Howard Hughes Corp
Form 10-Q
August 08, 2016
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended June 30, 2016

or

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission file number 001-34856

THE HOWARD HUGHES CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	36-4673192
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification number)

13355 Noel Road, 22nd Floor, Dallas, Texas 75240

(Address of principal executive offices, including zip code)

(214) 741-7744

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

Large accelerated filer		Accelerated filer
Non-accelerated filer	(Do not check if a smaller reporting company)	Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

The number of shares of common stock, $0.01 par value, outstanding as of August 8, 2016 was 39,833,975.

Table of Contents

THE HOWARD HUGHES CORPORATION

INDEX

	PAGE NUMBER
PART I FINANCIAL INFORMATION	
Item 1: Condensed Consolidated Financial Statements (Unaudited)	
Condensed Consolidated Balance Sheets as of June 30, 2016 and December 31, 2015	3
Condensed Consolidated Statements of Operations for the three and six months ended June 30, 2016 and 2015	4
Condensed Consolidated Statements of Comprehensive Income (Loss) for the three and six months ended June 30, 2016 and 2015	5

Condensed Consolidated Statements of Equity for the six months ended June 30, 2016 and 2015	6
Condensed Consolidated Statements of Cash Flows for the six months ended June 30, 2016 and 2015	7
Notes to Condensed Consolidated Financial Statements	9
Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations	32
Item 3: Quantitative and Qualitative Disclosures about Market Risk	59
Item 4: Controls and Procedures	60
PART II OTHER INFORMATION	60
Item 1: Legal Proceedings	60
Item 1A: Risk Factors	60
Item 6: Exhibits	60

SIGNATURE	61
EXHIBIT INDEX	62

2

Table of Contents

THE HOWARD HUGHES CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS

UNAUDITED

(In thousands, except share amounts)	June 30, 2016	December 31, 2015
Assets:		
Investment in real estate:		
Master Planned Community assets	$ 1,652,056	$ 1,642,842
Land	315,617	322,462
Buildings and equipment	1,910,016	1,772,401
Less: accumulated depreciation	(271,451)	(232,969)
Developments	915,157	1,036,927
Net property and equipment	4,521,395	4,541,663
Investment in Real Estate and Other Affiliates	65,834	57,811
Net investment in real estate	4,587,229	4,599,474
Cash and cash equivalents	670,800	445,301
Accounts receivable, net	40,152	32,203
Municipal Utility District receivables, net	163,639	139,946
Notes receivable, net	69	1,664
Deferred expenses, net	63,099	61,804
Prepaid expenses and other assets, net	692,631	441,190
Total assets	$ 6,217,619	$ 5,721,582
Liabilities:		
Mortgages, notes and loans payable	$ 2,651,805	$ 2,443,962
Deferred tax liabilities	158,177	89,221
Warrant liabilities	322,090	307,760
Uncertain tax position liability	9,588	1,396
Accounts payable and accrued expenses	572,772	515,354
Total liabilities	3,714,432	3,357,693
Commitments and Contingencies (see Note 15)		
Equity:		
Preferred stock: $.01 par value; 50,000,000 shares authorized, none issued	—	—
Common stock: $.01 par value; 150,000,000 shares authorized, 39,846,036 shares issued and 39,833,975 outstanding as of June 30, 2016 and 39,714,838 shares issued and outstanding as of December 31, 2015	398	398
Additional paid-in capital	2,853,880	2,847,823

Accumulated deficit	(329,480)	(480,215)
Accumulated other comprehensive loss	(24,152)	(7,889)
Treasury stock, at cost, 12,061 shares as of June 30, 2016 and 0 shares as of December 31, 2015	(1,231)	—
Total stockholders' equity	2,499,415	2,360,117
Noncontrolling interests	3,772	3,772
Total equity	2,503,187	2,363,889
Total liabilities and equity	$ 6,217,619	$ 5,721,582

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

THE HOWARD HUGHES CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

UNAUDITED

	Three Months Ended June 30,		Six Months Ended June 30,	
(In thousands, except per share amounts)	2016	2015	2016	2015
Revenues:				
Condominium rights and unit sales	$ 125,112	$ 86,513	$ 247,206	$ 121,370
Master Planned Community land sales	61,098	45,433	103,040	93,514
Minimum rents	42,036	36,989	83,345	72,183
Builder price participation	6,501	7,907	11,148	13,605
Tenant recoveries	10,923	10,701	21,451	20,368
Hospitality revenues	19,129	11,481	32,038	23,484
Other land revenues	2,759	3,145	5,792	6,438
Other rental and property revenues	4,593	6,994	7,797	13,291
Total revenues	272,151	209,163	511,817	364,253
Expenses and other income:				
Condominium rights and unit cost of sales	79,726	56,765	154,541	79,174
Master Planned Community cost of sales	29,008	24,236	44,696	48,132
Master Planned Community operations	7,806	11,963	17,400	21,946
Other property operating costs	15,236	19,634	30,978	37,779
Rental property real estate taxes	7,329	6,568	14,077	12,768
Rental property maintenance costs	2,753	2,900	5,885	5,644
Hospitality costs	14,242	8,893	24,717	17,971
Provision for doubtful accounts	(352)	1,266	2,689	2,075
Demolition costs	490	1,496	962	1,613
Development-related marketing costs	6,339	5,594	10,870	11,837
General and administrative	20,053	19,606	40,377	38,569
Other income, net	(9,067)	(399)	(9,426)	(1,863)
Gain on sale of 80 South Street Assemblage	—	—	(140,479)	—
Depreciation and amortization	24,952	25,069	47,924	46,579
Total expenses, net of other income	198,515	183,591	245,211	322,224
Operating income	73,636	25,572	266,606	42,029
Interest income	435	271	704	407
Interest expense	(16,533)	(14,685)	(32,526)	(27,931)
Warrant liability (loss) gain	(44,150)	42,620	(14,330)	(66,190)
Equity in earnings from Real Estate and Other Affiliates	20,275	1,081	22,207	2,869
Income (loss) before taxes	33,663	54,859	242,661	(48,816)

Provision for income taxes	26,693	4,274	91,926	6,558
Net income (loss)	6,970	50,585	150,735	(55,374)
Net income attributable to noncontrolling interests	—	(12)	—	(12)
Net income (loss) attributable to common stockholders	$ 6,970	$ 50,573	$ 150,735	$ (55,386)
Basic income (loss) per share:	$ 0.18	$ 1.28	$ 3.82	$ (1.40)
Diluted income (loss) per share:	$ 0.16	$ 0.18	$ 3.53	$ (1.40)

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

THE HOWARD HUGHES CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

UNAUDITED

	Three Months Ended June 30,		Six Months Ended June 30,	
(In thousands)	2016	2015	2016	2015
Net income (loss)	$ 6,970	$ 50,585	$ 150,735	$ (55,374)
Other comprehensive income (loss):				
Interest rate swaps (a)	(5,565)	196	(15,373)	708
Capitalized swap interest expense (b)	(254)	(53)	(317)	(112)
Pension adjustment (c)	(573)	—	(573)	—
Other comprehensive income (loss)	(6,392)	143	(16,263)	596
Comprehensive income (loss)	578	50,728	134,472	(54,778)
Comprehensive income attributable to noncontrolling interests	—	(12)	—	(12)
Comprehensive income (loss) attributable to common stockholders	$ 578	$ 50,716	$ 134,472	$ (54,790)

(a) Amounts are shown net of deferred tax benefit of $3.0 million and deferred tax benefit of $8.3 million for the three and six months ended June 30, 2016, respectively. For the three and six months ended June 30, 2015, amounts are shown net of deferred tax expense of $0.1 million and $0.6 million, respectively.
(b) Net of deferred tax benefit of $0 and $0.1 million for the three and six months ended June 30, 2016, respectively. For the three and six months ended June 30, 2015, amounts shown net of deferred tax benefit of both $0.1 million, respectively.
(c) Net of deferred tax benefit of $0.4 million for both the three and six months ended June 30, 2016, respectively. For both the three and six months ended June 30, 2015, amounts shown net of deferred tax benefit of $0, respectively.

See Notes to Condensed Consolidated Financial Statements.

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Table of Contents

THE HOWARD HUGHES CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF EQUITY

UNAUDITED

(In thousands, except share amounts)	Common stock Shares	Common stock Amount	Additional paid-in capital	Accumulated deficit	Accumulated other comprehensive income (loss)	Treasury stock Shares	Treasury stock Amount	Noncontrol interests
Balance, December 31, 2014	39,638,094	$ 396	$ 2,838,013	$ (606,934)	$ (7,712)	—	$ —	$ 3,743
Net loss		—	—	(55,386)	—	—	—	12
Preferred dividend payment on behalf of REIT subsidiary		—	—	—	—	—	—	29
Interest rate swaps, net of tax of $555		—	—	—	708	—	—	—
Capitalized swap interest, net of tax benefit of $41		—	—	—	(112)	—	—	—
Stock plan activity	76,911	2	4,253	—	—	—	—	—
Issuances of treasury stock	—	—	—	—	—	—	—	—
Balance, June 30, 2015	39,715,005	$ 398	$ 2,842,266	$ (662,320)	$ (7,116)	—	$ —	$ 3,784
Balance, December 31, 2015	39,714,838	$ 398	$ 2,847,823	$ (480,215)	$ (7,889)	—	$ —	$ 3,772
Net income		—	—	150,735	—	—	—	—
Interest rate swaps, net of tax of $8,245		—	—	—	(15,373)	—	—	—

Pension adjustment, net of tax of $350		—	—	—	(573)	—	—	—
Capitalized swap interest, net of tax benefit of $61		—	—	—	(317)	—	—	—
Stock plan activity	131,198	0	6,057	—	—	—	—	—
Treasury stock activity	—	—	—	—	—	(12,061)	(1,231)	—
Balance, June 30, 2016	39,846,036	$ 398	$ 2,853,880	$ (329,480)	$ (24,152)	(12,061)	$ (1,231)	$ 3,772

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

THE HOWARD HUGHES CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

UNAUDITED

(In thousands)	Six Months Ended June 30, 2016	2015
Cash Flows from Operating Activities:		
Net income (loss)	$ 150,735	$ (55,374)
Adjustments to reconcile net income (loss) to cash used in operating activities:		
Depreciation	41,126	37,155
Amortization	6,798	9,424
Amortization of deferred financing costs	3,747	3,192
Amortization of intangibles other than in-place leases	(710)	472
Straight-line rent amortization	(5,187)	(2,727)
Deferred income taxes	85,927	6,135
Restricted stock and stock option amortization	4,670	3,232
Gain on disposition of 80 South Street Assemblage	(140,479)	—
Warrant liability loss	14,330	66,190
Equity in earnings from Real Estate and Other Affiliates, net of distributions	(8,212)	1,437
Provision for doubtful accounts	2,689	2,075
Master Planned Community land acquisitions	(69)	(1,928)
Master Planned Community development expenditures	(70,678)	(83,868)
Master Planned Community cost of sales	41,310	44,792
Condominium development expenditures	(155,222)	(79,500)
Condominium rights and unit cost of sales	154,541	75,991
Percentage of completion revenue recognition from sale of condominium rights and unit sales	(247,206)	(121,370)
Net changes:		
Accounts and notes receivable	(3,230)	(1,115)
Prepaid expenses and other assets	2,616	15,520
Condominium deposits received	51,573	18,423
Deferred expenses	(1,659)	240
Accounts payable and accrued expenses	(24,798)	(11,030)
Condominium deposits held in escrow	(51,573)	(18,423)
Condominium deposits released from escrow	15,661	90,425
Other, net	(3,535)	(325)
Cash used in operating activities	(136,835)	(957)
Cash Flows from Investing Activities:		
Property and equipment expenditures	(7,339)	(3,863)

