as discussed below.

On February 9, 2011, we issued 13,512,500 shares of our Class A Common Stock, including 1,762,500 shares issued pursuant to the over-allotment option granted to the underwriters, at a price of \$4.30 per share.

On February 9, 2011, we issued an aggregate of 3,000,000 7.25% Tangible Equity Units (the "TEUs"), and on February 14, 2011, we issued an additional 450,000 TEUs pursuant to the over-allotment option granted to the underwriters. Each TEU initially consists of (i) a prepaid stock purchase contract (each a "Purchase Contract") and (ii) a senior subordinated amortizing note due February 15, 2014 (each, a "Senior Subordinated Amortizing Note"). As of October 31, 2013 and 2012, we had an aggregate principal amount of \$2.2 million and \$6.1 million, respectively, of Senior Subordinated Amortizing Notes outstanding. On each February 15, May 15, August 15 and November 15, K. Hovnanian will pay holders of Senior Subordinated Amortizing Notes equal quarterly cash installments of \$0.453125 per Senior Subordinated Amortizing Note, which cash payments in the aggregate will be equivalent to 7.25% per year with respect to each \$25 stated amount of TEUs. Each installment constitutes a payment of interest (at a rate of 12.072% per annum) and a partial repayment of principal on the Senior Subordinated Amortizing Notes, allocated as set forth in the amortization schedule provided in the indenture under which the Senior Subordinated Amortizing Notes were issued. The Senior Subordinated Amortizing Notes have a scheduled final installment payment date of February 15, 2014. If we elect to settle the Purchase Contracts early, holders of the Senior Subordinated Amortizing Notes will have the right to require K. Hovnanian to repurchase such holders' Senior Subordinated Amortizing Notes, except in certain circumstances as described in the indenture governing Senior Subordinated Amortizing Notes.

Unless settled earlier, on February 15, 2014 (subject to postponement under certain circumstances), each Purchase Contract will automatically settle and we will deliver a number of shares of Class A Common Stock based on the

applicable market value, as defined in the purchase contract agreement, which will be between 4.7655 shares and 5.8140 shares per Purchase Contract (subject to adjustment). Each TEU may be separated into its constituent Purchase Contract and Senior Subordinated Amortizing Note after the initial issuance date of the TEUs, and the separate components may be combined to create a TEU. The Senior Subordinated Amortizing Note component of the TEUs is recorded as debt, and the Purchase Contract component of the TEUs is recorded in equity as additional paid in capital. We have recorded \$68.1 million, the initial fair value of the Purchase Contracts, as additional paid in capital. As of October 31, 2013, 2.2 million Purchase Contracts have been converted into 10.4 million shares of our Class A Common Stock.

During the second quarter of fiscal 2012, we exchanged pursuant to agreements with bondholders approximately \$3.1 million aggregate principal amount of our Senior Subordinated Amortizing Notes for shares of our Class A Common Stock, as discussed in Note 10 to the Consolidated Financial Statements. These transactions resulted in a gain on extinguishment of debt of \$0.2 million for the year ended October 31, 2012. The gain is included in the Consolidated Statement of Operations as "Gain on extinguishment of debt."

On February 14, 2011, K. Hovnanian issued \$155.0 million aggregate principal amount of 11.875% Senior Notes due 2015. These notes were the subject of a November 2011 exchange offer discussed below. The net proceeds from the issuances of the 11.875% Senior Notes due 2015, Class A Common Stock described above, and Units were approximately \$286.2 million, a portion of which were used to fund the purchase through tender offers, on February 14, 2011, of the following series of K. Hovnanian's then outstanding senior and senior subordinated notes: approximately \$24.6 million aggregate principal amount of 8.0% Senior Notes due 2012, \$44.1 million aggregate principal amount of 8.875% Senior Subordinated Notes due 2012 and \$29.2 million aggregate principal amount of 7.75% Senior Subordinated Notes due 2013 (the "2013 Notes" and, together with the 2012 Senior Notes and the 2012 Senior Subordinated Notes, the "Tender Offer Notes"). On February 14, 2011, K. Hovnanian called for redemption on March 15, 2011 all Tender Offer Notes that were not tendered in the tender offers for an aggregate redemption price of approximately \$60.1 million. Such redemptions were funded with proceeds from the offerings of the Class A Common Stock, the TEUs and the 11.875% Senior Notes due 2015.

On May 4, 2011, K. Hovnanian issued an aggregate principal amount of \$12.0 million of additional 10.625% Senior Secured Notes due 2016 resulting in net proceeds of approximately \$11.6 million. On June 3, 2011, we used these net proceeds together with cash on hand, to fund the redemption of the remaining outstanding principal amount (\$0.5 million) of our 11.5% Senior Secured Notes due 2013 and the remaining outstanding principal amount (\$11.7 million) of our 18.0% Senior Secured Notes due 2017. These transactions, along with the tender offers and redemptions in February 2011 and March 2011 discussed above, resulted in a loss of \$3.1 million during the year ended October 31, 2011. The losses from the transactions are included in the Consolidated Statements of Operations as “(Loss) gain on extinguishment of debt.”

On November 1, 2011, we issued \$141.8 million aggregate principal amount of 5.0% Senior Secured Notes due 2021 (the “5.0% 2021 Notes”) and \$53.2 million aggregate principal amount of 2.0% Senior Secured Notes due 2021 (the “2.0% 2021 Notes”, and together with the 5.0% 2021 Notes the “2021 Notes”) in exchange for \$195.0 million of certain of our unsecured senior notes with maturities ranging from 2014 through 2017. Holders of the senior notes due 2014 and 2015 that were exchanged in the exchange offer also received an aggregate of approximately \$14.2 million in cash payments and all holders of senior notes that were exchanged in the exchange offer received accrued and unpaid interest (in the aggregate amount of approximately \$3.3 million). Costs associated with this transaction were \$4.7 million. The 5.0% 2021 Notes and the 2.0% 2021 Notes were issued as separate series under an indenture, but have substantially the same terms other than with respect to interest rate and related redemption provisions, and vote together as a single class. Due to the then-existing financial condition of K. Hovnanian as determined in accordance with ASC 470-60, “Accounting by Debtors and Creditors for Troubled Debt Restructurings” and because the holders of the senior notes that exchanged such notes for 2021 Notes granted K. Hovnanian a concession in the form of extended maturities and reduced interest rates, the accounting for the debt exchange was treated as a troubled debt restructuring. Under this accounting, the Company did not recognize any gain or loss on extinguishment of debt and the costs associated with the debt exchange were expensed as incurred as shown in “Other operations” in the Consolidated Statement of Operations. See Note 9 to the consolidated financial statements for further discussion.

The guarantees by K. Hovnanian JV Holdings, L.L.C. and its subsidiaries, except for certain joint ventures and joint venture holding companies (collectively, the “Secured Group”) with respect to the 2021 Notes are secured, subject to permitted liens and other exceptions, by a first-priority lien on substantially all of the assets of the members of the Secured Group. As of October 31, 2013, the collateral securing the guarantees included (1) \$72.9 million of cash and cash equivalents (subsequent to such date, cash uses include general business operations and real estate and other investments); (2) approximately \$74.4 million aggregate book value of real property of the Secured Group, which does not include the impact of inventory investments, home deliveries, or impairments thereafter and which may differ from the value if it were appraised, and (3) equity interests in guarantors that are members of the Secured Group. Members of the Secured Group also own equity in joint ventures, either directly or indirectly through ownership of joint venture holding companies, with a book value of \$44.1 million as of October 31, 2013; this equity is not pledged to secure, and is not collateral for, the 2021 Notes. Members of the Secured Group are “unrestricted subsidiaries” under K. Hovnanian's other senior notes, senior secured notes and senior subordinated amortizing notes, and thus have not guaranteed such indebtedness.

