

LGI Homes, Inc.
Form 10-K
March 09, 2016

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 December 31, 2015
Commission file number 001-36126

LGI HOMES, INC.
(Exact name of registrant as specified in its charter)

Delaware 46-3088013
(State or other jurisdiction of incorporation or (I.R.S. Employer Identification No.)
organization)

1450 Lake Robbins Drive, Suite 430, The Woodlands, 77380
Texas (Zip code)
(Address of principal executive offices)
(281) 362-8998
(Registrant's Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(b) of the Act:
Title of each class Name of each exchange on which registered
Common Stock (\$0.01 par value) NASDAQ

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
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 Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) 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 non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting

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company” in Rule 12b-2 of the Exchange Act.

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

(Do not check if a smaller reporting company)

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

As of June 30, 2015, the aggregate market value of the registrant’s common stock held by non-affiliates of the registrant was approximately \$316.6 million based on the closing price as reported on the NASDAQ Stock Market. As of March 7, 2016, there were 20,270,389 shares of the registrant’s common stock, par value \$.01 per share, issued and outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions from the registrant’s definitive Proxy Statement for the 2016 Annual Meeting of Stockholders are incorporated herein by reference (to the extent indicated) into Part III.

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PART I

Explanatory Note

Unless otherwise indicated or the context requires, “LGI,” the “Company,” “we,” “our” and “us” refer collectively to LGI Homes, Inc. and its subsidiaries. On November 13, 2013, we completed an initial public offering (the “IPO”) of 10,350,000 shares of our common stock. As a result of the reorganization transactions completed in connection with the IPO (the “Reorganization Transactions”), for accounting purposes, our historical results included herein present the combined assets, liabilities and results of operations of LGI Homes, Inc. since the date of its formation and LGI Homes Group, LLC, LGI Homes Corporate, LLC, LGI Homes II, LLC, LGI Homes-Sunrise Meadow, LLC, LGI Homes-Canyon Crossing, LLC, LGI Homes-Deer Creek, LLC and their direct and indirect subsidiaries prior to the IPO (collectively, our “Predecessor”). For the period subsequent to the IPO, the assets, liabilities and results of operations present the consolidated results of the Company.

Prior to the completion of the IPO, our Predecessor owned a 15% equity interest in and managed the day-to-day operations of four joint venture entities (the “LGI/GTIS Joint Ventures”). Concurrent with the IPO, LGI Homes, Inc. acquired all of the equity interests in the LGI/GTIS Joint Ventures that it did not own immediately prior to the IPO (the “GTIS Acquisitions”). Our financial statements present our Predecessor’s historical interest in the LGI/GTIS Joint Ventures using the equity method and our Predecessor’s share of the LGI/GTIS Joint Ventures’ net earnings are included in income from unconsolidated joint ventures. Effective November 13, 2013, we own all of the equity interests in the LGI/GTIS Joint Ventures and we account for them on a consolidated basis after such date.

ITEM 1. BUSINESS

General

We are one of the nation’s fastest growing public homebuilders in terms of percentage increase of home closings. We are engaged in the design, construction, marketing and sale of new homes in markets in Texas, Arizona, Florida, Georgia, New Mexico, South Carolina, North Carolina, Colorado, Washington and Tennessee. Our core markets include Houston, San Antonio, Dallas/Fort Worth, Austin, Phoenix, Tucson, Tampa, Orlando, Fort Myers, Atlanta, Albuquerque, Charlotte, Denver, Seattle, Colorado Springs, Nashville and Jacksonville. Our management team has been in the residential land development business since the mid-1990s. Since commencing home building operations in 2003, we have constructed and closed over 12,000 homes. During the year ended December 31, 2015, we had 3,404 home closings, compared to 2,356 home closings in 2014.

