HOVNANIAN ENTERPRISES INC
Form 10-Q
June 04, 2010

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)
[X] Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For quarterly period ended APRIL 30, 2010
OR

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

Commission file number 1-8551

Hovnanian Enterprises, Inc. (Exact Name of Registrant as Specified in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)

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

110 West Front Street, P.O. Box 500, Red Bank, NJ 07701 (Address of Principal Executive Offices)

732-747-7800 (Registrant's Telephone Number, Including Area Code)

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer”, “accelerated filer” and “smaller reporting

company” in Rule 12b-2 of the Exchange Act.
Large Accelerated Filer [ ] Accelerated Filer [X]
Non-Accelerated Filer [ ] (Do not check if smaller reporting company) Smaller Reporting Company [ ]

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. 63,079,514 shares of Class A Common Stock and 14,565,395 shares of Class B Common Stock were outstanding as of June 2, 2010.

HOVNANIAN ENTERPRISES, INC.

FORM 10-Q

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In Thousands Except Share Amounts)

ASSETS	April 30, 2010 (unaudited)	October 31, 2009 (1)
Homebuilding:		
Cash and cash equivalents	$448,142	$419,955
Restricted cash	126,569	152,674
Inventories:		
Sold and unsold homes and lots under development	617,951	631,302
Land and land options held for future development or sale	429,661	372,143
Consolidated inventory not owned:		
Specific performance options	22,028	30,534
Variable interest entities	36,839	45,436
Other options	19,659	30,498
Total consolidated inventory not owned	78,526	106,468
Total inventories	1,126,138	1,109,913
Investments in and advances to unconsolidated joint ventures	40,307	41,260
Receivables, deposits, and notes	55,717	44,418
Property, plant, and equipment – net	68,443	73,918
Prepaid expenses and other assets	90,376	98,159
Total homebuilding	1,955,692	1,940,297
Financial services:		
Cash and cash equivalents	10,430	6,737
Restricted cash	2,541	4,654
Mortgage loans held for sale or investment	58,054	69,546
Other assets	2,384	3,343
Total financial services	73,409	84,280

Total assets	$2,029,101	$2,024,577

(1) Derived from the audited balance sheet as of October 31, 2009.

See notes to condensed consolidated financial statements (unaudited).

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In Thousands Except Share Amounts)

LIABILITIES AND EQUITY	April 30, 2010 (unaudited)	October 31, 2009 (1)
Homebuilding:		
Nonrecourse land mortgages	$9,083	$-
Accounts payable and other liabilities	301,168	325,722
Customers' deposits	14,874	18,811
Nonrecourse mortgages secured by operating properties	21,089	21,507
Liabilities from inventory not owned	69,805	96,908
Total homebuilding	416,019	462,948
Financial services:		
Accounts payable and other liabilities	11,480	14,507
Mortgage warehouse line of credit	47,784	55,857
Total financial services	59,264	70,364
Notes payable:		
Senior secured notes	783,852	783,148
Senior notes	736,058	822,312
Senior subordinated notes	120,170	146,241
Accrued interest	24,471	26,078
Total notes payable	1,664,551	1,777,779
Income tax payable	26,294	62,354
Total liabilities	2,166,128	2,373,445
Equity:		
Hovnanian Enterprises, Inc. stockholders' equity deficit:		
Preferred stock, $.01 par value - authorized 100,000 shares; issued 5,600 shares at April 30, 2010 and at October 31, 2009 with a liquidation preference of $140,000	135,299	135,299
Common stock, Class A, $.01 par value – authorized		

200,000,000 shares; issued 74,765,527 shares at April 30, 2010 and 74,376,946 shares at October 31, 2009 (including 11,694,720 shares at April 30, 2010 and October 31, 2009 held in Treasury)	748	744
Common stock, Class B, $.01 par value (convertible to Class A at time of sale) – authorized 30,000,000 shares; issued 15,257,143 shares at April 30, 2010 and 15,265,067 shares at October 31, 2009 (including 691,748 shares at April 30, 2010 and October 31, 2009 held in Treasury)	153	153
Paid in capital - common stock	459,752	455,470
Accumulated deficit	(618,452)	(826,007)
Treasury stock - at cost	(115,257)	(115,257)
Total Hovnanian Enterprises, Inc. stockholders' equity deficit	(137,757)	(349,598)
Non-controlling interest in consolidated joint ventures	730	730
Total equity deficit	(137,027)	(348,868)
Total liabilities and equity	$2,029,101	$2,024,577

(1) Derived from the audited balance sheet as of October 31, 2009.

See notes to condensed consolidated financial statements (unaudited).

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In Thousands Except Per Share Data)
(unaudited)

	Three Months Ended April 30, 2010	2009	Six Months Ended April 30, 2010	2009
Revenues:				
Homebuilding:				
Sale of homes	$310,493	$381,698	$619,846	$740,750
Land sales and other revenues	1,033	7,274	3,719	13,687
Total homebuilding	311,526	388,972	623,565	754,437
Financial services	7,059	9,027	14,665	17,346
Total revenues	318,585	397,999	638,230	771,783
Expenses:				
Homebuilding:				
Cost of sales, excluding interest	256,926	351,148	516,742	691,823
Cost of sales interest	18,745	26,040	38,593	49,169
Inventory impairment loss and land option write-offs	1,186	310,194	6,152	420,375
Total cost of sales	276,857	687,382	561,487	1,161,367
Selling, general and administrative	42,359	60,822	85,431	131,866
Total homebuilding expenses	319,216	748,204	646,918	1,293,233
Financial services	5,631	6,510	11,026	13,258
Corporate general and administrative	14,203	18,359	30,416	49,269
Other interest	23,356	18,524	48,963	42,754
Other operations	1,767	4,935	3,664	6,559
Total expenses	364,173	796,532	740,987	1,405,073
Gain on extinguishment of debt	17,217	311,268	19,791	390,788
Income (loss) from unconsolidated joint ventures	391	(10,094)	18	(32,683)
Loss before income taxes	(27,980)	(97,359)	(82,948)	(275,185)

State and federal income tax provision (benefit):				
State	657	21,221	828	21,776
Federal	(3)	41	(291,331)	70
Total taxes	654	21,262	(290,503)	21,846
Net (loss) income	$(28,634)	$(118,621)	$207,555	$(297,031)
Per share data:				
Basic:				
(Loss) income per common share	$(0.36)	$(1.50)	$2.64	$(3.80)
Weighted average number of common shares outstanding	78,668	79,146	78,610	78,154
Assuming dilution:				
(Loss) income per common share	$(0.36)	$(1.50)	$2.60	$(3.80)
Weighted average number of common shares outstanding	78,668	79,146	79,794	78,154

See notes to condensed consolidated financial statements (unaudited).

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF EQUITY
(In Thousands Except Share Amounts)
(unaudited)

	A Common Stock		B Common Stock		Preferred Stock				
	Shares Issued and Outstanding	Amount	Shares Issued and Outstanding	Amount	Shares Issued and Outstanding	Amount	Paid-In Capital	Accumulated Deficit	T
Balance, November 1, 2009	62,682,226	$744	14,573,319	$153	5,600	$135,299	$455,470	$(826,007)	$(
Stock options amortization and issuances, net of tax	132,590	1					2,518		
Restricted stock amortization, issuances and forfeitures, net of tax	248,067	3					1,764		
Conversion of Class B to Class A Common Stock	7,924		(7,924)						
Net income								207,555	
Balance, April 30, 2010	63,070,807	$748	14,565,395	$153	5,600	$135,299	$459,752	$(618,452)	$(

See notes to condensed consolidated financial statements (unaudited).

