PULTEGROUP INC/MI/
Form 10-Q
October 28, 2011
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2011

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

Commission File Number 1-9804

PULTEGROUP, INC.

(Exact name of registrant as specified in its charter)

MICHIGAN	**38-2766606**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

100 Bloomfield Hills Parkway, Suite 300

Bloomfield Hills, Michigan 48304

(Address of principal executive offices) (Zip Code)

Registrant s telephone number, including area code (248) 647-2750

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

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES ¨ NO x

Number of shares of common stock outstanding as of October 21, 2011: 382,780,762

Table of Contents

PULTEGROUP, INC.

INDEX

		Page No.
PART I	**FINANCIAL INFORMATION**	
Item 1	**Financial Statements**	
	Condensed Consolidated Balance Sheets at September 30, 2011 and December 31, 2010	3
	Consolidated Statements of Operations for the three and nine months ended September 30, 2011 and 2010	4
	Consolidated Statements of Shareholders Equity for the nine months ended September 30, 2011 and 2010	5
	Consolidated Statements of Cash Flows for the nine months ended September 30, 2011 and 2010	6
	Notes to Condensed Consolidated Financial Statements	7
Item 2	**Management s Discussion and Analysis of Financial Condition and Results of Operations**	39
Item 3	**Quantitative and Qualitative Disclosures About Market Risk**	56
Item 4	**Controls and Procedures**	58
PART II	**OTHER INFORMATION**	
Item 2	**Unregistered Sales of Equity Securities and Use of Proceeds**	58
Item 6	**Exhibits**	59
SIGNATURES		60

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

PULTEGROUP, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

($000 s omitted)

	September 30, 2011 (Unaudited)	December 31, 2010 (Note)
ASSETS		
Cash and equivalents	$ 1,142,513	$ 1,470,625
Restricted cash	113,296	24,601
Unfunded settlements	16,529	12,765
House and land inventory	4,889,668	4,781,813
Land held for sale	134,563	71,055
Land, not owned, under option agreements	25,422	50,781
Residential mortgage loans available-for-sale	173,956	176,164
Investments in unconsolidated entities	37,184	46,313
Goodwill		240,541
Intangible assets, net	165,623	175,448
Other assets	450,522	567,963
Income taxes receivable	79,378	81,307
	$ 7,228,654	$ 7,699,376
LIABILITIES AND SHAREHOLDERS EQUITY		
Liabilities:		
Accounts payable, including book overdrafts of $47,645 and $63,594 in 2011 and 2010, respectively	$ 224,956	$ 226,466
Customer deposits	78,435	51,727
Accrued and other liabilities	1,445,305	1,599,940
Income tax liabilities	221,128	294,408
Senior notes	3,335,363	3,391,668
Total liabilities	5,305,187	5,564,209
Shareholders equity	1,923,467	2,135,167
	$ 7,228,654	$ 7,699,376

Note: The Condensed Consolidated Balance Sheet at December 31, 2010 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements.

See accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents

PULTEGROUP, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(000 s omitted, except per share data)

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	**2010**	**2011**	**2010**
Revenues:				
Homebuilding				
Home sale revenues	$ 1,101,368	$ 1,024,847	$ 2,783,602	$ 3,264,643
Land sale revenues	12,659	5,908	19,023	25,639
	1,114,027	1,030,755	2,802,625	3,290,282
Financial Services	27,904	27,009	71,720	93,738
Total revenues	1,141,931	1,057,764	2,874,345	3,384,020
Homebuilding Cost of Revenues:				
Home sale cost of revenues	947,817	952,788	2,422,525	2,907,339
Land sale cost of revenues	(2,935)	4,849	1,782	16,410
	944,882	957,637	2,424,307	2,923,749
Financial Services expenses	19,249	23,450	78,775	93,333
Selling, general, and administrative expenses	121,610	425,643	402,436	744,364
Other expense (income), net	259,187	672,979	274,765	673,772
Interest income	(1,122)	(2,601)	(3,704)	(7,672)
Interest expense	322	789	990	2,289
Equity in (earnings) loss of unconsolidated entities	303	3,704	(1,999)	(1,744)
Income (loss) before income taxes	(202,500)	(1,023,837)	(301,225)	(1,044,071)
Income tax expense (benefit)	(73,202)	(28,721)	(77,016)	(112,770)
Net income (loss)	$ (129,298)	$ (995,116)	$ (224,209)	$ (931,301)
Per share data:				
Net income (loss):				
Basic	$ (0.34)	$ (2.63)	$ (0.59)	$ (2.46)
Diluted	$ (0.34)	$ (2.63)	$ (0.59)	$ (2.46)
Cash dividends declared	$	$	$	$
Number of shares used in calculation:				
Basic	380,025	378,842	379,785	378,406
Diluted	380,025	378,842	379,785	378,406

See accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents

PULTEGROUP, INC.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

(000's omitted)