On October 2, 2012, K. Hovnanian issued \$577.0 million aggregate principal amount of 7.25% senior secured first lien notes due 2020 (the “First Lien Notes”) and \$220.0 million aggregate principal amount of 9.125% senior secured

second lien notes due 2020 (the "Second Lien Notes" and, together with the First Lien Notes, the "2020 Secured Notes") in a private placement (the "2020 Secured Notes Offering"). The net proceeds from the 2020 Secured Notes Offering, together with the net proceeds of the Units offering discussed below, and cash on hand, were used to fund the tender offer and consent solicitation with respect to the Company's then-outstanding 10.625% Senior Secured Notes due 2016 and the redemption of the remaining notes that were not purchased in the tender offer as described below.

The First Lien Notes are secured by a first-priority lien and the Second Lien Notes are secured by a second-priority lien, in each case, subject to permitted liens and other exceptions, on substantially all the assets owned by us, K. Hovnanian and the guarantors of such notes. At October 31, 2013, the aggregate book value of the real property that constituted collateral securing the 2020 Secured Notes was approximately \$526.0 million, which does not include the impact of inventory investments, home deliveries, or impairments thereafter and which may differ from the value if it were appraised. In addition, cash collateral that secured the 2020 Secured Notes was \$251.5 million as of October 31, 2013, which included \$5.2 million of restricted cash collateralizing certain letters of credit. Subsequent to such date, cash uses include general business operations and real estate and other investments.

The First Lien Notes are redeemable in whole or in part, at our option at any time prior to October 15, 2015 at 100% of the principal amount plus an applicable "Make-Whole Amount." We may also redeem some or all of the First Lien Notes at 105.438% of principal commencing October 15, 2015, at 103.625% of principal commencing October 15, 2016, at 101.813% of principal commencing October 15, 2017 and 100% of principal commencing October 15, 2018. In addition, we may redeem up to 35% of the aggregate principal amount of the First Lien Notes prior to October 15, 2015 with the net cash proceeds from certain equity offerings at 107.25% of principal.

The Second Lien Notes are redeemable in whole, or in part, at our option at any time prior to November 15, 2015 at 100% of the principal amount plus an applicable “Make-Whole Amount.” We may also redeem some or all of the Second Lien Notes at 106.844% of principal commencing November 15, 2015, at 104.563% of principal commencing November 15, 2016, at 102.281% of principal commencing November 15, 2017 and 100% of principal commencing November 15, 2018. In addition, we may redeem up to 35% of the aggregate principal amount of the Second Lien Notes prior to November 15, 2015 with the net cash proceeds from certain equity offerings at 109.125% of principal.

Also on October 2, 2012, the Company and K. Hovnanian issued \$100,000,000 aggregate stated amount of 6.0% Exchangeable Note Units (the “Units”) (equivalent to 100,000 Units). Each \$1,000 stated amount of Units initially consists of (1) a zero coupon Senior Exchangeable note due December 1, 2017 (a “Senior Exchangeable Note”) issued by K. Hovnanian, which bears no cash interest and has an initial principal amount of \$768.51 per Senior Exchangeable Note, and that will accrete to \$1,000 at maturity and (2) a Senior Amortizing note due December 1, 2017 (a “Senior Amortizing Note”) issued by K. Hovnanian, which has an initial principal amount of \$231.49 per Senior Amortizing Note, bears interest at a rate of 11.0% per annum, and has a final installment payment date on December 1, 2017. Each Unit may be separated into its constituent Senior Exchangeable Note and Senior Amortizing Note after the initial issuance date of the Units, and the separate components may be combined to create a Unit.

Each Senior Exchangeable Note had an initial principal amount of \$768.51 (which will accrete to \$1,000 over the term of the Exchangeable Note at an annual rate of 5.17% from the date of issuance, calculated on a semi-annual bond equivalent yield basis). Holders may exchange their Senior Exchangeable Notes at their option at any time prior to 5p.m., New York City time, on the business day immediately preceding December 1, 2017. Each Senior Exchangeable Note will be exchangeable for shares of Class A Common Stock at an initial exchange rate of 185.5288 shares of Class A Common Stock per Senior Exchangeable Note (equivalent to an initial exchange price, based on \$1,000 principal amount at maturity, of approximately \$5.39 per share of Class A Common Stock). The exchange rate will be subject to adjustment in certain events. If certain corporate events occur prior to the maturity date, the Company will increase the applicable exchange rate for any holder who elects to exchange its Senior Exchangeable Notes in connection with such corporate event. In addition, holders of Senior Exchangeable Notes will also have the right to require K. Hovnanian to repurchase such holders’ Senior Exchangeable Notes upon the occurrence of certain of these corporate events. As of October 31, 2013, 18,305 Senior Exchangeable Notes have been converted into 3.4 million shares of our Class A Common Stock, all of which were converted during the first quarter of fiscal 2013.

On each June 1 and December 1 (each, an “installment payment date”) K. Hovnanian will pay holders of Senior Amortizing Notes equal semi-annual cash installments of \$30.00 per Senior Amortizing Note (except for the June 1, 2013 installment payment, which was \$39.83 per Senior Amortizing Note), which cash payment in the aggregate will be equivalent to 6.0% per year with respect to each \$1,000 stated amount of Units. Each installment will constitute a payment of interest (at a rate of 11.0% per annum) and a partial repayment of principal on the Senior Amortizing Note. Following certain corporate events that occur prior to the maturity date, holders of the Senior Amortizing Notes will have the right to require K. Hovnanian to repurchase such holders’ Senior Amortizing Notes.

The net proceeds of the Units offering, along with the net proceeds from the 2020 Secured Notes Offering previously discussed, and cash on hand, were used to fund the tender offer and consent solicitation with respect to the Company's then outstanding 10.625% Senior Secured Notes due 2016 and redemption of the remaining notes that were not purchased in the tender offer as described below.

On October 2, 2012, pursuant to a cash tender offer and consent solicitation, we purchased in a fixed-price tender offer approximately \$637.2 million aggregate principal amount of 10.625% Senior Secured Notes due 2016 for approximately \$691.3 million, plus accrued and unpaid interest. Subsequently, all 10.625% Senior Secured Notes due 2016 that were not tendered in the tender offer (approximately \$159.8 million) were redeemed for an aggregate redemption price of approximately \$181.8 million. The tender offer and redemption resulted in a loss on extinguishment of debt of \$87.0 million, including the write-off of unamortized discounts and fees. The loss is included in the Consolidated Statement of Operations as "(Loss) gain on extinguishment of debt."

During the year ended October 31, 2012, we repurchased for cash in the open market and privately negotiated transactions \$21.0 million principal amount of our 6.25% Senior Notes due 2016, \$61.1 million principal amount of our 7.5% Senior Notes due 2016, \$37.4 million principal amount of our 8.625% Senior Notes due 2017, and \$2.0 million principal amount of our 11.875% Senior Notes due 2015. The aggregate purchase price for these repurchases was \$72.2 million, plus accrued and unpaid interest. These repurchases resulted in a gain on extinguishment of debt of \$48.4 million for the year ended October 31, 2012, net of the write-off of unamortized discounts and fees. The gain is included in the consolidated statement of operations as "(Loss) gain on extinguishment of debt." Certain of these repurchases were funded with the proceeds from our April 11, 2012 issuance of 25,000,000 shares of our Class A Common Stock (see Note 15 to the Consolidated Financial Statements).

In addition, during the year ended October 31, 2012, pursuant to agreements with bondholders we exchanged \$7.8 million principal amount of our 6.25% Senior Notes due 2016, \$4.0 million principal amount of our 7.5% Senior Notes due 2016 and \$18.3 million of our outstanding 8.625% Senior Notes due 2017 for shares of our Class A Common Stock, as discussed in Notes 9 and 15 to the Consolidated Financial Statements. These transactions were treated as a substantial modification of debt, resulting in a gain on extinguishment of debt of \$9.3 million for the year ended October 31, 2012. The gain is included in the Consolidated Statement of Operations as “(Loss) gain on extinguishment of debt.”

On September 16, 2013, K. Hovnanian issued an aggregate principal amount of \$41.6 million of its 6.25% Senior Notes due 2016. The Notes were issued as additional 6.25% Senior Notes due 2016 under the indenture dated as of August 8, 2005. The net proceeds from this offering were used to fund the redemption on October 15, 2013 of all of K. Hovnanian’s outstanding 6.5% Senior Notes due 2014 and 6.375% Senior Notes due 2014 and to pay related fees and expenses.