The following is a summary of our history:

2003 - LGI Homes began operations building homes in the Houston market

2006 - We entered the San Antonio market

2009 - We entered the Dallas/Ft. Worth market

2010 - We formed our first LGI/GTIS Joint Venture

2011:

- We entered the Phoenix market and formed our Southwest Division

- We expanded our Texas Division by entering the Austin market

2012 - An LGI/GTIS Joint Venture entered the Tampa market and we formed our Florida Division

2013:

- We expanded our Florida Division by entering the Orlando market

- We entered the Atlanta market and formed our Southeast Division

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- We expanded our Southwest Division by entering the Tucson and Albuquerque markets
- LGI Homes, Inc. was formed. We completed our IPO, Reorganization Transactions and GTIS Acquisitions

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2014:

- We expanded our Southeast Division by entering the Charlotte market and acquiring the homebuilding related assets of Oakmont Home Builders, Inc. and its affiliate in that market
- We expanded our Southwest Division by entering the Denver market
- We launched our first Terrata Homes community in the San Antonio market

2015:

- We expanded our Florida Division by entering the Jacksonville market
- We expanded our Southwest Division with start-up operations in the Colorado Springs market
- We expanded our Southeast Division with start-up operations in the Nashville market
- We entered and formed our Northwest Division with start-up operations in the Seattle market

LGI Homes, Inc. is a Delaware corporation incorporated on July 9, 2013. Our principal executive offices are located at 1450 Lake Robbins Drive, Suite 430, The Woodlands, Texas 77380, and our telephone number is (281) 362-8998. Information on or linked to our website is not incorporated by reference into this Annual Report on Form 10-K unless expressly noted.

Business Opportunities

We believe there is a significant opportunity to continue to grow in our existing markets. Given our knowledge of and proven success in these markets, as well as the favorable demographic and economic trends forecasted for these markets, we expect to continue to grow in these markets.

We see opportunities to develop properties with multiple product lines within the same communities which we believe will enable us to grow our business by increasing the number of price points in some of our existing markets. Our current product offerings include entry-level homes and move-up homes sold under our LGI Homes brand, and our premium move-up homes, which are sold under our Terrata Homes brand.

Our Terrata Homes brand allows us to leverage our systems and process approach, including our distinguished customer centric sales system, to deliver move-in ready homes with standardized features at a higher price point, with sales prices starting at \$350,000 for homes larger than 2,500 square feet. Our first Terrata Homes community is Potranco Ranch in San Antonio, Texas. Our second Terrata Homes community is Riverchase Estates in Lancaster, South Carolina, 30 miles south of Charlotte, North Carolina. During 2015, we closed 33 Terrata Homes with an average sales price of \$408,000.

We expect to continue to pursue a flexible land acquisition strategy of purchasing or optioning finished lots, if they can be acquired at attractive prices, or purchasing raw land for residential development. We generally target land acquisitions that are further away from urban centers than many other suburban communities but have access to major thoroughfares, retail districts and centers of business. These target areas that are further away from urban centers result in a better value for the homeowner through either lower price points or larger lot sizes. We consider development opportunities that meet our profit and return objectives, including opportunities which may involve the sale of home sites as a part of the product mix. We will continue to focus on entry-level home buyers, and expect our home closings in communities with higher price points or those that include the sales of home sites will be less than 5% of our annual home closings during 2016. In addition, during 2016 we plan to further diversify our entry level offerings with more townhome products in select markets.

We intend to continue to expand into new markets where we identify opportunities to build homes and develop communities that meet our profit and return objectives. One of the keys to our successful geographic expansion has been our unique operating model. After successfully implementing this operating model in the Houston market, we expanded into 13 additional markets, and have start-up operations in three additional markets, including Nashville,

Tennessee, Seattle, Washington and Colorado Springs, Colorado that are expected to open for sales in 2016. In addition, during October 2014, we completed our first acquisition of another home-builder when we acquired the homebuilding related assets and liabilities of Oakmont Home Builders, Inc. and its affiliate (collectively, "Oakmont") in Charlotte, North Carolina. We will continue to evaluate potential opportunities, including acquisitions of other homebuilders and further diversifying our products, to expand our presence in our existing markets or to expand into new markets.