(Unaudited)

	Common Stock Shares	Common Stock $	Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings (Accumulated Deficit)	Total Shareholders Equity
Shareholders Equity, January 1, 2011	382,028	$ 3,820	$ 2,972,919	$ (1,519)	$ (840,053)	$ 2,135,167
Stock awards, net of cancellations	983	10	(10)			
Stock repurchases	(267)	(2)	(2,081)		62	(2,021)
Stock-based compensation	37		14,444			14,444
Comprehensive income (loss):						
Net income (loss)					(224,209)	(224,209)
Change in fair value of derivatives, net of tax				137		137
Foreign currency translation adjustments				(51)		(51)
Total comprehensive income (loss)						(224,123)
Shareholders Equity, September 30, 2011	382,781	$ 3,828	$ 2,985,272	$ (1,433)	$ (1,064,200)	$ 1,923,467
Shareholders Equity, January 1, 2010	380,690	$ 3,807	$ 2,935,737	$ (2,249)	$ 257,145	$ 3,194,440
Stock option exercises	902	9	8,659			8,668
Stock awards, net of cancellations	1,105	11	(11)			
Stock repurchases	(313)	(3)	(2,501)		(611)	(3,115)
Stock-based compensation			27,480			27,480
Comprehensive income (loss):						
Net income (loss)					(931,301)	(931,301)
Change in fair value of derivatives, net of tax				251		251
Foreign currency translation adjustments						
Total comprehensive income (loss)						(931,050)
Shareholders Equity, September 30, 2010	382,384	$ 3,824	$ 2,969,364	$ (1,998)	$ (674,767)	$ 2,296,423

See accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents

PULTEGROUP, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

($000 s omitted)

(Unaudited)

	For The Nine Months Ended September 30,	
	2011	**2010**
Cash flows from operating activities:		
Net income (loss)	$ (224,209)	$ (931,301)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Write-down of land and deposits and pre-acquisition costs	11,419	92,549
Goodwill impairments	240,541	656,298
Amortization and depreciation	24,629	34,930
Stock-based compensation expense	14,444	27,480
Equity in (earnings) loss of unconsolidated entities	(1,999)	(1,744)
Distributions of earnings from unconsolidated entities	5,042	3,531
Loss on debt repurchases	3,537	
Other, net	2,741	5,659
Increase (decrease) in cash due to:		
Restricted cash	690	(586)
Inventories	(174,231)	(65,622)
Residential mortgage loans available-for-sale	2,182	13,409
Income taxes receivable	1,929	818,003
Other assets	102,509	78,618
Accounts payable, accrued and other liabilities	(99,674)	109,971
Income tax liabilities	(73,280)	(42,609)
Net cash provided by (used in) operating activities	(163,730)	798,586
Cash flows from investing activities:		
Distributions from unconsolidated entities	4,388	3,893
Investments in unconsolidated entities	(3,749)	(22,666)
Net change in loans held for investment	449	9,898
Change in restricted cash related to letters of credit	(89,385)	
Proceeds from the sale of fixed assets	9,449	1,240
Capital expenditures	(15,162)	(11,647)
Net cash provided by (used in) investing activities	(94,010)	(19,282)
Cash flows from financing activities:		
Net repayments (borrowings) under Financial Services credit arrangements		(18,394)
Repayments of other borrowings	(68,351)	(1,415)
Issuance of common stock		8,668
Stock repurchases	(2,021)	(3,115)
Net cash provided by (used in) financing activities	(70,372)	(14,256)
Net increase (decrease) in cash and equivalents	(328,112)	765,048
Cash and equivalents at beginning of period	1,470,625	1,858,234

Cash and equivalents at end of period	$ 1,142,513	$ 2,623,282
Supplemental Cash Flow Information:		
Interest paid (capitalized), net	$ (29,457)	$ (12,871)
Income taxes paid (refunded), net	$ (5,665)	$ (884,602)

See accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents

PULTEGROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Basis of presentation and significant accounting policies

Basis of presentation

PulteGroup, Inc. (PulteGroup) is a publicly-held holding company traded on the New York Stock Exchange under the ticker symbol PHM . The consolidated financial statements include the accounts of PulteGroup and all of its direct and indirect subsidiaries (collectively, the Company) and variable interest entities in which the Company is deemed to be the primary beneficiary. While the Company s subsidiaries engage primarily in the homebuilding business, the Company also has mortgage banking operations, conducted principally through Pulte Mortgage LLC (Pulte Mortgage), and title operations.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, certain information and disclosures normally included in the Company s annual financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to the SEC rules and regulations. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. Operating results for the interim periods presented are not necessarily indicative of the results that may be expected for the full year. These financial statements should be read in conjunction with the Company s consolidated financial statements and footnotes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010.

Use of estimates

The preparation of financial statements in conformity with United States generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Reclassifications

Certain prior period amounts have been reclassified to conform to the current year presentation.