Operating property improvements	(5,712)	(4,401)
Property developments and redevelopments	(214,276)	(364,044)
Proceeds from grant to reimburse development costs	2,915	—
Proceeds from disposition of 80 South Street Assemblage, net	378,257	—
Proceeds from insurance claims	3,107	—
Investment in KR Holdings, LLC	—	9,121
Distributions from Real Estate and Other Affiliates	12,002	—
Note issued to Real Estate Affiliate	(25,000)	—
Proceeds from repayment of note to Real Estate Affiliate	25,000	—
Investments in Real Estate and Other Affiliates, net	(11,813)	(501)
Change in restricted cash	4,658	(1,485)
Cash provided by (used in) investing activities	161,799	(365,173)
Cash Flows from Financing Activities:		
Proceeds from mortgages, notes and loans payable	207,561	310,822
Principal payments on mortgages, notes and loans payable	(4,492)	(14,900)
Deferred financing costs	(1,303)	(1,614)
Taxes paid on vested restricted stock	(1,231)	—
Cash provided by financing activities	200,535	294,308
Net change in cash and cash equivalents	225,499	(71,822)
Cash and cash equivalents at beginning of period	445,301	560,451
Cash and cash equivalents at end of period	$ 670,800	$ 488,629

Table of Contents

THE HOWARD HUGHES CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

UNAUDITED

	Six Months Ended June 30,	
(In thousands)	2016	2015
Supplemental Disclosure of Cash Flow Information:		
Interest paid	$ 57,335	$ 48,460
Interest capitalized	28,681	23,074
Income taxes paid	3,067	2,067
Non-Cash Transactions:		
Special Improvement District bond transfers associated with land sales	3,386	3,340
Property developments and redevelopments	—	(4,534)
Accrued interest on construction loan borrowing	3,005	1,359
MPC Land contributed to Real Estate Affiliates	—	15,234
Special Improvement District bond transfer to Real Estate Affiliate	—	(1,518)
Capitalized stock compensation	1,387	1,262

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

NOTE 1 BASIS OF PRESENTATION AND ORGANIZATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”), with intercompany transactions between consolidated subsidiaries eliminated for interim financial statements. In accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X as issued by the Securities and Exchange Commission (the “SEC”), these condensed consolidated financial statements do not include all of the information and disclosures required by GAAP for complete financial statements. Readers of this Quarterly Report on Form 10-Q (“Quarterly Report”) should refer to The Howard Hughes Corporation’s (“HHC” or the “Company”) audited Consolidated Financial Statements which are included in the Company’s Annual Report on Form 10-K (the “Annual Report”) for the fiscal year ended December 31, 2015, filed on February 29, 2016 with the SEC. Certain amounts in 2015 have been reclassified to conform to 2016 presentation. In the opinion of management, all normal recurring adjustments necessary for a fair presentation of the financial position, results of operations, comprehensive income (loss), cash flows and equity for the interim periods have been included. The results for the three and six months ended June 30, 2016 are not necessarily indicative of the results that may be expected for the year ended December 31, 2016.

Management has evaluated for disclosure or recognition all material events occurring subsequent to the date of the condensed consolidated financial statements up to the date and time this Quarterly Report was filed.

NOTE 2 RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In June 2016, the FASB issued ASU 2016-13, “Financial Instruments—Credit Losses.” The standard modifies the impairment model for most financial assets, including trade accounts receivables and loans, and will require the use of an “expected loss” model for instruments measured at amortized cost. Under this model, entities will be required to estimate the lifetime expected credit loss on such instruments and record an allowance to offset the amortized cost basis of the financial asset, resulting in a net presentation of the amount expected to be collected on the financial asset. The effective date of the standard is for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2019 for public companies. We are currently evaluating the impact of adopting ASU 2016-13 on our consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, “Improvements to Employee Share-Based Payment Accounting.” The standard amends several aspects of accounting for share-based payment transactions, including the accounting for income taxes, forfeitures and statutory tax withholding requirements, as well as classification in the statement of cash flows. The new guidance will require entities to recognize all income tax effects of awards in the income statement when the awards vest or are settled. It also will allow an employer to repurchase more of an employee’s shares for tax withholding purposes without triggering liability accounting and to make a policy election to account for forfeitures as they occur. ASU 2016-09 will be effective as of January 1, 2017. Early adoption is permitted. We are currently evaluating the impact of adopting ASU 2016-09 on our consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, "Leases." ASU 2016-02, codified in Accounting Standards Codification ("ASC") 842, amends the existing accounting standards for lease accounting, including requiring lessees to recognize most leases on their balance sheets and making targeted changes to lessor accounting. ASU 2016-02 will be effective beginning in the first quarter of 2019. Early adoption of ASU 2016-02 is permitted. The new Leases standard requires a modified retrospective transition approach for all leases existing at, or entered into after, the date of initial application. We are currently evaluating the impact of adopting ASU 2016-02 on our consolidated financial statements.

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

In February 2015, the FASB issued ASU 2015-02, "Consolidation (Topic 810) - Amendments to the Consolidation Analysis." The standard modifies whether: (1) fees paid to a decision maker or service provider represent a variable interest; (2) a limited partnership or similar entity has the characteristics of a variable interest entity ("VIE") per consolidation guidance in ASC 810-10-65; and (3) a reporting entity is the primary beneficiary of a VIE. The effective date of the standard is for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015 for public companies. We adopted the standard as of January 1, 2016, and there was no impact on our consolidated financial statements.

In May 2014, the FASB and International Accounting Standards Board ("IASB") issued ASU 2014-09 "Revenues from Contracts with Customers (Topic 606)." The standard's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In doing so, companies will need to use more judgment and make more estimates than under current guidance. These may include identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. The effective date of this standard is for fiscal years, and interim periods within those years, beginning after December 15, 2017. Early adoption is permitted after December 15, 2016. Entities have the option of using either a full retrospective or a modified approach. Preliminary assessments of our revenue streams indicate that after adoption we will not be able to recognize revenue for condominium projects on a percentage of completion basis and generally revenue will be recognized when the units close and the title has transferred to the buyer. We are continuing to evaluate the new guidance to determine the impact on our consolidated financial statements.

In August 2014, the FASB issued ASU 2014-15, "Presentation of Financial Statements — Going Concern: Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern." This ASU requires management to assess an entity's ability to continue as a going concern. This ASU is effective for the annual and interim periods ending after December 15, 2016 and for annual and interim periods thereafter. We do not expect the adoption of this ASU to have an impact on our consolidated financial statements.

NOTE 3 SPONSOR AND MANAGEMENT WARRANTS

On November 9, 2010, we issued warrants to purchase shares of our common stock to certain of our sponsors (the "Sponsor Warrants"). The exercise price for the warrants of $50.00 per share and the number of shares of common stock underlying each warrant are subject to adjustment for future stock dividends, splits or reverse splits of our common stock or certain other events. The 1,916,667 of Sponsor Warrants outstanding are exercisable at any time and expire on November 9, 2017.

In November 2010 and February 2011, we entered into certain agreements (the "Management Warrants") with David R. Weinreb, our Chief Executive Officer, Grant Herlitz, our President, and Andrew C. Richardson, our Chief Financial Officer, in each case prior to his appointment to such position to purchase shares of our common stock. The

Management Warrants represent 2,862,687 underlying shares, which may be adjusted pursuant to a net settlement option, were issued pursuant to such agreements at fair value in exchange for a combined total of approximately $19.0 million in cash from such executives at the commencement of their respective employment. Mr. Weinreb and Mr. Herlitz's warrants have exercise prices of $42.23 per share and Mr. Richardson's warrants have an exercise price of $54.50 per share. Generally, the Management Warrants become exercisable in November 2016 and expire in February 2018.

As of June 30, 2016, the estimated $124.1 million fair value for the Sponsor Warrants representing warrants to purchase 1,916,667 shares and the estimated $198.0 million fair value for the Management Warrants representing warrants to purchase 2,862,687 shares have been recorded as liabilities because the holders of these warrants could require us to settle such warrants in cash upon a change of control. The estimated fair values for the outstanding Sponsor Warrants and Management Warrants were $123.1 million and $184.7 million, respectively, as of December 31, 2015. The fair values

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

were estimated using an option pricing model and Level 3 inputs due to the unavailability of comparable market data, as further discussed in Note 7 – Fair Value of Financial Instruments. Decreases and increases in the fair value of the Sponsor Warrants and the Management Warrants are recognized as either warrant liability gains or losses, respectively, in the condensed consolidated statements of operations.

NOTE 4 EARNINGS PER SHARE

Basic earnings (loss) per share ("EPS") is computed by dividing net income (loss) available to common stockholders by the weighted average number of common shares outstanding. Diluted EPS is computed after adjusting the numerator and denominator of the basic EPS computation for the effects of all potentially dilutive common shares. The dilutive effect of options and nonvested stock issued under stock based compensation plans is computed using the "treasury stock" method. The dilutive effect of the Sponsor Warrants and Management Warrants is computed using the if converted method. Gains associated with the changes in the fair value of the Sponsor Warrants and Management Warrants are excluded from the numerator in computing diluted earnings per share because inclusion of such gains in the computation would be anti dilutive.

Information related to our EPS calculations is summarized as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(In thousands, except per share amounts)	2016	2015	2016	2015
Basic EPS:				
Numerator:				
Net income (loss)	$ 6,970	$ 50,585	$ 150,735	$ (55,374)
Net income attributable to noncontrolling interests	—	(12)	—	(12)
Net income (loss) attributable to common stockholders	$ 6,970	$ 50,573	$ 150,735	$ (55,386)
Denominator:				
Weighted average basic common shares outstanding	39,492	39,468	39,483	39,467
Diluted EPS:				
Numerator:				

Net income (loss) attributable to common stockholders	$ 6,970	$ 50,573	$ 150,735	$ (55,386)
Less: Warrant liability gain	—	(42,620)	—	—
Adjusted net income (loss) attributable to common stockholders	$ 6,970	$ 7,953	$ 150,735	$ (55,386)
Denominator:				
Weighted average basic common shares outstanding	39,492	39,468	39,483	39,467
Restricted stock and stock options	337	438	324	—
Warrants	2,835	3,291	2,835	—
Weighted average diluted common shares outstanding	42,664	43,197	42,642	39,467
Basic income (loss) per share:	$ 0.18	$ 1.28	$ 3.82	$ (1.40)
Diluted income (loss) per share:	$ 0.16	$ 0.18	$ 3.53	$ (1.40)

The diluted EPS computation for the three and six months ended June 30, 2016 excludes 363,000 stock options and 402,500 stock options, respectively, because their inclusion would have been anti-dilutive. The diluted EPS computation for the

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

three and six months ended June 30, 2016 excludes 8,729 shares of restricted stock and 9,254 shares of restricted stock, respectively, because performance conditions have not been met.

The diluted EPS computation for the three months ended June 30, 2015 excludes 125,769 stock options. The diluted EPS computation for the six months ended June 30, 2015 excludes 1,048,750 stock options, 242,055 shares of restricted stock, 1,916,667 shares of common stock underlying the Sponsors Warrants and 2,862,687 shares of common stock underlying the Management Warrants because their inclusion would have been anti-dilutive.

NOTE 5 RECENT TRANSACTIONS

On March 16, 2016, we sold the 80 South Street Assemblage ("80 South Street") for net cash proceeds of $378.3 million, resulting in a pre-tax gain of $140.5 million. 80 South Street was comprised of a 42,694 square foot lot with certain air rights, providing total residential and commercial development rights of 817,784 square feet that had been acquired over the course of 2014 and 2015.

NOTE 6 IMPAIRMENT

We review our real estate assets for potential impairment indicators whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. GAAP related to the impairment or disposal of long lived assets requires that if impairment indicators exist and expected undiscounted cash flows generated by the asset are less than its carrying amount, an impairment provision should be recorded to write down the carrying amount of the asset to its fair value. The impairment analysis does not consider the timing of future cash flows and whether the asset is expected to earn an above or below market rate of return.