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Unique Operating Model

We developed our unique operating model based on our belief that there is a more effective and efficient method of constructing and selling homes. We are focused on maintaining an appropriate supply of move-in ready homes to fuel our dynamic sales force. We believe that the key competitive advantages of our operational business model include our sales and marketing expertise; recruitment, selection, training and development of our people; our disciplined land acquisition process; our commitment to systems and processes across our organization; and our quality assurance and quality control procedures associated with our homebuilding operations.

Our unique operating model has been refined since our inception. We believe our operating model will be effective with respect to home sales across all price points, including in our new markets. We believe that our business model can be adapted as needed, for the requirements of individual communities and new geographic markets.

Sales and Marketing

We utilize a well-defined sales and marketing approach to identify leads for our communities and to educate potential buyers on the process and benefits of homeownership. For many of our communities, our marketing efforts are focused on converting renters of apartments and single-family homes into homeowners.

We use extensive print and digital advertising to attract potential homebuyers. We employ sophisticated marketing techniques such as direct mail, newspaper advertisements, social media and interactive online media as well as directional signage and billboards to attract and drive potential homebuyers to our sales centers.

Our print advertising methods are extensive and have proven to be highly effective in placing potential homebuyers in front of our highly trained sales professionals. Direct mail has also proven to be very effective in reaching our target market and communicating our core message of value and dream fulfillment.

With respect to our communities with higher price points or that include the sale of home sites, our sales and marketing approaches are tailored to the potential purchasers of such homes and home sites and include more involvement by real estate agents and brokers.

Across all price points, our marketing strategy calls for a balanced approach of corporate support and local expertise to attract potential homebuyers in a focused, efficient and cost-effective manner. Our proprietary customer relationship management system provides our management team with tools to continually monitor and measure the performance level of every sales professional through each phase of the sales process. Utilization of these tools allows us to assess the cost effectiveness of a particular advertising campaign and marketing medium as well as the strengths and weaknesses of every member of our sales team.

Our marketing efforts are generally designed to encourage the prospective homebuyer to call our sales offices to schedule an appointment and our primary objective is to establish direct communication between the prospective homebuyer and the salesperson. Our professional salespeople are well-trained to determine specific needs and wants of the potential homebuyer and to provide the potential homebuyer with all information required to make a buying decision.

Our sales offices are open approximately 12 hours per day, 360 days per year, and generally staffed by two to five sales professionals and supported by an independent on-site loan officer. Our commission-based sales professionals provide potential homebuyers with a comprehensive and thorough understanding of the steps required to achieve homeownership. Throughout the sales process, our sales professionals learn about the current housing situation of the potential homebuyers and seek to understand their individual needs while also educating them on the value we provide

through superior quality and affordable prices.

We provide information regarding floor plans and pricing, credit and income qualifications and conduct tours of our homes based on the potential homebuyer's budget. In addition, we provide each potential homebuyer with a comprehensive introduction to the community and the surrounding area, providing them with detailed information regarding utilities, schools, homeowners association dues and restrictions, local entertainment and nearby dining and shopping options. We provide our potential homebuyers with a clear understanding of who we are by sharing our history, vision and values. As a result of our transparent approach, potential homebuyers receive all this information before making a buying decision, which we believe eliminates confusion during the home buying process and sets clear expectations. In addition, the potential home buyers benefit from the availability of move-in ready homes by seeing the completed or near-completed home that they will own.

