AV Homes, Inc.
Form 10-Q
November 03, 2014

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 the quarterly period ended September 30, 2014.

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ____________ to _____________.

001-07395
Commission File Number

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

Delaware	23-1739078
(State or other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
8601 N. Scottsdale Rd., Suite 225, Scottsdale, Arizona	85253
(Address of Principal Executive Offices)	(Zip Code)

(480) 214-7400
(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 x No o

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

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

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

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

As of October 28, 2014, there were 22,096,612 shares of common stock, $1.00 par value, issued and outstanding.

AV HOMES, INC. AND SUBSIDIARIES
FORM 10-Q

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PART I. Financial Information

ITEM 1. FINANCIAL STATEMENTS

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AV HOMES, INC. AND SUBSIDIARIES
Consolidated Balance Sheets
($000's omitted)

	September 30, 2014 (unaudited)	December 31, 2013
Assets		
Cash and cash equivalents	$181,845	$144,727
Restricted cash	12,774	3,956
Land and other inventories	382,839	240,078
Receivables, net	4,093	3,893
Property and equipment, net	36,443	37,844
Investments in unconsolidated entities	16,308	1,230
Prepaid expenses and other assets	20,964	11,138
Assets held for sale	4,325	23,862
Goodwill	5,975	—
Total Assets	$665,566	$466,728
Liabilities and Equity		
Liabilities		
Accounts payable	$21,759	$9,757
Accrued and other liabilities	20,940	14,280
Customer deposits and deferred revenues	5,282	2,323
Estimated development liability for sold land	33,050	33,232
Notes payable	299,981	105,402
Total Liabilities	381,012	164,994
Equity		
Common stock, par value $1 per share		
Authorized: 50,000,000 shares		
Issued: 22,198,951 shares outstanding at September 30, 2014		
22,097,252 shares outstanding at December 31, 2013	22,199	22,097
Additional paid-in capital	396,392	394,504
Accumulated deficit	(131,018)	(127,481)
	287,573	289,120
Treasury stock: at cost, 110,874 shares at September 30, 2014 and December 31, 2013	(3,019)	(3,019)
Total AV Homes stockholders’ equity	284,554	286,101
Non-controlling interests	—	15,633
Total Equity	284,554	301,734
Total Liabilities and Equity	$665,566	$466,728

See notes to consolidated financial statements.

AV HOMES, INC. AND SUBSIDIARIES
Consolidated Statements of Operations and Comprehensive Income (Loss)
($000's omitted, except per share data)
(unaudited)

	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
Revenues				
Real estate revenues				
Homebuilding and amenity	$73,611	$34,167	$152,612	$79,420
Land sales	12,942	674	29,168	9,556
Other real estate	88	57	173	496
Total real estate revenues	86,641	34,898	181,953	89,472
Expenses				
Real estate expenses				
Homebuilding and amenity	70,400	32,725	148,415	78,515
Land sales	8,672	95	20,910	5,352
Other real estate	114	1,255	868	2,654
Total real estate expenses	79,186	34,075	170,193	86,521
Impairment charges, net	—	(970)	—	(925)
General and administrative expenses	4,016	3,885	12,264	11,882
Interest income and other	(85)	(101)	(258)	(203)
Interest expense	2,841	(1,020)	2,952	2,515
Total expenses	85,958	35,869	185,151	99,790
Equity in earnings (loss) from unconsolidated entities	(5)	(7)	(10)	(84)
Income (loss) before income taxes	678	(978)	(3,208)	(10,402)
Income tax (expense) benefit	—	—	—	—
Net income (loss) and comprehensive income (loss)	678	(978)	(3,208)	(10,402)
Net income (loss) attributable to non-controlling interests in consolidated entities	—	899	329	899
Net income (loss) and comprehensive income (loss) attributable to AV Homes stockholders	$678	$(1,877)	$(3,537)	$(11,301)
Reconciliation of net income (loss) to loss attributable to common stockholders				
Net income (loss)	$678	$(1,877)	$(3,537)	$(11,301)
Deemed dividend related to beneficial conversion feature of convertible preferred stock (Note 1)	—	(11,894)	—	(11,894)
Income (loss) attributable to AV Homes common stockholders	$678	$(13,771)	$(3,537)	$(23,195)
Basic and Diluted Income (Loss) Per Share	$0.03	$(0.86)	$(0.16)	$(1.67)

See notes to consolidated financial statements.

AV HOMES, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
($000's omitted)
(unaudited)

	Nine Months Ended September 30,	
	2014	2013
OPERATING ACTIVITIES		
Net loss (including net income or loss attributable to non-controlling interests)	$(3,208)	$(10,402)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	2,425	2,064
Amortization of stock-based compensation	2,141	976
Impairment charges, net	—	(925)
Equity loss from unconsolidated entities	10	84
Loss from disposal of assets	—	22
Changes in operating assets and liabilities:		
Restricted cash	(8,818)	334
Receivables, net	(200)	406
Land and other inventories	(111,226)	(32,071)
Assets held for sale	19,537	(1,228)
Income tax receivable	—	1,293
Prepaid expenses and other assets	469	744
Accounts payable, estimated development liability, and accrued and other liabilities	14,168	5,298
Customer deposits and deferred revenues	2,105	2,310
NET CASH USED IN OPERATING ACTIVITIES	(82,597)	(31,095)
INVESTING ACTIVITIES		
Investment in property and equipment	(549)	(856)
Proceeds from sales of property and equipment	12	—
Acquisition of Royal Oak Homes	(62,684)	—
Investment in unconsolidated entities	(1,955)	(99)
Return of capital from unconsolidated entities	33	—
NET CASH USED IN INVESTING ACTIVITIES	(65,143)	(955)
FINANCING ACTIVITIES		
Net proceeds from issuance of common shares	—	35,805
Net proceeds from issuance of preferred shares	—	92,042
Gross proceeds from issuance of 8.5% Notes	200,000	—
Debt issuance costs	(9,220)	—
Principal payments of notes	(5,421)	—
Other financing activities, net	(501)	555
NET CASH PROVIDED BY FINANCING ACTIVITIES	184,858	128,402
INCREASE IN CASH AND CASH EQUIVALENTS	37,118	96,352
Cash and cash equivalents at beginning of period	144,727	79,815
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$181,845	$176,167

See notes to consolidated financial statements.

AV HOMES, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (unaudited)
September 30, 2014
($000's omitted, except share and per share data)

Note 1 - Summary of Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements include the accounts of AV Homes, Inc. and all subsidiaries, partnerships and other entities in which AV Homes, Inc. (“AV Homes," “we,” “us,” “our,” or “the Company”) has a controlling interest. Our investments in unconsolidated entities in which we have less than a controlling interest are accounted for using the equity method. The interim consolidated financial statements have been prepared, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC"). Accordingly, they do not include all information and footnotes required by U.S generally accepted accounting principles ("GAAP") for complete financial statements. These statements reflect all normal and recurring adjustments which, in the opinion of management, are necessary to present fairly the financial position, results of operations and cash flows of AV Homes at September 30, 2014 and for all periods presented. These statements should be read in conjunction with our consolidated financial statements and notes thereto included in AV Homes' Annual Report on Form 10-K for the year ended December 31, 2013. All significant intercompany accounts and transactions have been eliminated in consolidation. Certain prior year amounts in the consolidated statement of cash flows have been reclassified to conform to the current year’s presentation.