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In Thousands)
(unaudited)

	Six Months Ended April 30, 2010	Six Months Ended April 30, 2009
Cash flows from operating activities:		
Net income (loss)	$207,555	$(297,031)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation	6,457	9,286
Compensation from stock options and awards	4,515	8,943
Stock option cancellations	-	12,269
Amortization of bond discounts and deferred financing costs	2,471	620
(Gain) loss on sale and retirement of property and assets	(43)	108
(Income) loss from unconsolidated joint ventures	(18)	32,683
Distributions of earnings from unconsolidated joint ventures	1,697	1,518
Gain on extinguishment of debt	(19,791)	(390,788)
Inventory impairment and land option write-offs	6,152	420,375
Decrease (increase) in assets:		
Mortgage notes receivable	11,492	31,467
Restricted cash, receivables, prepaids, deposits and other assets	24,911	34,498
Inventories	(22,377)	217,448
State and Federal income tax assets	-	126,826
(Decrease) increase in liabilities:		
State and Federal income tax	(36,060)	40,427
Customers' deposits	(3,937)	(6,361)
Accounts payable, interest and other accrued liabilities	(56,518)	(138,222)
Net cash provided by operating activities	126,506	104,066
Cash flows from investing activities:		
Net proceeds from sale of property and assets	153	861
Purchase of property, equipment and other fixed assets and acquisitions	(947)	(262)
Investments in and advances to unconsolidated joint ventures	(2,553)	(9,660)
Distributions of capital from unconsolidated joint ventures	1,827	4,488
Net cash used in investing activities	(1,520)	(4,573)

Cash flows from financing activities:		
Proceeds (payments) from mortgages and notes	8,665	(453)
Net proceeds related to revolving credit agreement (including deferred financing costs)	-	100,000
Net payments related to mortgage warehouse line of credit	(8,074)	(35,610)
Deferred financing costs from note issuances	(1,391)	(3,586)
Principal payments and debt repurchases	(92,306)	(224,764)
Net cash used in financing activities	(93,106)	(164,413)
Net increase (decrease) in cash and cash equivalents	31,880	(64,920)
Cash and cash equivalents balance, beginning of period	426,692	848,056
Cash and cash equivalents balance, end of period	$458,572	$783,136

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In Thousands - Unaudited)
(Continued)

	Six Months Ended April 30,	
	2010	2009
Supplemental disclosures of cash flow:		
Cash paid (received) during the period for:		
Interest, net of capitalized interest	$89,370	$96,763
Income taxes	$(254,443)	$(145,408)

Supplemental disclosure of noncash financing activities:

In the first quarter of fiscal 2009, the Company issued $29.3 million of 18.0% Senior Secured Notes due 2017 in exchange for $71.4 million of unsecured senior notes.

See notes to condensed consolidated financial statements (unaudited).

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - UNAUDITED

Hovnanian Enterprises, Inc. (“the Company”, “the Parent”, “we”, “us” or “our”) has reportable segments consisting of six Homebuilding segments (Northeast, Mid-Atlantic, Midwest, Southeast, Southwest and West) and the Financial Services segment (see Note 15).

The accompanying unaudited Condensed Consolidated Financial Statements include our accounts and those of all wholly-owned subsidiaries after elimination of all intercompany balances and transactions. Certain immaterial prior year amounts have been reclassified to conform to the current year presentation.

1. The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, all adjustments for interim periods presented have been made, which include normal recurring accruals and deferrals necessary for a fair presentation of our consolidated financial position, results of operations, and cash flows. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates, and these differences could have a significant impact on the financial statements. Results for interim periods are not necessarily indicative of the results which might be expected for a full year. The balance sheet at October 31, 2009 has been derived from the audited Consolidated Financial Statements at that date but does not include all of the information and footnotes required by GAAP for complete financial statements.

Effective July 1, 2009, the Financial Accounting Standards Board (“FASB”) established the Accounting Standards Codification (“ASC”) as the primary source of accounting principles generally accepted in the United States of America (“US GAAP”) recognized by the FASB to be applied by nongovernmental entities. Although the establishment of the ASC did not change US GAAP, it did change the way we refer to US GAAP throughout this document to reflect the updated referencing convention.

2. For the three and six months ended April 30, 2010, the Company’s total stock-based compensation expense was $2.2 million and $4.5 million, respectively. Included in this total stock-based compensation expense was the vesting of stock options of $1.3 million and $2.5 million for the three and six months ended April 30, 2010, respectively.

3. Interest costs incurred, expensed and capitalized were:

	Three Months Ended April 30,		Six Months Ended April 30,	
(In thousands)	2010	2009	2010	2009
Interest capitalized at beginning of period	$159,026	$176,258	$164,340	$170,107
Plus interest incurred(1)	38,201	47,588	78,342	101,098
Less cost of sales interest expensed	18,745	26,040	38,593	49,169
Less other interest expensed(2)(3)	23,356	18,524	48,963	42,754
Interest capitalized at end of period(4)	$155,126	$179,282	$155,126	$179,282

(1) Data does not include interest incurred by our mortgage and finance subsidiaries.
(2) Our assets that qualify for interest capitalization (inventory under development) do not exceed our debt, and therefore, the portion of interest not covered by qualifying assets must be directly expensed.
(3) Interest on completed homes and land in planning, which does not qualify for capitalization, must be expensed directly.
(4) We have incurred significant inventory impairments in recent years, which are determined based on total inventory including capitalized interest. However, the capitalized interest amounts shown above are gross amounts before allocating any portion of the impairments to capitalized interest.

4. Accumulated depreciation at April 30, 2010 and October 31, 2009 amounted to $71.5 million and $67.4 million, respectively, for our homebuilding property, plant and equipment.

5. We record impairment losses on inventories related to communities under development and held for future development when events and circumstances indicate that they may be impaired and the undiscounted cash flows estimated to be generated by those assets are less than their related carrying amounts. If the expected undiscounted cash flows are less than the carrying amount, then the community is written down to its fair value. We estimated the fair value of each impaired community by determining the present value of the estimated future cash flows at a discount rate commensurate with the risk of the respective community. For the six months ended April 30, 2010, our discount rates used for the impairments recorded ranged from 17.5% to 18.5%. Should the estimates or expectations used in determining cash flows or fair value decrease or differ from current estimates in the future, we may be required to recognize additional impairments. We recorded inventory impairments, which are presented in the Condensed Consolidated Statements of Operations as “Inventory impairment and land option write-offs” and deducted from Inventory of $1.2 million and $301.1 million for the three months ended April 30, 2010 and 2009, respectively, and $4.5 million and $396.8 million for the six months ended April 30, 2010 and 2009, respectively.

The following table represents inventory impairments by homebuilding segment for the three and six months ended April 30, 2010 and 2009:

(Dollars in millions)	Three Months Ended April 30, 2010			Three Months Ended April 30, 2009		
	Number of Communities	Dollar Amount of Impairment	Pre-Impairment Value(1)	Number of Communities	Dollar Amount of Impairment	Pre-Impairment Value(1)
Northeast	1	$0.5	$1.0	8	$108.0	$175.7
Mid-Atlantic	1	0.2	0.9	24	13.4	54.3
Midwest	-	-	-	4	4.0	12.0
Southeast	1	-	0.2	41	17.6	49.9
Southwest	1	0.1	0.2	29	23.4	52.3
West	1	0.4	0.4	37	134.7	255.7
Total	5	$1.2	$2.7	143	$301.1	$599.9

(Dollars in millions)	Six Months Ended April 30, 2010			Six Months Ended April 30, 2009		
	Number of Communities	Dollar Amount of Impairment	Pre-Impairment Value(1)	Number of Communities	Dollar Amount of Impairment	Pre-Impairment Value(1)
Northeast	2	$3.1	$5.7	19	$161.6	$326.8

Mid-Atlantic	2	0.5	1.5	37	26.3	95.3
Midwest	-	-	-	4	4.0	12.0
Southeast	6	0.4	1.2	56	25.5	82.3
Southwest	1	0.1	0.2	34	26.4	63.1
West	1	0.4	0.4	40	153.0	299.5
Total	12	$4.5	$9.0	190	$396.8	$879.0

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

"Homebuilding-Inventory impairment loss and land option write-offs" on the Condensed Consolidated Statements of Operations also includes write-offs of options, and approval, engineering and capitalized interest costs that we record when we redesign communities and/or abandon certain engineering costs and we do not intend to exercise options in various locations because the communities' proforma profitability is not projected to produce adequate returns on investment commensurate with the risk. The total write-offs were zero and $9.1 million for the three months ended April 30, 2010 and 2009, respectively, and $1.7 million and $23.6 million for the six months ended April 30, 2010 and 2009, respectively. Occasionally, these write-offs are offset by recovered deposits (sometimes through legal action) that had been written off in a prior period as walk-away costs.