Each investment in Real Estate and Other Affiliates as discussed in Note 8 – Real Estate and Other Affiliates is evaluated periodically for recoverability and valuation declines that are other-than-temporary. If the decrease in value of our investment in a Real Estate and Other Affiliate is deemed to be other-than-temporary, our investment in such Real Estate and Other Affiliate is reduced to its estimated fair value.

No impairment charges were recorded during the six months ended June 30, 2016 or June 30, 2015. We continually evaluate our strategic alternatives with respect to each of our properties and may revise our strategy from time to time,

including our intent to hold the asset on a long-term basis or the timing of potential asset dispositions. For example, we may decide to sell property that is held for use, and the sale price may be less than the carrying amount. As a result, these changes in strategy could result in impairment charges in future periods.

NOTE 7 FAIR VALUE OF FINANCIAL INSTRUMENTS

ASC 820, Fair Value Measurement, emphasizes that fair value is a market-based measurement that should be determined on the assumptions market participants would use in pricing an asset or liability. The standard establishes a hierarchal disclosure framework which prioritizes and ranks the level of market price observability used in measuring assets or liabilities at fair value. Market price observability is impacted by a number of factors, including the type of investment and the characteristics specific to the asset or liability. Assets or liabilities with readily available active quoted prices or for which fair value can be measured from actively quoted prices generally will have a higher degree of market price observability and a lesser degree or judgment used in measuring fair value.

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

The following table presents the fair value measurement hierarchy levels required under ASC 820 for each of our assets and liabilities that are measured at fair value on a recurring basis:

	June 30, 2016 Fair Value Measurements Using				December 31, 2015 Fair Value Measurements Using			
(In thousands)	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:								
Cash equivalents	$ 378,535	$ 378,535	$ —	$ —	$ 18	$ 18	$ —	$ —
Liabilities:								
Warrants	322,090	—	—	322,090	307,760	—	—	307,760
Interest Rate Swaps & Caps	27,729	—	27,729	—	4,217	—	4,217	—

Cash equivalents consist of registered money market mutual funds which invest in United States treasury securities that are valued at the net asset value of the underlying shares in the funds as of the close of business at the end of each period.

The fair values of interest rate swaps are determined using the market standard methodology of netting the discounted future fixed cash payments and the discounted expected variable cash receipts. The variable cash receipts are based on an expectation of future interest rates derived from observable market interest rate curves.

The valuation of warrants is based on an option pricing model, utilizing inputs which are classified as Level 3 due to the unavailability of comparable market data. The following table presents a rollforward of the valuation of our Sponsor and Management warrants:

(In thousands)	2016	2015
Balance as of January 1	$ 307,760	$ 366,080
Warrant liability loss (a)	14,330	66,190
Balance as of June 30	$ 322,090	$ 432,270

(a) All losses during 2016 and 2015 were unrealized. Changes in the fair value of the Sponsor and Management Warrants are recognized in net income as a warrant liability gain or loss.

The inputs to the valuation model include the fair value of stock related to the warrants, exercise price and term of the warrants, expected volatility, risk-free interest rate and dividend yield and, with respect to the Management Warrants, a discount for lack of marketability. Generally, an increase in expected volatility would increase the fair value of the liability, while a decrease in expected volatility would decrease the fair value of the liability, but the impact of the volatility on fair value diminishes as the market value of the stock increases above the strike price. As the period of restriction lapses, the marketability discount reduces to zero and increases the fair value of the warrants.

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

The significant unobservable inputs used in the fair value measurement of our warrants as of June 30, 2016 and December 31, 2015 are as follows:

	Unobservable Inputs	
	Expected Volatility (a)	Marketability Discount (b)
June 30, 2016	30.9%	5.0% - 7.0%
December 31, 2015	27.4%	10.0% - 12.0%

(a) Based on our implied equity volatility.
(b) Represents the discount rate for lack of marketability of the Management Warrants.

The estimated fair values of our financial instruments that are not measured at fair value on a recurring basis are as follows:

		June 30, 2016		December 31, 2015	
(In thousands)	Fair Value Hierarchy	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Assets:					
Cash	Level 1	$ 292,265	$ 292,265	$ 445,283	$ 445,283
Notes receivable, net (a)	Level 3	69	69	1,664	1,664
Liabilities:					
Fixed-rate debt	Level 2	$ 1,108,453	$ 1,122,964	$ 1,141,381	$ 1,137,166
Variable-rate debt	Level 2	1,553,786	1,553,786	1,314,973	1,314,973

(a) Notes receivable is shown net of an allowance of $0.6 million as of June 30, 2016 and $0.2 million as of December 31, 2015.

Notes receivable are carried at net realizable value which approximates fair value. The estimated fair values are based on certain factors, such as current interest rates, terms of the note and credit worthiness of the borrower.

The fair value of fixed-rate debt in the table above, not including our Senior Notes (please refer to Note 9 – Mortgages, Notes and Loans Payable), was estimated based on a discounted future cash payment model, which includes risk premiums and a risk free rate derived from the current London Interbank Offered Rate ("LIBOR") or U.S. Treasury obligation interest rates. The discount rates reflect our judgment as to what the approximate current lending rates for loans or groups of loans with similar maturities and credit quality would be if credit markets were operating efficiently and assuming that the debt is outstanding through maturity. The fair values of our Senior Notes, included in fixed-rate debt in the table above, are based upon the last trade price closest to the end of the period presented.

The carrying amounts for our variable-rate debt approximate fair value given that the interest rates are variable and adjust with current market rates for instruments with similar risks and maturities.

The carrying amounts of cash and cash equivalents and accounts receivable approximate fair value because of the short term maturity of these instruments.

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

NOTE 8 REAL ESTATE AND OTHER AFFILIATES

In the ordinary course of business, we enter into partnerships or joint ventures primarily for the development and operations of real estate assets that are referred to as “Real Estate and Other Affiliates.” These partnerships or joint ventures are accounted for in accordance with FASB ASC 810 Consolidation.

In accordance with ASC 810, we assess our joint ventures at inception to determine if any meet the qualifications of a VIE. We consider a partnership or joint venture a VIE if: (a) the total equity investment is not sufficient to permit the entity to finance its activities without additional subordinated financial support; (b) characteristics of a controlling financial interest are missing (either the ability to make decisions through voting or other rights, the obligation to absorb the expected losses of the entity or the right to receive the expected residual returns of the entity); or (c) the voting rights of the equity holders are not proportional to their obligations to absorb the expected losses of the entity and/or their rights to receive the expected residual returns of the entity, and substantially all of the entity’s activities either involve or are conducted on behalf of an investor that has disproportionately few voting rights. Upon the occurrence of certain events outlined in ASC 810, we reassess our initial determination of whether the partnership or joint venture is a VIE.

We perform a qualitative assessment of each VIE to determine if we are the primary beneficiary, as required by ASC 810. A company has a controlling financial interest and must consolidate the VIE if it has both (1) the power to direct the activities of the VIE that most significantly impact the VIE’s performance, and (2) “benefits,” defined as the obligation to absorb the losses of the VIE that potentially could be significant to the VIE or the right to receive benefits from the VIE that potentially could be significant to the VIE. The variable interest model requires a reporting entity to reevaluate whether an entity is a VIE upon the occurrence of certain significant events as listed in ASC 810-10-35-4, including any event that changes the design of the entity and calls into question the entity’s sufficiency of equity at risk or characteristics of a controlling financial interest (i.e. amendments to legal governing documents, returns or additions of equity, curtailments or modifications to activities in a way that impacts the equity at risk, etc.).

We account for investments in joint ventures which are not VIEs where we own a non-controlling interest and investments in joint ventures deemed to be VIEs for which we are not considered to be the primary beneficiary but have significant influence using the equity method. We use the cost method to account for investments where we do not have significant influence over the joint venture’s operations and financial policies. Generally, the operating agreements with respect to our Real Estate Affiliates provide that assets, liabilities and funding obligations are shared in accordance with our ownership percentages.

15

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

Our investment in Real Estate and Other Affiliates that are reported on the equity and cost methods are as follows:

	Economic/Legal Ownership				Carrying Value		Share of Earnings/Dividends			
							Three Months Ended		Six Months Ended June 30,	
	June 30,		December 31,		June 30,	December 31,	June 30,			
($ in Thousands)	2016		2015		2016	2015	2016	2015	2016	2015
Equity Method Investments										
Master Planned Communities:										
The Summit (a)	—	(a)	—	(a)	$ 20,926	$ 12,052	$ 8,874	$ —	$ 8,874	$ —
Operating Assets:										
Grandview SHG, LLC (a)	35.00	%	—	%	8,179	—	22	—	41	—
Millennium Woodlands Phase II, LLC (b) (c)	81.43	%	81.43	%	—	—	22	(489)	35	(1,150)
Stewart Title	50.00	%	50.00	%	3,521	3,715	154	302	256	496
Clark County Las Vegas Stadium, LLC (c)	50.00	%	50.00	%	11,345	11,050	454	401	295	284
The Metropolitan Downtown Columbia (d)	50.00	%	50.00	%	3,961	4,872	205	(89)	(512)	(408)
Woodlands Sarofim	20.00	%	20.00	%	2,673	2,588	42	35	95	75
Strategic Developments:										
Circle T Ranch and Power Center (a)	50.00	%	50.00	%	4,956	9,128	10,498	—	10,498	—
HHMK Development (c)	50.00	%	50.00	%	10	10	—	10	—	549

KR Holdings (c)	50.00	%	50.00	%	758	689	4	911	9	1,276
m.flats (formerly Parcel C) (a) (c)	50.00	%	50.00	%	2,473	7,070	—	—	—	—
Constellation (a) (c)	50.00	%	50.00	%	2,685	2,685	—	—	—	—
					61,487	53,859	20,275	1,081	19,591	1,122
Cost method investments					4,347	3,952	—	—	2,616	1,747
Investment in Real Estate and Other Affiliates					$ 65,834	$ 57,811	$ 20,275	$ 1,081	$ 22,207	$ 2,869

(a) Please refer to the discussion below for a description of the joint venture ownership structure.
(b) Millennium Woodlands Phase II, LLC was placed into service in the third quarter 2014. The investment balance is in a deficit position, which is reported in Accounts payable and accrued expenses. As of July 20, 2016, we acquired our joint venture partner's interest in this property, as discussed in Note 5 – Recent Transactions.
(c) Equity method variable interest entity ("VIE"). As of first quarter 2016, m.flats was no longer a VIE.
(d) The Metropolitan Downtown Columbia was placed into service in the first quarter 2015.

We are not the primary beneficiary of any of the VIEs listed above because we do not have the power to direct activities that most significantly impact the economic performance of such joint ventures and therefore we report our interests using the equity method. Our maximum exposure to loss as a result of these investments is limited to the aggregate carrying value of the investment as we have not provided any guarantees or otherwise made firm commitments to fund amounts on behalf of these VIEs. The aggregate carrying value of the unconsolidated VIEs was $13.3 million and $21.5 million as of June 30, 2016 and December 31, 2015, and was classified as Investment in Real Estate and Other Affiliates in the condensed consolidated balance sheets.

As of June 30, 2016 approximately $134.6 million of indebtedness was secured by the properties owned by our Real Estate and Other Affiliates of which our share was approximately $74.6 million based upon our economic ownership. All of this indebtedness is without recourse to us.

We are the primary beneficiary of one VIE which is consolidated in the financial statements. The creditors of the consolidated VIE do not have recourse to us. As of June 30, 2016, the carrying values of the assets and liabilities associated with the operations of the consolidated VIE were $21.5 million and $1.2 million, respectively. As of December 31, 2015, the carrying values of the assets and liabilities associated with the operations of the consolidated VIE were $21.5 million and $1.1 million, respectively. The assets of the VIE are restricted for use only by the particular VIE and are not available for our general operations.

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

Our recent significant investments in Real Estate Affiliates and the related accounting considerations are described below.