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Recruitment, Training and Development

We focus on identifying and attracting the best talent and providing them with world-class training and continuous development. We directly invest in our sales professionals by conducting an intensive 100-day introductory training program consisting of 30 days of initial in-depth, in-house education about our time-proven selling strategies, which includes a two-week intensive training program at our headquarters, and an additional 70 days of secondary training at the local division. Our continued commitment to our sales personnel is reflected in the ongoing weekly training sessions held in each of our sales offices coupled with quarterly regional training events. We also work closely with our subcontractors and construction managers, training them using a comprehensive construction manual that outlines the most efficient way to build an LGI home. Many of our subcontractors have worked on our homes since we commenced homebuilding operations in 2003, and therefore, are familiar with our business model.

Homebuilding Operations

Our homebuilding operations are organized and managed by divisions:

Texas	Southwest	Southeast	Florida	Northwest
Houston, TX	Phoenix, AZ	Atlanta, GA	Tampa, FL	Seattle, WA
Dallas/Ft. Worth, TX	Tucson, AZ	Charlotte, NC	Orlando, FL	
San Antonio, TX	Albuquerque, NM	Nashville, TN	Fort Myers, FL	
Austin, TX	Denver, CO		Jacksonville, FL	
	Colorado Springs, CO			

Our five divisions are aggregated into one reporting segment. See Note 17 “Segment Information” to our consolidated financial statements included in Part II. Item 8 of this Annual Report on Form 10-K.

Our even-flow, or continuous, construction methodology enables us to build and maintain an inventory of move-in ready homes that are available for immediate sale. We offer a set number of floor plans in each community with standardized features that commonly include upgrades such as granite countertops, appliances and ceramic tile flooring. Our homes are designed to meet the preferences of our target market of potential homebuyers and enable cost efficient and effective construction processes. We have developed a collection of home designs, which can be modified for local conditions and market preferences, and implemented across multiple communities to maximize efficiency. We maintained an average home completion time of approximately 45 to 60 days during 2015 and 2014; the homes closed during 2015 ranged from 1,100 to 4,000 square feet with prices ranging from the \$110,000's to the \$475,000's.

We believe in 2016 and beyond, we will continue to focus on our target market of entry level homebuyers. Our townhome product in select markets will further enable us to offer affordable (well-priced) products in desirable locations. We expect that sales of Terrata Homes will represent less than 5% of our home closings through 2016. We expect to continue to utilize our even flow construction methodology in communities with homes at all of our price points and will maintain our focus on marketing complete or move-in ready homes with standardized features.

We employ experienced construction management professionals to perform the tasks of general contractors for home construction in each of our communities. Our employees provide the purchasing, construction management and quality assurance for the homes we build, while third-party subcontractors provide the material and labor components of our homes. In each of our markets, we employ construction managers with local market knowledge and expertise. Additionally, our construction managers monitor our compliance with zoning and other regulations, production schedules, and quality standards for their projects.

We endeavor to obtain favorable pricing from subcontractors through long-term relationships and consistent workflow. As we have expanded into new markets outside of Texas, the employees that we have hired in those markets have brought long-term relationships with several subcontracting firms. We have expanded upon existing relationships with subcontracting firms also located in Texas. A number of our trade partners have subcontracted on our projects since we commenced homebuilding operations in 2003. We purchase some components and materials centrally to leverage our purchasing power to achieve volume discounts, a practice that often reduces costs and ensures timely deliveries. We typically do not store significant inventories of construction materials, except for work in progress materials for homes under construction. Consistency of our trade partners is an integral part of our homebuilding operations that also leads us to reduced warranty costs. We believe in building long lasting relationships with our trade partners in order to provide consistent, quality and timely deliveries across our markets. We also work closely with our construction managers and subcontractors and train them using a comprehensive construction manual that outlines the most efficient

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way to build an LGI home. We believe our emphasis on developing and educating our employees and subcontractors is a key differentiator relative to our peers.

Throughout our homebuilding operations, we utilize a paperless purchase order system to conduct business with our subcontractors and suppliers. Our master build schedule allows our trade partners to receive their specific task from our electronic system and plan several weeks in advance before starting their work. This means of communication allows our subcontractors to schedule their crews efficiently, thereby allowing for better pricing and better quality of work. Typically, our contractors are paid every two weeks, which contributes to the strength of our business relationships with them.