As of October 31, 2013, we had \$992.0 million of outstanding senior secured notes (\$978.6 million, net of discount), comprised of \$577.0 million 7.25% Senior Secured First Lien Notes due 2020 (the “First Lien Notes”), \$220.0 million 9.125% Senior Secured Second Lien Notes due 2020 (the “Second Lien Notes” and, together with the First Lien Notes, the “2020 Secured Notes”), \$53.2 million 2.0% Senior Secured Notes due 2021 (the “2.0% 2021 Notes”) and \$141.8 million 5.0% Senior Secured Notes due 2021 (the “5.0% 2021 Notes” and together with the 2.0% 2021 Notes, the “2021 Notes”). As of October 31, 2013, we also had \$462.6 million of outstanding senior notes (\$461.2 million, net of discount), comprised of \$21.4 million 6.25% Senior Notes due 2015, \$172.7 million 6.25% Senior Notes due 2016, \$86.5 million 7.5% Senior Notes due 2016, \$121.0 million 8.625% Senior Notes due 2017 and \$60.8 million 11.875% Senior Notes due 2015. In addition, as of October 31, 2013, we had outstanding \$20.9 million 11.0% Senior Amortizing Notes due 2017 (issued as a component of our 6.0% Exchangeable Note Units), \$66.6 million Senior Exchangeable Notes due 2017 (issued as a component of our 6.0% Exchangeable Note Units) and \$2.2 million 7.25% Senior Subordinated Amortizing Notes (issued as a component of our 7.25% Tangible Equity Units). Except for K. Hovnanian, the issuer of the notes, our home mortgage subsidiaries, joint ventures and subsidiaries holding interests in our joint ventures, certain of our title insurance subsidiaries and our foreign subsidiary, we and each of our subsidiaries are guarantors of the senior secured, senior, senior amortizing, senior exchangeable and senior subordinated amortizing notes outstanding at October 31, 2013 (see Note 23 to the Consolidated Financial Statements). In addition, the 2021 Notes are guaranteed by the Secured Group. Members of the Secured Group do not guarantee K. Hovnanian's other indebtedness.

The indentures governing the notes do not contain any financial maintenance covenants, but do contain restrictive covenants that limit, among other things, the Company’s ability and that of certain of its subsidiaries, including K. Hovnanian, to incur additional indebtedness (other than certain permitted indebtedness, refinancing indebtedness and non-recourse indebtedness), pay dividends and make distributions on common and preferred stock, repurchase subordinated indebtedness with (respect to certain of the senior secured notes), make other restricted payments, make investments, sell certain assets, incur liens, consolidate, merge, sell or otherwise dispose of all or substantially all assets and enter into certain transactions with affiliates. The indentures also contain events of default which would permit the holders of the notes to declare the notes to be immediately due and payable if not cured within applicable grace periods, including the failure to make timely payments on the notes or other material indebtedness, the failure to

comply with agreements and covenants and specified events of bankruptcy, and insolvency and, with respect to the indentures governing the senior secured notes, the failure of the documents granting security for the senior secured notes to be in full force and effect and the failure of the liens on any material portion of the collateral securing the senior secured notes to be valid and perfected. As of October 31, 2013, we believe we were in compliance with the covenants of the indentures governing our outstanding notes.

Under the terms of the indentures, we have the right to make certain redemptions and, depending on market conditions and covenant restrictions, may do so from time to time. We also continue to evaluate our capital structure and may also continue to make debt purchases and/or exchanges for debt or equity from time to time through tender offers, open market purchases, private transactions, or otherwise, or seek to raise additional debt or equity capital, depending on market conditions and covenant restrictions.

If our consolidated fixed charge coverage ratio, as defined in the indentures governing our senior secured and senior notes (other than the senior exchangeable notes) is less than 2.0 to 1.0, we are restricted from making certain payments, including dividends, and from incurring indebtedness other than certain permitted indebtedness, refinancing indebtedness, and non-recourse indebtedness. As a result of this restriction, we are currently restricted from paying dividends, which are not cumulative, on our 7.625% Series A Preferred Stock. We anticipate we will continue to be restricted from paying dividends for the foreseeable future. Our inability to pay dividends is in accordance with covenant restrictions and will not result in a default under our debt instruments or otherwise affect compliance with any of the covenants contained in the debt instruments.

In June 2013, K. Hovnanian, as borrower, and we and certain of our subsidiaries, as guarantors, entered into a five-year \$75 million unsecured revolving credit facility (the "Credit Facility") with Citicorp USA, Inc., as administrative agent and issuing bank, and Citibank, N.A., as a lender. The Credit Facility is available for both letters of credit and general corporate purposes. The Credit Facility does not contain any financial maintenance covenants, but does contain certain restrictive covenants that track those contained in our indenture governing the First Lien Notes, which are described above. The Credit Facility also contains certain customary events of default which would permit the administrative agent at the request of the required lenders to, among other things, declare all loans then outstanding to be immediately due and payable if not cured within applicable grace periods, including the failure to make timely payments of amounts payable under the Credit Facility or other material indebtedness or the acceleration of other material indebtedness, the failure to comply with agreements and covenants or for representations or warranties to be correct in all material respects when made, specified events of bankruptcy and insolvency, and the entry of a material judgment against a loan party. Outstanding borrowings under the Credit Facility accrue interest at an annual rate equal to either, as selected by K. Hovnanian, (i) the alternate base rate plus the applicable spread determined on the date of such borrowing or (ii) an adjusted LIBOR rate plus the applicable spread determined as of the date two business days prior to the first day of the interest period for such borrowing. As of October 31, 2013, there were no borrowings and \$25.8 million of letters of credit outstanding under the Credit Facility and as of such date, we believe we were in compliance with the covenants under the Credit Facility.

In addition to the Credit Facility, we have certain stand alone cash collateralized letter of credit agreements and facilities under which there were a total of \$5.1 million and \$29.5 million of letters of credit outstanding as of October 31, 2013 and 2012, respectively. These agreements and facilities require us to maintain specified amounts of cash as collateral in segregated accounts to support the letters of credit issued thereunder, which will affect the amount of cash we have available for other uses. As of October 31, 2013 and 2012, the amount of cash collateral in these segregated accounts was \$5.2 million and \$30.7 million, respectively, which is reflected in "Restricted cash and cash equivalents" on the Consolidated Balance Sheets.

Our wholly owned mortgage banking subsidiary, K. Hovnanian American Mortgage, LLC ("K. Hovnanian Mortgage"), originates mortgage loans primarily from the sale of our homes. Such mortgage loans and related servicing rights are sold in the secondary mortgage market within a short period of time. In certain instances, we retain the servicing rights for a small amount of loans. Our secured Master Repurchase Agreement with JPMorgan Chase Bank, N.A. ("Chase Master Repurchase Agreement"), which was amended on June 28, 2013 to extend the maturity date to June 27, 2014, is a short-term borrowing facility that provides up to \$50.0 million through maturity. The loan is secured by the mortgages held for sale and is repaid when we sell the underlying mortgage loans to permanent investors. Interest is payable monthly on outstanding advances at an adjusted LIBOR rate, which was 0.168% at October 31, 2013, subject to a floor of 1%, plus the applicable margin of 2.5%. Therefore, at October 31, 2013, the interest rate was 3.5%. As of October 31, 2013, the aggregate principal amount of all borrowings outstanding under the Chase Master Repurchase Agreement was \$33.6 million.

K. Hovnanian Mortgage has another secured Master Repurchase Agreement with Customers Bank ("Customers Master Repurchase Agreement"), which was amended on May 28, 2013 to extend the maturity date to May 27, 2014, that is a short-term borrowing facility that provides up to \$37.5 million through maturity. The loan is secured by the mortgages held for sale and is repaid when we sell the underlying mortgage loans to permanent investors. Interest is payable

daily or as loans are sold to permanent investors on outstanding advances at the current LIBOR subject to a floor of 0.5% plus the applicable margin ranging from 3.0% to 5.5% based on the takeout investor and type of loan. As of October 31, 2013, the aggregate principal amount of all borrowings outstanding under the Customers Master Repurchase Agreement was \$30.7 million.