Subsequent events

The Company evaluated subsequent events up until the time the financial statements were filed with the Securities and Exchange Commission (SEC).

Other expense (income), net

Other expense (income), net as reflected in the Consolidated Statements of Operations consists of the following (000 s omitted):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Write-off of deposits and pre-acquisition costs	$ 2,296	$ 1,133	$ 6,628	$ 3,985
Loss on debt retirements			3,537	
Lease exit and related costs *(a)*	114	6,675	6,301	9,287
Amortization of intangible assets	3,275	3,275	9,825	9,825
Goodwill impairments	240,541	654,923	240,541	656,298

Miscellaneous expense (income), net	12,961	6,973	7,933	(5,623)
	$ 259,187	$ 672,979	$ 274,765	$ 673,772

(a) *Excludes lease exit and related costs classified within Financial Services expenses.*

Table of Contents

PULTEGROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Unaudited)

1. Basis of presentation and significant accounting policies (continued)

Restricted cash

The Company maintains certain cash balances that are restricted as to their use. Restricted cash consists primarily of deposits maintained with financial institutions under certain cash-collateralized letter of credit agreements (see Note 10). The remaining balances relate to certain other accounts with restrictions, including customer deposits on home sales that are temporarily restricted by regulatory requirements until title transfers to the homebuyer.

Notes receivable

In certain instances, the Company may accept consideration for land sales or other transactions in the form of a note receivable. The counterparties for these transactions are generally land developers or other strategic investors. The Company considers the creditworthiness of the counterparty when evaluating the relative risk and return involved in pursuing the applicable transaction. Due to the unique facts and circumstances surrounding each receivable, the Company actively monitors each individual receivable separately and assesses the need for an allowance for each receivable on an individual basis. Factors considered as part of this assessment include the counterparty s payment history, the value of any underlying collateral, communications with the counterparty, knowledge of the counterparty s financial condition and plans, and the current and expected economic environment. Allowances are recorded in other expense (income), net when it becomes likely that some amount will not be collectible. Such receivables are reported net of allowance for credit losses within other assets. Notes receivable are written off when it is determined that collection efforts will no longer be pursued. Interest income is recognized as earned. The following represents the Company s notes receivable and related allowance for credit losses at September 30, 2011 and December 31, 2010 ($000 s omitted):

	September 30, 2011	December 31, 2010
Notes receivable, gross	$ 77,968	$ 77,853
Allowance for credit losses	(40,960)	(20,877)
Notes receivable, net	$ 37,008	$ 56,976

The increase in the allowance for credit losses during 2011 relates to the recording of additional reserves as well as reclassifications of reserved receivable balances. The Company also records other receivables from various parties in the normal course of business, including amounts due from municipalities, insurance companies, and vendors. Such receivables are generally non-interest bearing and non-collateralized, payable either on demand or upon the occurrence of a specified event, and are generally reported in other assets. See *Residential mortgage loans available-for-sale* in Note 1 for a discussion of the Company s receivables related to mortgage operations.

Earnings per share

Basic earnings per share is computed by dividing income (loss) available to common shareholders (the numerator) by the weighted-average number of common shares, adjusted for non-vested shares of restricted stock (the denominator) for the period. Computing diluted earnings per share is similar to computing basic earnings per share, except that the denominator is increased to include the dilutive effects of stock options, restricted stock units, and non-vested shares of restricted stock. Any stock options that have an exercise price greater than the average market price are considered to be anti-dilutive and are excluded from the diluted earnings per share calculation. For the three and nine months ended September 30, 2011 and 2010, all stock options, restricted stock units, and non-vested restricted stock were excluded from the calculation as they were anti-dilutive due to the net loss recorded during each period.

Unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents are participating securities and, therefore, are included in computing earnings per share pursuant to the two-class method. The two-class method determines earnings per share for each class of common stock and participating securities according to dividends or dividend equivalents and their respective participation rights in undistributed earnings. Although the Company s outstanding restricted stock and restricted stock units are considered participating securities, there were no earnings attributable to restricted shareholders during the three and nine months ended September 30, 2011 or 2010.

Table of Contents

PULTEGROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Unaudited)

1. Basis of presentation and significant accounting policies (continued)

Land, not owned, under option agreements

In the ordinary course of business, the Company enters into land option agreements in order to procure land for the construction of homes in the future. Pursuant to these land option agreements, the Company generally provides a deposit to the seller as consideration for the right to purchase land at different times in the future, usually at predetermined prices. Under Accounting Standards Codification (ASC) 810, Consolidation (ASC 810), if the entity holding the land under option is a variable interest entity (VIE), the Company s deposit represents a variable interest in that entity. If the Company is determined to be the primary beneficiary of the VIE, then the Company is required to consolidate the VIE.