The Summit

During the first quarter 2015, we formed DLV/HHPI Summerlin, LLC ("The Summit") a joint venture with Discovery Land Company ("Discovery"). At formation, we contributed land with a book basis of $13.4 million and transferred Special Improvement District ("SID") bonds related to such land with a carrying value of $1.3 million to the joint venture at an agreed upon capital contribution value of $125.4 million, or $226,000 per acre. Discovery is required to fund up to a maximum of $30.0 million cash as its capital contribution, and we have no further capital obligations. The gain on the contributed land will be recognized in Equity in earnings from Real Estate and Other Affiliates as the joint venture sells lots.

After receipt of our capital contribution and a 5.0% preferred return, Discovery is entitled to a 5.0% return on its capital contributions, if any, plus cash distributions by the joint venture until it has received two times its equity contribution. Any further cash distributions are shared 50/50. Discovery is the manager of the project, and development began in the second quarter 2015. As of July 15, 2016, the project has contracted for approximately $122.3 million in land sales, of which $48.2 million in lot closings were completed in the second quarter 2016, resulting in Equity in earnings to us of $8.9 million. Given the nature of the venture's capital structure, our share of the venture's income producing activities is recognized based on the Hypothetical Liquidation Book Value ("HLBV") method, which is an amount equal to the change in our underlying share of the hypothetical distribution assuming all of the venture's net assets were liquidated at book value.

Grandview SHG, LLC

In January 2016, we entered into a joint venture with Grandview SHG, LLC ("Grandview") which purchased a hotel located at 33 Peck Slip in the Seaport District of New York. We advanced a bridge loan of $25.0 million at a 5.0% interest rate to the joint venture at closing to expedite the acquisition, which was repaid in full in June 2016. In the second quarter 2016, upon completion of a refinancing of the property with a $36.0 million redevelopment loan, we made an additional capital contribution of $2.3 million. Our total investment in the joint venture is $8.2 million as of June 30, 2016. We and our partner are in the process of evaluating potential development plans for the property.

Millennium Woodlands Phase II

On July 20, 2016, we purchased our joint venture partner's 18.57% interest in Millennium Woodlands Phase II for $4.0 million and distributed excess cash of approximately $0.5 million to the partners. The venture developed, owns and operates a 314 unit multi-family property in The Woodlands. Simultaneously with the buyout, we replaced the joint venture's existing $37.7 million loan and secured a $42.5 million fixed-rate loan at 3.39% maturing August 1, 2028.

Circle T Ranch and Power Center

On June 1, 2016, the Circle T Ranch joint venture sold approximately 74 acres. As a result of the land sale, in the three and six months ended June 30, 2016 we recognized $10.5 million as our share of the joint venture earnings in Equity in earnings from Real Estate and Other Affiliates.

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

m.flats

On October 4, 2013, we entered into a joint venture agreement with a local developer, Kettler, Inc. (“Kettler”), to construct an apartment complex with ground floor retail in Downtown Columbia, Maryland. We contributed approximately five acres of land having a book value of $4.0 million to the joint venture and subsequently incurred an additional $3.1 million in capitalized development costs for a total book value contribution of $7.1 million. Our land was valued at $23.4 million, or $53,500 per constructed unit. In January 2016, the venture closed on an $88.0 million construction loan which is non-recourse to us and bears interest at one-month LIBOR plus 2.40% with an initial maturity date of February 2020, with three, one-year extension options. At loan closing, Kettler contributed $16.1 million in cash, of which $7.3 million was distributed to us. This transaction was accounted for as a partial sale of the land for which we recognized a net profit of $0.2 million in the three months ended March 30, 2016. We contributed $2.4 million in the three months ended June 30, 2016, and we are required to fund an additional $3.9 million into this joint venture.

Constellation

On January 24, 2014, we entered into a joint venture with a national multi-family real estate developer, The Calida Group (“Calida”), to construct, own and operate a 124-unit gated luxury apartment development in downtown Summerlin. We own 50% of the venture and unanimous consent of the partners is required for all major decisions. This project represents the first residential development in Summerlin’s 400-acre downtown. In the first quarter 2015, we contributed a 4.5-acre parcel of land with an agreed value of $3.2 million in exchange for a 50% interest in the venture. Our partner contributed $3.2 million of cash for their 50% interest, is the development manager, funded all pre-development activities, obtained construction financing in the first quarter 2015 and provided guarantees required by the lender. The project is financed by a $15.8 million construction loan which is non-recourse to us, of which $9.3 million is outstanding as of June 30, 2016. In the fourth quarter 2015, we contributed an additional $1.0 million to the joint venture to fund development costs. Upon a sale of the property, we are entitled to 50% of the proceeds up to, and 100% of the proceeds in excess of, an amount determined by applying a 7.0% capitalization rate to net operating income. The venture commenced construction in February 2015 and will complete the project in phases. The first units are currently available for rent, and we expect new tenants to take occupancy in the third quarter 2016.

NOTE 9 MORTGAGES, NOTES AND LOANS PAYABLE

Mortgages, notes and loans payable are summarized as follows:

(In thousands)	June 30, 2016	December 31, 2015
Fixed-rate debt:		
Collateralized mortgages, notes and loans payable	$ 1,059,210	$ 1,087,642
Special Improvement District bonds	49,243	53,739
Variable-rate debt:		
Collateralized mortgages, notes and loans payable (a)	1,553,786	1,314,973
Deferred Financing Costs, net of accumulated amortization of $14.7 million and $12.7 million, respectively	(10,434)	(12,392)
Total mortgages, notes and loans payable	$ 2,651,805	$ 2,443,962

(a) As more fully described below, $207.6 million and $209.5 million of variable rate debt has been swapped to a fixed-rate for the term of the related debt as of June 30, 2016 and December 31, 2015, respectively.

18

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

The following table presents our mortgages, notes, and loans payable by property:

($ In thousands)	Maturity (a)	Interest Rate			Maximum Facility Amount	Carrying Value June 30, 2016	Carrying Value December 31, 2015
Master Planned Communities							
Bridgeland Credit Facility	November 2022	4.60	%		$ 65,000	$ 59,349	$ 40,072
Summerlin South SID Bonds - S124	December 2019	5.95	%			141	159
Summerlin South SID Bonds - S128	December 2020	6.05	%			487	534
Summerlin South SID Bonds - S128C	December 2030	6.05	%			4,728	4,856
Summerlin South SID Bonds - S132	December 2020	6.00	%			1,494	1,676
Summerlin South SID Bonds - S151	June 2025	6.00	%			4,349	4,534
Summerlin South SID Bonds - S159	June 2035	6.00	%			6,614	9,020
Summerlin West SID Bonds - S808/S810	April 2031	6.00	%			—	1,047
Summerlin West SID Bonds - S812	October 2035	6.00	%			27,844	28,328
The Woodlands Master Credit Facility	August 2018	3.20	%	(b)	200,000	192,662	192,663
Master Planned Communities Total						297,668	282,889
Operating Assets							
10-60 Columbia Corporate Centers	May 2022	2.81	%	(b)(c)		80,000	80,000
70 Columbia Corporate Center	July 2019	2.70	%	(b)		20,000	20,000
Columbia Regional Building	March 2018	2.45	%	(b)	23,008	22,188	22,188
Downtown Summerlin	July 2019	2.70	%	(b)	311,800	293,732	289,804
Downtown Summerlin SID Bonds - S108	December 2016	5.95	%			235	235
Downtown Summerlin SID Bonds - S128	December 2030	6.05	%			3,350	3,350

Embassy Suites at Hughes Landing	October 2020	2.95	% (b)	37,100	28,829	20,064
One Hughes Landing	December 2029	4.30	%		52,000	52,000
Two Hughes Landing	December 2030	4.20	%		48,000	48,000
1725-35 Hughes Landing Boulevard	June 2019	2.10	% (b)	143,000	103,968	89,677
Hughes Landing Retail	December 2018	2.40	% (b)	36,575	32,465	28,726
1701 Lake Robbins	April 2017	5.81	%		4,600	4,600
Millennium Waterway Apartments	June 2022	3.75	%		55,584	55,584
110 N. Wacker	October 2019	5.21	% (d)		24,593	26,481
9303 New Trails	December 2023	4.88	%		12,558	12,734
One Lakes Edge	November 2016	2.70	% (b)	73,525	69,646	67,517
Outlet Collection at Riverwalk	October 2018	3.20	% (b)	64,400	56,100	56,100
3831 Technology Forest Drive	March 2026	4.50	%		22,573	22,759
The Westin at The Woodlands	August 2019	3.10	% (b)	69,300	49,788	33,361
The Woodlands Resort & Conference Center	December 2020	3.20	% (b)		85,000	85,000
Ward Village	September 2016	3.46	% (b)(e)	250,000	238,716	238,716
20/25 Waterway Avenue	May 2022	4.79	%		14,000	14,112
3 Waterway Square	August 2028	3.94	%		52,000	52,000
4 Waterway Square	December 2023	4.88	%		36,777	37,293
Capital lease obligations	various	3.60	%		28	52
Operating Assets Total					1,406,730	1,360,353
Strategic Developments						
HHC 242 Self Storage Facility	October 2021	3.05	% (b)	6,658	866	—
HHC 2978 Self Storage Facility	January 2022	3.05	% (b)	6,368	—	—
Lakeland Village Center	May 2020	2.80	% (b)	14,000	8,514	—
Merriweather Post Pavilion	October 2021	2.45	% (b)	9,500	158	—
One Merriweather	February 2020	2.60	% (b)	49,900	3,988	—
Three Hughes Landing	December 2017	2.80	% (b)	65,455	33,200	23,268
Waiea and Anaha Condominiums	November 2019	7.20	% (b)	600,000	150,025	27,817
Strategic Developments Total					196,751	51,085
Other Corporate Financing Arrangements	June 2018	3.00	%		17,372	18,794
Senior Notes	October 2021	6.88	%		750,000	750,000
Unamortized underwriting fees					(6,282)	(6,767)
Deferred Financing Costs, net					(10,434)	(12,392)

Total mortgages, notes, and loans payable	$ 2,651,805	$ 2,443,962

(a) Maturity date includes any extension periods that can be exercised at our option at the initial maturity date, subject to customary extension terms that based on current property performance projections, we expect to meet. Such terms may include but are not limited to minimum debt service coverage, minimum occupancy levels and other performance criteria.
(b) The interest rate presented is based on the one month LIBOR rate, which was 0.45% at June 30, 2016.

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

(c) $40.0 million of the outstanding principal balance is swapped to a 3.41% fixed-rate through maturity.
(d) The $24.6 million outstanding principal balance is swapped to a 5.21% fixed-rate through maturity.
(e) $143.0 million of the outstanding principal balance is swapped to a 3.81% fixed-rate through maturity. As of June 30, 2016 there is no undrawn availability on this facility. Management expects to refinance this note in the third quarter 2016.

The weighted average interest rate on our mortgages, notes and loans payable, excluding interest rate hedges, was 4.56% and 4.44% as of June 30, 2016 and December 31, 2015, respectively.

All of the mortgage debt is secured by the individual properties listed in the table above and is non-recourse to HHC, except for:

(i) $750.0 million of Senior Notes;
(ii) $311.8 million financing for the Downtown Summerlin development which has an initial maximum recourse of 35% of the outstanding balance, which will reduce to 15.0% upon completion of the project and achievement of a 1.15:1.0 debt service coverage ratio. The recourse further reduces to 10% upon achievement of a 1.25:1.0 debt service coverage ratio, a 90% occupancy level, and average tenant sales of at least $500.00 per net rentable square foot. As of June 30, 2016, 35% of the outstanding loan balance remains recourse to HHC;
(iii) $64.4 million of construction financing for the Outlet Collection at Riverwalk with an initial maximum recourse of 50% of the outstanding balance, which will be reduced to 25.0% upon completion of the project and the achievement of an 11.0% debt yield and a minimum level of tenant sales per square foot for twelve months. As of June 30, 2016, 50% of the outstanding loan balance remains recourse to HHC;
(iv) $17.4 million of Other Corporate Financing Arrangements; and
(v) $7.0 million of the 110 N. Wacker mortgage.