K. Hovnanian Mortgage has a third secured Master Repurchase Agreement with Credit Suisse First Boston Mortgage Capital LLC (“Credit Suisse Master Repurchase Agreement”), which was amended on January 2, 2013, that is a short-term borrowing facility that provides up to \$50.0 million through June 20, 2014. The loan is secured by the mortgages held for sale and is repaid when we sell the underlying mortgage loans to permanent investors. Interest is payable monthly on outstanding advances at the Credit Suisse Cost of Funds, which was 0.48% at October 31, 2013, plus the applicable margin ranging from 3.75% to 4.0% based on the takeout investor and type of loan. As of October 31, 2013, the aggregate principal amount of all borrowings outstanding under the Credit Suisse Master Repurchase Agreement was \$27.4 million.

The Chase Master Repurchase Agreement, Customers Master Repurchase Agreement and Credit Suisse Master Repurchase Agreement (together, the “Master Repurchase Agreements”) require K. Hovnanian Mortgage to satisfy and maintain specified financial ratios and other financial condition tests. Because of the extremely short period of time mortgages are held by K. Hovnanian Mortgage before the mortgages are sold to investors (generally a period of a few weeks), the immateriality to us on a consolidated basis of the size of the Master Repurchase Agreements, the levels required by these financial covenants, our ability based on our immediately available resources to contribute sufficient capital to cure any default, were such conditions to occur, and our right to cure any conditions of default based on the terms of the agreement, we do not consider any of these covenants to be substantive or material. As of October 31, 2013, we believe we were in compliance with the covenants under the Master Repurchase Agreements.

Total inventory, excluding consolidated inventory not owned, increased \$87.1 million during the year ended October 31, 2013. Total inventory, excluding consolidated inventory not owned, increased in the Mid-Atlantic by \$39.4 million, in the Midwest \$25.0 million, in the Southeast by \$12.6 million and in the Southwest by \$59.2 million. This increase was partially offset by decreases in the Northeast of \$46.4 million and in the West of \$2.7 million. The increases were primarily attributable to new land purchases and land development during fiscal 2013, offset by home deliveries. The decreases in the Northeast and West during fiscal 2013 were due to delivering homes at a faster pace than purchasing new land to replenish our inventory. During fiscal 2013, we incurred \$2.4 million in impairments, primarily in the Northeast. In addition, we wrote-off costs in the amount of \$2.6 million during fiscal 2013 related to land options that expired or that we terminated, as the communities' forecasted profitability was not projected to produce adequate returns on investment commensurate with the risk. In the last few years, we have been able to acquire new land parcels at prices that we believe will generate reasonable returns under current homebuilding market conditions. There can be no assurances that this trend will continue in the near term. Substantially all homes under construction or completed and included in inventory at October 31, 2013 are expected to be closed during the next 12 months.

The total inventory increase discussed above excluded the increase in consolidated inventory not owned of \$10.2 million. Consolidated inventory not owned consists of specific performance options and other options that were added to our balance sheet in accordance with accounting principles generally accepted in the United States. The increase from October 31, 2012 to October 31, 2013, was primarily due to sale and leaseback of certain model homes and land banking transactions during fiscal 2013. During fiscal 2012 and 2013, we sold and leased back certain of our model homes with the right to participate in the potential profit when each home is sold to a third party at the end of the respective lease. As a result of our continued involvement for accounting purposes in accordance with ASC 360-20-40-38, these sale and leaseback transactions are considered a financing rather than a sale for accounting purposes. Therefore, for purposes of our Consolidated Balance Sheet, at October 31, 2013, inventory of \$47.6 million was recorded to "Consolidated inventory not owned - other options", with a corresponding amount of \$45.7 million recorded to "Liabilities from inventory not owned". In addition, we entered into a land banking arrangement in fiscal 2012 with GSO Capital Partners LP ("GSO") that continued in fiscal 2013 whereby we sold a portfolio of our land parcels to GSO, and GSO provided us an option to purchase back finished lots on a quarterly basis. Because of our option to repurchase these parcels, for accounting purposes in accordance with ASC 360-20-40-38, this transaction is considered a financing rather than a sale. For purposes of our Consolidated Balance Sheet, at October 31, 2013, inventory of \$52.4 million was recorded to "Consolidated inventory not owned - other options", with a corresponding amount of \$41.4 million recorded to "Liabilities from inventory not owned" for the amount of net cash received from the transactions. From time to time we enter into option agreements that include specific performance requirements, whereby we are required to purchase a minimum number of lots. Because of our obligation to purchase these lots, for accounting purposes in accordance with ASC 360-20-40-38, we are required to record this inventory on our Consolidated Balance Sheets. As of October 31, 2013, we had \$0.8 million of specific performance options recorded on our Consolidated Balance Sheets to "Consolidated inventory not owned - specific performance options", with a corresponding amount recorded to "Liabilities from inventory not owned".

When possible, we option property for development prior to acquisition. By optioning property, we are only subject to the loss of the cost of the option and predevelopment costs if we choose not to exercise the option (other than with respect to specific performance options discussed above). As a result, our commitment for major land acquisitions is reduced. The costs associated with optioned properties are included in "Land and land options held for future development or sale inventory". Also included in "Land and land options held for future development or sale

inventory" are amounts associated with inventory in mothballed communities. We mothball (or stop development on) certain communities when we determine the current performance does not justify further investment at the time. That is, we believe we will generate higher returns if we decide against spending money to improve land today and save the raw land until such times as the markets improve or we determine to sell the property. As of October 31, 2013, we have mothballed land in 50 communities. The book value associated with these communities at October 31, 2013 was \$115.9 million, net of impairment charges recorded in prior periods of \$431.6 million. We continually review communities to determine if mothballing is appropriate. During fiscal 2013, we mothballed one community, re-activated three previously mothballed communities and sold one mothballed community. Our inventory representing "Land and land options held for future development or sale" at October 31, 2013, on the Consolidated Balance Sheets, increased by \$6.2 million compared to October 31, 2012. The increase was primarily due to the acquisition of new land in all segments during fiscal 2013, offset by the movement of certain of our communities from held for future development to sold and unsold homes and lots under development during the period, combined with land sales in the Northeast and Southwest.

Inventories held for sale, which are land parcels where we have decided not to build homes, represented \$2.7 million of our total inventories at October 31, 2013, and are reported at the lower of carrying amount or fair value less costs to sell. In determining fair value for land held for sale, management considers, among other things, prices for land in recent comparable sale transactions, market analysis studies, which include the estimated price a willing buyer would pay for the land (other than in a forced liquidation sale) and recent bona fide offers received from outside third parties.

The following tables summarize home sites included in our total residential real estate. The increase in total home sites available at October 31, 2013 compared to October 31, 2012 is attributable to signing new land option agreements and acquiring new land parcels, offset by terminating certain option agreements and delivering homes.