In applying the provisions of ASC 810, the Company evaluates all land option agreements with VIEs to determine whether the Company is the primary beneficiary. The Company generally has little control or influence over the operations of these VIEs due to the Company s lack of an equity interest in them. The VIE is generally protected from the first dollar of loss under the Company s land option agreement due to the Company s deposit. Likewise, the VIE s gains are generally capped based on the purchase price within the land option agreement. Additionally, creditors of the VIE have no recourse against the Company, and the Company does not provide financial or other support to these VIEs other than as stipulated in the land option agreements. The Company s maximum exposure to loss related to these VIEs is generally limited to the Company s deposits and pre-acquisition costs under the applicable land option agreements. In recent years, the Company has canceled a significant number of land option agreements, which has resulted in significant write-offs of the related deposits and pre-acquisition costs but has not exposed the Company to the overall risks or losses of the applicable VIEs. No VIEs required consolidation under ASC 810 at either September 30, 2011 or December 31, 2010.

Additionally, the Company determined that certain land option agreements represent financing arrangements pursuant to ASC 470-40, Accounting for Product Financing Arrangements (ASC 470-40), even though the Company has no direct obligation to pay these future amounts. As a result, the Company recorded $25.4 million and $50.8 million at September 30, 2011 and December 31, 2010, respectively, to land, not owned, under option agreements with a corresponding increase to accrued and other liabilities. Such amounts represent the remaining purchase price under the land option agreements, some of which are with VIEs, in the event the Company exercises the purchase rights under the agreements.

The following provides a summary of the Company s interests in land option agreements as of September 30, 2011 and December 31, 2010 ($000 s omitted):

	September 30, 2011			December 31, 2010		
	Deposits and Pre-acquisition Costs	Total Purchase Price	Land, Not Owned, Under Option Agreements	Deposits and Pre-acquisition Costs	Total Purchase Price	Land, Not Owned, Under Option Agreements
Consolidated VIEs	$ 9,046	$ 32,834	$ 20,681	$ 41,813	$ 51,773	$ 42,401
Unconsolidated VIEs	25,077	297,880		10,280	202,214	
Other land option agreements	22,952	466,201	4,741	42,970	455,481	8,380
	$ 57,075	$ 796,915	$ 25,422	$ 95,063	$ 709,468	$ 50,781

The above summary includes land option agreements consolidated under ASC 470-40 as well as all other land option agreements. The remaining purchase price (total purchase price less deposit) of all land option agreements totaled $760.4 million at September 30, 2011 and $670.5 million at December 31, 2010.

Table of Contents

PULTEGROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Unaudited)

1. Basis of presentation and significant accounting policies (continued)

Residential mortgage loans available-for-sale

Substantially all of the loans originated by the Company are sold in the secondary mortgage market within a short period of time after origination. In accordance with ASC 825, Financial Instruments, the Company has elected the fair value option for its portfolio loans available-for-sale. Election of the fair value option for residential mortgage loans available-for-sale allows a better offset of the changes in fair values of the loans and the derivative instruments used to economically hedge them without having to apply complex hedge accounting provisions. The Company does not designate any derivative instruments as accounting hedges. Fair values for agency residential mortgage loans available-for-sale are determined based on quoted market prices for comparable instruments. Fair values for non-agency residential mortgage loans available-for-sale are determined based on purchase commitments from whole loan investors and other relevant market information available to management. At September 30, 2011 and December 31, 2010, residential mortgage loans available-for-sale had an aggregate fair value of $174.0 million and $176.2 million, respectively, and an aggregate outstanding principal balance of $166.5 million and $175.9 million, respectively. The net gain (loss) resulting from changes in fair value of residential mortgage loans available-for-sale totaled $0.8 million and $(0.9) million for the three months ended September 30, 2011 and 2010, respectively, and $(0.6) million and $1.0 million for the nine months ended September 30, 2011 and 2010, respectively, and was included in Financial Services revenues. These changes in fair value were mostly offset by changes in fair value of the corresponding hedging instruments. Net gains from the sale of mortgages were $16.1 million and $15.6 million for the three months ended September 30, 2011 and 2010, respectively, and $41.2 million and $50.7 million for the nine months ended September 30, 2011 and 2010, respectively, and have been included in Financial Services revenues.

Mortgage servicing rights

The Company sells its servicing rights monthly on a flow basis through fixed price servicing contracts. In accordance with Staff Accounting Bulletin No. 109, the Company recognizes the fair value of its rights to service a mortgage loan as revenue at the time of entering into an interest rate lock commitment with a borrower. Due to the short period of time the servicing rights are held, the Company does not amortize the servicing asset. The servicing sales contracts provide for the reimbursement of payments made by the purchaser if loans prepay within specified periods of time, generally within 90 to 120 days after sale. The Company establishes reserves for this liability at the time the sale is recorded. Such reserves totaled $0.4 million and $0.5 million at September 30, 2011 and December 31, 2010, respectively, and are included in accrued and other liabilities. Servicing rights recognized in Financial Services revenues totaled $1.9 million and $4.2 million for the three months ended September 30, 2011 and 2010, respectively, and $10.6 million and $17.0 million for the nine months ended September 30, 2011 and 2010, respectively.