Use of Estimates

The preparation of our consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

TPG Investment in Company

On June 19, 2013, we entered into a Securities Purchase Agreement (the "Purchase Agreement") by and among AV Homes and TPG Aviator, L.P. ("TPG Aviator") pursuant to which TPG Aviator agreed to acquire 2,557,474 shares of AV Homes’ common stock, par value $1.00 per share (the “Common Stock"), at a purchase price of $14.65 per share, and 665,754 shares of a newly authorized series of AV Homes’ preferred stock, designated as Series A Contingent Convertible Cumulative Redeemable Preferred Stock, par value $0.10 per share (the “Series A Preferred Stock"), at a purchase price and liquidation preference of $146.50 per share, for an aggregate investment in AV Homes by TPG Aviator of $135,000.

On June 20, 2013, AV Homes and TPG Aviator closed the transactions (the “TPG Investment") contemplated by the Purchase Agreement, and AV Homes issued to TPG Aviator the Common Stock and the Series A Preferred Stock in the amounts and in exchange for the purchase price described above.

On September 18, 2013, we held a special meeting of stockholders at which our stockholders: (1) approved the right to convert, at the option of the Company or the holders of the Series A Preferred Stock, the Series A Preferred Stock into 6,657,543 shares of our Common Stock and (2) approved TPG Aviator's pre-emptive rights following the approval of such conversion to participate in future issuances of our Common Stock or securities convertible into or exercisable for our Common Stock. Following the meeting of stockholders, we provided notice to TPG Aviator of our intention to convert the Series A Preferred Stock as of September 18, 2013. The Common Stock issuable upon conversion of the Series A Preferred Stock was issued on September 19, 2013 and the Series A Preferred Stock was cancelled.

In accordance with GAAP, before its conversion, the Series A Preferred Stock was classified outside of permanent equity because the redemption provisions were not solely within our control. We incurred approximately $7,212 of transaction fees in connection with the TPG Investment, which have been offset against the proceeds received. The contingent beneficial conversion feature of the Series A Preferred Stock was recognized upon stockholder approval of the conversion and amortized at the time of conversion by treating it as a deemed dividend in retained earnings and crediting additional paid-in capital for $11,894, consequently resulting in no diminution in total shareholders' equity or book value per share. We have assessed the provisions of the Series A Preferred Stock and concluded that the impact of any embedded derivative features was not material.

Cash and Cash Equivalents and Restricted Cash

We consider all highly liquid investments purchased with an initial maturity of three months or less to be cash equivalents. As of September 30, 2014, our cash and cash equivalents were invested primarily in money market accounts that invest primarily in U.S. government securities. Due to the short maturity period of the cash equivalents, the carrying amount of these instruments approximates their fair values.

Our cash items that are restricted as to withdrawal or usage include deposits of $12,774 and $3,956 as of September 30, 2014 and December 31, 2013, respectively. The balance as of September 30, 2014 is comprised primarily of $11,985 on deposit as an interest reserve to comply with the terms of our Senior Secured Credit Facility.

Land and Other Inventories

Land and Other Inventories include expenditures for land acquisition, construction, land development, construction costs for homeowners association amenities, and direct and allocated indirect costs, including interest cost capitalized until development and construction are substantially completed. These costs are assigned to components of Land and Other Inventories based on specific identification, relative sales value, or area allocation methods.

Land and Other Inventories are stated at cost unless the asset is determined to be impaired, in which case the asset is written to its fair value, in accordance with Accounting Standards Codification (ASC) 360, Property, Plant and Equipment ("ASC 360").

We evaluate our Land and Other Inventories for impairment on a quarterly basis in accordance with ASC 360 to reflect market conditions, including a consideration of supply of new and resale homes for sale in the respective market, level of foreclosure activity and competition. For assets held and used, if indicators are present, we perform an impairment test in which the asset is reviewed for impairment by comparing the estimated future undiscounted cash flows to be generated by the asset to its carrying value. If such cash flows are less than the asset's carrying value, the carrying value is written down to its estimated fair value. Generally, fair value is determined by discounting the estimated cash flows at a rate commensurate with the inherent risks associated with the asset and related estimated cash flow streams. The discount rate used in the determination of fair value would vary, depending on the state of development. Assumptions and estimates used in the determination of the estimated future cash flows are based on expectations of future operations and economic conditions and certain factors described below. Changes to these assumptions could significantly affect the estimates of future cash flows, which could affect the potential for future impairments. Due to the uncertainties of the estimation process, actual results could differ significantly from such estimates.

During the three and nine months ended September 30, 2014, our impairment assessment resulted in no impairment charges. During the three and nine months ended September 30, 2013, our impairment assessment resulted in impairment charges of $0 and $33, respectively, which related to homes completed or under construction. During the three months ended September 30, 2013, we changed our plans to sell certain assets, resulting in the reclassification of these assets to land and other inventories and a reversal of previously recorded impairment expense of $958. This reversal was the result of measuring these assets at the lower of the original carrying amount or the fair value at the date of the decision not to sell, in accordance with ASC 360-10-35-44.

Receivables, net

Receivables, net includes amounts in transit or due from title companies for house closings; membership dues related to our amenity operations; and contracts and mortgage notes receivable from the sale of land.

Property and Equipment, net

Property and Equipment, net are stated at cost and depreciation is computed by the straight-line method over the following estimated useful lives of the assets: land improvements 10 to 25 years; buildings and improvements 8 to 39 years; and machinery, equipment and fixtures 3 to 7 years. Maintenance and operating expenses of equipment utilized in the development of land are capitalized to land inventory. Repairs and maintenance are expensed as incurred.

Property and Equipment, net includes certain amenities such as club facilities, dining facilities, and golf courses owned by us. These amenities include expenditures for land, construction, and direct and allocated costs, including interest cost incurred during development and construction.

Each reporting period, we review our Property and Equipment, net for indicators of impairment in accordance with ASC 360. For our amenities, which are located within our housing communities, indicators of potential impairment are similar to those of our housing communities (described above), as these factors may impact our ability to generate revenues at our amenities or cause construction costs to increase. In addition, we factor in the collectability and potential delinquency of the fees due for our amenities. For the three and nine months ended September 30, 2014 and 2013, we did not identify indicators of impairments for Property and Equipment. During 2013, management changed its plans to sell certain assets, resulting in the reclassification of these assets from assets held for sale to Property and Equipment, net. There was no change in the carrying value in these assets due to this reclassification.

Assets Held for Sale

We classify assets held for sale in accordance with the criteria set forth in ASC 360. We continue to opportunistically sell non-core commercial and industrial assets, as well as scattered lot positions and land assets that are in excess of our needed supply in a given market. Under this plan, assets that meet the criteria above are classified as held for sale. For assets held for sale, if indicators are present, we perform an impairment test in which the asset is reviewed for impairment by comparing the fair value (estimated sales price) less cost to sell the asset to its carrying value. If such fair value less cost to sell is less than the asset's carrying value, the carrying value is written down to its estimated fair value less cost to sell.