Certain of our loans contain provisions which grant the lender a security interest in the operating cash flow of the property that represents the collateral for the loan. Certain mortgage notes may be prepaid, but may be subject to a prepayment penalty equal to a yield maintenance premium, defeasance, or a percentage of the loan balance. As of June 30, 2016, land, buildings and equipment and developments with a cost basis of $2.4 billion have been pledged as collateral for our mortgages, notes and loans payable.

As of June 30, 2016, we were in compliance with all of the financial covenants related to our debt agreements.

Master Planned Communities

On November 9, 2015, we refinanced $15.2 million of existing debt in connection with closing on a modification which increased the Bridgeland Credit Facility to $65.0 million. The facility bears interest at three-month LIBOR plus 3.15%, with a 4.60% floor, and has an initial maturity date of November 2020 with two, one-year extension options. The proceeds are intended to provide working capital at Bridgeland for development efforts necessary to meet the demand of homebuilders for finished lots in the community.

The Woodlands Master Credit Facility was amended and restated on July 31, 2015 to a $200.0 million maximum facility amount consisting of a $100.0 million term loan and a $100.0 million revolver (together, the "TWL Facility"). The TWL Facility bears interest at one-month LIBOR plus 2.75% and has an August 2016 initial maturity date with two, one–year extension options. In July, we exercised our first one-year extension option, which requires a reduction of the total commitment to $175.0 million and semi-annual principal payments of $25.0 million beginning on December 31, 2016 and continuing through a second, optional one-year extension period. The TWL Facility and The Woodlands Resort & Conference Center loans are recourse to the entities that directly own The Woodlands operations. The TWL Facility also contains certain covenants that, among other things, require the maintenance of specified financial ratios, limit the incurrence of additional recourse indebtedness at The Woodlands, and limit distributions from The Woodlands to us based

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

on a loan to value test. The amendment also modified certain covenants to allow for more construction loan guarantees by the entities that directly own The Woodlands than would otherwise have been permitted by the prior facility.

The Summerlin MPC uses SID bonds to finance certain common infrastructure improvements. These bonds are issued by the municipalities and are secured by the assessments on the land. The majority of proceeds from each bond issued is held in a construction escrow and disbursed to us as infrastructure projects are completed, inspected by the municipalities and approved for reimbursement. Accordingly, the SID bonds have been classified as debt, and the Summerlin MPC pays the debt service on the bonds semi annually. As Summerlin sells land, the buyers assume a proportionate share of the bond obligation at closing, and the residential sales contracts provide for the reimbursement of the principal amounts that we previously paid with respect to such proportionate share of the bond. In 2016, no new SID bonds have been issued and $3.4 million in obligations were assumed by buyers.

Operating Assets

Our $250.0 million first mortgage financing secured by the Ward Centers bears interest at LIBOR plus 2.50% and matures on September 29, 2016. There was no undrawn availability on the $238.7 million balance as of June 30, 2016, and a refinance of the facility is currently underway and expected to close in the third quarter 2016.

Strategic Developments

On February 25, 2016, we closed on a $49.9 million non-recourse construction loan for One Merriweather. The loan bears interest at one-month LIBOR plus 2.15% with an initial maturity date of February 25, 2020, with a one-year extension option. $0.2 million was drawn on this loan as of June 30, 2016.

On January 27, 2016, we closed on a $6.4 million non-recourse construction loan for the HHC 2978 Self-Storage Facility, bearing interest at one-month LIBOR plus 2.60% with an initial maturity date of January 2020, with two, one-year extension options. No amounts were drawn on this loan as of June 30, 2016.

Corporate

On October 2, 2013, we issued $750.0 million in aggregate principal amount of 6.875% Senior Notes due 2021 (the “Senior Notes”). Interest is payable semiannually, on April 1 and October 1 of each year. At any time prior to October 1, 2016, we may redeem up to 35% of the Senior Notes at a price equal to 106.875% using the proceeds from equity offerings. We may redeem all or part of the Senior Notes at any time with a declining call premium thereafter to maturity. The Senior Notes contain customary terms and covenants for non investment grade senior notes and have no maintenance covenants.

NOTE 10 DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

We are exposed to interest rate risk related to our variable interest rate debt, and we manage this risk by utilizing interest rate derivatives. Our objective in using interest rate derivatives is to add stability to interest costs by reducing our exposure to interest rate movements. To accomplish this objective, we use interest rate swaps, forward-starting swaps, and caps as part of our interest rate risk management strategy. As of June 30, 2016, we had interest rate swaps with gross notional amounts of $207.6 million and a $100.0 million interest rate cap, both of which were designated as effective cash flow hedges of interest rate risk. We also have $250.0 million in gross notional amounts of forward-starting interest rate swaps that become effective December 31, 2017 to hedge a portion of anticipated future fixed-rate debt issuance.

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

Interest rate swaps designated as cash flow hedges involve the receipt of variable amounts from a counterparty in exchange for the Company's fixed rate payments over the life of the agreements without exchange of the underlying notional amount. The three forward-starting interest rate swaps are designated as cash flow hedges of the variability of the anticipated interest rate of our long-term financing needs at our Downtown Summerlin property. Interest rate caps designated as cash flow hedges involve the receipt of variable amounts from a counterparty if interest rates rise above the strike rate on the contract in exchange for an up front premium.

The effective portion of changes in the fair value of derivatives designated and that qualify as cash flow hedges is recorded in Accumulated Other Comprehensive Income ("AOCI") and is subsequently reclassified into earnings in the period that the hedged forecasted transaction affects earnings. The ineffective portion of the change in fair value of the derivatives is recognized directly in earnings. During the six months ended June 30, 2016 and June 30, 2015, the ineffective portion recorded in earnings was insignificant.

If the derivative contracts are terminated prior to their maturity, the amounts previously recorded in AOCI are recognized into earnings over the period that the hedged transaction impacts earnings. If the hedging relationship is discontinued because it is probable that the forecasted transaction will not occur according to the original strategy, any related amounts previously recorded in AOCI are recognized in earnings immediately.

Amounts reported in AOCI related to derivatives will be reclassified to interest expense as interest payments are made on our variable rate debt. Over the next 12 months, we estimate that an additional $1.3 million will be reclassified to interest expense.

The table below presents the fair value of our derivative financial instruments, which are included in accounts payable and accrued liabilities in the condensed consolidated balance sheets:

(In thousands)	June 30, 2016	December 31, 2015
Interest Rate Swaps & Caps	$ 3,037	$ 2,292
Forward-Starting Swaps	24,692	1,925

Total derivatives designated as hedging instruments	$ 27,729	$ 4,217

22

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

The tables below present the effect of our derivative financial instruments on the condensed consolidated statements of operations for the three and six months ended June 30, 2016 and 2015:

	Three Months Ended June 30,			Three Months Ended June 30,	
	2016	2015		2016	2015
(In thousands) Cash Flow Hedges	Amount of (Loss) Recognized in OCI	Amount of (Loss) Recognized in OCI	Location of Loss Reclassified from AOCI into Earnings	Amount of (Loss) Reclassified from AOCI into Earnings	Amount of (Loss) Reclassified from AOCI into Earnings
Interest Rate Swaps & Caps	$ (328)	$ (240)	Interest Expense	$ (367)	$ (436)
Forward-Starting Swaps	(5,629)	—	Interest Expense	—	—
	$ (5,957)	$ (240)		$ (367)	$ (436)

	Six Months Ended June 30,			Six Months Ended June 30,	
	2016	2015		2016	2015
(In thousands) Cash Flow Hedges	Amount of (Loss) Recognized in OCI	Amount of (Loss) Recognized in OCI	Location of Loss Reclassified from AOCI into Earnings	Amount of (Loss) Reclassified from AOCI into Earnings	Amount of (Loss) Reclassified from AOCI into Earnings
Interest Rate Swaps & Caps	$ (1,206)	$ (103)	Interest Expense	$ (743)	$ (811)
Forward-Starting Swaps	(14,910)	—	Interest Expense	—	—
	$ (16,116)	$ (103)		$ (743)	$ (811)

NOTE 11 INCOME TAXES

Unrecognized tax benefits pursuant to uncertain tax positions were $36.5 million as of June 30, 2016 and December 31, 2015, respectively, none of which would impact our effective tax rate.

We have significant permanent differences, primarily from warrant liability gains and losses and changes in valuation allowances that cause our effective tax rate to deviate from statutory rates. The effective tax rates, based upon actual operating results, were 79.3% and 37.9% for the three and six months ended June 30, 2016 compared to 7.8% and (13.4)% for the three and six months ended June 30, 2015. The changes in the tax rates were primarily attributable to changes in the warrant liability, valuation allowance related to our deferred tax assets, as well as other items which are permanent differences for tax purposes.

The increase in deferred tax liabilities between December 31, 2015 and June 30, 2016 is due primarily to the utilization of federal tax assets used to offset the tax gain on the sale of the 80 South Street Assemblage.

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

NOTE 12 STOCK BASED PLANS

Our stock based plans are described and informational disclosures are provided in the Notes to the Consolidated Financial Statements included in our Form 10-K for the year ended December 31, 2015.

Stock Options

The following table summarizes our stock option plan:

	Stock Options	Weighted Average Exercise Price
Stock Options outstanding at December 31, 2015	1,086,040	$ 77.11
Granted	136,500	108.64
Forfeited	(33,000)	118.23
Stock Options outstanding at June 30, 2016	1,189,540	79.55

Compensation costs related to stock options were $0.5 million and $2.3 million for the three and six months ended June 30, 2016, respectively, of which $0.2 million and $0.8 million were capitalized to development projects during the same periods. Stock option costs were $1.2 million and $1.8 million for the three and six months ended June 30, 2015, respectively, of which $0.6 million and $1.1 million were capitalized to development projects during the same periods.

Restricted Stock

The following table summarizes restricted stock activity:

	Restricted Stock	Weighted Average Grant Date Fair Value

Restricted stock outstanding at December 31, 2015	242,556	$ 100.15
Granted	131,198	65.79
Vested	(37,670)	83.47
Forfeited	(4,985)	86.48
Restricted Stock outstanding at June 30, 2016	331,099	88.64

Compensation expense related to restricted stock awards was $1.8 million and $3.4 million for the three and six months ended June 30, 2016, respectively, of which $0.3 million and $0.6 million were capitalized to development projects during the same periods. Compensation expense related to restricted stock awards was $1.4 million and $2.5 million for the three and six months ended June 30, 2015, respectively, of which $0.3 million and $0.5 million were capitalized to development projects during the same periods.

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

NOTE 13 OTHER ASSETS AND LIABILITIES

Prepaid Expenses and Other Assets

The following table summarizes the significant components of Prepaid expenses and other assets.

(In thousands)	June 30, 2016	December 31, 2015
Condominium receivables (a)	$ 423,906	$ 191,037
Condominium deposits	91,661	55,749
Special Improvement District receivable	72,594	72,558
In-place leases	17,033	22,139
Below-market ground leases	19,155	19,325
Above-market tenant leases	2,714	3,581
Equipment, net of accumulated depreciation of $4.7 million and $3.9 million, respectively	18,182	18,772
Security and escrow deposits	9,855	17,599
Tenant incentives and other receivables	9,873	10,480
Prepaid expenses	8,205	8,474
Federal income tax receivable	12,106	11,972
Intangibles	4,124	4,045
Uncertain tax position asset	143	112
Other	3,080	5,347
	$ 692,631	$ 441,190

(a) Of the total Condominium receivables, $329.7 million are expected to be collected in 2016 and $94.2 million are expected to be collected in 2017, consistent with anticipated closings of the respective condominium projects.

The $251.4 million net increase primarily relates to the following increases: a $232.9 million increase in condominium receivables, which represents revenue recognized in excess of buyer deposits received for our Ward Village Condominium projects, an increase in condominium deposits of $35.9 million due to deposits for sales of units and $0.2 million in other increases.