The following table represents write-offs of such costs (after giving effect to any recovered deposits in the applicable period) and the number of lots walked away from by homebuilding segment for the three and six months ended April 30, 2010 and 2009:

	Three Months Ended April 30,				Six Months Ended April 30,			
	2010		2009		2010		2009	
(Dollars in millions)	Number of Walk-Away Lots	Dollar Amount of Write-Offs	Number of Walk-Away Lots	Dollar Amount of Write-Offs	Number of Walk-Away Lots	Dollar Amount of Write-Offs	Number of Walk-Away Lots	Dollar Amount of Write-Offs
Northeast	-	$(0.1)	103	$2.2	259	$1.5	606	$6.5
Mid-Atlantic	173	0.1	452	2.3	184	0.1	1,902	8.5
Midwest	-	-	158	1.4	-	(0.1)	158	1.4
Southeast	-	-	-	(0.4)	-	0.1	153	(0.1)
Southwest	409	-	474	3.3	409	0.1	758	6.7
West	-	-	-	0.3	-	-	-	0.6
Total	582	$-	1,187	$9.1	852	$1.7	3,577	$23.6

We have decided to mothball (or stop development on) certain communities in some of our segments where we have determined the current performance does not justify further investment at this time. When we decide to mothball a community, the inventory is reclassified from “Sold and unsold homes and lots under development” to “Land and land options held for future development or sale”. During the second quarter of fiscal 2010, we mothballed three communities and re-activated six previously mothballed communities, which is the primary cause of the net change in the book value of our mothballed communities of $11.9 million, net of an impairment reserve balance of $29.8 million. As of April 30, 2010, the net book value associated with our 67 total mothballed communities was $275.9 million, net of an impairment reserve balance of $530.8 million.

6. We establish a warranty accrual for repair costs under $5,000 per occurrence to homes, community amenities and land development infrastructure. We accrue for warranty costs as part of cost of sales at the time each home is closed and title and possession have been transferred to the homebuyer. In addition, we accrue for warranty costs over

$5,000 per occurrence as part of our general liability insurance deductible, which is expensed as selling, general and administrative costs. For homes delivered in fiscal 2010 and 2009, our deductible under our general liability insurance is $20 million per occurrence with an aggregate $20 million for liability claims and an aggregate $21.5 million for construction defect claims. Additions and charges in the warranty reserve and general liability accrual for the three and six months ended April 30, 2010 and 2009 were as follows:

(In thousands)	Three Months Ended April 30, 2010	Three Months Ended April 30, 2009	Six Months Ended April 30, 2010	Six Months Ended April 30, 2009
Balance, beginning of period	$130,544	$125,976	$127,869	$125,738
Additions	9,543	9,533	19,445	21,047
Charges incurred	(12,737)	(16,622)	(19,964)	(27,898)
Balance, end of period	$127,350	$118,887	$127,350	$118,887

Warranty accruals are based upon historical experience. We engage a third-party actuary that uses our historical warranty data and other data to assist management estimate our unpaid claims, claim adjustment expenses and incurred but not reported claims reserves for the risks that we are assuming under the general liability and workers compensation programs. The estimates include provisions for inflation, claims handling and legal fees.

Insurance claims paid by our insurance carriers were $4.9 million and $9.2 million for the three months ended April 30, 2010 and 2009, respectively, and $10.2 million and $19.5 million for the six months ended April 30, 2010 and 2009, respectively.

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

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

As previously reported in the Company's 10-Q for the quarter ended January 31, 2010, the Company has been engaged in discussions with the U. S. Environmental Protection Agency ("EPA") and the U. S. Department of Justice ("DOJ") regarding alleged violations of storm water discharge requirements. In resolution of this matter, in April 2010 we agreed to the terms of a Consent Decree with the EPA, DOJ and the states of Virginia, Maryland, West Virginia and the District of Columbia (collectively the "States"). The Consent Decree, which was lodged in federal district court in April, is subject to a thirty-day public comment period which began in May 2010 and to court approval. The terms of the Consent Decree require us to pay a fine of $1.0 million collectively to the United States and the States and to perform under the terms of the Consent Decree for a minimum of three years, which includes implementing certain operational and training measures nationwide to facilitate ongoing compliance with storm water regulations.

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

The Company is also involved in the following litigation:

A subsidiary of the Company has been named as a defendant in a purported class action suit filed on May 30, 2007 in the United States District Court for the Middle District of Florida, Randolph Sewell, et al., v. D'Allesandro & Woodyard, et al., alleging violations of the federal securities acts, among other allegations, in connection with the sale of some of the subsidiary's homes in Fort Myers, Florida. Plaintiffs filed an amended complaint on October 19, 2007. Plaintiffs sought to represent a class of certain home purchasers in southwestern Florida and sought damages, rescission of certain purchase agreements, restitution of out-of-pocket expenses, and attorneys' fees and costs. The Company's subsidiary filed a Motion to Dismiss the amended complaint on December 14, 2007. Following oral argument on the Motion in September 2008, the court dismissed the amended complaint with leave for plaintiffs to amend. Plaintiffs filed a second amended complaint on October 31, 2008. The Company's subsidiary filed a Motion to Dismiss this second amended complaint. The Court dismissed portions of the second amended complaint. The Court dismissed additional portions of the second amended complaint on April 28, 2010. While we have determined that a loss related to this case is not probable, it is not possible to estimate a loss or range of loss related to this matter at this time.

8. Cash and cash equivalents include cash deposited in checking accounts, overnight repurchase agreements, certificates of deposit, Treasury Bills and government money market funds with maturities of 90 days or less when purchased. Our cash balances are held at a few financial institutions and may, at times, exceed insurable amounts. We believe we help to mitigate this risk by depositing our cash in major financial institutions. At April 30, 2010, $300.7 million of the total cash and cash equivalents was in cash equivalents, the book value of which approximates fair value.

9. In connection with the issuance of our senior secured first lien notes in the fourth quarter of fiscal 2009, we terminated our revolving credit facility and refinanced the borrowing capacity thereunder. Also in connection with the refinancing, we entered into certain stand alone cash collateralized letter of credit agreements and facilities under which there were a total of $107.5 million and $130.3 million of letters of credit outstanding as of April 30, 2010 and October 31, 2009, respectively. These agreements and facilities require us to maintain specified amounts of cash as collateral in segregated accounts to support the letters of credit issued thereunder, which will affect the amount of cash we have available for other uses. As of April 30, 2010 and October 31, 2009, the amount of cash collateral in these segregated accounts was $111.4 million and $135.2 million, respectively, which is reflected in "Restricted cash" on the Condensed Consolidated Balance Sheets.

Our wholly owned mortgage banking subsidiary, K. Hovnanian American Mortgage, LLC ("K. Hovnanian Mortgage"), originates mortgage loans primarily from the sale of our homes. Such mortgage loans and related servicing rights are sold in the secondary mortgage market within a short period of time. Our secured Master Repurchase Agreement with Citibank, N.A. is a short-term borrowing facility that provides up to $50 million through April 5, 2011. The loan is secured by the mortgages held for sale and is repaid when we sell the underlying mortgage loans to permanent investors. Interest is payable upon the sale of each mortgage loan to a permanent investor at LIBOR plus 4.00%. As of April 30, 2010, the aggregate principal amount of all borrowings under the Master Repurchase Agreement was $47.8 million. The Master Repurchase Agreement requires K. Hovnanian Mortgage to satisfy and maintain specified financial ratios and other financial condition tests. Because of the extremely short period of time mortgages are held by K. Hovnanian Mortgage before the mortgages are sold to investors (generally a period of a few weeks), the immateriality to us on a consolidated basis of the size of the facility, the levels required by these financial covenants, our ability based on our immediately available resources to contribute sufficient capital to cure any default, were such conditions to occur, and our right to cure any conditions of default based on the terms of the Master Repurchase Agreement, we do not consider any of these covenants to be substantive or material. As of April 30, 2010, we believe we were in compliance with the covenants of the Master Repurchase Agreement.

10. At April 30, 2010, we had $797.2 million ($783.9 million net of discount) of outstanding senior secured notes, comprised of $0.5 million 11 1/2% Senior Secured Notes due 2013, $785.0 million 10 5/8% Senior Secured Notes due

2016 and $11.7 million 18% Senior Secured Notes due 2017. At April 30, 2010 we also had $737.9 million of outstanding senior notes ($736.1 million net of discount), comprised of $35.5 million 8% Senior Notes due 2012, $56.4 million 6 1/2% Senior Notes due 2014, $38.2 million 6 3/8% Senior Notes due 2014, $66.4 million 6 1/4% Senior Notes due 2015, $173.2 million 6 1/4% Senior Notes due 2016, $172.3 million 7 1/2% Senior Notes due 2016 and $195.9 million 8 5/8% Senior Notes due 2017. In addition, we had $120.2 million of outstanding senior subordinated notes, comprised of $66.7 million 8 7/8% Senior Subordinated Notes due 2012, and $53.5 million 7 3/4% Senior Subordinated Notes due 2013.