During the nine months ended September 30, 2014, we sold assets held for sale with a carrying value of $19,943 for cash proceeds of $27,074 for a gain of $7,131. During the nine months ended September 30, 2013, we sold assets held for sale with a carrying value of $4,581 for cash proceeds of $7,130 for a gain of $2,549.

Investments in Partnerships and LLCs

When we are either deemed to hold the controlling interest in a voting interest entity or deemed to be the primary beneficiary of a variable interest entity ("VIE") we are required to consolidate the investment. The primary beneficiary of a VIE is the entity that has both of the following characteristics: (a) the power to direct the activities of a VIE that most significantly impact the VIE's economic performance and (b) the obligation to absorb the majority of losses of the VIE or the right to receive the majority of benefits from the VIE. Investments where we don't hold the controlling interest and we are not the primary beneficiary are accounted for under the equity method.

Factors considered when determining if we hold the controlling interest in a voting interest entity include who holds the general partnership or managing member interests, which partner or member makes the day-to-day decisions regarding the operations of the entity, and whether or not the other partners or members have substantive participating rights. With respect to VIEs, our variable interests may be in the form of (1) equity ownership, (2) contracts to purchase assets and/or (3) loans provided by us to the investor. We examine specific criteria and use judgment when determining if we are the primary beneficiary of a VIE. Factors considered in determining whether we are the primary beneficiary include risk and reward sharing, experience and financial condition of other partner(s), sufficiency of equity to conduct the operations of the entity, voting rights, involvement in decisions significantly impacting the entity's economic performance, level of economic disproportionality between us and the other partner(s) and contracts to purchase assets from VIEs.

Non-Controlling Interest

At December 31, 2013, we consolidated an investment in an LLC where AV Homes was determined to be the primary beneficiary due to a related party affiliation. Therefore, the LLC's financial statements were consolidated in our financial statements and the other partner's equity in the LLC was recorded as non-controlling interest as a component of consolidated equity. At June 30, 2014, we were no longer considered the primary beneficiary of this LLC due to a discontinuation of a related party affiliation, resulting in shared power between the remaining members. As the

Company no longer has the power, on a stand-alone basis, to direct the activities of the LLC that most significantly impact the LLC's economic performance, the Company deconsolidated this LLC, in accordance with ASC 810, Consolidation and ASC 360, Property, Plant, and Equipment. As this transaction involves the deconsolidation of in-substance real estate, the Company has accounted for the deconsolidation under ASC 360-20, Real Estate Sales. In determining whether a gain should be recognized as part of this transaction, ASC 360-20-40-10 Real Estate Sales, requires that a sufficient amount of cash be received in order to recognize a gain on transactions within the scope of ASC 360. As the Company did not receive any proceeds from this transaction, and as there was not a culmination of an earning process, we recognized our investment in the venture at our carry over cost basis and therefore no gain or loss was recognized. The Company will reflect future earnings, contributions and distributions on an equity method basis. At September 30, 2014 and December 31, 2013, non-controlling interest was $0 and $15,633, respectively.

Purchase Accounting

When acquiring a business, we allocate the purchase price of real estate to the tangible and intangible assets and liabilities acquired based on their estimated fair values. In making estimates of fair values for this purpose, we use a number of sources, including independent appraisals and information obtained about each property as a result our pre-acquisition due diligence and its marketing and housing activities.

Goodwill

Goodwill, if any, arises from business combinations and represents the excess of the cost of an acquired entity over the net fair value amounts that were assigned to the identifiable assets acquired and the liabilities assumed. Goodwill is tested for impairment at the reporting unit level on an annual basis and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of the reporting unit below its carrying value.

Revenues

In accordance with ASC 360, revenues from the sales of housing units are recognized when the sales are closed and title passes to the purchasers. In addition, revenues from land sales are recognized in full at closing, provided the buyer's initial and continuing investment is adequate, any financing is considered collectible and there is no significant continuing involvement. Sales incentives are included in Real estate revenue-Homebuilding in the accompanying consolidated statements of operations and comprehensive income (loss).

Warranty Costs

Warranty reserves for houses are established to cover estimated costs for materials and labor with regard to warranty-type claims to be incurred subsequent to the closing of a house. Reserves are determined based on historical data and other relevant factors. We have, and require our subcontractors to have, general liability, property, errors and omissions, workers compensation, and other business insurance. These insurance policies protect us against a portion of our risk of loss from claims, subject to certain self-insured per occurrence and aggregate retentions, deductibles, and available policy limits. We may have recourse against subcontractors for certain claims relating to workmanship and materials. Warranty reserves are included in Accrued and Other Liabilities in the accompanying consolidated balance sheets.

During the three and nine months ended September 30, 2014 and 2013, changes in the warranty reserve consisted of the following:

	Three Months		Nine Months	
	2014	2013	2014	2013
Accrued warranty reserve, beginning of period	$806	$497	$639	$549
Reserve provided	467	161	933	376
Payments	(234)	(202)	(533)	(469)
Accrued warranty reserve, end of period	$1,039	$456	$1,039	$456

Income Taxes

Income taxes have been provided using the liability method under ASC 740, Income Taxes (“ASC 740”). The liability method is used in accounting for income taxes where deferred income tax assets and liabilities are determined based on differences between financial reporting and tax basis of assets and liabilities and are measured using the enacted tax rates and laws that are expected to be in effect when the differences reverse.

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. Our cumulative loss position over the evaluation period and the uncertain and volatile market conditions provided significant evidence supporting the need for a valuation allowance. During the nine months ended September 30, 2014, we recognized an increase of $747 in the valuation allowance, primarily attributable to the year to date net loss. As of September 30, 2014, our deferred tax asset valuation allowance was $130,979. In future periods, the valuation allowance could be reduced based on sufficient evidence indicating that it is more likely than not that a portion of our deferred tax assets will be realized.

Any interest or penalties that have been assessed in the past have been minimal and immaterial to our financial results. In the event we are assessed any interest or penalties in the future, we plan to include them in our statement of operations and comprehensive income (loss) as income tax expense.

Share-Based Compensation

The Amended and Restated 1997 Incentive and Capital Accumulation Plan (2005 Restatement), as amended, (the “Incentive Plan”) provides for the grant of stock options, stock appreciation rights, stock awards, performance awards, and stock units to officers, employees and directors of AV Homes. The exercise prices of stock options may not be less than the stock exchange closing price of our common stock on the date of grant. Stock option awards under the Incentive Plan generally expire 10 years after the date of grant. On June 2, 2011, our stockholders approved the Amended and Restated 1997 Incentive and Capital Accumulation Plan (2011 Restatement) (the "Incentive Plan") to, among other things, increase the aggregate number of shares of our common stock, par value $1.00 per share, authorized for issuance under the Incentive Plan from 1,500,000 shares to 2,200,000 shares and extend the term of the Incentive Plan until October 25, 2020.

As of September 30, 2014, an aggregate of 1,050,722 shares of our common stock, subject to certain adjustments, were reserved for issuance under the Incentive Plan, including an aggregate of 818,858 options, restricted stock units and stock units granted. There were 231,864 shares available for grant at September 30, 2014.

As of September 30, 2014, there was $2,010 of unrecognized compensation expense related to unvested restricted stock units. That expense is expected to be recognized over a weighted-average period of 2.0 years years.

As of September 30, 2014 there was $3,831 of unrecognized compensation expense related to unvested stock options. That expense is expected to be recognized over a weighted-average period of 3.0 years years.