Derivative instruments and hedging activities

The Company is exposed to market risks from commitments to lend, movements in interest rates, and cancelled or modified commitments to lend. A commitment to lend at a specific interest rate (an interest rate lock commitment) is a derivative financial instrument (interest rate is locked to the borrower). In order to reduce these risks, the Company uses other derivative financial instruments to economically hedge the interest rate lock commitment. These financial instruments include forward contracts on mortgage-backed securities and whole loan investor commitments. The Company does not use any derivative financial instruments for trading purposes. The Company enters into one of the aforementioned derivative financial instruments upon entering into interest rate lock commitments. Changes in the fair value of the interest rate lock commitment and the other derivative financial instruments are recognized in current period earnings and the fair value is reflected in other assets or other liabilities. The gains and losses are included in Financial Services revenues.

Fair values for interest rate lock commitments, including the value of servicing rights, are based on market prices for similar instruments. At September 30, 2011 and December 31, 2010, the Company had interest rate lock commitments in the amount of $209.0 million and $99.0 million, respectively, which were originated at interest rates prevailing at the date of commitment. Because the Company can terminate a loan commitment if the borrower does not comply with the terms of the contract, and some loan commitments may expire without being drawn upon,

these commitments do not necessarily represent future cash requirements of the Company. The Company evaluates the creditworthiness of these transactions through its normal credit policies.

Table of Contents

PULTEGROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Unaudited)

1. Basis of presentation and significant accounting policies (continued)

Forward contracts on mortgage-backed securities are commitments to either purchase or sell a specified financial instrument at a specified future date for a specified price and may be settled in cash, by offsetting the position, or through the delivery of the financial instrument. Whole loan investor commitments are obligations of the investor to buy loans at a specified price within a specified time period. Forward contracts on mortgage-backed securities are the predominant derivative financial instruments used by the Company to minimize the market risk during the period from the time the Company extends an interest rate lock to a loan applicant until the time the loan is sold to an investor. Forward contracts on mortgage-backed securities are valued based on market prices for similar instruments. Fair values for whole loan investor commitments are based on market prices for similar instruments from the specific whole loan investor. At September 30, 2011, the Company had unexpired forward contracts and whole loan investor commitments of $337.4 million and $5.4 million, respectively, compared with cash forward contracts on mortgage-backed securities and whole loan investor commitments of $198.0 million and $59.0 million, respectively, at December 31, 2010.

There are no credit-risk-related contingent features within the Company s derivative agreements. Gains and losses on interest rate lock commitments are substantially offset by corresponding gains or losses on forward contracts on mortgage-backed securities and whole loan investor commitments. At September 30, 2011, the maximum length of time that the Company was exposed to the variability in future cash flows of derivative instruments was approximately 75 days.

The fair value of the Company s derivative instruments and their location in the Consolidated Balance Sheet is summarized below ($000 s omitted):

	September 30, 2011		December 31, 2010	
	Other Assets	Other Liabilities	Other Assets	Other Liabilities
Interest rate lock commitments	$ 7,157	$ 4	$ 2,756	$ 64
Forward contracts	167	6,385	4,217	673
Whole loan commitments	83	19	2,319	
	$ 7,407	$ 6,408	$ 9,292	$ 737

New accounting pronouncements

In May 2011, the FASB issued Accounting Standards Update No. 2011-04, Fair Value Measurement (ASU 2011-04), which amends Accounting Standards Codification (ASC) 820 to clarify existing guidance and minimize differences between U.S. GAAP and International Financial Reporting Standards (IFRS). ASU 2011-04 requires entities to provide information about valuation techniques and unobservable inputs used in Level 3 fair value measurements and provide a narrative description of the sensitivity of Level 3 measurements to changes in unobservable inputs. ASU 2011-04 will be effective for the Company s fiscal year beginning January 1, 2012 and is not expected to have a material impact on the Company s financial statements.

In June 2011, the FASB issued Accounting Standards Update No. 2011-05, Statement of Comprehensive Income (ASU 2011-05), which requires entities to present net income and other comprehensive income in either a single continuous statement or in two separate, but consecutive, statements of net income and other comprehensive income. ASU 2011-05 will not impact the Company s reported results of operations but will impact the Company s financial statement presentation as the Company currently presents items of other comprehensive income in the statement of changes in equity. ASU 2011-05 will be effective for the Company s fiscal year beginning January 1, 2012.