	Total	Contracted	Remaining
	Home	Not	Home
	Sites	Delivered	Sites
			Available
October 31, 2013:			
Northeast	4,768	220	4,548
Mid-Atlantic	5,598	271	5,327
Midwest	4,792	605	4,187
Southeast	3,835	308	3,527
Southwest	7,060	677	6,383
West	6,044	86	5,958
Consolidated total	32,097	2,167	29,930
Unconsolidated joint ventures	2,613	225	2,388
Total including unconsolidated joint ventures	34,710	2,392	32,318
Owned	16,326	1,645	14,681
Optioned	15,523	274	15,249
Construction to permanent financing lots	248	248	-
Consolidated total	32,097	2,167	29,930
Lots controlled by unconsolidated joint ventures	2,613	225	2,388
Total including unconsolidated joint ventures	34,710	2,392	32,318
October 31, 2012:			
Northeast	4,363	264	4,099
Mid-Atlantic	5,878	266	5,612
Midwest	3,204	427	2,777
Southeast	2,179	235	1,944
Southwest	5,753	506	5,247
West	6,642	191	6,451
Consolidated total	28,019	1,889	26,130
Unconsolidated joint ventures	1,774	256	1,518
Total including unconsolidated joint ventures	29,793	2,145	27,648
Owned	16,427	1,499	14,928
Optioned	11,418	216	11,202
Construction to permanent financing lots	174	174	-
Consolidated total	28,019	1,889	26,130
Lots controlled by unconsolidated joint ventures	1,774	256	1,518
Total including unconsolidated joint ventures	29,793	2,145	27,648

The following table summarizes our started or completed unsold homes and models, excluding unconsolidated joint ventures, in active and substantially completed communities. Started or completed unsold homes decreased in total, and on a per active selling community basis, from October 31, 2012 to October 31, 2013, primarily due to increased sales pace in many of our homebuilding markets. Model homes decreased in total from October 31, 2012 to October 31, 2013, primarily due to model homes that were sold to a third party in sales lease-back transactions during fiscal 2013.

	October 31, 2013			October 31, 2012		
	Unsold			Unsold		
	Homes	Models	Total	Homes	Models	Total
Northeast	95	14	109	116	9	125
Mid-Atlantic	78	9	87	65	7	72
Midwest	17	8	25	19	22	41
Southeast	57	9	66	55	10	65
Southwest	346	13	359	355	19	374
West	40	8	48	39	6	45
Total	633	61	694	649	73	722
Started or completed unsold homes and models per active selling communities(1)	3.3	0.3	3.6	3.8	0.4	4.2

Active selling communities (which are communities that are open for sale with 10 or more home sites available) (1) were 192 and 172 at October 31, 2013 and 2012, respectively. Ratio does not include substantially completed communities, which are communities with less than 10 home sites available.

Homebuilding restricted cash and cash equivalents decreased \$31.4 million to \$10.3 million at October 31, 2013 compared to October 31, 2012. The decrease was primarily related to the release of cash securitizing letters of credit as we transitioned from having letters of credit issued under our letter of credit agreements and facilities that required cash collateral to having letters of credit issued under our new Credit Facility that does not require any cash collateral. Also contributing to the decrease was a reduction in our surety bond escrow cash requirements during fiscal 2013.

Investments in and advances to unconsolidated joint ventures decreased \$9.6 million during the fiscal year ended October 31, 2013. The decrease was primarily due to reduced advances at October 31, 2013 as compared to October 31, 2012. Partially offsetting this decrease was an increase related to the investment in two new homebuilding joint ventures during fiscal 2013. As of October 31, 2013, we had investments in seven homebuilding joint ventures and one land development joint venture. We have no guarantees associated with our unconsolidated joint ventures, other than guarantees limited only to performance and completion of development, environmental indemnification and standard warranty and representation against fraud misrepresentation and similar actions, including a voluntary bankruptcy.

Receivables, deposits and notes decreased \$16.7 million from October 31, 2012 to \$45.1 million at October 31, 2013. The decrease was primarily due to a decrease in receivables for home closings as a result of cash in transit from various title companies at the end of the respective periods. In addition, although we received reimbursements from our insurance carriers for certain warranty claims, we also increased our allowance for doubtful accounts related to certain other of our insurance receivables and other note receivables.

Property, plant and equipment decreased \$2.3 million during the year ended October 31, 2013 primarily due to depreciation and a small amount of disposals, which were offset by minor additions for leasehold improvements during the period.

Prepaid expenses and other assets were as follows as of:

(In thousands)	October 31, 2013	October 31, 2012	Dollar Change
Prepaid insurance	\$3,213	\$1,729	\$1,484
Prepaid project costs	23,841	24,008	(167)
Net rental properties	1,975	5,430	(3,455)
Other prepaids	30,055	26,086	3,969
Other assets	267	9,441	(9,174)
Total	\$59,351	\$66,694	\$(7,343)

Prepaid insurance increased due to premium payments made on certain liability insurance policies during fiscal 2013. These costs are amortized over the life of the associated insurance policy, which can be one to three years. Prepaid project costs consist of community specific expenditures that are used over the life of the community. Such prepaids are expensed as homes are delivered. Net rental properties decreased primarily due to the sale of our last senior residential rental property during the second quarter of fiscal 2013. The remaining balance of net rental properties represents leasehold improvements for an office building that we fully sub-lease. Other prepaids increased primarily as a result of fees paid in connection with our new Credit Facility entered into during the third quarter of fiscal 2013, along with prepaid payroll taxes related to the timing of the Company's payroll at October 31, 2013. Other assets decreased mainly due to the sale of Company-owned life insurance policies to a third party during fiscal 2013 for approximately book value.

Financial Services - Mortgage loans held for sale consist primarily of residential mortgages receivable held for sale, of which \$109.7 million and \$115.0 million at October 31, 2013 and October 31, 2012, respectively, were being temporarily warehoused and are awaiting sale in the secondary mortgage market. The decrease in mortgage loans held for sale from October 31, 2012 was primarily related to the timing of loans closed during fourth quarter of fiscal 2013 compared to the fourth quarter of fiscal 2012.

Financial Services – Other assets decreased \$6.0 million to \$4.3 million at October 31, 2013 compared to October 31, 2012. The decrease is related to the closing of mortgages in the first quarter of fiscal 2013, which were funded in the fourth quarter of fiscal 2012, in anticipation of home closings on the last days of October 2012 that did not occur until early November, due to weather-related delays from Hurricane Sandy.

Nonrecourse mortgages were \$62.9 million at October 31, 2013 and \$38.3 million at October 31, 2012. The increase was primarily due to new mortgages for communities in the Northeast, the Mid-Atlantic, the Midwest, the Southwest and the West obtained during fiscal 2013, along with increased borrowings on certain of our existing non-recourse mortgages. Offsetting the increase was a decrease related to a property in the Mid-Atlantic, which we had previously acquired when our partner in a land development joint venture transferred its interest in the venture to us, that was foreclosed on in fiscal 2013. As a result, the non-recourse liability of \$9.5 million and corresponding inventory balance were taken off our balance sheet for the second quarter of fiscal 2013. Also offsetting the increase during the period were principal payments made on certain of our existing non-recourse mortgages.

Accounts payable and other liabilities are as follows as of:

(In thousands)	October 31, 2013	October 31, 2012	Dollar Change
Accounts payable	\$98,585	\$89,310	\$9,275

Reserves	136,029	129,025	7,004
Accrued expenses	26,454	29,969	(3,515)
Accrued compensation	39,704	26,625	13,079
Other liabilities	6,992	21,581	(14,589)
Total	\$307,764	\$296,510	\$11,254

The increase in accounts payable was primarily due to the higher volume of deliveries in the fourth quarter of fiscal 2013 compared to the fourth quarter of fiscal 2012, along with a change in the scheduled timing of certain of our monthly payments. Reserves increased during the period as new accruals for general liability insurance exceeded payments for warranty related claims. The decrease in accrued expenses is primarily due to decreases in property tax accruals and amortization of abandoned lease space accruals. The increase in accrued compensation is primarily due to increased bonus accruals as profitability increased in many of our markets, as well as for the consolidated Company, in fiscal 2013. Other liabilities decreased primarily due to installment payments made to a former joint venture partner for the buy-out of their share of the joint venture during fiscal 2012.

Customer deposits increased to \$30.1 million at October 31, 2013 from \$23.8 million at October 31, 2012. This increase is primarily attributable to the increase in backlog as of October 31, 2013.

Liabilities from inventory not owned increased \$10.1 million to \$87.9 million at October 31, 2013 from \$77.8 million at October 31, 2012. The increase is primarily due to the model home and land banking programs described above with the change in inventory not owned discussion.

Financial Services - Accounts payable and other liabilities decreased \$4.7 million to \$32.9 million at October 31, 2013. The decrease primarily related to the decrease in restricted cash in our title company during the period, due to a decrease in the volume and timing of home closings during the fourth quarter of fiscal 2013 compared to the fourth quarter of fiscal 2012.