Earnings (Loss) Per Share

Basic earnings (loss) per share is computed by dividing net income (loss) attributable to AV Homes stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of AV Homes. The computation of diluted loss per share for the nine months ended September 30, 2014 and 2013 did not assume the effect of restricted stock units, employee stock options, the 4.50% Notes, the 7.50% Notes, or the 7.50% Exchange Notes because the effects were antidilutive. The computation of diluted loss per share for the three months ended September 30, 2014 and 2013 did not assume the effect of employee stock options, the 4.50% Notes, the 7.50% Notes, or the 7.50% Exchange Notes because the effects were antidilutive.

The weighted average number of shares outstanding in calculating basic and diluted earnings per share includes the cancellation of 0 shares and 7,870 shares of common stock and the issuance of 0 and 35,603 shares of common stock for the three and nine months ended September 30, 2014, respectively, and the cancellation of 0 shares and 2,364 shares of common stock and the issuance of 6,676,371 and 9,241,978 shares of common stock for the three and nine months ended September 30, 2013, respectively. In accordance with ASC 260, Earnings Per Share, non-vested restricted shares are not included in basic earnings per share until the vesting requirements are met.

The following table represents a reconciliation of the net loss and weighted average shares outstanding for the calculation of basic and diluted loss per share for the three and nine months ended September 30, 2014 and 2013:

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	Three Months		Nine Months	
	2014	2013	2014	2013
Numerator:				
Basic and diluted income (loss) per share	$678	$(1,877)	$(3,537)	$(11,301)
Deemed dividend related to the beneficial conversion feature	—	$(11,894)	—	$(11,894)
Income (loss) attributable to common stockholders	678	(13,771)	(3,537)	(23,195)
Denominator:				
Basic weighted average shares outstanding	21,953,484	16,097,335	21,941,293	13,927,716
Diluted weighted average shares outstanding	22,071,236	16,097,335	21,941,293	13,927,716
Basic income (loss) per share	$0.03	$(0.86)	$(0.16)	$(1.67)
Diluted income (loss) per share	$0.03	$(0.86)	$(0.16)	$(1.67)

Comprehensive Income (Loss)

Net loss and comprehensive loss are the same for the three and nine months ended September 30, 2014 and 2013.

Recent Accounting Pronouncements

In August 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-15, “Presentation of Financial Statements - Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity’s Ability to Continue as a Going Concern” (“ASU 2014-15”), which requires management to evaluate, in connection with preparing financial statements for each annual and interim reporting period, whether there are conditions or events, considered in the aggregate, that raise substantial doubt about an entity’s ability to continue as a going concern within one year after the date that the financial statements are issued (or within one year after the date that the financial statements are available to be issued when applicable) and provide related disclosures. ASU 2014-15 is effective for the annual period ending after December 15, 2016, and for annual and interim periods thereafter. Early adoption is permitted. We believe the adoption of this guidance will not have a material effect on our consolidated financial statements.

In June 2014, the FASB issued ASU No. 2014-12, “Compensation - Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period” (“ASU 2014-12”). The amendments in ASU 2014-12 require that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. A reporting entity should apply existing guidance in Accounting Standards Codification Topic No. 718, “Compensation - Stock Compensation” (“ASC 718”), as it relates to awards with performance conditions that affect vesting to account for such awards. The amendments in ASU 2014-12 are effective for annual periods and interim periods within those annual periods beginning after December 15, 2015. Early adoption is permitted. Entities may apply the amendments in ASU 2014-12 either: (a) prospectively to all awards granted or modified after the effective date; or (b) retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter. We believe the adoption of this guidance will not have a material effect on our consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers" (“ASU 2014-09"). The standard is a comprehensive new revenue recognition model that requires revenue to be recognized in a manner to depict the transfer of goods or services to a customer at an amount that reflects the consideration expected to be received in exchange for those goods or services. ASU 2014-09 is effective for the Company for fiscal and interim periods beginning January 1, 2017 and early application is not permitted. We are currently evaluating the impact that the standard will have on our financial condition, results of operations, cash flows, and disclosures.

In July 2013, the FASB issued ASU 2013-11, "Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists" ("ASU 2013-11"). This update requires companies to present an unrecognized tax benefit, or a portion of an unrecognized tax benefit, as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward, unless certain conditions exist. ASU

2013-11 was effective for our interim and annual periods beginning January 1, 2014. The adoption of ASU 2013-11 did not have a material impact on our consolidated financial position or results of operations.
Note 2 - Royal Oak Homes Acquisition

On March 13, 2014, we acquired substantially all of the assets and certain of the liabilities of Royal Oak Homes, LLC ("Royal Oak") and certain land positions from an affiliate of Royal Oak. Royal Oak and its affiliate acquire and develop raw land and construct single family homes in the Central Florida area. The transaction will expand our presence in Central Florida and our existing presence in the Poinciana market. With over 2,500 primary residential lots owned or controlled, Royal Oak enhances our position in a key growth market. The total purchase price paid under the acquisition agreements was approximately $65,000 in cash, which includes a potential $3,000 payment related to an earn-out covering the financial results for 2014 and 2015. The earn-out has a preliminary fair value of $2,500. The actual amount of the earn-out may be more or less than the $3,000 target amount based on the performance of the Royal Oak business through the end of 2015. We will not pay any earn-out amounts unless the Royal Oak business achieves at least 50% of the target amount of financial performance. The results of Royal Oak are included in the Company's consolidated financial statements from the acquisition date of March 13, 2014.

The Royal Oak acquisition was accounted for in accordance with ASC 805, Business Combinations ("ASC 805"). We recorded the acquired assets and liabilities at their estimated fair value. We determined the estimated fair values with the assistance of appraisals or valuations performed by independent third-party specialists, discounted cash flow analyses, quoted market prices where available, and estimates by management. To the extent the consideration transferred exceeded the fair value of the net assets acquired in this transaction, such excess was assigned to goodwill.

We acquired substantially all of the assets of Royal Oak, including all of its real estate, land acquisition agreements and permits, and certain of its leases, contracts, commitments and purchase orders. We also assumed certain liabilities of Royal Oak, including the liabilities and obligations relating to the acquired contracts but excluding certain home warranty obligations relating to homes sold by Royal Oak prior to the acquisition. We will, however, provide warranty administrative services of up to $150 with respect to these home warranty obligations for the two years following the closing of the acquisition.
The following table summarizes the preliminary calculation of the fair value of the total consideration transferred to Royal Oak and its affiliate and the provisional amounts of assets acquired and liabilities assumed as of the acquisition date:

Preliminary calculation of purchase price consideration

Cash paid for Royal Oak net assets	$25,848
Cash paid for bulk land purchase	28,009
Contingent consideration (earn-out)	2,500
Debt repaid at closing	8,827
Total consideration	$65,184
Assets acquired and liabilities assumed	
Assets	
Prepaids and other current assets	$582
Land and other inventories	60,313
Property, plant and equipment	366
Trade name	614
Goodwill	5,975
Total assets acquired	67,850
Liabilities	
Accounts payable	1,343
Accrued and other liabilities	469
Customer deposits	854
Total liabilities assumed	2,666
Total net assets acquired	$65,184

Fair value

Cash and equivalents, other assets, accounts payable, and accrued and other liabilities were generally stated at historical carrying values given the short-term nature of these assets and liabilities. Liabilities were recorded at historical carrying values in accordance with ASC 805.