Table of Contents

PULTEGROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Unaudited)

2. Goodwill and intangible assets

Goodwill

Goodwill, which represents the cost of acquired companies in excess of the fair value of the net assets at the acquisition date, is subject to annual impairment testing in the fourth quarter of each year or when events or changes in circumstances indicate the carrying amount may not be recoverable. Recorded goodwill has been allocated to the Company s reporting units based on the relative fair value of each acquired reporting unit. Management evaluates the recoverability of goodwill by comparing the carrying value of the Company s reporting units to their fair value. Fair value is determined using discounted cash flows, supplemented by market-based assessments of fair value. Impairment is measured as the difference between the resulting implied fair value of goodwill and its recorded carrying value. The determination of fair value is significantly impacted by estimates for each of the Company s markets related to current valuations, current and future economic conditions, and the Company s strategic plans. Due to uncertainties in the estimation process and significant volatility in demand for new housing, actual results could differ significantly from such estimates.

The Company recorded $1.5 billion of goodwill in connection with the merger with Centex Corporation (Centex), which was completed in August 2009. All goodwill associated with prior transactions has been previously written-off. Since the Centex merger, the Company has recorded impairments at various times of the associated goodwill. These impairments have resulted from a variety of factors, including, among other things, deteriorations in market conditions, the Company s operating results falling below previously forecasted levels, and a sustained decline in the Company s market capitalization since the Centex merger.

In the third quarters of both 2011 and 2010, the Company performed event-driven assessments of the recoverability of goodwill. These assessments were necessary primarily due to sustained declines in the Company s market capitalization. In performing the goodwill impairment analyses, the Company followed similar approaches using management s estimates of the future cash flows for each reporting unit, which are required to consider the decrease in the Company s market capitalization. The results of these analyses determined that goodwill impairment charges of $240.5 million and $654.9 million in the third quarters of 2011 and 2010, respectively, were required. The Company also recorded a goodwill impairment charge of $1.4 million in the second quarter of 2010 in conjunction with the completion of its business combination accounting for the Centex merger. Goodwill impairment charges are reflected in other expense (income), net.

The following summarizes the change in goodwill during 2011 ($000 s omitted):

Reporting Segment	Balance at December 31, 2010	Additions	Impairments	Disposals	Balance at September 30, 2011
East	$ 60,494	$	$ (60,494)	$	$
Gulf Coast	92,095		(92,095)		
West	87,952		(87,952)		
Total goodwill	$ 240,541	$	$ (240,541)	$	$

Table of Contents

PULTEGROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Unaudited)

2. Goodwill and intangible assets (continued)

The following summarizes the change in goodwill during 2010 ($000 s omitted):

Reporting Segment	Balance at December 31, 2009	Additions	Impairments	Disposals	Balance at September 30, 2010
East	$ 327,032	$ 1,104	$ (267,642)	$	$ 60,494
Gulf Coast	353,434	679	(262,018)		92,095
West	213,859	731	(126,638)		87,952
Financial Services	1,593			(1,593)	
Total goodwill	$ 895,918	$ 2,514	$ (656,298)	$ (1,593)	$ 240,541

Intangible assets

Intangible assets consist of trademarks and tradenames acquired in connection with the 2009 acquisition of Centex and the 2001 acquisition of Del Webb. These intangible assets were valued at the respective acquisition dates and are being amortized over 20-year lives. The ultimate realization of these assets is dependent upon estimates of future earnings and benefits that the Company expects to generate from their use. In both the third quarters of 2011 and 2010, the Company performed event-driven assessments of the recoverability of these assets using projected undiscounted cash flows. In each instance, the Company determined that no impairment existed. However, if expectations of future results and cash flows decrease significantly or if our strategy related to the use of such intangible assets changes, the related intangible assets may be impaired.

3. Restructuring

The Company has taken a series of actions in recent years both in response to the challenging operating environment and in connection with the Centex merger that were designed to reduce ongoing operating costs and improve operating efficiencies. As a result of the combination of these actions, the Company incurred total restructuring charges as summarized below ($000 s omitted):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Employee severance benefits	$ 663	$ 7,444	$ 9,195	$ 12,275
Lease exit costs	101	7,113	6,401	9,767
Other		987	11	1,556
Total restructuring charges	$ 764	$ 15,544	$ 15,607	$ 23,598

Of the total restructuring costs reflected in the above table, $0.1 million and $1.1 million for the three and nine months ended September 30, 2011, respectively, and $1.7 million and $3.2 million for the three and nine months ended September 30, 2010, respectively, are included within

Financial Services expenses. All other employee severance benefits are included within selling, general and administrative expenses while all other lease exit and other costs are included in other expense (income), net. The remaining liabilities for employee severance benefits and exited leases totaled $1.9 million and $34.0 million, respectively, at September 30, 2011 and $8.0 million and $41.7 million, respectively, at December 31, 2010. Substantially all of the employee severance benefits will be paid in 2011 while cash expenditures related to lease exit costs will be incurred over the remaining terms of the applicable leases, which generally extend several years. The restructuring costs relate to each of the Company s reportable segments and were not material to any one segment.