Financial Services - Mortgage warehouse lines of credit decreased \$15.8 million from \$107.5 million at October 31, 2012, to \$91.7 million at October 31, 2013. The decrease correlates to the decrease in the volume of mortgage loans held for sale during the period, along with the decrease in financial services other assets, discussed above.

Accrued interest increased \$8.1 million to \$28.3 million at October 31, 2013 as compared to October 31, 2012. This increase is due to the timing of semi-annual interest payments on our bonds.

Income taxes payable of \$6.9 million at October 31, 2012 decreased \$3.6 million during the year ended October 31, 2013 to \$3.3 million primarily due to the release of reserves for a federal tax position that was settled with the Internal Revenue Service during the first quarter of fiscal 2013, offset by state tax expense.

Results of Operations

Total Revenues

Compared to the prior period, revenues increased (decreased) as follows:

(Dollars in thousands)	Year Ended		
	October 31, 2013	October 31, 2012	October 31, 2011
Homebuilding:			
Sale of homes	\$378,747	\$333,106	\$(255,025)
Land sales	(14,077)	5,043	19,925
Other revenues	(7,762)	3,043	657
Financial services	8,992	9,254	(2,492)
Total change	\$365,900	\$350,446	\$(236,935)
Total revenues percent change	24.6 %	30.9 %	(17.3)%

Homebuilding

Sale of homes revenues increased \$378.7 million, or 26.9%, for the year ended October 31, 2013, increased \$333.1 million, or 31.1%, for the year ended October 31, 2012 and decreased \$255.0 million, or 19.2%, for the year ended October 31, 2011. The increased revenues in fiscal 2013 were primarily due to the number of home deliveries increasing 12.6% and the average price per home increasing to \$338,839 from \$300,595 in fiscal 2012. The increased revenues in fiscal 2012 were primarily due to the number of home deliveries increasing 22.0% and the average price per home increasing to \$300,595 from \$279,873 in 2011. The decreased revenues in fiscal 2011 were primarily due to the number of home deliveries declining 19.0% and the decrease in average price per home. The fluctuations in

average prices were a result of the geographic and community mix of our deliveries, as well as price increases in certain of our individual communities. During fiscal 2013 and 2012, we were able to raise prices in a number of our communities. For information on land sales, see the section titled “Land Sales and Other Revenues” below.

Information on homes delivered by segment is set forth below:

(Housing Revenue in thousands)	Year Ended		
	October 31, 2013	October 31, 2012	October 31, 2011
Northeast:			
Housing revenues	\$279,695	\$218,396	\$179,866
Homes delivered	617	505	399
Average price	\$453,314	\$432,467	\$450,792
Mid-Atlantic:			
Housing revenues	\$288,323	\$268,880	\$199,061
Homes delivered	623	649	524
Average price	\$462,798	\$414,299	\$379,887
Midwest:			
Housing revenues	\$162,758	\$106,539	\$70,465
Homes delivered	657	477	360
Average price	\$247,730	\$223,352	\$195,736
Southeast:			
Housing revenues	\$146,264	\$113,347	\$79,146
Homes delivered	535	482	339
Average price	\$273,391	\$235,160	\$233,469
Southwest:			
Housing revenues	\$684,258	\$515,757	\$418,631
Homes delivered	2,331	2,003	1,726
Average price	\$293,547	\$257,492	\$242,544
West:			
Housing revenues	\$223,029	\$182,661	\$125,305
Homes delivered	503	560	484
Average price	\$443,398	\$326,180	\$258,895
Consolidated total:			
Housing revenues	\$1,784,327	\$1,405,580	\$1,072,474
Homes delivered	5,266	4,676	3,832
Average price	\$338,839	\$300,595	\$279,873
Unconsolidated joint ventures:			
Housing revenues	\$306,174	\$320,657	\$172,343
Homes delivered	664	680	384
Average price	\$461,105	\$471,554	\$448,810
Total including unconsolidated joint ventures:			
Housing revenues	\$2,090,501	\$1,726,237	\$1,244,817
Homes delivered	5,930	5,356	4,216
Average price	\$352,530	\$322,300	\$295,260

The increase in housing revenues and deliveries during year ended October 31, 2013, as compared to year ended October 31, 2012, was primarily attributed to market improvements demonstrated by an increase in sales pace per community from 28.1 to 30.7 for fiscal 2012 and 2013, respectively. Housing revenues and average sales prices in

2013 increased in all of our homebuilding segments combined by 26.9% and 12.7%, respectively. In our homebuilding segments, homes delivered increased in fiscal 2013 as compared to fiscal 2012 by 22.2%, 37.7%, 11.0%, and 16.4%, in the Northeast, Midwest, Southeast, and Southwest, respectively, and decreased by 4.0% and 10.2% in the Mid-Atlantic and West, respectively.

The increase in housing revenues and deliveries during the year ended October 31, 2012, as compared to year ended October 31, 2011, was primarily attributed to market improvements demonstrated by an increase in sales pace per community from 21.3 to 28.1 for fiscal 2011 and 2012, respectively. Housing revenues and average sales prices in 2012 increased in all of our homebuilding segments combined by 31.1% and 7.4%, respectively. In our homebuilding segments, homes delivered increased in fiscal 2012 as compared to fiscal 2011 by 26.6%, 23.9%, 32.5%, 42.2%, 16.0% and 15.7% in the Northeast, Mid-Atlantic, Midwest, Southeast, Southwest and West, respectively.

Quarterly housing revenues and net sales contracts by segment, excluding unconsolidated joint ventures, for the years ending October 31, 2013, 2012 and 2011 are set forth below:

(In thousands)	Quarter Ended			
	October 31, 2013	July 31, 2013	April 30, 2013	January 31, 2013
Housing revenues:				
Northeast	\$105,914	\$66,447	\$53,099	\$54,234
Mid-Atlantic	89,048	89,123	57,706	52,447
Midwest	53,313	37,918	39,356	32,172
Southeast	45,276	35,265	37,119	28,605
Southwest	220,948	181,593	160,988	120,728
West	63,595	52,030	61,308	46,095
Consolidated total	\$578,094	\$462,376	\$409,576	\$334,281
Sales contracts (net of cancellations):				
Northeast	\$68,499	\$69,118	\$86,311	\$45,356
Mid-Atlantic	71,797	79,104	89,896	69,922
Midwest	59,808	57,066	60,898	39,988
Southeast	42,901	54,581	51,479	33,263
Southwest	149,594	195,403	235,517	159,269
West	50,747	39,322	55,461	49,148
Consolidated total	\$443,346	\$494,594	\$579,562	\$396,946

(In thousands)	Quarter Ended			
	October 31, 2012	July 31, 2012	April 30, 2012	January 31, 2012
Housing revenues:				
Northeast	\$71,675	\$63,811	\$49,834	\$33,077
Mid-Atlantic	76,259	75,075	64,432	53,113
Midwest	36,579	28,213	23,590	18,157
Southeast	47,328	24,432	21,462	20,125
Southwest	170,913	139,407	114,284	91,153
West	66,521	40,543	38,892	36,705
Consolidated total	\$469,275	\$371,481	\$312,494	\$252,330
Sales contracts (net of cancellations):				
Northeast	\$68,779	\$54,575	\$54,887	\$28,198
Mid-Atlantic	63,208	55,399	82,121	49,622
Midwest	40,446	43,100	45,431	28,408
Southeast	43,624	38,562	39,305	24,471
Southwest	153,700	166,120	166,529	103,860
West	71,108	65,640	61,670	30,206
Consolidated total	\$440,865	\$423,396	\$449,943	\$264,765

(In thousands)	Quarter Ended			
	October 31, 2011	July 31, 2011	April 30, 2011	January 31, 2011
Housing revenues:				
Northeast	\$57,014	\$43,443	\$36,126	\$43,284
Mid-Atlantic	49,050	57,104	46,643	46,263
Midwest	21,249	17,716	17,466	14,034
Southeast	29,064	17,894	16,684	15,504
Southwest	126,204	107,861	97,339	87,227
West	30,555	32,461	32,716	29,573
Consolidated total	\$313,136	\$276,479	\$246,974	\$235,885
Sales contracts (net of cancellations):				
Northeast	\$40,014	\$56,427	\$57,394	\$37,435
Mid-Atlantic	56,269	73,986	55,874	52,013
Midwest	20,863	21,273	20,521	12,331
Southeast	20,775	28,301	23,345	15,640
Southwest	101,549	113,370	104,010	85,787
West	38,953	38,950	32,423	22,282
Consolidated total	\$278,423	\$332,307	\$293,567	\$225,488

Contracts per average active selling community in fiscal 2013 were 30.7 compared to fiscal 2012 of 28.1. Our reported level of sales contracts (net of cancellations) has been impacted by the increase in the pace of sales in all of the Company's segments, due to improved market conditions and lower interest rates on mortgages during fiscal 2013. Cancellation rates represent the number of cancelled contracts in the quarter divided by the number of gross sales contracts executed in the quarter. For comparison, the following are historical cancellation rates, excluding unconsolidated joint ventures.