During the three months ended January 31, 2010, the remaining $13.6 million of our 6% Senior Subordinated Notes due 2010 matured and was paid. In addition, during the three and six months ended April 30, 2010, we repurchased in open market transactions $25.0 million principal amount of our 6 1/2% Senior Notes due 2014, $35.5 million and $45.5 million principal amount of our 6 3/8% Senior Notes due 2014, respectively, $15.9 million principal amount of our 6 1/4% Senior Notes due 2015, $0.4 million and $1.4 million principal amount of 8 7/8% Senior Subordinated Notes due 2012, respectively, and $10.8 million and $11.1 million principal amount of 7 3/4% Senior Subordinated Notes due 2013, respectively. The aggregate purchase price for these repurchases was $70.0 million and $78.7 million, respectively, plus accrued and unpaid interest. These repurchases resulted in a gain on extinguishment of debt of $17.2 million and $19.8 million for the three and six months ended April 30, 2010, respectively, net of the write-off of unamortized discounts and fees. The gains from the repurchases are included in the Condensed Consolidated Statement of Operations for the three and six months ended April 30, 2010 as “Gain on extinguishment of debt”.

We and each of our subsidiaries are guarantors of the senior secured, senior and senior subordinated notes, except for K. Hovnanian Enterprises, Inc. (“K. Hovnanian”), the issuer of the notes, certain of our financial services subsidiaries, joint ventures and subsidiaries holding interests in our joint ventures and our foreign subsidiary (see Note 20). The indentures governing the senior secured, senior and senior subordinated notes do not contain any financial maintenance covenants, but do contain restrictive covenants that limit, among other things, the Company’s ability and that of certain of its subsidiaries, including K. Hovnanian, the issuer of the senior secured, senior and senior subordinated notes, to incur additional indebtedness (other than certain permitted indebtedness, refinancing indebtedness and non-recourse indebtedness), pay dividends and make distributions on common and preferred stock, repurchase senior notes and senior subordinated notes (with respect to the senior secured first-lien notes indenture), make other restricted payments, make investments, sell certain assets, incur liens, consolidate, merge, sell or otherwise dispose of all or substantially all assets and enter into certain transactions with affiliates. The indentures also contain events of default which would permit the holders of the senior secured, senior, and senior subordinated notes to declare those notes to be immediately due and payable if not cured within applicable grace periods, including the failure to make timely payments on the notes or other material indebtedness, the failure to comply with agreements and covenants and specified events of bankruptcy, and insolvency and, with respect to the indentures governing the senior secured notes, the failure of the documents granting security for the senior secured notes to be in full force and effect and the failure of the liens on any material portion of the collateral securing the senior secured notes to be valid and perfected. As of April 30, 2010, we believe we were in compliance with the covenants of the indentures governing our outstanding notes. Under the terms of the indentures, we have the right to make certain redemptions and, depending on market conditions and covenant restrictions, may do so from time to time. We may also continue to make debt purchases and/or exchanges from time to time through tender offers, open market purchases, private transactions, or otherwise depending on market conditions and covenant restrictions.

If our consolidated fixed charge coverage ratio, as defined in the indentures governing our senior secured, senior, and senior subordinated notes, is less than 2.0 to 1.0, we are restricted from making certain payments, including dividends, and from incurring indebtedness other than certain permitted indebtedness, refinancing indebtedness, and non-recourse indebtedness. As a result of this restriction, we are currently restricted from paying dividends on our 7.625% Series A Preferred Stock. If current market trends continue or worsen, we will continue to be restricted from paying dividends through fiscal 2010, and possibly beyond. Our inability to pay dividends is in accordance with covenant restrictions and will not result in a default under our bond indentures or otherwise affect compliance with any of the covenants contained in the bond indentures.

The 10 5/8% Senior Secured Notes due 2016 are secured by a first-priority lien, the 11 1/2% Senior Secured Notes due 2013 are secured by a second-priority lien and the 18% Senior Secured Notes due 2017 are secured by a third-priority lien, in each case, subject to permitted liens and other exceptions, on substantially all the assets owned by us, K. Hovnanian (the issuer of the senior secured notes) and the guarantors, in the case of the 11 1/2% Senior Secured Notes due 2013 and the 18% Senior Secured Notes due 2017, to the extent such assets secure obligations under the 10 5/8% Senior Secured Notes due 2016. At April 30, 2010, the aggregate book value of the real property collateral securing these notes was approximately $801.3 million, which does not include the impact of inventory investments, home deliveries, or impairments thereafter and which may differ from the appraised value. In addition, cash collateral securing these notes was $428.4 million as of April 30, 2010, which includes $111.4 million of restricted cash also collateralizing certain letters of credit. Subsequent to such date, cash uses include general business operations and real estate and other investments.

11. Each share of Class A Common Stock entitles its holder to one vote per share and each share of Class B Common Stock entitles its holder to ten votes per share. The amount of any regular cash dividend payable on a share of Class A Common Stock will be an amount equal to 110% of the corresponding regular cash dividend payable on a share of Class B Common Stock. If a shareholder desires to sell shares of Class B Common Stock, such stock must be converted into shares of Class A Common Stock.

Basic earnings per share is computed by dividing net income (the “numerator”) by the weighted-average number of common shares, adjusted for non-vested shares of restricted stock (the “denominator”) for the period. Computing diluted earnings per share is similar to computing basic earnings per share, except that the denominator is increased to include the dilutive effects of options and non-vested shares of restricted stock. Any options that have an exercise price greater than the average market price are considered to be anti-dilutive and are excluded from the diluted earnings per share calculation. For the six months ended April 30, 2010, diluted earnings per common share is computed using the weighted average number of shares outstanding adjusted for the 1.2 million incremental shares attributed to non-vested stock and outstanding options to purchase common stock. For the three months ended April 30, 2010, all stock options and non-vested restricted stock were excluded from the calculation as they were anti-dilutive during the period. As a result, the calculation of diluted earnings per share excludes 1.4 million, 1.2 million and 1.2 million of incremental shares attributed to non-vested stock and outstanding options to purchase stock for the three months ended April 30, 2010 and the three and six months ended April 30, 2009, respectively.

On July 3, 2001, our Board of Directors authorized a stock repurchase program to purchase up to 4 million shares of Class A Common Stock. There have been no purchases during the six months ended April 30, 2010. As of April 30, 2010, 3.4 million shares of Class A Common Stock have been purchased under this program.

12. On July 12, 2005, we issued 5,600 shares of 7.625% Series A Preferred Stock, with a liquidation preference of $25,000. Dividends on the Series A Preferred Stock are not cumulative and are payable at an annual rate of 7.625%. The Series A Preferred Stock is not convertible into the Company’s common stock and is redeemable in whole or in part at our option at the liquidation preference of the shares beginning on the fifth anniversary of their issuance. The Series A Preferred Stock is traded as depositary shares, with each depositary share representing 1/1000th of a share of Series A Preferred Stock. The depositary shares are listed on the NASDAQ Global Market under the symbol “HOVNP”. During the three and six months ended April 30, 2010 and 2009, we did not make any dividend payments on the Series A Preferred Stock as a result of covenant restrictions in the indentures governing our senior secured, senior and senior subordinated notes discussed above. We anticipate we will be restricted from paying dividends for the foreseeable future.