Table of Contents

PULTEGROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Unaudited)

4. Inventory and land held for sale

Major components of the Company s inventory were as follows ($000 s omitted):

	September 30, 2011	December 31, 2010
Homes under construction	$ 1,445,313	$ 1,331,618
Land under development	2,582,854	2,541,829
Land held for future development	861,501	908,366
	$ 4,889,668	$ 4,781,813

The Company capitalizes interest cost into inventory during the active development and construction of the Company s communities. Each layer of capitalized interest is amortized over a period that approximates the average life of communities under development. Interest expense is allocated over the period based on the cyclical timing of unit settlements. Interest expensed to Homebuilding cost of revenues for the three and nine months ended September 30, 2011 included $1.0 million and $2.3 million, respectively, of capitalized interest related to land and community valuation adjustments, compared with $7.6 million and $13.8 million for the three and nine months ended September 30, 2010, respectively. During the three and nine months ended September 30, 2011, the Company capitalized all of its Homebuilding interest costs into inventory because the level of the Company s active inventory exceeded the Company s debt levels. During the three and nine months ended September 30, 2010, the Company capitalized all of its Homebuilding interest costs into inventory except for $0.9 million and $1.5 million, respectively, that was expensed directly to interest expense.

Information related to interest capitalized into homebuilding inventory is as follows ($000 s omitted):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Interest in inventory, beginning of period	$ 358,806	$ 310,622	$ 323,379	$ 239,365
Interest capitalized	55,230	67,794	167,367	203,979
Interest expensed	(48,693)	(48,501)	(125,403)	(113,429)
Interest in inventory, end of period	$ 365,343	$ 329,915	$ 365,343	$ 329,915
Interest incurred*	$ 55,230	$ 68,740	$ 167,367	$ 205,473

* *Homebuilding interest incurred includes interest on senior debt, short-term borrowings, and other financing arrangements and excludes interest incurred by the Financial Services segment and certain other interest costs.*

Table of Contents

PULTEGROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Unaudited)

4. Inventory and land held for sale (continued)

Land valuation adjustments and write-offs

Land and community valuation adjustments

In accordance with ASC 360, Property, Plant, and Equipment (ASC 360), the Company records valuation adjustments on land inventory and related communities under development when events and circumstances indicate that they may be impaired and when the cash flows estimated to be generated by those assets are less than their carrying amounts. Such indicators include gross margin or sales paces significantly below expectations, construction costs or land development costs significantly in excess of budgeted amounts, significant delays or changes in the planned development for the community, and other known qualitative factors. For communities that are not yet active, a significant additional consideration includes an evaluation of the probability, timing, and cost of obtaining necessary approvals from local municipalities and any potential concessions that may be necessary in order to obtain such approvals. The Company also considers potential changes to the product offerings in a community and any alternative strategies for the land, such as the sale of the land either in whole or in parcels. A portion of the Company s land inventory and communities under development demonstrated potential impairment indicators during the three and nine months ended September 30, 2011 and 2010, and were accordingly tested for impairment. As required by ASC 360, the Company compared the expected undiscounted cash flows for these communities to their carrying value. For those communities whose carrying values exceeded the expected undiscounted cash flows, the Company calculated the fair value of the community in accordance with ASC 360. Impairment charges are required to be recorded if the fair value of the community s inventory is less than its carrying value.

The Company determines the fair value of a community s inventory primarily using a combination of market comparable land transactions, where available, and discounted cash flow models. These estimated cash flows are significantly impacted by estimates related to expected average selling prices and sales incentives, expected sales paces and cancellation rates, expected land development and construction timelines, and anticipated land development, construction, and overhead costs. The assumptions used in the discounted cash flow models are specific to each community tested for impairment and typically do not assume improvements in market conditions in the near term. Due to uncertainties in the estimation process, the significant volatility in demand for new housing, and the long life cycles of many communities, actual results could differ significantly from such estimates. The Company s determination of fair value also requires discounting the estimated cash flows at a rate commensurate with the inherent risks associated with each of the assets and related estimated cash flow streams. The discount rate used in determining each community s fair value depends on the stage of development of the community and other specific factors that increase or decrease the inherent risks associated with the community s cash flow streams. For example, communities that are entitled and near completion will generally require a lower discount rate than communities that are not entitled and consist of multiple phases spanning several years of development and construction activity.