Quarter	2013	2012	2011	2010	2009
First	16 %	21 %	22 %	21 %	31 %
Second	15 %	16 %	20 %	17 %	24 %
Third	17 %	20 %	18 %	23 %	23 %
Fourth	23 %	23 %	21 %	24 %	24 %

Another common and meaningful way to analyze our cancellation trends is to compare the number of contract cancellations as a percentage of the beginning backlog. The following table provides this historical comparison, excluding unconsolidated joint ventures.

Quarter	2013	2012	2011	2010	2009
First	12 %	18 %	18 %	13 %	22 %
Second	15 %	21 %	22 %	17 %	31 %
Third	12 %	18 %	20 %	15 %	23 %
Fourth	14 %	18 %	18 %	25 %	20 %

Historically, most cancellations occur within the legal rescission period, which varies by state but is generally less than two weeks after the signing of the contract. Cancellations also occur as a result of a buyer's failure to qualify for a mortgage, which generally occurs during the first few weeks after signing. However, beginning in fiscal 2007 and continuing through fiscal 2009, we started experiencing higher than normal numbers of cancellations later in the construction process. These cancellations were related primarily to falling prices, sometimes due to new discounts offered by us and other builders, leading the buyer to lose confidence in their contract price and due to tighter mortgage underwriting criteria leading to some customers' inability to be approved for a mortgage loan. In some cases, the buyer will walk away from a significant nonrefundable deposit that we recognize as other revenues. Our cancellations as a percentage of beginning backlog for fiscal 2013 were lower than what we believe to be normalized levels for the fourth quarter of 2013. Our cancellation rate based on gross sales contracts for fiscal 2013 was more typical of what we believe to be more normalized levels, except for the fourth quarter of fiscal 2013, which increased in conjunction with the slowdown in sales during August and September 2013. However, in October and November 2013, sales returned to prior year levels. It is difficult to predict what cancellation rates will be in the future.

An important indicator of our future results is recently signed contracts and our home contract backlog for future deliveries. Our consolidated contract backlog, excluding unconsolidated joint ventures, by segment is set forth below:

(Dollars In thousands)	October 31, 2013	October 31, 2012	October 31, 2011
Northeast:			
Total contract backlog	\$105,006	\$115,416	\$108,645
Number of homes	220	264	265
Mid-Atlantic:			
Total contract backlog	\$141,168	\$118,773	\$137,303
Number of homes	271	266	325
Midwest:			
Total contract backlog	\$150,716	\$95,716	\$44,870
Number of homes	605	427	226
Southeast:			
Total contract backlog	\$98,656	\$62,696	\$30,080
Number of homes	308	235	124
Southwest:			
Total contract backlog	\$216,367	\$160,840	\$86,388
Number of homes	677	506	331
West:			
Total contract backlog	\$50,526	\$78,877	\$32,914
Number of homes	86	191	116
Totals:			
Total consolidated contract backlog	\$762,439	\$632,318	\$440,200
Number of homes	2,167	1,889	1,387

Our net contracts for the full years of fiscal 2013 and 2012, excluding unconsolidated joint ventures, increased 7.9% and increased 27.7%, respectively, as compared to the prior fiscal year. In the month of November 2013, excluding unconsolidated joint ventures, we signed an additional 345 net contracts amounting to \$133.5 million in contract value.

Total cost of sales on our Consolidated Statements of Operations includes expenses for consolidated housing and land and lot sales, including inventory impairment loss and land option write-offs (defined as “land charges” in the tables below). A breakout of such expenses for housing sales and housing gross margin is set forth below:

(Dollars In thousands)	Year Ended			
	October 31, 2013	October 31, 2012	October 31, 2011	
Sale of homes	\$1,784,327	\$1,405,580	\$1,072,474	
Cost of sales, net of impairment reversals and excluding interest expense	1,426,032	1,155,643	905,253	
Homebuilding gross margin, before cost of sales interest expense and land charges	358,295	249,937	167,221	
Cost of sales interest expense, excluding land sales interest expense	51,939	48,843	57,016	
Homebuilding gross margin, after cost of sales interest expense, before land charges	306,356	201,094	110,205	
Land charges	4,965	12,530	101,749	
Homebuilding gross margin, after cost of sales interest expense and land charges	\$301,391	\$188,564	\$8,456	
Gross margin percentage, before cost of sales interest expense and land charges	20.1	% 17.8	% 15.6	%
Gross margin percentage, after cost of sales interest expense, before land charges	17.2	% 14.3	% 10.3	%
Gross margin percentage after cost of sales interest expense and land charges	16.9	% 13.4	% 0.8	%

Cost of sales expenses as a percentage of consolidated home sales revenues are presented below:

	Year Ended		October 31,		October 31,	
	October 31, 2013		October 31, 2012		October 31, 2011	
Sale of homes	100	%	100	%	100	%
Cost of sales, net of impairment						

reversals and excluding interest:						
Housing, land and development costs	70.0	%	71.1	%	71.9	%
Commissions	3.3	%	3.4	%	3.5	%
Financing concessions	1.4	%	1.7	%	2.0	%
Overheads	5.2	%	6.0	%	7.0	%
Total cost of sales, before interest expense and land charges	79.9	%	82.2	%	84.4	%
Gross margin percentage, before cost of sales interest expense and land charges	20.1	%	17.8	%	15.6	%
Cost of sales interest	2.9	%	3.5	%	5.3	%
Gross margin percentage, after cost of sales interest expense and before land charges	17.2	%	14.3	%	10.3	%

We sell a variety of home types in various communities, each yielding a different gross margin. As a result, depending on the mix of communities delivering homes, consolidated gross margin may fluctuate up or down. Total homebuilding gross margin percentage, before interest expense and land impairment and option write off charges, increased to 20.1% for the year ended October 31, 2013, compared to 17.8% for the same period last year. The increase in gross margin percentage was primarily due to the mix of higher margin homes delivered during the year ended October 31, 2013 compared to the prior year. This mix change is a result of delivering more homes in communities where we acquired the land more recently at lower costs than land acquired before the housing downturn. In addition, during fiscal 2013 and 2012 we saw an increase in the pace of sales in some of our markets and, as a result, in a majority of communities we were able to increase base prices and increase lot premiums. For the years ended October 31, 2013, 2012 and 2011, gross margin was favorably impacted by the reversal of prior period inventory impairments of \$60.5 million, \$75.7 million and \$91.8 million, respectively, which represented 3.4%, 5.4% and 8.6%, respectively, of "Sale of homes" revenue. During fiscal 2011, there was a declining pace of sales in our markets which led to intense competition in many of our specific community locations. In order to attempt to maintain a reasonable pace of absorption, we increased incentives, reduced lot location premiums, and lowered some base prices, all of which significantly impacted our margins and resulted in significant inventory impairments.