13. On August 4, 2008, we announced that our Board of Directors adopted a shareholder rights plan (the “Rights Plan”) designed to preserve shareholder value and the value of certain income tax assets primarily associated with net operating loss carryforwards (“NOL”) and built-in losses under Section 382 of the Internal Revenue Code. Our ability to

use NOLs and built-in losses would be limited if there was an “ownership change” under Section 382. This would occur if shareholders owning (or deemed under Section 382 to own) 5% or more of our stock increase their collective ownership of the aggregate amount of our outstanding shares by more than 50 percentage points over a defined period of time. The Rights Plan was adopted to reduce the likelihood of an “ownership change” occurring as defined by Section 382. Under the Rights Plan, one right was distributed for each share of Class A Common Stock and Class B Common Stock outstanding as of the close of business on August 15, 2008. Effective August 15, 2008, if any person or group acquires 4.9% or more of the outstanding shares of Class A Common Stock without the approval of the Board of Directors, there would be a triggering event causing significant dilution in the voting power of such person or group. However, existing stockholders who owned, at the time of the Rights Plan’s adoption, 4.9% or more of the outstanding shares of Class A Common Stock will trigger a dilutive event only if they acquire additional shares. The approval of the Board of Directors’ decision to adopt the Rights Plan may be terminated by the Board at any time, prior to the Rights being triggered. The Rights Plan will continue in effect until August 15, 2018, unless it expires earlier in accordance with its terms. The approval of the Board of Directors’ decision to adopt the Rights Plan was submitted to a stockholder vote and approved at a Special Meeting of stockholders held on December 5, 2008. Also at the Special Meeting on December 5, 2008, our stockholders approved an amendment to our Certificate of Incorporation to restrict certain transfers of Class A Common Stock in order to preserve the tax treatment of our net operating loss carryforwards and built-in losses under Section 382 of the Internal Revenue Code. Subject to certain exceptions pertaining to pre-existing 5% stockholders and Class B stockholders, the transfer restrictions in the amended Certificate of Incorporation generally restrict any direct or indirect transfer (such as transfers of our stock that result from the transfer of interests in other entities that own our stock) if the effect would be to: (i) increase the direct or indirect ownership of our stock by any person (or public group) from less than 5% to 5% or more of our common stock; (ii) increase the percentage of our common stock owned directly or indirectly by a person (or public group) owning or deemed to own 5% or more of our common stock; or (iii) create a new public group. Transfers included under the transfer restrictions include sales to persons (or public groups) whose resulting percentage ownership (direct or indirect) of common stock would exceed the 5% thresholds discussed above, or to persons whose direct or indirect ownership of common stock would by attribution cause another person (or public group) to exceed such threshold.

14. Total income tax provision was $0.7 million for the three months ended April 30, 2010, primarily due to an increase in tax reserves for uncertain tax positions. The total income tax benefit was $290.5 million for the six months ended April 30, 2010, primarily due to the benefit recognized for a federal net operating loss carryback. On November 6, 2009, President Obama signed the Worker, Homeownership, and Business Assistance Act of 2009, under which the Company was able to carryback its 2009 net operating loss five years to previously profitable years that were not available to the Company for carryback prior to this tax legislation. We recorded a benefit for the carryback of $291.3 million in the first quarter of fiscal 2010. We received $274.1 million of the federal income tax refund in the second quarter of 2010 and expect to receive the remaining $17.2 million later this fiscal year.

Deferred federal and state income tax assets primarily represent the deferred tax benefits arising from temporary differences between book and tax income which will be recognized in future years as an offset against future taxable income. If the combination of future years income (or loss) and the reversal of the timing differences results in a loss, such losses can be carried back to income in prior years, if available, or carried forward to future years to recover the deferred tax assets. In accordance with ASC 740 “Income Taxes” (ASC 740), we evaluate our deferred tax assets quarterly to determine if valuation allowances are required. ASC 740 requires that companies assess whether valuation allowances should be established based on the consideration of all available evidence using a "more likely than not" standard. Given the continued downturn in the homebuilding industry during 2007, 2008 and 2009, which has resulted in additional inventory and intangible impairments, we were in a three year cumulative loss position as of October 31, 2009. According to ASC 740, a three-year cumulative loss is significant negative evidence in considering whether deferred tax assets are realizable, and in this circumstance, the Company does not rely on projections of future taxable income to support the recovery of deferred tax assets. Our valuation allowance for current and deferred tax assets increased $7.6 million during the three months ended April 30, 2010 due to reserving for the federal tax benefit generated from the losses during the period. However, the allowance decreased $273.9 million during the six months ended April 30, 2010 primarily due to the impact of the federal net operating loss carryback recorded in the first quarter of 2010. At April 30, 2010, our total valuation allowance amounted to $713.7 million.

15. Our operating segments are components of our business for which discrete financial information is available and reviewed regularly by the chief operating decision-maker, our Chief Executive Officer, to evaluate performance and make operating decisions. We have 22 homebuilding operating segments, and therefore, it is impractical to provide segment disclosures for this many segments. As such, we have aggregated the homebuilding operating segments into six reportable segments.

Our homebuilding operating segments are aggregated into reportable segments based primarily upon geographic proximity, similar regulatory environments, land acquisition characteristics and similar methods used to construct and sell homes. The Company's reportable segments consist of the following six homebuilding segments and a financial services segment:

Homebuilding:
(1) Northeast (New Jersey, New York, Pennsylvania)
(2) Mid-Atlantic (Delaware, Maryland, Virginia, West Virginia, Washington D.C.)
(3) Midwest (Illinois, Kentucky, Minnesota, Ohio)
(4) Southeast (Florida, Georgia, North Carolina, South Carolina)
(5) Southwest (Arizona, Texas)
(6) West (California)

Financial Services

Operations of the Company's Homebuilding segments primarily include the sale and construction of single-family attached and detached homes, attached townhomes and condominiums, mid-rise condominiums, urban infill and active adult homes in planned residential developments. In addition, from time to time, the homebuilding segments include land sales. Operations of the Company's Financial Services segment include mortgage banking and title services provided to the homebuilding operations' customers. We do not retain or service mortgages that we originate but rather sell the mortgages and related servicing rights to investors.

Corporate and unallocated primarily represents operations at our headquarters in Red Bank, New Jersey. This includes our executive offices, information services, human resources, corporate accounting, training, treasury, process redesign, internal audit, construction services, and administration of insurance, quality, and safety. It also includes interest income and interest expense resulting from interest incurred that cannot be capitalized in inventory in the Homebuilding segments, as well as, the gains or losses on extinguishment of debt from debt repurchases or exchanges.

Evaluation of segment performance is based primarily on operating earnings from continuing operations before provision for income taxes ("(Loss) income before income taxes"). (Loss) income before income taxes for the Homebuilding segments consist of revenues generated from the sales of homes and land, (loss) income from unconsolidated entities, management fees and other income, less the cost of homes and land sold, selling, general and administrative expenses, interest expense and non-controlling interest expense. Income before income taxes for the Financial Services segment consist of revenues generated from mortgage financing, title insurance and closing services, less the cost of such services and certain selling, general and administrative expenses and interest expenses incurred by the Financial Services segment.

Operational results of each segment are not necessarily indicative of the results that would have occurred had the segment been an independent, stand-alone entity during the periods presented.

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

(In thousands)	Three Months Ended April 30, 2010	Three Months Ended April 30, 2009	Six Months Ended April 30, 2010	Six Months Ended April 30, 2009
Revenues:				
Northeast	$57,046	$86,402	$126,507	$173,447
Mid-Atlantic	67,716	71,336	134,739	140,841
Midwest	16,117	23,965	39,549	50,995
Southeast	22,375	33,663	47,160	68,787
Southwest	103,823	115,708	186,371	203,968
West	44,491	57,024	88,970	113,368
Total homebuilding	311,568	388,098	623,296	751,406
Financial services	7,059	9,027	14,665	17,346
Corporate and unallocated	(42)	874	269	3,031
Total revenues	$318,585	$397,999	$638,230	$771,783
(Loss) income before income taxes:				
Northeast	$(4,551)	$(130,209)	$(14,772)	$(230,311)
Mid-Atlantic	1,522	(22,240)	2,121	(49,756)
Midwest	(3,785)	(10,034)	(6,025)	(14,742)
Southeast	(2,767)	(23,971)	(4,955)	(40,032)
Southwest	7,045	(30,702)	10,936	(39,724)
West	(4,534)	(155,144)	(10,407)	(195,787)
Homebuilding loss before income taxes	(7,070)	(372,300)	(23,102)	(570,352)
Financial services	1,428	2,517	3,639	4,088
Corporate and unallocated	(22,338)	272,424	(63,485)	291,079
Loss before income taxes	$(27,980)	$(97,359)	$(82,948)	$(275,185)

(In thousands)	April 30, 2010	October 31, 2009
Assets:		
Northeast	$538,963	$559,257
Mid-Atlantic	184,159	200,908
Midwest	57,375	54,560
Southeast	64,427	60,441
Southwest	197,987	191,495
West	208,185	163,710
Total homebuilding	1,251,096	1,230,371
Financial services	73,409	84,280
Corporate and unallocated	704,596	709,926
Total assets	$2,029,101	$2,024,577

16. Per ASC 810 "Consolidation" ("ASC 810"), a Variable Interest Entity ("VIE") is created when (i) the equity investment at risk is not sufficient to permit the entity to finance its activities without additional subordinated financial support

from other parties or (ii) equity holders either (a) lack direct or indirect ability to make decisions about the entity, (b) are not obligated to absorb expected losses of the entity or (c) do not have the right to receive expected residual returns of the entity if they occur. If an entity is deemed to be a VIE pursuant to ASC 810, an enterprise that absorbs a majority of the expected losses of the VIE is considered the primary beneficiary and must consolidate the VIE.