These increases were partially offset by the following decreases: a net $7.7 million decrease in security and escrow deposits mostly attributable to our January 2016 investment in the Grandview SHG, LLC joint venture; a decrease of $5.1 million relating primarily to the amortization of in-place leases; a net decrease in other prepaids of $2.3 million which was primarily due to the reimbursement from a tenant in the three months ended June 30, 2016; and a $2.5 million decrease in other small net changes.

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

Accounts Payable and Accrued Expenses

The following table summarizes the significant components of Accounts payable and accrued expenses.

(In thousands)	June 30, 2016	December 31, 2015
Construction payables	$ 193,847	$ 185,731
Deferred income	114,634	117,700
Condominium deposit liabilities	87,428	50,192
Accounts payable and accrued expenses	37,687	33,928
Tenant and other deposits	32,896	31,193
Accrued interest	16,627	16,504
Accrued payroll and other employee liabilities	20,142	31,271
Accrued real estate taxes	12,935	15,134
Interest rate swaps	27,729	4,217
Above-market ground leases	2,034	2,113
Other	26,813	27,371
	$ 572,772	$ 515,354

Total accounts payable and accrued expenses increased by $57.4 million. This net increase primarily includes the following increases: a $37.2 million increase in condominium deposits liability; an increase of $3.8 million in accounts payable and accrued expenses; an increase of $8.1 million in construction payables; an increase of $23.5 million in interest rate swaps liability primarily due to a decrease in fair value of the forward-starting swaps; and $1.8 million in other immaterial increases.

These increases are partially offset by the following decreases: decrease of $11.1 million in accrued payroll and other employee liabilities due to payment in the first quarter 2016 of the 2015 annual incentive bonus; a decrease of $2.2 million in accrued real estate taxes related to timing of payments; a decrease of $3.1 million in deferred income; and $0.6 million in other immaterial decreases.

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

NOTE 14 ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS) ("AOCI")

The following table summarizes AOCI for the period indicated:

	For the Three Months Ended June 30, 2016	For the Three Months Ended June 30, 2015
Balance as of March 31	$ (17,760)	$ (7,259)
Other comprehensive loss before reclassifications	(6,759)	(293)
Loss reclassified from accumulated other comprehensive loss to net income (loss)	367	436
Net current-period other comprehensive income (loss)	(6,392)	143
Balance as of June 30	$ (24,152)	$ (7,116)

	For the Six Months Ended June 30, 2016	For the Six Months Ended June 30, 2015
Balance as of December 31	$ (7,889)	$ (7,712)
Other comprehensive loss before reclassifications	(17,006)	(215)
Loss reclassified from accumulated other comprehensive loss to net income (loss)	743	811
Net current-period other comprehensive loss	(16,263)	596
Balance as of June 30	$ (24,152)	$ (7,116)

The following table summarizes the amounts reclassified out of AOCI for the period indicated:

	Amounts reclassified from Accumulated Other Co Income (Loss)		
Accumulated Other Comprehensive Income (Loss) Components	For the Three Months Ended June 30, 2016	For the Six Months Ended June 30, 2016	Affected line item in the Statement of Operations
Losses on cash flow hedges	$ 588	$ 1,193	Interest expense

Interest rate swap contracts	(221)	(450)	Provision for income taxes
Total reclassifications for the period	$ 367	$ 743	Net of tax

Accumulated Other Comprehensive Income (Loss) Components	Amounts reclassified from Accumulated Other Comprehensive Income (Loss) For the Three Months Ended June 30, 2015	For the Six Months Ended June 30, 2015	Affected line item in the Statement of Operations
Losses on cash flow hedges	$ 705	$ 1,301	Interest expense
Interest rate swap contracts	(269)	(490)	Provision for income taxes
Total reclassifications for the period	$ 436	$ 811	Net of tax

NOTE 15 COMMITMENTS AND CONTINGENCIES

In the normal course of business, from time to time, we are involved in legal proceedings relating to the ownership and operations of our properties. In management's opinion, the liabilities, if any, that may ultimately result from such legal actions are not expected to have a material effect on our consolidated financial position, results of operations or liquidity.

We had outstanding letters of credit and surety bonds totaling $98.4 million and $86.1 million as of June 30, 2016 and December 31, 2015, respectively. These letters of credit and bonds were issued primarily in connection with insurance requirements, special real estate assessments and construction obligations.

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

On June 27, 2013, the City of New York executed the amended and restated ground lease for South Street Seaport. The restated lease terms provide for annual fixed base rent of $1.2 million starting July 1, 2013 with an expiration of December 30, 2072, including our options to extend. The rent escalates at 3.0% compounded annually. On July 1, 2048 the base rent will be adjusted to the higher of the fair market value or the then base rent. In addition to the annual base rent, we are required to make annual payments of $210,000 as additional rent through the term of the lease. The additional rent escalates annually at the Consumer Price Index. Simultaneously with the execution of the lease, we executed a completion guaranty for the redevelopment of Pier 17 by 2017.

In the fourth quarter 2012, the historic area of South Street Seaport suffered damage due to flooding as a result of Superstorm Sandy. Reconstruction efforts are ongoing and the property has only partially operated over the last three years. We have received $54.1 million in insurance proceeds, and we recognized Other income of $6.2 million and $0.3 million for the six months ended June 30, 2016 and June 30, 2015, respectively, for the receipt of insurance proceeds related to our claim. This matter is currently being litigated with an insurance carrier, and there can be no assurance that we will collect additional insurance proceeds.

NOTE 16 SEGMENTS

We have three business segments which offer different products and services. Our three segments are managed separately because each requires different operating strategies and management expertise and are reflective of management's operating philosophies and methods. In addition, our segments or assets within such segments could change in the future as development of certain properties commences or other operational or management changes occur. All operations are within the United States, and we do not distinguish or group our combined operations on a geographic basis. Our reportable segments are as follows:

· Master Planned Communities ("MPCs") – includes the development and sale of land, in large scale, long term community development projects in and around Las Vegas, Nevada; Houston, Texas; and Columbia, Maryland.

· Operating Assets – includes retail, office, hospitality and multi-family properties along with other real estate investments. These assets are currently generating revenues, and are comprised of commercial real estate properties developed or acquired by us, and properties where we believe there is an opportunity to redevelop, reposition, or sell to improve segment performance or to recycle capital.

- Strategic Developments – includes our residential condominium and commercial property projects currently under development and all other properties held for development which have no substantial operations.

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

The assets included in each segment as of June 30, 2016, are contained in the following chart:

Master Planned Communities	Operating Assets		Strategic Developments
	Retail	Office	Under Construction
• Bridgeland	Columbia Regional Building	10-70 Columbia Corporate Center	Ae'o
• Maryland	Cottonwood Square	Columbia Office Properties	Anaha
• Summerlin	Creekside Village Green (b)	1725-35 Hughes Landing Boulevard (b)	Constellation (a)
• The Woodlands	Downtown Summerlin	One Hughes Landing	HHC 242 Self-Storage
• The Woodlands Hills	Hughes Landing Retail (b)	Two Hughes Landing	HHC 2978 Self-Storage
	1701 Lake Robbins	2201 Lake Woodlands Drive	Lakeland Village Center
	Landmark Mall	9303 New Trails	m.flats (formerly Parcel C) (a)
Other	Outlet Collection at Riverwalk	110 N. Wacker	One Merriweather
• The Summit (a)	Park West	ONE Summerlin (b)	Three Hughes Landing
	South Street Seaport	3831 Technology Forest Drive	Waiea
	(under construction)	3 Waterway Square	
	Ward Village	4 Waterway Square	Other
	20/25 Waterway Avenue	1400 Woodloch Forest	Alameda Plaza
	Waterway Garage Retail		AllenTowne
			Bridges at Mint Hill
	Multi-family	Other	Century Plaza Mall
	Millennium Waterway Apartments	Clark County Las Vegas Stadium (a)	Circle T Ranch and Power Center (a)
	Millennium Woodlands Phase II (a)	Kewalo Basin Harbor	
		Merriweather Post Pavilion	Cottonwood Mall
	One Lakes Edge (b)	Stewart Title of Montgomery County, TX (a)	80% Interest in Fashion Show Air Rights
	85 South Street		
	The Metropolitan Downtown Columbia (a) (b)	Summerlin Hospital Medical Center (a)	Gateway Towers
			Ke Kilohana
		The Woodlands Parking Garages	Kendall Town Center
	Hospitality	Woodlands Sarofim #1 (a)	Lakemoor (Volo) Land

Embassy Suites at Hughes Landing (b)	Maui Ranch Land
Grandview SHG, LLC (a)	The Outlet Collection at Elk Grove
The Woodlands Resort & Conference Center	Two Merriweather
	West Windsor
The Westin at The Woodlands (c)	

(a) A non-consolidated investment. Refer to Note 8 – Real Estate and Other Affiliates.
(b) Asset was placed in service and moved from the Strategic Developments segment to the Operating Assets segment during 2015.
(c) Asset was placed in service and moved from the Strategic Developments segment to the Operating Assets segment during 2016.

Our segments are managed separately, therefore, we use different operating measures to assess operating results and allocate resources among the segments. The one common operating measure used to assess operating results for the business segments is Real Estate Property Earnings Before Taxes ("REP EBT"), which represents the operating revenues of the properties less property operating expenses and adjustments for interest, as further described below. We believe that REP EBT provides useful information about the operating performance of all of our properties.

REP EBT, as it relates to our business, is defined as net income (loss) excluding general and administrative expenses, corporate other income, corporate interest income, corporate interest and depreciation expense, provision for income taxes, and warrant liability gain (loss). We present REP EBT because we use this measure, among others, internally to assess the core operating performance of our assets. We also present this measure because we believe certain investors use it as a measure of a company's historical operating performance and its ability to service and incur debt. We believe that the inclusion of certain adjustments to net income (loss) to calculate REP EBT is appropriate to provide additional information to investors.

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

Segment operating results are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(In thousands)	2016	2015	2016	2015
Master Planned Communities				
Land sales	$ 61,098	$ 45,433	$ 103,040	$ 93,514
Builder price participation	6,501	7,907	11,148	13,606
Minimum rents	142	215	282	429
Other land revenues	2,749	3,140	5,772	6,426
Other rental and property revenues	17	9	20	7
Total revenues	70,507	56,704	120,262	113,982
Cost of sales – land	29,008	24,236	44,696	48,132
Land sales operations	5,506	9,721	12,806	17,300
Land sales real estate and business taxes	2,300	2,242	4,594	4,646
Depreciation and amortization	81	95	164	190
Interest income	(5)	(15)	(21)	(31)
Interest expense (*)	(5,004)	(4,684)	(10,343)	(9,446)
Equity in earnings in Real Estate and Other Affiliates	(8,874)	—	(8,874)	—
Total expenses, net of other income	23,012	31,595	43,022	60,791
MPC EBT	47,495	25,109	77,240	53,191
Operating Assets				
Minimum rents	41,811	36,697	82,929	71,009
Tenant recoveries	10,914	10,693	21,437	20,266
Hospitality revenues	19,129	11,481	32,038	23,484
Other rental and property revenues	4,416	6,971	7,499	13,245
Total revenues	76,270	65,842	143,903	128,004
Other property operating costs	13,830	18,350	27,948	35,836
Real estate taxes	6,709	5,990	12,851	11,510
Rental property maintenance costs	2,645	2,785	5,646	5,412
Hospitality costs	14,242	8,893	24,717	17,971
Provision for doubtful accounts	(353)	1,266	2,626	2,075
Demolition costs	6	1,496	478	1,613
Development-related marketing costs	1,988	2,748	3,088	5,014
Depreciation and amortization	22,613	22,887	43,814	41,649
Other income, net	(2,750)	—	(3,113)	—
Interest income	(8)	(9)	(16)	(19)

Interest expense	10,116	7,629	19,269	14,123
Equity in earnings from Real Estate and Other Affiliates	(899)	(160)	(2,826)	(1,044)
Total expenses, net of other income	68,139	71,875	134,482	134,140
Operating Assets EBT	8,131	(6,033)	9,421	(6,136)
Strategic Developments				
Minimum rents	83	77	134	744
Tenant recoveries	9	8	14	102
Condominium rights and unit sales	125,112	86,513	247,206	121,370
Other land revenues	10	5	20	12
Other rental and property revenues	160	14	278	39
Total revenues	125,374	86,617	247,652	122,267
Condominium rights and unit cost of sales	79,726	56,765	154,541	79,174
Other property operating costs	1,406	1,284	3,030	1,943
Real estate taxes	620	578	1,226	1,258
Rental property maintenance costs	108	115	239	232
Provision for doubtful accounts	1	—	63	—
Demolition costs	484	—	484	—
Development-related marketing costs	4,351	2,846	7,782	6,823
Depreciation and amortization	660	601	1,319	1,617
Other income, net	—	—	(244)	(334)
Interest income	(125)	(166)	(131)	(166)
Interest expense (*)	(1,899)	(1,580)	(3,033)	(3,385)
Equity in earnings from Real Estate and Other Affiliates	(10,502)	(921)	(10,507)	(1,825)
Gain on sale of 80 South Street Assemblage	—	—	(140,479)	—
Total expenses, net of other income	74,830	59,522	14,290	85,337
Strategic Developments EBT	50,544	27,095	233,362	36,930
REP EBT	$ 106,170	$ 46,171	$ 320,023	$ 83,985

(*) Negative interest expense amounts are due to interest capitalized in our Master Planned Communities and Strategic Developments segments related to Operating Assets segment debt and the Senior Notes.