Reflected as inventory impairment loss and land option write-offs in cost of sales (“land charges”), we have written-off or written-down certain inventories totaling \$5.0 million, \$12.5 million, and \$101.7 million during the years ended October 31, 2013, 2012, and 2011, respectively, to their estimated fair value. See “Note 13 to the Consolidated Financial Statements” for an additional discussion. During the years ended October 31, 2013, 2012, and 2011, we wrote-off residential land options and approval and engineering costs totaling \$2.6 million, \$2.7 million, and \$24.3 million, respectively, which are included in the total land charges mentioned above. When a community is redesigned or abandoned, engineering costs are written-off. Option, approval and engineering costs are written-off when a community’s pro forma profitability is not projected to produce adequate returns on the investment commensurate with the risk and when we believe it is probable we will cancel the option. Such write-offs were located in all of our segments in fiscal 2011 and 2012 and all segments except the West in 2013. The inventory impairments amounted to \$2.4 million, \$9.8 million, and \$77.5 million for the years ending October 31, 2013, 2012 and 2011, respectively. In fiscal 2013 and 2012, inventory impairments were lower than they had been in several years as we began to see some stabilization in the prices and sales pace in some of our segments as reflected by the overall improvement of the housing industry. In fiscal 2011, the majority of the impairments were in the Northeast and West segments. Impairments in the Northeast were primarily due to increased weakness in the market, primarily in Northern New Jersey and communities now classified as held for sale or sold and thus adjusted to fair value. In the West, where we had significant competition from foreclosures, we had reduced prices in order to maintain sales pace. This was especially true in some of the more fringe markets in our West segment. It is difficult to predict if this trend will continue, and should it become necessary to further lower prices, or should the estimates or expectations used in determining estimated cash flows or fair value decrease or differ from current estimates in the future, we may need to recognize additional impairments.

Below is a breakdown of our lot option walk-aways and impairments by segment for fiscal 2013. In 2013, we walked away from 9.4% of all the lots we controlled under option contracts. The remaining 90.6% of our option lots are in communities that we believe remain economically feasible.

The following table represents lot option walk-aways by segment for the year ended October 31, 2013:

(In millions)	Dollar	Number of	% of	Total	Walk-Away	
	Amount				Walk-Away	Option
	of Walk	Lots	Lots	Lots(1)	Option Lots	
	Away					
Northeast	\$0.7	642	39.8	% 3,319	19.3	%
Mid-Atlantic	0.1	280	17.4	% 3,245	8.6	%
Midwest	0.2	161	10.0	% 2,109	7.6	%
Southeast	0.2	192	11.9	% 2,672	7.2	%
Southwest	1.4	336	20.9	% 5,059	6.6	%
West	-	-	0	% 730	0	%
Total	\$2.6	1,611	100.0	% 17,134	9.4	%

(1) *Includes lots optioned at October 31, 2013 and lots optioned that the Company walked away from in the year ended October 31, 2013.*

We can incur costs while investigating land options, whereby we decided not to pursue the opportunity before we control the lots. These costs are expensed in the period we decided to no longer pursue the opportunity. For the year ended October 31, 2013, such costs were not significant and are therefore not shown in the tables above. In addition, we sometimes walk-away from a lot option when we have only incurred costs of less than \$50,000, such costs are not shown in the tables above.

The following table represents impairments by segment for the year ended October 31, 2013:

	Dollar		Pre-	% of Pre-		
(In millions)	Amount of	% of	(2) Impairment	Impairment		
	Impairment	Impairments	Value(1)	Value		
Northeast	\$2.4	100.0	% \$7.7	31.2	%	
Mid-Atlantic	-	0	% 0.1	0	%	
Midwest	-	0	% -	0	%	
Southeast	-	0	% 0.4	0	%	
Southwest	-	0	% -	0	%	
West	-	0	% -	0	%	
Total	\$2.4	100.0	% \$8.2	29.3		

(1) *Represents carrying value, net of prior period impairments, if any, at the time of recording the applicable period's impairments.*

(2) *During the year ended October 31, 2013, the Mid-Atlantic had an impairment totaling \$2 thousand and the Southeast had an impairment totaling \$17 thousand.*

Land Sales and Other Revenues

Land sales and other revenues consist primarily of land and lot sales. A breakout of land and lot sales is set forth below:

(In thousands)	Year Ended		
	October 31, 2013	October 31, 2012	October 31, 2011
Land and lot sales	\$17,711	\$31,788	\$26,745
Cost of sales, net of impairment reversals and excluding interest	16,012	24,158	8,648
Land and lot sales gross margin, excluding interest	1,699	7,630	18,097
Land sales interest expense	291	5,695	17,660
Land and lot sales gross margin, including interest	\$1,408	\$1,935	\$437

Land sales are ancillary to our residential homebuilding operations and are expected to continue in the future but may significantly fluctuate up or down. Although we budget land sales, they are often dependent upon receiving approvals and entitlements, the timing of which can be uncertain. As a result, projecting the amount and timing of land sales is difficult. There were 14 land sales in the year ended October 31, 2013, compared to 16 in the same period of the prior year, which resulted in a decrease of \$14.1 million in land sales revenue. There were 11 land sales in the year ended October 31, 2011, which resulted in an increase of \$5.0 million in land sales revenue in fiscal 2012.

Land sales and other revenues decreased \$21.8 million and increased \$8.1 million for the years ended October 31, 2013 and 2012 compared to the same period in the prior year. Other revenues include income from contract cancellations where the deposit has been forfeited due to contract terminations, interest income, cash discounts, buyer walk-aways, and miscellaneous one-time receipts. The decrease for the year ended October 31, 2013, compared to the year ended October 31, 2012, was mainly due to the decrease in land sales discussed above, a \$3.0 million decrease in interest income recognized from a note receivable, as well as minor fluctuations spread across the various components of other revenues. The primary reason for the increase in land sales and other revenues for fiscal 2012 was due to the increase in land sales mentioned above, along with a \$1.0 million increase in interest income recognized from a note receivable. The remaining increase relates to minor fluctuations among the various components of other revenues.

Homebuilding Selling, General and Administrative

Homebuilding selling, general and administrative (“SGA”) expenses increased \$23.7 million to \$165.8 million for the year ended October 31, 2013 as compared to the year ended October 31, 2012. This increase was due to higher

insurance costs and construction defect reserves and additional reserves for a receivable from an insurance provider and a receivable related to a prior year land sale. However, these expenses increased by less than the increase in revenues. Therefore, SGA expenses as a percentage of homebuilding revenues improved to 9.2% for the year ended October 31, 2013 compared to 9.8% for the year ended October 31, 2012. SGA decreased to \$142.1 million for the year ended October 31, 2012 from \$161.5 million for the year ended October 31, 2011. These decreases in SGA expenses were the result of reduced costs through administrative consolidation and other cost saving measures.

Homebuilding Operations by Segment

Financial information relating to the Company's operations was as follows:

Segment Analysis (Dollars in thousands, except average sales price)

	Years Ended October 31,			Variance	
	2013	2013 Compared to 2012	2012	2012 Compared to 2011	2011
Northeast					
Homebuilding revenue	\$282,855	\$49,529	\$233,326	\$31,342	\$201,984
Income (loss) before income taxes	\$1,519	\$6,202	\$(4,683)	\$94,593	\$(99,276)
Homes delivered	617	112	505	106	399
Average sales price	\$453,314	\$20,847	\$432,467	\$(18,325)	\$450,792
Mid-Atlantic					
Homebuilding revenue	\$289,303	\$16,223	\$273,080	\$73,364	\$199,716
Income (loss) before income taxes	\$24,388	\$7,126	\$17,262	\$34,548	\$(17,286)
Homes delivered	623	(26)	649	125	524
Average sales price	\$462,798	\$48,499	\$414,299	\$34,412	\$379,887
Midwest					
Homebuilding revenue	\$163,485	\$56,766	\$106,719	\$36,152	\$70,567
Income (loss) before income taxes	\$12,270	\$12,017	\$253	\$9,230	\$(8,977)
Homes delivered	657	180	477	117	360
Average sales price	\$247,730	\$24,378	\$223,352	\$27,616	\$195,736
Southeast					
Homebuilding revenue	\$147,570	\$18,886			