The Company determined the fair value of inventory on a lot-by-lot basis primarily using a combination of market comparable land transactions, where available, and discounted cash flow models, and independent appraisals were also utilized in certain instances. These estimated cash flows are significantly impacted by estimates related to expected average home selling prices and sales incentives, expected sales paces and cancellation rates, expected land development and construction timelines, and anticipated land development, construction, and overhead costs. Such estimates must be made for each individual community and may vary significantly between communities.

The fair values for acquired intangible assets were determined based on valuations performed by independent valuation specialists. The $614 of acquired intangible assets relates to trade names that will generally be amortized over three years. Amortization expense for these assets totaled $52 and $121 for the three and nine months ended September 30, 2014, respectively, which is included in the consolidated statements of operations within homebuilding expense.

The Company has completed its preliminary analysis of its business combination accounting as of September 30, 2014. For the three months ended September 30, 2014, goodwill decreased by $218 due to a post-closing purchase price adjustment, offset by an increase of $217 due to a revision of the valuation of acquired inventory, for a net decrease of $1. The Company has not completed its final review of certain other assets and liabilities. Final determinations of the values of assets acquired and liabilities assumed may result in adjustments to the values presented above and a corresponding adjustment to goodwill. As such, the Company has not completed the assignment of goodwill to reporting units or its determination of the amount of goodwill that is expected to be deductible for tax purposes at this time.

Transaction and integration costs

Transaction and integration costs directly related to the Royal Oak acquisition, including legal, accounting and broker fees, totaled $37 and $1,057 for the three and nine months ended September 30, 2014, respectively, the majority of which are included in the consolidated statements of operations within corporate general and administrative expenses. Such costs were expensed as incurred in accordance with ASC 805.

Goodwill

As of the acquisition date, goodwill includes the expected economic value attributable to Royal Oak's assembled workforce. The acquisition provides increased scale and presence in an existing market with immediate revenue opportunities through an established backlog.

Supplemental pro forma information

The following represents pro forma operating results as if Royal Oak had been included in the Company's consolidated statements of operations as of the beginning of the fiscal years presented:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Revenue	$86,641	$48,809	$195,089	$127,223
Net income (loss)	678	(356)	(1,418)	(7,524)
Income (loss) per common share - basic and diluted	$0.03	$(0.76)	$(0.06)	$(1.39)

The supplemental pro forma operating results have been determined after adjusting the operating results of Royal Oak to reflect additional amortization that would have been recorded assuming the fair value adjustments to intangible assets had been applied as of January 1, 2014 and 2013. Certain other adjustments, including those related to conforming accounting policies and adjusting acquired inventory to fair value, have not been reflected in the supplemental pro forma operating results due to the impracticability of estimating such impacts. These results may not be indicative of future operating results.

Note 3 - Land and Other Inventories

Land and Other Inventories consist of the following:

	September 30, 2014	December 31, 2013
Active Adult		
Land held for future development or sale	$20,845	$58,423
Land developed and in process of development	84,986	57,138
Homes completed or under construction	48,179	25,478
Total Active Adult	154,010	141,039
Primary Residential		
Land developed and in process of development	163,768	77,983
Homes completed or under construction	56,435	11,013
Total Primary Residential	220,203	88,996
Land developed and in process of development-Other	8,626	10,043
	$382,839	$240,078

We capitalize interest to inventories during the period of development in accordance with ASC 835, Interest ("ASC 835"). Homebuilding interest capitalized as cost of inventories is included in cost of sales as related units or lots are sold. To the extent our homebuilding debt exceeds our qualified assets, as defined in ASC 835, we expense a portion of interest incurred. Qualified homebuilding assets consist of land, lots and homes, excluding finished unsold homes or finished models, that are under development or construction.

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The following table represents interest incurred, interest capitalized, and interest expense for the three and nine months ended September 30, 2014 and 2013:

	Three Months		Nine Months	
	2014	2013	2014	2013
Interest incurred	$6,716	$2,324	$11,403	$6,974
Interest capitalized	(3,875)	(3,344)	(8,451)	(4,459)
Interest expense	$2,841	$(1,020)	$2,952	$2,515

Interest expense for the three month period ended September 30, 2013 is negative due to an immaterial correction of the amounts capitalized in the previous 2013 quarters.

Note 4 - Investments in Partnerships and LLCs

We participate in entities with equity interests ranging from 20% to 58% for the purpose of acquiring and/or developing land in which we may or may not have a controlling interest or be the primary beneficiary. We determine the method for accounting for our investment at inception or upon a reconsideration event.

In May 2012, we entered into an agreement with JEN Arizona 4, LLC to form a limited liability company, EM 646, LLC (“EM 646”). We hold a 58.2% interest in the venture, which was organized for the purpose of acquiring, entitling, developing, and distributing specific sections of real property located in Mesa, Arizona. The property was acquired in November 2012 and is distributed to the partners at cost, once certain entitlements and development activities are completed. On May 14, 2014, EM 646 distributed $7,085 of developed land to AV Homes.

As of December 31, 2013, our consolidated balance sheet included $33,997 of Land and other inventories owned by EM 646. As of September 30, 2014, we were no longer considered the primary beneficiary of EM 646 and therefore deconsolidated this entity. The decrease from December 31, 2013 to September 30, 2014 is due to the distribution of a portion of the land out of the joint venture to the partners and to the aforementioned deconsolidation of the entity from our financial statements. The investment in EM 646 is accounted for as an equity method investment as of September 30, 2014. As of September 30, 2014, our consolidated balance sheet included $15,120 in Investments in unconsolidated entities related to the EM 646 joint venture.

We and our equity partners make capital contributions to the entity on a pro rata basis. The obligation to make such capital contributions is governed by the entity’s operating agreement. As of September 30, 2014, this entity was financed by partner equity and does not have third-party debt. In addition, we have not provided any guarantees to the entity or our equity partner. The assets of our investee can only be used to settle obligations of the investee.

We share in the profits and losses of unconsolidated entities generally in accordance with our ownership interests. We and our equity partners make initial and ongoing capital contributions to these unconsolidated entities on a pro rata basis. The obligation to make capital contributions is governed by each unconsolidated entity’s respective operating agreement. We made contributions totaling $1,955 and $99 to our unconsolidated entities during the nine months ended September 30, 2014 and 2013, respectively. The balance of our investments in unconsolidated entities was $16,308 and $1,230 at September 30, 2014 and December 31, 2013, respectively. The increase is due to the Company no longer being considered the primary beneficiary, resulting in the EM 646 entity being unconsolidated at September 30, 2014.

Note 5 - Debt

Our notes payable are summarized as follows:

	September 30, 2014	December 31, 2013
4.50% Convertible Notes due 2024 (a)	$—	$5,402
7.50% Senior Convertible Notes due 2016	55,481	55,500
7.50% Senior Exchange Convertible Notes due 2016	44,500	44,500
8.50% Senior Notes due 2019	200,000	—
Senior Secured Credit Facility	—	—
Total	$299,981	$105,402

(a) These Notes were tendered and repaid on April 1, 2014.