Table of Contents

THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

The following reconciles REP EBT to GAAP income (loss) before taxes:

Reconciliation of REP EBT to GAAP income (loss) before taxes	Three Months Ended June 30,		Six Months Ended June 30,	
(In thousands)	2016	2015	2016	2015
REP EBT	$ 106,170	$ 46,171	$ 320,023	$ 83,985
General and administrative	(20,053)	(19,606)	(40,377)	(38,569)
Corporate interest expense, net	(13,023)	(13,235)	(26,097)	(26,447)
Warrant liability gain (loss)	(44,150)	42,620	(14,330)	(66,190)
Corporate other income, net	6,317	396	6,069	1,529
Corporate depreciation and amortization	(1,598)	(1,487)	(2,627)	(3,124)
Income (loss) before taxes	$ 33,663	$ 54,859	$ 242,661	$ (48,816)

The following reconciles segment revenues to GAAP consolidated revenues:

Reconciliation of Segment Basis Revenues to GAAP Revenues	Three Months Ended June 30,		Six Months Ended June 30,	
(In thousands)	2016	2015	2016	2015
Master Planned Communities	$ 70,507	$ 56,704	$ 120,262	$ 113,982
Operating Assets	76,270	65,842	143,903	128,004
Strategic Developments	125,374	86,617	247,652	122,267
Total revenues	$ 272,151	$ 209,163	$ 511,817	$ 364,253

The assets by segment and the reconciliation of total segment assets to the total assets in the condensed consolidated balance sheets are summarized as follows:

(In thousands)	June 30, 2016	December 31, 2015
Master Planned Communities	$ 2,006,094	$ 2,022,524
Operating Assets	2,496,917	2,365,724
Strategic Developments	1,525,312	1,138,695
Total segment assets	6,028,323	5,526,943

Corporate and other	189,296	194,639
Total assets	$ 6,217,619	$ 5,721,582

The $386.6 million increase in the Strategic Developments segment asset balance as of June 30, 2016 compared to December 31, 2015 is primarily due to the net change resulting from receipt of sale proceeds in excess of our cost basis relating to the 80 South Street Assemblage transaction and increased development expenditures primarily at Waiea, Anaha, Ae'o and One Merriweather. These increases were partially offset by sales recognized and deposits utilized for construction at Waiea and Anaha, and placing The Westin at The Woodlands in service in the Operating Assets segment.

The increase in the Operating Assets segment asset balance as of June 30, 2016 of $131.2 million compared to December 31, 2015 is primarily due to placing The Westin at The Woodlands in service and additional development expenditures at South Street Seaport.

The decrease in the MPC segment assets primarily relates to distributions of cash from the MPC segment to the corporate parent.

Table of Contents

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

The following discussion and analysis should be read in conjunction with the Consolidated Financial Statements and Notes included in this Quarterly Report and in the Company's Form 10-K for the year ended December 31, 2015. All references to numbered Notes are to specific notes to our Condensed Consolidated Financial Statements included in this Quarterly Report.

Forward-looking information

We may make forward-looking statements in this Quarterly Report and in other reports that we file with the SEC. In addition, our management may make forward-looking statements orally to analysts, investors, creditors, the media and others.

Forward-looking statements include:

- projections and expectations regarding our revenues, operating income, net income, earnings per share, REP EBT, Net Operating Income ("NOI"), capital expenditures, income tax, other contingent liabilities, dividends, leverage, capital structure or other financial items;
- forecasts of our future economic performance; and
- descriptions of assumptions underlying or relating to any of the foregoing.

In this Quarterly Report, we make forward-looking statements discussing our expectations about:

- capital required for our operations and development opportunities for the properties in our Operating Assets and Strategic Developments segments;
- expected performance of our Master Planned Communities segment and other current income producing properties; and
- future liquidity, development opportunities, development spending and management plans.

Forward-looking statements give our current expectations relating to our financial condition, results of operations, plans, objectives, future performance and business. You can identify forward-looking statements by the fact that they do not relate strictly to current or historical facts. These statements may include words such as "anticipate," "believe," "estimate," "expect," "forecast," "intend," "likely," "may," "plan," "project," "realize," "should," "transform," "would," and ot similar expression. Forward-looking statements should not be relied upon. They give our expectations about the future

and are not guarantees.

There are several factors, many beyond our control, which could cause results to differ materially from our expectations. These risk factors are described in our Annual Report on Form 10-K for the year ended December 31, 2015 (the "Annual Report") and are incorporated herein by reference. Any factor could, by itself, or together with one or more other factors, adversely affect our business, results of operations or financial condition. There may be other factors that we have not described in this Quarterly Report or in our Annual Report that could cause results to differ from our expectations. These forward-looking statements present our estimates and assumptions as of the date of this Quarterly Report. Except as may be required by law, we undertake no obligation to modify or revise any forward-looking statements to reflect events or circumstances occurring after the date of this Quarterly Report.

Real Estate Property Earnings Before Taxes

We use a number of operating measures for assessing operating performance of properties within our segments, some of which may not be common among all three of our segments. We believe that investors may find some operating measures more useful than others when separately evaluating each segment. One common operating measure used to assess operating results for our business segments is Real Estate Property Earnings Before Taxes ("REP EBT"). We believe REP EBT provides useful information about the operating performance of our properties because it excludes certain non-

recurring and non-cash items which we believe are not indicative of our core business. REP EBT may be calculated differently by other companies in our industry, limiting its usefulness as a comparative measure.

REP EBT, as it relates to our business, is defined as net income (loss) excluding general and administrative expenses, corporate other income, corporate interest income, corporate interest and depreciation expense, provision for income taxes, and warrant liability gain (loss). We present REP EBT because we use this measure, among others, internally to assess the core operating performance of our assets. We also present this measure because we believe certain investors use it as a measure of a company's historical operating performance and its ability to service and incur debt. We believe that the inclusion of certain adjustments to net income (loss) to calculate REP EBT is appropriate to provide additional information to investors. A reconciliation of REP EBT to consolidated net income (loss) as computed in accordance with GAAP has been presented in Note 16 – Segments. We also provide a measure of Adjusted Operating Assets REP EBT, which excludes depreciation and amortization, demolition costs and development-related marketing costs. A reconciliation of Adjusted Operating Assets EBT to Operating Assets EBT is included in the Operating Assets discussion.

REP EBT and Adjusted Operating Assets REP EBT should not be considered as alternatives to GAAP net income (loss) attributable to common stockholders or GAAP net income (loss), as they have limitations as analytical tools, and should not be considered in isolation, or as a substitute for analysis of our results as reported under GAAP. Some of the limitations of these metrics are that they do not include the following:

- cash expenditures, or future requirements for capital expenditures or contractual commitments;
- corporate general and administrative expenses;
- interest expense on our corporate debt;
- income taxes that we may be required to pay;
- any cash requirements for replacement of fully depreciated or amortized assets; and
- limitations on, or costs related to, transferring earnings from our Real Estate and Other Affiliates to us.

Operating Assets Net Operating Income

We believe that net operating income ("NOI") is a useful supplemental measure of the performance of our Operating Assets because it provides a performance measure that, when compared year over year, reflects the revenues and expenses directly associated with owning and operating real estate properties and the impact on operations from trends in rental and occupancy rates and operating costs. We define NOI as operating revenues (rental income, tenant recoveries and other revenue) less operating expenses (real estate taxes, repairs and maintenance, marketing and other property expenses). NOI excludes straight line rents and amortization of tenant incentives, net interest expense, ground rent amortization, demolition costs, amortization, depreciation, development-related marketing costs and Equity in earnings from Real Estate and Other Affiliates. We use NOI to evaluate our operating performance on a property-by-property basis because NOI allows us to evaluate the impact that factors, which vary by property, such as lease structure, lease rates and tenant base have on our operating results, gross margins and investment returns.

Although we believe that NOI provides useful information to investors about the performance of our Operating Assets, due to the exclusions noted above, NOI should only be used as an additional measure of the financial performance of such assets and not as an alternative to GAAP net income (loss). For reference, and as an aid in understanding our computation of NOI, a reconciliation of Operating Assets NOI to Operating Assets REP EBT has been presented in the Operating Assets segment discussion below.

Results of Operations

Our revenues are primarily derived from the sale of individual lots to homebuilders at our master planned communities, from tenants at our operating assets in the form of fixed minimum rents, overage rent and recoveries of operating expenses and from the sale of condominium units.

Table of Contents

The following table reflects our results of operations for the three and six months ended June 30, 2016 and 2015, respectively:

	Three Months Ended June 30,			Six Months Ended June 30,		
(In thousands, except per share amounts)	2016	2015	Change	2016	2015	Change
Revenues						
MPC segment revenues	$ 70,507	$ 56,704	$ 13,803	$ 120,262	$ 113,982	$ 6,280
Operating Assets segment revenues	76,270	65,842	10,428	143,903	128,004	15,899
Strategic Developments segment revenues	125,374	86,617	38,757	247,652	122,267	125,385
Total revenues	$ 272,151	$ 209,163	$ 62,988	$ 511,817	$ 364,253	$ 147,564
MPC segment REP EBT	$ 47,495	$ 25,109	$ 22,386	$ 77,240	$ 53,191	$ 24,049
Operating Assets segment REP EBT	8,131	(6,033)	14,164	9,421	(6,136)	15,557
Strategic Developments segment REP EBT	50,544	27,095	23,449	233,362	36,930	196,432
Total segment REP EBT (a)	106,170	46,171	59,999	320,023	83,985	236,038
General and administrative	(20,053)	(19,606)	(447)	(40,377)	(38,569)	(1,808)
Corporate interest expense, net	(13,023)	(13,235)	212	(26,097)	(26,447)	350
Warrant liability (loss) gain	(44,150)	42,620	(86,770)	(14,330)	(66,190)	51,860
Corporate other income, net	6,317	396	5,921	6,069	1,529	4,540
Corporate depreciation and amortization	(1,598)	(1,487)	(111)	(2,627)	(3,124)	497
Provision for income taxes	(26,693)	(4,274)	(22,419)	(91,926)	(6,558)	(85,368)
Net income (loss)	6,970	50,585	(43,615)	150,735	(55,374)	206,109
Net income attributable to noncontrolling interests	—	(12)	12	—	(12)	12
Net income (loss) attributable to common stockholders	$ 6,970	$ 50,573	$ (43,603)	$ 150,735	$ (55,386)	$ 206,121
Diluted income (loss) per share	$ 0.16	$ 0.18	$ (0.02)	$ 3.53	$ (1.40)	$ 4.94

(a) Total segment REP EBT includes depreciation and amortization expense. Non-cash total segment depreciation and amortization, primarily relating to Operating Assets recently placed into service, is currently offsetting the net operating income generated from these properties because they typically will not stabilize for 12 – 36 months after they are placed into service, but the full amount of their annual depreciation and amortization begins when they are placed into service. The following table shows the amounts included in segment REP EBT related to non-cash depreciation and amortization:

	Three Months Ended June 30,			Six Months Ended June 30,		
(In thousands)	2016	2015	Change	2016	2015	Change
Total segment depreciation and amortization	$ 23,354	$ 23,583	$ (229)	$ 45,297	$ 43,456	$ 1,841

Total revenues for the three and six months ended June 30, 2016 increased compared to the same period in 2015 due to higher revenues in our MPC, Operating Assets and Strategic Developments segments. The MPC segment revenues increase is due to higher residential land sales in our MPCs for the three and six months ended June 30, 2016 as compared to the same periods in 2015. Strategic Developments segment revenue increased due to higher revenue related to sales at our Waiea and Anaha condominium projects, which are currently reported on the percentage of completion method. Operating Assets segment revenue increased primarily due to assets placed in service in 2016 and 2015, including 1725-1735 Hughes Landing Boulevard, The Westin at The Woodlands, Embassy Suites at Hughes Landing, Hughes Landing Retail, One Lakes Edge and ONE Summerlin, and the ongoing stabilization of Downtown Summerlin.