The table below provides, as of the date indicated, the number of communities for which the Company recognized impairment charges, the fair value of those communities at such date (net of impairment charges), and the amount of impairment charges recognized ($ in millions):

	2011			2010		
Quarter Ended	Number of Communities Impaired	Fair Value of Communities Impaired, Net of Impairment Charges	Impairment Charges	Number of Communities Impaired	Fair Value of Communities Impaired, Net of Impairment Charges	Impairment Charges
March 31	1	$ 0.5	$ 0.1	10	$ 7.2	$ 4.5
June 30	6	6.7	3.3	16	35.1	25.6
September 30	3	6.4	1.5	28	33.4	57.4

	$ 4.9	$ 87.5

PULTEGROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Unaudited)

4. Inventory and land held for sale (continued)

The Company recorded these valuation adjustments within Homebuilding home sale cost of revenues. During the three months ended September 30, 2011, the Company reviewed each of its land positions for potential impairment indicators and performed detailed impairment calculations for 15 communities. The average discount rate used in the Company s determination of fair value for the impaired communities was 12%. During 2011, the Company has experienced relative stability in market conditions consistent with its expectations, which resulted in total valuation adjustments significantly below those experienced in recent years. However, if conditions in the homebuilding industry or the Company s local markets worsen in the future, if the current difficult market conditions extend beyond the Company s expectations, or if the Company s strategy related to certain communities changes, the Company may be required to evaluate its assets, including additional projects, for future impairments or write-downs, which could result in future charges that might be significant.

Net realizable value adjustments land held for sale

The Company acquires land primarily for the construction of homes for sale to customers but may periodically elect to sell select parcels of land to third parties for commercial or other development. Additionally, the Company may determine that certain of its land assets no longer fit into its strategic operating plans. Assuming the criteria in ASC 360 are met, the Company classifies any such land as land held for sale.

In accordance with ASC 360, the Company values land held for sale at the lower of carrying value or fair value less costs to sell. In determining the fair value of land held for sale, the Company considers recent legitimate offers received, prices for land in recent comparable sales transactions, and other factors. Based on this review, a portion of the Company s land held for sale has been written down to net realizable value. The Company recognized net realizable value adjustments (recoveries) of $0.1 million and $(0.1) million during the three and nine months ended September 30, 2011, respectively, and $0.6 million and $1.0 million during the three and nine months ended September 30, 2010, respectively. The Company records these net realizable value adjustments within Homebuilding land sale cost of revenues.

The Company s land held for sale was as follows ($000 s omitted):

	September 30, 2011	December 31, 2010
Land held for sale, gross	$ 181,373	$ 124,919
Net realizable value reserves	(46,810)	(53,864)
Land held for sale, net	$ 134,563	$ 71,055

Write-off of deposits and pre-acquisition costs

From time to time, the Company writes off certain deposits and pre-acquisition costs related to land option contracts the Company no longer plans to pursue. Such decisions take into consideration changes in local market conditions, the willingness of land sellers to modify terms of the related purchase agreement, the timing of required land takedowns, the availability and best use of necessary incremental capital, and other factors. The Company wrote off (net of recoveries) deposits and pre-acquisition costs in the amount of $2.3 million and $6.6 million during the three and nine months ended September 30, 2011, respectively, and $1.1 million and $4.0 million during the three and nine months ended September 30, 2010, respectively. The Company records these write-offs of deposits and pre-acquisition costs within other expense (income), net.

16

PULTEGROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Unaudited)

5. Segment information

The Company s Homebuilding operating segments are engaged in the acquisition and development of land primarily for residential purposes within the continental United States and the construction of housing on such land. As part of its ongoing efforts to structure the Company for profitability in the face of challenging market conditions, the Company realigned its organizational structure during the second quarter of 2011, which reduced the number of reportable segments from four to three. The operating data by segment provided in this note have been reclassified to conform to the current presentation. Accordingly, the Company s reportable Homebuilding segments are as follows:

East:	*Connecticut, Delaware, Georgia, Maryland, Massachusetts, New Jersey, New York,*
	North Carolina, Pennsylvania, Rhode Island, South Carolina, Tennessee, Virginia
Gulf Coast:	*Florida, Texas*
West:	*Arizona, California, Colorado, Hawaii, Illinois, Indiana, Michigan, Minnesota, Missouri,*
	Nevada, New Mexico, Ohio, Oregon, Washington

The Company also has one reportable segment for its financial services operations, which consist of mortgage banking and title operations. The Company s Financial Services segment operates generally in the same markets as the Company s Homebuilding segments.

Evaluation of segment performance is based on operating earnings before provision for income taxes which, for the Homebuilding segments, is defined as home sale revenues and land sale revenues less home sale cost of revenues, land sale cost of revenues, and certain selling, general, and administrative and other expenses, plus equity income from unconsolidated entities, attributable to the Homebuilding segments. Operating earnings for the Financial Services segment is defined as revenues less costs associated with the Company s mortgage and title operations and certain selling, general, and administrative expenses incurred by or allocated to the Financial Services segment. Each reportable segment generally follows the same accounting policies described in Note 1 Summary of Significant Accounting Policies to the consolidated financial statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010.

Table of Contents

PULTEGROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Unaudited)

5. Segment information (continued)

	Operating Data by Segment ($000 s omitted)			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Revenues:				
East	$ 379,662	$ 321,817	$ 951,918	$ 1,108,220
Gulf Coast	342,860	277,699	878,448	881,906