We made interest payments of $7,619 and $7,807 for the nine months ended September 30, 2014 and 2013, respectively. We were in compliance with all debt covenants as of September 30, 2014 and December 31, 2013.

8.50% Senior Notes due 2019

On June 30, 2014, we completed an underwritten offering for $200,000 aggregate principal amount of our 8.50% Senior Notes due 2019 (the "8.50% Notes"). The 8.50% Notes mature on July 1, 2019 unless earlier converted, redeemed or repurchased.

Interest: Interest on the 8.50% Notes is 8.50% per year, payable semi-annually in arrears in cash on January 1 and July 1 of each year, commencing January 1, 2015.

Optional redemption: The 8.50% Notes will be redeemable at our option, in whole or in part, at any time on or after July 1, 2016, at certain redemption prices, together with accrued and unpaid interest, if any, to, but excluding, the date of redemption.

- At any time prior to July 1, 2016, we may redeem up to 35% of the original principal amount of the notes with the proceeds of certain equity offerings at a redemption price of 108.500% of the principal amount of the notes, together with accrued and unpaid interest, if any, to, but excluding, the date of redemption.

- At any time prior to July 1, 2016, we may also redeem some or all of the notes at a price equal to 100% of the principal amount of the notes, plus a "make-whole premium," together with accrued and unpaid interest, if any, to, but excluding, the date of redemption.

- On or after July 1, 2016, we may, at our option, redeem the Notes, in whole or in part, at any time and from time to time, at the following redemption prices (expressed in percentages of the principal amount thereof), plus accrued and unpaid interest, if any, to, but excluding, the redemption date (subject to the right of holders of record on the relevant record date to receive interest due on the relevant interest payment date falling prior to or on the redemption date), if redeemed during the 12-month period beginning on July 1 of each year indicated below:

Year	Percentage
2016	106.375%
2017	103.188%
2018 and thereafter	100.000%

Financial covenants: The indenture will limit our ability to enter into and execute certain business transactions and agreements.

Exchange offer; registration rights: In connection with the issuance of the notes, we entered into an agreement with the initial purchasers obligating us to file a registration statement with the SEC within 360 days so that the initial purchasers can:

- exchange the notes for registered notes having substantially the same terms as the notes and evidencing the same indebtedness as the notes, and

- exchange the related note guarantees for registered guarantees having substantially the same terms as the original note guarantees.

We have assessed the 8.50% Notes and concluded that the impact of any embedded derivative features are not material as of September 30, 2014.

Senior Secured Credit Facility

On April 7, 2014, we entered into a $65,000 senior secured credit facility with JPMorgan Chase Bank, N.A., as agent, a lender and a letter of credit issuer. The other lenders and letter of credit issuers include Royal Bank of Canada and Credit Suisse AG. In August 2014, we increased the senior secured credit facility by $25,000 with the addition of Citibank, N.A. as an additional lender.

The senior secured credit facility includes revolving credit and letter of credit facilities in an aggregate principal amount of up to $90,000, with an "accordion" feature that allows us, with the consent of the lenders, to increase the aggregate amount to $175,000. The senior secured credit facility also includes a swing line loan facility in an aggregate principal amount of up to $30,000. The maximum amount available under the senior secured credit facility is limited to 100% of cash maintained in a borrowing base account, to the extent it exceeds the interest reserve, escrowed deposits and funds payable to us following the sale of real property, plus the following, subject to certain limitations:

- 85% of the appraised value of our real property that is under contract or under construction and is or is planned to be single-family residential housing units or model homes; plus
- 65% of the appraised value of our finished lots and lots under development; plus
- 50% of the appraised value of our entitled lands that are not finished lots or lots under development.

To be included in this borrowing base, the real property must be owned by us or one of our subsidiaries that guaranties the senior credit facility and it must be appraised, pledged as collateral and meet certain other criteria. At September 30, 2014, we had sufficient qualified assets in the borrowing base to cover the full capacity and had no borrowings outstanding.

Note 6 - Estimated Development Liability for Sold Land

The estimated development liability consists primarily of utilities improvements in Rio Rico and Poinciana for more than 8,000 home sites previously sold, in most cases prior to 1980, and is summarized as follows:

	September 30, 2014	December 31, 2013
Gross estimated unexpended costs	$35,935	$36,117
Less costs relating to unsold home sites	(2,885)	(2,885)
Estimated development liability for sold land	$33,050	$33,232

The estimated development liability for sold land is reduced by actual expenditures and is evaluated and adjusted, as appropriate, to reflect management's estimate of potential costs. In addition, we obtain third-party engineer evaluations and adjust this liability to reflect changes in the estimated costs. Cash expenditures associated with these obligations were $151 and $17 during the three months ended September 30, 2014 and 2013, respectively, and $176 and $46 during the nine months ended September 30, 2014 and 2013, respectively. Future increases or decreases of costs for construction, material and labor, as well as other land development and utilities infrastructure costs, may have a significant effect on the estimated development liability.

Note 7 - Commitments and Contingencies

We are involved in various pending litigation matters primarily arising in the normal course of our business. These cases are in various procedural stages. Although the outcome of these matters cannot be determined, we believe it is probable, in accordance with ASC 450-20, Loss Contingencies, that certain claims may result in costs and expenses estimated at approximately $0 and $275, which have been accrued in the accompanying consolidated balance sheets as of September 30, 2014 and December 31, 2013, respectively. The decrease from December 31, 2013 is due to a settlement that was paid in the nine month period ended September 30, 2014. Liabilities or costs arising out of these and other currently pending litigation is not expected to have a material adverse effect on our business, consolidated financial position, results of operations or cash flows.

Performance bonds, issued by third party entities, are used primarily to guarantee our performance to construct improvements in our various communities. As of September 30, 2014, we had outstanding performance bonds of approximately $29,405. The amount of outstanding performance bonds could fluctuate depending on the level of development activity. We do not believe that it is likely any of these outstanding performance bonds will be drawn upon.

Note 8 - Segments

Our current operations include the following reportable segments: the development, sale and management of active adult communities; the development and sale of primary residential communities; and the sale of commercial, industrial or other land.

Our operating segments are defined as a component of an enterprise for which discrete financial information is available and is reviewed regularly by the chief operating decision maker, to evaluate performance and make operating decisions. We have identified our chief operating decision maker as the Chief Executive Officer.