General and administrative expenses for the three and six months ended June 30, 2016 increased compared to the same periods in 2015. For the three months ended June 30, 2016, the increase is primarily due to $0.8 million of higher compensation costs related to headcount, offset by $0.6 million of decreased travel costs compared to the same period in the prior year. For the six months ended June 30, 2016, the increase is primarily due to $1.2 million of higher compensation costs related to headcount compared to the same period in the prior year.

Provision for income taxes increased for the three and six months ended June 30, 2016 due to increases in pre-tax earnings, as noted on the Condensed Consolidated Statement of Operations, adjusted to exclude the non-taxable warrant gain (loss) which has no impact on our tax provision.

Table of Contents

We have significant permanent differences, primarily due to warrant liability gains and losses and changes in valuation allowances that cause our effective tax rate to deviate greatly from statutory rates. The effective tax rates, based upon actual operating results were 79.3% and 37.9% for the three and six months ended June 30, 2016 compared to 7.8% and (13.4)% for the three and six months ended June 30, 2015. The changes in the tax rate were primarily attributable to changes in the warrant liability, valuation allowance related to our deferred tax asset, as well as other items which are permanent differences for tax purposes. If changes in the warrant liability, valuation allowance, unrecognized tax benefits, and other material discrete adjustments to deferred tax liabilities were excluded from the effective tax rate computation, the adjusted effective tax rates would have been 36.7% and 37.0% for the three and six months ended June 30, 2016, respectively, compared to 34.9% and 34.7% for three and six months ended June 30, 2015.

The decrease in Net income attributable to common stockholders for the three months ended June 30, 2016 compared to the same period in 2015 is primarily due to a higher warrant liability loss, offset by increased REP EBT in our MPC, Operating Assets and Strategic Developments segments. The increase in Net income (loss) attributable to common stockholders for the six months ended June 30, 2016 compared to the same period in 2015 is primarily due to a gain on the sale of the 80 South Street Assemblage included in Strategic Developments segment REP EBT, significant growth in earnings from condominium rights and unit sales in Strategic Developments segment revenues, a lower warrant liability loss and moderately increased REP EBT in our MPC and Operating Assets segments. These increases were partially offset by an increased provision for income taxes.

Please refer to the individual segment operations sections that follow for explanations of segment performance.

Segment Operations

Please refer to Note 16 - Segments for additional information including reconciliations of our segment basis results to generally accepted accounting principles (“GAAP”) basis results.

Table of Contents

Master Planned Communities Revenues and Expenses(*)

For the three months ended June 30, 2016 and 2015

(In thousands, except %)

	Bridgeland		Maryland Communities		Summerlin		The Woodlands		The Woo Hills
(In thousands)	2016	2015	2016	2015	2016	2015	2016	2015	2016
Land sales (e)	$ 4,500	$ 1,495	$ —	$ —	$ 55,212	$ 34,832	$ 1,386	$ 9,106	$ —
Builder price participation	180	398	—	—	5,425	6,280	896	1,229	—
Minimum rents	—	—	—	—	142	215	—	—	—
Other land sale revenues	34	65	2	1	2,604	1,676	104	1,398	5
Other rental and property revenues	—	—	—	—	13	9	—	—	4
Total revenues	4,714	1,958	2	1	63,396	43,012	2,386	11,733	9
Cost of sales - land	1,532	532	—	—	26,904	20,592	572	3,112	—
Land sales operations	1,259	942	39	99	1,811	3,671	2,350	5,006	47
Land sales real estate and business taxes	251	73	158	162	613	919	1,255	1,060	23
Depreciation and amortization	23	29	5	6	23	30	30	30	—
Total expenses	3,065	1,576	202	267	29,351	25,212	4,207	9,208	70
Operating income	1,649	382	(200)	(266)	34,045	17,800	(1,821)	2,525	(61)
Interest expense, net (a)	(2,220)	(2,320)	2	(7)	(4,090)	(3,537)	1,443	1,296	(144)
	—	—	—	—	(8,874)	—	—	—	—

Equity in earnings in Real Estate and Other Affiliates									
MPC REP EBT	$ 3,869	$ 2,702	$ (202)(c)	$ (259)(c)	$ 47,009	$ 21,337	$ (3,264)(d)	$ 1,229	$ 83
Gross Margin % (b)	66.0 %	64.4 %	NM	NM	51.3 %	40.9 %	58.7 %	65.8 %	NM

(*) For a reconciliation of MPC REP EBT to consolidated income (loss) before taxes, refer to Note 16 – Segments.

(a) Negative interest expense amounts relate to interest capitalized on debt assigned to our Operating Assets segment and corporate debt.
(b) Gross Margin % is the ratio of Land sales less Cost of sales-land, divided by Land sales.
(c) The negative MPC REP EBT in Maryland is due to no land sales in 2016 or 2015; however, certain costs such as real estate taxes and administrative expenses continue to be incurred.
(d) The number of residential lots sold decreased from 43 to nine for the three months ended June 30, 2016 compared to the same period in 2015, resulting in negative MPC REP EBT at The Woodlands.
(e) Land sales includes deferred revenue from land sales closed in a previous period which met criteria for recognition in the current period.
NM – Not meaningful

Interest expense, net reflects the amount of interest that is capitalized at the project level.

Although our business does not involve the sale or resale of homes, we believe that net new home sales are an important indicator of future demand for our superpad sites and lots; therefore, we use this statistic where relevant in the discussion of our MPC operating results. Net new home sales reflect home sales made by homebuilders, less cancelations. Cancelations occur when a home buyer signs a contract to purchase a home, but later fails to qualify for a home mortgage or is unable to provide an adequate down payment to complete the home sale.

Table of Contents

Master Planned Communities Revenues and Expenses(*)

For the six months ended June 30, 2016 and 2015

(In thousands, except %)

	Bridgeland		Maryland Communities		Summerlin		The Woodlands		The Woo Hills
(In thousands)	2016	2015	2016	2015	2016	2015	2016	2015	2016
Land sales (e)	$ 8,782	$ 6,073	$ —	$ —	$ 80,004	$ 71,120	$ 14,254	$ 16,321	$ —
Builder price participation	435	522	—	—	9,314	10,542	1,399	2,542	—
Minimum rents	—	—	—	—	282	429	—	—	—
Other land sale revenues	109	201	3	53	5,421	3,455	234	2,717	5
Other rental and property revenues	—	—	—	—	16	7	—	—	4
Total revenues	9,326	6,796	3	53	95,037	85,553	15,887	21,580	9
Cost of sales - land	2,979	2,203	—	—	36,045	40,387	5,672	5,542	—
Land sales operations	2,262	1,930	120	202	4,317	6,363	6,008	8,802	99
Land sales real estate and business taxes	487	147	323	328	1,155	1,855	2,583	2,288	46
Depreciation and amortization	47	59	10	10	47	61	60	60	—
Total expenses	5,775	4,339	453	540	41,564	48,666	14,323	16,692	145
Operating income	3,551	2,457	(450)	(487)	53,473	36,887	1,564	4,888	(136)
Interest expense, net (a)	(4,686)	(4,597)	(7)	(17)	(8,456)	(7,056)	3,066	2,517	(281)
Equity in earnings in Real Estate	—	—	—	—	(8,874)	—	—	—	—

and Other Affiliates									
MPC REP EBT	$ 8,237	$ 7,054	$ (443)(c)	$ (470)(c)	$ 70,803	$ 43,943	$ (1,502)(d)	$ 2,371	$ 145
Gross Margin % (b)	66.1 %	63.7 %	NM	NM	54.9 %	43.2 %	60.2 %	66.0 %	NM

(*) For a reconciliation of MPC REP EBT to consolidated income (loss) before taxes, refer to Note 16 – Segments.

(a) Negative interest expense amounts relate to interest capitalized on debt assigned to our Operating Assets segment and corporate debt.
(b) Gross margin % is the ratio of Land sales less Cost of sales-land, divided by Land sales.
(c) The negative MPC REP EBT in Maryland is due to no land sales in 2016 or 2015; however, certain costs such as real estate taxes and administrative expenses continue to be incurred.
(d) The number of residential lots sold decreased from 89 to 26 for the six months ended June 30, 2016 compared to the same period in 2015, resulting in negative MPC REP EBT at The Woodlands.
(e) Land sales includes deferred revenue from land sales closed in a previous period which met criteria for recognition in the current period.
NM – Not meaningful

MPC revenues vary between periods based on economic conditions and several factors such as, but not limited to, location, availability of land for sale, development density and residential or commercial use. Gross margin for each MPC may vary from period to period based on the locations of the land sold and the related costs associated with developing the land sold. Reported results may differ significantly from actual cash flows generated principally because cost of sales for GAAP purposes is derived from margins calculated using carrying values, projected future improvements and other capitalized project costs in relation to projected future land sale revenues. Carrying values, generally, represent acquisition and development costs reduced by any previous impairment charges. Development expenditures are capitalized and generally not reflected in the condensed consolidated statements of operations in the current period.

Builder price participation revenue is based on an agreed-upon percentage of the estimated sales price of the home relative to the base lot price.

Cost of sales – land includes both actual and estimated future costs allocated based upon relative sales value to the lots or land parcels in each of the villages and neighborhoods in our MPCs.

Table of Contents

Summary of MPC Land Sales Closed in the Three Months Ended June 30,

	Land Sales		Acres Sold		Number of Lots/Units		Price per acre		Price per lot	
($ In thousands)	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015
Bridgeland										
Residential										
Single family - detached	$ 4,656	$ 1,495	12.9	3.7	68	19	$ 361	$ 404	$ 68	$ 79
Total	4,656	1,495	12.9	3.7	68	19	361	404	68	79
$ Change	3,161		9.2		49		(43)		(11)	
% Change	211.4%		248.6%		257.9%		(10.6%)		(13.9%)	
Maryland Communities										
No land sales										
Summerlin										
Residential										
Superpad sites	26,987	29,256	53.4	52.0	316	155	505	563	85	189
Custom lots	505	3,775	0.3	2.5	1	6	1,683	1,510	505	629
Commercial										
Not-for-profit	348	—	10.0	—	—	—	35	—	—	—
Other	—	3,136	—	3.6	—	—	—	871	—	—
Total	27,840	36,167	63.7	58.1	317	161	437	622	87	205
$ Change	(8,327)		5.6		156		(185)		(118)	
% Change	(23.0%)		9.6%		96.9%		(29.7%)		(57.6%)	
The Woodlands										
Residential										
Single family - detached	1,386	7,052	2.3	12.2	9	43	603	578	154	164
Commercial										