Land Acquisition Policies and Development

We continue to be an active and opportunistic acquirer of land for residential development in our markets. We source land from a wide range of landowners, brokers, lenders and other land development companies. We generally acquire finished lots and raw land in affordable locations that are further away from urban centers than many other suburban communities but have access to major thoroughfares, retail districts and centers of business. We conduct thorough due diligence on each of our potential land acquisitions, and we look at numerous opportunities before finding one that meets our requirements. We test the market and speak with potential homebuyers before committing to purchase land. We also maintain a pipeline of desirable land positions for replacement communities and new communities. We increased our active communities from 39 as of December 31, 2014 to 52 as of December 31, 2015. We also increased our lot inventory from 19,883 owned or controlled lots as of December 31, 2014 to 23,915 owned or controlled lots as of December 31, 2015.

Our allocation of capital for land investment is performed at the corporate level with a disciplined approach to portfolio management. Our Acquisitions Committee meets periodically and consists of our Chief Executive Officer, Chief Financial Officer, Chief Operating Officer, and Executive Vice President of Acquisitions. Annually, our divisions prepare a strategic plan for their respective geographic areas. Supply and demand are analyzed to ensure land investment is targeted appropriately. The long-term plan is compared on an ongoing basis to evolving realities in the marketplace and is then adjusted to the extent necessary.

We have also purchased larger tracts of land across our markets which will provide us with more opportunities to build homes with multiple price points in our communities. We believe that our land development expertise will allow us to meet our growth and profit objectives with respect to opportunities in which we are the developer. Similar to our home building operations, our personnel oversee the contractors who perform the development work. Our land development projects may include the sale of home sites as a part of the project.

We have strong relationships with the land brokerage community in all of our markets. We believe that in the brokerage community, we have a reputation for knowing our business, having the capital to close deals, and making accurate and timely decisions that benefit both the buyer and seller. For these reasons, we believe that brokers routinely notify us when desirable tracts of land are available for purchase.

In our land acquisition process, projects of interest are evaluated at the division level using an extensive due diligence checklist which includes assessing the permitting and regulatory requirements, environmental considerations, local market conditions, and anticipated floor plans, pricing, and financial returns. We also determine the number of residents in the market and rental households that are within driving distance to the proposed project and conduct test marketing which includes mailings to prospective homebuyers to get their feedback on our potential land acquisition. By testing the market before entering it and acquiring land in it, we are able to assess the level of interest in the location and amenities, determine the cost of rent in the area, and assess the size of the market opportunity. The amount of information that we are able to ascertain about potential home buyers, including renters, allows us to better

identify the opportunity to sell move-in ready homes.

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The table below shows (i) home closings by division for the year ended December 31, 2015 and (ii) our owned or controlled lots by division as of December 31, 2015.

Division	Year Ended	As of December 31, 2015		
	December 31, 2015 Home Closings	Owned ⁽¹⁾	Controlled	Total
Texas	1,856	10,720	2,174	12,894
Southwest	565	1,679	1,013	2,692
Florida	396	1,571	357	1,928
Southeast	587	3,516	2,370	5,886
Northwest	—	111	404	515
Total	3,404	17,597	6,318	23,915

⁽¹⁾ Of the 17,597 owned lots as of December 31, 2015, 11,863 were raw/under development lots and 5,734 were finished lots.

Homes in Inventory

When entering a new community, we build a sufficient number of move-in ready homes to meet our budgets. We base future home starts on closings. As homes are closed, we start more homes to maintain our inventory. As of December 31, 2015, we had a total of 684 completed homes and 1,026 homes in progress.

The following is a summary of our homes in inventory by division as of December 31, 2015 (dollar values in thousands):

Division