Based on the provisions of ASC 810, we have concluded that, whenever we option land or lots from an entity and pay a non-refundable deposit, a VIE is created under condition (ii) (b) and (c) of the previous paragraph. We have been deemed to have provided subordinated financial support, which refers to variable interests that will absorb some or all of an entity's expected theoretical losses if they occur. For each VIE created with a significant nonrefundable option fee (we currently define significant as greater than $100,000 because we have determined that in the aggregate the VIEs related to deposits of this size or less are not material), we compute expected losses and residual returns based on the probability of future cash flows as outlined in ASC 810. If we are deemed to be the primary beneficiary of the VIE, we consolidate it on our balance sheet. The fair value of the VIE inventory, as of the date of consolidation, is reported as "Consolidated inventory not owned - variable interest entities".

Typically, the determining factor in whether or not we are the primary beneficiary is the nonrefundable deposit amount as a percentage of the total purchase price because it determines the amount of the first risk of loss we take on the contract. The higher this percentage deposit, the more likely we are to be the primary beneficiary. Other important criteria that impact the outcome of the analysis are the probability of getting the property through the approval process for residential homes, because this impacts the ultimate value of the property, as well as determining who is the party responsible (seller or buyer) for funding the approval process and development work that will take place prior to our decision to exercise the option.

Management believes the guidance for VIEs was not clearly thought out for application in the homebuilding industry for land and lot options, because we can have an option and put down a small deposit as a percentage of the purchase price and still have to consolidate the entity. Our exposure to loss as a result of our involvement with the VIE is only the deposit, not its total assets consolidated on our balance sheet. In certain cases, we will have to place inventory the VIE has optioned to other developers on our balance sheet. In addition, if the VIE has creditors, its debt will be placed on our balance sheet even though the creditors have no recourse against us. Based on these observations, we believe consolidating VIEs based on land and lot option deposits does not reflect the economic realities or risks of owning and developing land.

At April 30, 2010, all seven VIEs we were required to consolidate were the result of our options to purchase land or lots from the selling entities. We paid cash deposits to these VIEs totaling $6.0 million. Our option deposits represent our maximum exposure to loss. The fair value of the property owned by these VIEs, as of the date of consolidation, was $36.8 million. Because we do not own an equity interest in any of the unaffiliated VIEs that we must consolidate pursuant to ASC 810, we generally have little or no control or influence over the operations of these entities or their owners. When our requests for financial information are denied by the land sellers, certain assumptions about the assets and liabilities of such entities are required. In most cases, we determine the fair value of the assets of the consolidated entities based on the remaining contractual purchase price of the land or lots we are purchasing. In these cases, it is assumed that the entities funded the acquisition of the property with debt and the only asset recorded is the land or lots we have the option to buy with a related offset for the assumed third party financing of the variable interest entity. At April 30, 2010, the balance reported in liabilities from inventory not owned related to these VIEs was $30.9 million. Creditors of these seven VIEs have no recourse against us.

We will continue to control land and lots using options. Including the deposits with the seven VIEs described above, at April 30, 2010, we had total cash and letters of credit deposits amounting to approximately $27.3 million to purchase land and lots with a total purchase price of $552.7 million. Not all our deposits are with VIEs. The maximum exposure to loss is limited to the deposits, although some deposits are refundable at our request or refundable if certain conditions are not met.

17. We enter into homebuilding and land development joint ventures from time to time as a means of accessing lot positions, expanding our market opportunities, establishing strategic alliances, managing our risk profile, leveraging our capital base and enhancing returns on capital. Our homebuilding joint ventures are generally entered into with third-party investors to develop land and construct homes that are sold directly to third party homebuyers. Our land development joint ventures include those entered into with developers and other homebuilders as well as financial investors to develop finished lots for sale to the joint venture’s members or other third parties. The tables set forth below summarize the combined financial information related to our unconsolidated homebuilding and land development joint ventures that are accounted for under the equity method.

(Dollars in thousands)		April 30, 2010	
	Homebuilding	Land Development	Total
Assets:			
Cash and cash equivalents	$16,312	$462	$16,774
Inventories	283,820	71,600	355,420
Other assets	15,014	675	15,689
Total assets	$315,146	$72,737	$387,883
Liabilities and equity:			
Accounts payable and accrued liabilities	$16,443	$14,316	$30,759
Notes payable	176,388	37,654	214,042
Total liabilities	192,831	51,970	244,801
Equity of:			
Hovnanian Enterprises, Inc.	32,788	3,158	35,946
Others	89,527	17,609	107,136
Total equity	122,315	20,767	143,082
Total liabilities and equity	$315,146	$72,737	$387,883
Debt to capitalization ratio	59%	64%	60%

(Dollars in thousands)		October 31, 2009	
	Homebuilding	Land Development	Total
Assets:			
Cash and cash equivalents	$22,502	$1,539	$24,041
Inventories	281,556	83,833	365,389
Other assets	25,889	87	25,976
Total assets	$329,947	$85,459	$415,406
Liabilities and equity:			
Accounts payable and accrued liabilities	$19,236	$17,108	$36,344
Notes payable	193,567	40,051	233,618
Total liabilities	212,803	57,159	269,962
Equity of:			
Hovnanian Enterprises, Inc.	32,183	9,068	41,251
Others	84,961	19,232	104,193
Total equity	117,144	28,300	145,444
Total liabilities and equity	$329,947	$85,459	$415,406
Debt to capitalization ratio	62%	59%	62%

As of both April 30, 2010 and October 31, 2009, we had advances outstanding of approximately $11.5 million to these unconsolidated joint ventures, which were included in the "Accounts payable and accrued liabilities" balances in the table above. On our Condensed Consolidated Balance Sheets our "Investments in and advances to unconsolidated joint ventures" amounted to $40.3 million and $41.3 million at April 30, 2010 and October 31, 2009, respectively. In some cases, our net investment in these joint ventures is less than our proportionate share of the equity reflected in the table above because of the differences between asset impairments recorded against our joint venture investments and any impairments recorded in the applicable joint venture. During the first six months of fiscal 2010, we did not write down any joint venture investments based on our determination that none of the investments in our joint ventures have sustained an other than temporary impairment during that period.

	For the Three Months Ended April 30, 2010		
(Dollars in thousands)	Homebuilding	Land Development	Total
Revenues	$33,970	$3,989	$37,959
Cost of sales and expenses	(30,115)	(13,027)	(43,142)
Joint venture net income (loss)	$3,855	$(9,038)	$(5,183)
Our share of net income	$510	$30	$540

	For the Three Months Ended April 30, 2009		
(Dollars in thousands)	Homebuilding	Land Development	Total
Revenues	$23,996	$2,142	$26,138
Cost of sales and expenses	(118,563)	(2,242)	(120,805)
Joint venture net loss	$(94,567)	$(100)	$(94,667)
Our share of net loss	$(18,082)	$(366)	$(18,448)

	For the Six Months Ended April 30, 2010		
(Dollars in thousands)	Homebuilding	Land Development	Total
Revenues	$55,681	$10,260	$65,941
Cost of sales and expenses	(51,409)	(16,151)	(67,560)
Joint venture net income (loss)	$4,272	$(5,891)	$(1,619)
Our share of net income (loss)	$519	$(411)	$108

	For the Six Months Ended April 30, 2009		
(Dollars in thousands)	Homebuilding	Land Development	Total
Revenues	$48,927	$3,491	$52,418
Cost of sales and expenses	(160,365)	(4,577)	(164,942)
Joint venture net loss	$(111,438)	$(1,086)	$(112,524)
Our share of net loss	$(18,678)	$(460)	$(19,138)

Income (loss) from unconsolidated joint ventures is reflected as a separate line in the accompanying Condensed Consolidated Statements of Operations and reflects our proportionate share of the income (loss) of these unconsolidated homebuilding and land development joint ventures. The difference between our share of the income (loss) from these unconsolidated joint ventures disclosed in the tables above for the three and six months ended April 30, 2009 compared to the Condensed Consolidated Statements of Operations is due primarily to the write down of our investment in joint ventures where we determined that our investment had an other than temporary impairment. For the three and six months ended April 30, 2010, the minor difference is primarily due to one joint venture that had net income for which we do not get any share of the profit because of the cumulative equity position of the joint venture and the reclassification of the intercompany portion of management fee income from certain joint ventures, and the deferral of income for lots purchased by us from certain joint ventures. Our ownership interests in the joint ventures vary but are generally less than or equal to 50%. In determining whether or not we must consolidate joint ventures where we are the manager of the joint venture, we assess whether the other partners have specific rights to overcome the presumption of control by us as the manager of the joint venture. In most cases, the presumption is overcome because the joint venture agreements require that both partners agree on establishing the operating and capital decisions of the partnership, including budgets, in the ordinary course of business.