The following table summarizes our information for reportable segments for the three and nine months ended September 30, 2014 and 2013:

	Three Months		Nine Months	
	2014	2013	2014	2013
Operating income (loss):				
Active Adult Communities				
Revenues				
Homebuilding	$37,783	$17,304	$77,802	$35,910
Amenity	1,953	1,793	5,876	5,349
Total Revenues	39,736	19,097	83,678	41,259
Expenses				
Homebuilding	30,127	13,662	61,774	28,877
Homebuilding Selling, General and Administrative	4,191	2,390	11,664	7,663
Amenity	2,030	2,070	5,848	6,177
Segment operating income (loss)	3,388	975	4,392	(1,458)
Primary Residential Communities				
Revenues				
Homebuilding	33,345	14,658	67,353	36,330
Amenity	530	412	1,581	1,831
Total Revenues	33,875	15,070	68,934	38,161
Expenses				
Homebuilding	28,431	12,132	56,991	28,762
Homebuilding Selling, General and Administrative	5,169	1,960	10,637	5,183

Amenity	462	536	1,505	1,923
Segment operating income (loss)	(187)	442	(199)	2,293
Commercial and industrial and other land sales				
Revenues	12,942	674	29,168	9,556

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Expenses	8,672	95	20,910	5,352
Segment operating income	4,270	579	8,258	4,204
Other operations				
Revenues	88	57	173	496
Expenses	3	118	48	303
Segment operating income (loss)	85	(61)	125	193
Operating income	7,556	1,935	12,576	5,232
Unallocated income (expenses):				
Interest income and other	85	101	258	203
Equity loss from unconsolidated entities	(5)	(7)	(10)	(84)
Corporate general and administrative expenses	(4,016)	(3,885)	(12,264)	(11,882)
Interest expense	(2,841)	1,020	(2,952)	(2,515)
Other real estate expenses	(101)	(1,100)	(816)	(2,314)
Reversal of impairment charge	—	958	—	958
Income (loss) before income taxes	678	(978)	(3,208)	(10,402)
Income tax expense	—	—	—	—
Net income (loss) attributable to non-controlling interests	$—	$899	$329	$899
Net income (loss) attributable to AV Homes	$678	$(1,877)	$(3,537)	$(11,301)

Note 9 - Fair Value Disclosures

ASC 820, Fair Value Measurements and Disclosures (“ASC 820”), provides guidance for using fair value to measure assets and liabilities, defines fair value, establishes a framework for measuring fair value under GAAP, expands disclosures about fair value measurements, and establishes a fair value hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

The accounting standards require that assets and liabilities carried at fair value be classified and disclosed in one of the following three categories:

Level 1: Fair value determined based on quoted market prices in active markets for identical assets and liabilities.

Level 2: Fair value determined using significant observable inputs, such as quoted prices for similar assets or liabilities or quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, or inputs that are derived principally from or corroborated by observable market data, by correlation or other means.

Level 3: Fair value determined using significant unobservable inputs, such as discounted cash flows, or similar techniques.

The carrying value of cash and cash equivalents, restricted cash, receivables, and accounts payable approximates the fair value due to their short-term maturities.

The majority of our non-financial instruments, which include Land and Other Inventories and Property and Equipment, are not required to be carried at fair value on a recurring basis. However, if certain triggering events occur such that a non-financial instrument is required to be evaluated for impairment, a resulting asset impairment would require that the non-financial instrument be recorded at the lower of historical cost or its fair value.

For assets held for sale (vacant land parcels available for sale), we perform a quarterly impairment test in which the asset is reviewed for impairment by comparing the fair value (estimated sales price) less cost to sell the asset to its carrying value. If such fair value less cost to sell is less than the asset's carrying value, the carrying value is written down to its estimated fair value less cost to sell.

For assets held and used, if indicators are present, we perform an impairment test in which the asset is reviewed for impairment by comparing the estimated future undiscounted cash flows to be generated by the asset to its carrying value. If such cash flows are less than the asset's carrying value, the carrying value is written down to its estimated fair value. Generally, fair value is determined by discounting the estimated cash flows at a rate commensurate with the inherent risks associated with the asset and related estimated cash flow streams. The discount rate used in the determination of fair value would vary depending on the stage of development. Assumptions and estimates used in the determination of the estimated future cash flows are based on expectations of future operations and economic conditions and certain factors described below. Changes to these assumptions could significantly affect the estimates of future cash flows which could affect the potential for future impairments. Due to the uncertainties of the estimation process, actual results could differ significantly from such estimates.

The carrying amounts and fair values of our financial instruments at September 30, 2014 and December 31, 2013 are as follows:

	September 30, 2014		December 31, 2013	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Notes Payable:				
4.50% Notes	$—	$—	$5,402	$5,425
7.50% Notes and 7.50% Exchange Notes	$99,981	$102,960	$100,000	$111,775
8.50% Senior Notes	$200,000	$198,000	$—	$—
Contingent consideration (earn-out)	$2,500	$2,500	$—	$—

In estimating the fair value of financial instruments, we used the following methods and assumptions:

8.50% Senior Notes, 7.50% Notes, 7.50% Exchange Notes, and 4.50% Notes: At September 30, 2014 and December 31, 2013, the fair value of the 7.50% Notes, 7.50% Exchange Notes, and the 4.50% Notes is estimated, based on quoted or estimated market prices. These fall within Level 2 of the fair value hierarchy.

Contingent consideration ("earn-out"): This was first recognized as part of the purchase price paid for the Royal Oak acquisition in the first quarter of 2014 and falls within Level 3 of the fair value hierarchy. There has been no change in the balance of the earn-out and no gain or loss has been recognized related to the earn-out since inception. A Monte Carlo model was used to value the earn-out by simulating earnings, applying the terms of the earn-out in each simulated path, determining the average payment in each year across all the trials of the simulation, and calculating the sum of the present values of the payments in each year. The primary inputs and key assumptions of this Monte Carlo model include the following:

- Cost of debt: 7%
- Earnings volatility: 5% for 2014 and 15% for 2015
- Market risk premium: 6%
- Asset beta: 1.2

Given a range in the asset beta from 0.5 to 1.50 and a range in the earnings volatility from 5% to 25%, the valuation of the earn-out could vary from $2,428 to $2,642.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
($000's omitted, except share and per share data)

Executive Overview
We are engaged in the business of homebuilding, community development and the sale for third-party development of land in Florida, Arizona and North Carolina. We also engage to a limited degree in other real estate activities, such as the operation of amenities. We manage our business through three reportable segments:
• the development, sale and management of active adult communities;
• the development and sale of primary residential communities; and
• the sale of commercial, industrial or other land.

For the three months ended September 30, 2014, we derived 46% of our revenues from active adult, 39% of our revenues from primary residential, and 15% of our revenues from the commercial, industrial and other land segments, respectively. For the nine months ended September 30, 2014, we derived 46% of our revenues from active adult, 38% of our revenues from primary residential and 16% of our revenues from commercial, industrial and other land segments, respectively.

Our primary business is the development of land and the construction and sale of homes for people of all ages, including active adults. Our current homebuilding sales activities include existing locations in Florida, Arizona and North Carolina, with additional communities in the pipeline for each state. While we have historically generated more than half of our homebuilding revenues from our active adult community segment, we have invested and intend to continue to invest in our primary residential community segment in order to provide us with a diversified and well-balanced portfolio. We generate a smaller portion of our revenues from the sale of land from our portfolio of legacy land holdings that we sell in favorable market conditions. While we have in the past acquired land with the intention to resell to developers and other third parties, we now purchase land for the purpose of developing communities and will opportunistically sell existing non-core commercial and industrial assets, as well as scattered lot positions and land assets, that are in excess of our needed supply in a given market.

Solivita and Vitalia at Tradition, our active adult communities in Central Florida, and CantaMia in Goodyear, Arizona, currently serve as our flagship communities as we pursue the active adult segment. In addition, we are adding active adult communities in Raleigh-Durham, North Carolina and Mesa, Arizona, named Creekside at Bethpage and Encore at Eastmark, respectively. These communities will broaden our geographic footprint and product offering, and should provide us with future participation in the longer term growth of demand from the wave of Baby Boomers entering their retirement years.