Typically, our unconsolidated joint ventures obtain separate project specific mortgage financing. Generally, the amount of such financing is targeted to be no more than 50% of the joint venture's total assets. However, because of impairments realized in the joint ventures the average debt to capitalization ratio of our joint ventures is currently 60%. This financing is obtained on a non-recourse basis, with guarantees from us limited only to performance and completion of development, environmental indemnification, standard warranty and representation against fraud, misrepresentation and other similar actions, including a voluntary bankruptcy filing. In some instances, the joint venture entity is considered a VIE under ASC 810 due to the returns being capped to the equity holders; however, in these instances, we are not the primary beneficiary, and therefore we do not consolidate these entities.

18. Recent Accounting Pronouncements - In December 2007, the FASB issued an update to ASC 810. The amended guidance contained in ASC 810 requires a noncontrolling interest in a subsidiary to be reported as equity and the amount of consolidated net income or loss specifically attributable to the noncontrolling interest to be identified in the consolidated financial statements. Our net income or loss attributable to noncontrolling interest is insignificant for all periods presented and therefore reported in "Other operations" in the Condensed Consolidated Statements of Operations. It also calls for consistency in the manner of reporting changes in the parent's ownership interest and requires fair value measurement of any noncontrolling equity investment retained in a deconsolidation. We implemented this standard effective November 1, 2009, resulting in a change in the classification of noncontrolling interests on the balance sheets and statements of equity.

In June 2009, the FASB issued an update to ASC 810, which amends the existing quantitative guidance used in determining the primary beneficiary of a VIE by requiring entities to qualitatively assess whether an enterprise is a primary beneficiary, based on whether the entity has (i) power over the most significant activities of the VIE and (ii) an obligation to absorb losses or the right to receive benefits that could be potentially significant to the VIE and requires enhanced disclosures to provide more information about an enterprise's involvement in a variable interest entity. This statement also requires ongoing assessments of whether an enterprise is the primary beneficiary of a variable interest entity. This statement is effective for us on November 1, 2010. We are currently evaluating the impact, if any, that this statement may have on our consolidated financial statements.

19. ASC 820, "Fair Value Measurements and Disclosures" ("ASC 820"), provides a framework for measuring fair value, expands disclosures about fair-value measurements and establishes a fair-value hierarchy which prioritizes the inputs used in measuring fair value summarized as follows:

Level 1	Fair value determined based on quoted prices in active markets for identical assets.
Level 2	Fair value determined using significant other observable inputs.
Level 3	Fair value determined using significant unobservable inputs.

Our financial instruments measured at fair value on a recurring basis are summarized below:

(In thousands)	Fair Value Hierarchy	Fair Value at April 30, 2010	Fair Value at October 31, 2009

Mortgage loans held for sale (1)	Level 2	$55,022	$65,786
Interest rate lock commitments	Level 2	331	254
Forward contracts	Level 2	(845)	(702)
		$54,508	$65,338

(1) The aggregate unpaid principal balance is $54.4 million.

We elected the fair-value option for its loans held for sale for mortgage loans originated subsequent to October 31, 2008 in accordance with ASC 825, "Financial Instruments" ("ASC 825"), which permits us to measure at fair value on a contract-by-contract basis. Management believes that the election of the fair value option for loans held for sale improves financial reporting by mitigating volatility in reported earnings caused by measuring the fair value of the loans and the derivative instruments used to economically hedge them without having to apply complex hedge accounting provisions. In addition, the fair value of these servicing rights is included in the Company's loans held for sale as of April 30, 2010. Prior to February 1, 2008, the fair value of the servicing rights was not recognized until the related loan was sold. Fair value of the servicing rights is determined based on values in the Company's servicing sales contracts. Fair value of loans held for sale is based on independent quoted market prices, where available, or the prices for other mortgage whole loans with similar characteristics.

The assets accounted for under ASC 825 are initially measured at fair value. Gains and losses from initial measurement and subsequent changes in fair value are recognized in the Financial Services segment's earnings (loss). The changes in fair values that are included in earnings (loss) are shown, by financial instrument and financial statement line item, below:

	Three Months Ended April 30, 2010		
(In thousands)	Loans Held For Sale	Mortgage Loan Commitments	Forward Contracts
Increase (decrease) in fair value included in net income (loss), all reflected in financial services revenues	$168	$70	$(258)

	Three Months Ended April 30, 2009		
(In thousands)	Loans Held For Sale	Mortgage Loan Commitments	Forward Contracts
(Decrease) increase in fair value included in net income (loss), all reflected in financial services revenues	$(613)	$405	$487

	Six Months Ended April 30, 2010		
(In thousands)	Loans Held For Sale	Mortgage Loan Commitments	Forward Contracts
(Decrease) increase in fair value	$(305)	$76	$(143)

included in net income
(loss), all reflected in
financial services revenues

	Six Months Ended April 30, 2009		
(In thousands)	Loans Held For Sale	Mortgage Loan Commitments	Forward Contracts
Increase (decrease) in fair value included in net income (loss), all reflected in financial services revenues	$1,526	$508	$(1,410)

The Financial Services segment had a pipeline of loan applications in process of $347.7 million at April 30, 2010. Loans in process for which interest rates were committed to the borrowers totaled approximately $107.0 million as of April 30, 2010. Substantially all of these commitments were for periods of 60 days or less. Since a portion of these commitments is expected to expire without being exercised by the borrowers, the total commitments do not necessarily represent future cash requirements.

The Financial Services segment uses investor commitments and forward sales of mandatory mortgage-backed securities (“MBS”) to hedge its mortgage-related interest rate exposure. These instruments involve, to varying degrees, elements of credit and interest rate risk. Credit risk is managed by entering into MBS forward commitments, option contracts with investment banks, federally regulated bank affiliates and loan sales transactions with permanent investors meeting the segment’s credit standards. The segment’s risk, in the event of default by the purchaser, is the difference between the contract price and fair value of the MBS forward commitments and option contracts. At April 30, 2010, the segment had open commitments amounting to $38.5 million to sell MBS with varying settlement dates through July 12, 2010.

Our financial instruments consist of cash and cash equivalents, restricted cash, receivables, deposits and notes, accounts payable and other liabilities, customer deposits, mortgage loans held for sale or investment, nonrecourse land and operating properties mortgages, letter of credit agreements and facilities, mortgage warehouse line of credit, accrued interest, and the senior secured, senior and senior subordinated notes payable. The fair value of financial instruments is determined by reference to various market data and other valuation techniques, as appropriate. The fair value of each of the senior secured, senior and senior subordinated notes is estimated based on the quoted market prices for the same or similar issues or on the current rates offered to us for debt of the same remaining maturities. The fair value of the senior secured, senior and senior subordinated notes is estimated at $867.2 million, $634.8 million and $113.0 million, respectively, as of April 30, 2010 and $788.2 million, $603.5 million and $113.3 million, respectively, as of October 31, 2009. The fair value of our other financial instruments approximates their recorded values.

The Company’s assets measured at fair value on a nonrecurring basis are those assets for which the Company has recorded valuation adjustments and write-offs during the three and six months ended April 30, 2010. The assets measured at fair value on a nonrecurring basis are all within the Company’s Homebuilding operations and are summarized below:

Non-financial Assets

			Three Months Ended April 30, 2010	
(In thousands)	Fair Value Hierarchy	Pre-Impairment Amount	Total Losses	Fair Value

Sold and unsold homes and lots under development	Level 3	$1,744	$(760)	$984
Land and land options held for future development or sale	Level 3	$1,000	$(500)	$500

			Six Months Ended April 30, 2010	
(In thousands)	Fair Value Hierarchy	Pre-Impairment Amount	Total Losses	Fair Value
Sold and unsold homes and lots under development	Level 3	$3,386	$(1,389)	$1,997
Land and land options held for future development or sale	Level 3	$5,629	$(3,120)	$2,509

20. Hovnanian Enterprises, Inc., the parent company (the "Parent") is the issuer of publicly traded common stock and preferred stock, which is represented by depository shares. One of its wholly owned subsidiaries, K. Hovnanian Enterprises, Inc. (the "Subsidiary Issuer"), acts as a finance entity that as of April 30, 2010 had issued and outstanding $797.2 million face value of senior secured notes ($783.9 million, net of discount), $737.9 million face value of senior notes ($736.1 million, net of discount), and $120.2 million of senior subordinated notes. The senior secured notes, senior notes and senior subordinated notes are fully and unconditionally guaranteed by the Parent.

In addition to the Parent, each of the wholly owned subsidiaries of the Parent other than the Subsidiary Issuer (collectively, the "Guarantor Subsidiaries"), with the exception of certain of our financial service subsidiaries, joint ventures, subsidiaries holding interests in our joint ventures and our foreign subsidiary (collectively, the "Non-guarantor Subsidiaries"), have guaranteed fully and unconditionally, on a joint and several basis, the obligations of the Subsidiary Issuer to pay principal and interest under the senior secured notes, senior notes and senior subordinated notes.

In lieu of providing separate financial statements for the Guarantor Subsidiaries, we have included the accompanying condensed consolidating financial statements. Management does not believe that separate financial statements of the Guarantor Subsidiaries are material to users of our consolidated financial statements. Therefore, separate financial statements and other disclosures concerning the Guarantor Subsidiaries are not presented.

The following condensed consolidating financial statements present the results of operations, financial position and cash flows of (i) the Parent, (ii) the Subsidiary Issuer, (iii) the Guarantor Subsidiaries, (iv) the Non-guarantor Subsidiaries and (v) the eliminations to arrive at the information for Hovnanian Enterprises, Inc. on a consolidated basis.

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
CONDENSED CONSOLIDATING BALANCE SHEET
APRIL 30, 2010
(In Thousands)

	Parent	Subsidiary Issuer	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
ASSETS:						
Homebuilding	$14,185	$446,104	$1,297,196	$198,207	$ -	$1,955,692
Financial services			3,173	70,236		73,409
Income taxes receivable (payable)						
Investments in and amounts due to and from consolidated subsidiaries	(130,380)	2,011,707	(1,778,763)	(215,420)	112,856	-
Total assets	$(116,195)	$2,457,811	$(478,394)	$53,023	$112,856	$2,029,101
LIABILITIES AND EQUITY:						
Homebuilding	$	$	$406,786	$9,233	$	$416,019
Financial services			2,916	56,348		59,264
Notes payable		1,664,379	172			1,664,551
Income taxes payable	21,562		4,732			26,294
Stockholders' (deficit) equity	(137,757)	793,432	(893,000)	(13,288)	112,856	(137,757)
Non-controlling interest in consolidated joint ventures				730		730
Total liabilities and equity	$(116,195)	$2,457,811	$(478,394)	$53,023	$112,856	$2,029,101

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
CONDENSED CONSOLIDATING BALANCE SHEET
OCTOBER 31, 2009
(In Thousands)

	Parent	Subsidiary Issuer	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
ASSETS:						
Homebuilding	$14,752	$449,096	$1,285,699	$190,750	$	$1,940,297
Financial services			5,885	78,395		84,280
Income taxes receivable (payable)						
Investments in and amounts	(308,706)	2,067,571	(1,573,827)	(209,735)	24,697	-

due to and from consolidated subsidiaries						
Total assets	$(293,954)	$2,516,667	$(282,243)	$59,410	$24,697	$2,024,577
LIABILITIES AND EQUITY:						
Homebuilding	$	$469	$454,718	$7,761	$	$462,948
Financial services			5,651	64,713		70,364
Notes payable		1,777,658	121			1,777,779
Income tax payable	55,644		6,710			62,354
Stockholders' (deficit) equity	(349,598)	738,540	(749,443)	(13,794)	24,697	(349,598)
Non-controlling interest in consolidated joint ventures				730		730
Total liabilities and equity	$(293,954)	$2,516,667	$(282,243)	$59,410	$24,697	$2,024,577

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS
THREE MONTHS ENDED APRIL 30, 2010
(In Thousands)

	Parent	Subsidiary Issuer	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Revenues:						
Homebuilding	$4	$(123)	$312,600	$286	$(1,241)	$311,526
Financial services			1,447	5,612		7,059
Intercompany charges		32,996	(43,685)	(431)	11,120	-
Equity in pretax (loss) income of consolidated subsidiaries	(25,762)				25,762	-
Total revenues	(25,758)	32,873	270,362	5,467	35,641	318,585
Expenses:						
Homebuilding	2,092	38,515	315,040	(428)	3,323	358,542
Financial services	130		1,370	4,308	(177)	5,631
Total expenses	2,222	38,515	316,410	3,880	3,146	364,173
Gain on extinguishment of debt		17,217				17,217
(Loss) income from unconsolidated joint ventures			(274)	665		391
(Loss) income before income taxes	(27,980)	11,575	(46,322)	2,252	32,495	(27,980)
State and federal income tax provision (benefit)	654	4,051	(6,291)	1,314	926	654
Net (loss) income	$(28,634)	$7,524	$(40,031)	$938	$31,569	$(28,634)

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS
THREE MONTHS ENDED APRIL 30, 2009
(In Thousands)

	Parent	Subsidiary Issuer	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Revenues:						
Homebuilding	$	$833	$386,021	$1,126	$992	$388,972
Financial services			2,123	6,904		9,027
Intercompany charges		59,724	(70,421)	(444)	11,141	-
Equity in pretax (loss) income of consolidated subsidiaries	(96,443)				96,443	-

Total revenues	(96,443)	60,557	317,723	7,586	108,576	397,999
Expenses:						
Homebuilding	807	48,726	742,301	1,682	(3,494)	790,022
Financial services	109		1,760	4,732	(91)	6,510
Total expenses	916	48,726	744,061	6,414	(3,585)	796,532
Gain on extinguishment of debt		311,038	230			311,268
Loss from unconsolidated joint ventures			(9,557)	(537)		(10,094)
(Loss) income before income taxes	(97,359)	322,869	(435,665)	635	112,161	(97,359)
State and federal income tax provision (benefit)	21,262	113,004	(109,401)	(1,431)	(2,172)	21,262
Net (loss) income	$(118,621)	$209,865	$(326,264)	$2,066	$114,333	$(118,621)

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS
SIX MONTHS ENDED APRIL 30, 2010
(In Thousands)

	Parent	Subsidiary Issuer	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Revenues:						
Homebuilding	$8	$(163)	$625,875	$326	$(2,481)	$623,565
Financial services			2,906	11,759		14,665
Intercompany charges		64,559	(89,904)	(872)	26,217	-
Equity in pretax (loss) income of consolidated subsidiaries	(78,340)				78,340	-
Total revenues	(78,332)	64,396	538,877	11,213	102,076	638,230
Expenses:						
Homebuilding	4,356	79,119	639,614	(1,107)	7,979	729,961
Financial services	260		2,791	8,327	(352)	11,026
Total expenses	4,616	79,119	642,405	7,220	7,627	740,987
Gain on extinguishment of debt		19,791				19,791
(Loss) income from unconsolidated joint ventures			(668)	686		18
(Loss) income before income taxes	(82,948)	5,068	(104,196)	4,679	94,449	(82,948)
State and federal Income tax (benefit) provision	(290,503)	1,774	(297,840)	1,538	294,528	(290,503)
Net (loss) income	$207,555	$3,294	$193,644	$3,141	$(200,079)	$207,555

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS
SIX MONTHS ENDED APRIL 30, 2009
(In Thousands)

	Parent	Subsidiary Issuer	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Revenues:						
Homebuilding	$	$2,966	$752,821	$1,126	$(2,476)	$754,437
Financial services			3,821	13,525		17,346
Intercompany charges		125,967	(140,857)	(517)	15,407	-
Equity in pretax (loss) income of consolidated						

subsidiaries	(253,953)				253,953	-
Total revenues	(253,953)	128,933	615,785	14,134	266,884	771,783
Expenses:						
Homebuilding	20,858	103,180	1,276,290	1,690	(10,203)	