Our current selling community count includes 25 locations, 18 in Florida, five in Arizona, and two in North Carolina, with additional communities in the pipeline for each state. Our current closing community count includes 18 locations, 14 in Florida and four in Arizona, with additional communities in the pipeline for both states and North Carolina.

The primary residential market is a segment that we continue to invest in to create a more diversified portfolio that mitigates cyclical impact over time. In the second half of 2013, we acquired over 800 lots in five new communities in the Phoenix market and began home sales and construction on these lots in late 2014 along with current building in our existing communities in the Phoenix market. Additionally, we are building out our existing communities in Central Florida and our lot positions within the recently acquired Royal Oak Homes and are expanding into new markets in North Carolina and Jacksonville, Florida. Replacement lot positions may require new acquisitions of developed lots or platted or unplatted undeveloped land, or we may decide to develop current land holdings, depending on market conditions within the submarket of these assets.

Factors affecting our results of operations

Our business is significantly influenced by a number of factors that affect our revenues, costs and capital expenditures, including those described below. In managing our business and the influence of these factors, we track several key operating metrics described below. This discussion includes forward-looking statements that are based on our current expectations. See ‘‘Risk factors’’ and ‘‘Special notes concerning forward-looking statements.’’

Revenue factors

General market conditions. Demand for housing in the United States is driven by a variety of factors including, among other things population growth, household income, mortgage rates, affordability, consumer confidence and employment levels. The supply of available housing varies from time to time based on a number of factors, including, among other things, home starts, inventories of existing homes available for sale and activities of speculative investors. Various housing indices have improved from 2013 to 2014, however the pace of improvement has moderated in the third quarter of 2014. While we believe that higher interest rates are inevitable and may have a moderating effect on demand and pricing, we believe this impact will be outweighed by the other factors driving increased sales activity as overall new home sales remain low compared with historical levels. We believe that any sustained rise in interest rates will be indicative of a stronger macroeconomic environment that will support a continued recovery in the homebuilding industry.

Demographic trends. As a substantial part of our business focuses on the active adult population, demographic trends have an impact on our results of operations. We believe that we will benefit from the long-term growth in demand for active adult communities as a result of the Baby Boomer generation entering their retirement years.

Cost factors

Subcontractors. Substantially all of our construction work is done by third-party subcontractors with our company acting as the general contractor. Our costs of using subcontractors is significantly influenced by the cost and availability of skilled labor in the markets where we operate.

Raw materials. We use drywall, cement, steel, lumber, and insulation, among other things, in the construction of our homes. Our subcontractors contract with third parties for these raw materials. From time to time, there may be shortages in these raw materials during periods of strong demand for housing that could cause delays in and increase our costs of home construction, which in turn could negatively affect our operating results.

Homebuilding expenses. Selling, general and administrative expenses are included in Homebuilding Expenses and are comprised of expenses not directly associated with the acquisition of lots and construction of homes, such as advertising, expenses associated with operating model homes, and salaries and commissions of sales personnel.

Corporate expenses. Corporate general and administrative expenses are included in General and Administrative Expenses and include costs associated with our executive, marketing, finance, accounting, legal, information services and human resources functions at the corporate level.

Other factors

Inflation. We may be adversely affected during periods of inflation because of higher land and construction costs. Inflation may also increase our financing costs. While we attempt to pass on to our customers increases in our costs through increased sales prices, market forces may limit our ability to do so. If we are unable to raise sales prices enough to compensate for higher costs, or if mortgage interest rates increase significantly, our revenues, gross margins and net income could be adversely affected.

Working capital. Our business is capital intensive and requires or may require expenditures for land and infrastructure development, housing construction, funding of operating deficits, real estate taxes, HOA deficits and interest expense, as well as potential new acquisitions of real estate and real estate–related assets. We manage our inventory levels through monitoring land development and home starts. We believe our efforts to opportunistically sell land that we have decided not to develop will help reduce and diversify land holdings and associated carrying costs.

Key operating metrics

Contracts signed. Net contracts signed for a given period represents the number of contracts we have entered into with homebuyers for the purchase and sale of homes, less the number of contracts that were cancelled in the same period. We consider a home sales contract cancelled when the customer terminates the contract.

Home starts. Home starts is the number of new homes on which we have started construction in a given period. Home starts are monitored by management in order to minimize the time between contract signing and closing.

Closings. Closings represents the number of home sales closed in the period. We recognize revenue equal to the sales price of a home when the sales are closed and title passes to the purchasers.

Backlog. Backlog is the number of homes we are building that are under contract for sale that have not closed as of the end of the period being presented. The dollar value of backlog is the revenue anticipated to be realized at closing equal to the purchase price provided in the applicable contract. Backlog is an important indicator of home closings and homebuilding revenues in future periods.

Average sales price. Average sales price represents total revenue for a given period divided by the number of closings for such period.

Seasonality

Our quarterly operating results generally fluctuate by season. We typically experience the highest new home order activity in the winter and spring months, although new order activity is also highly dependent on the number of actively selling communities and the timing of new community openings and closings as well as other market factors. We may experience higher liquidity demands during the first half of the calendar year as we incur the costs associated with new construction resulting from the increased sales volume. If, due to construction delays or other reasons, we are unable to deliver our expected number of homes in the second half of the calendar year, our full year results of operations may be adversely affected.

The following table provides a comparison of certain financial data related to our operations for the three and nine months ended September 30, 2014 and 2013:

	Three Months		Nine Months	
	2014	2013	2014	2013
Operating income (loss):				
Active Adult Communities				
Revenues				
Homebuilding	$37,783	$17,304	$77,802	$35,910
Amenity	1,953	1,793	5,876	5,349
Total Revenues	39,736	19,097	83,678	41,259
Expenses				
Homebuilding	30,127	13,662	61,774	28,877
Homebuilding Selling, General and Administrative	4,191	2,390	11,664	7,663
Amenity	2,030	2,070	5,848	6,177
Segment operating income (loss)	3,388	975	4,392	(1,458)
Primary Residential Communities				
Revenues				
Homebuilding	33,345	14,658	67,353	36,330
Amenity	530	412	1,581	1,831
Total Revenues	33,875	15,070	68,934	38,161
Expenses				
Homebuilding	28,431	12,132	56,991	28,762
Homebuilding Selling, General and Administrative	5,169	1,960	10,637	5,183
Amenity	462	536	1,505	1,923
Segment operating income (loss)	(187)	442	(199)	2,293

Commercial and industrial and other land sales				
Revenues	12,942	674	29,168	9,556

Expenses	8,672	95	20,910	5,352
Segment operating income	4,270	579	8,258	4,204
Other operations				
Revenues	88	57	173	496
Expenses	3	118	48	303
Segment operating income (loss)	85	(61)	125	193
Operating income	7,556	1,935	12,576	5,232
Unallocated income (expenses):				
Interest income and other	85	101	258	203
Equity loss from unconsolidated entities	(5)	(7)	(10)	(84)
Corporate general and administrative expenses	(4,016)	(3,885)	(12,264)	(11,882)
Interest expense	(2,841)	1,020	(2,952)	(2,515)
Other real estate expenses	(101)	(1,100)	(816)	(2,314)
Reversal of impairment charge	—	958	—	958
Income (loss) before income taxes	678	(978)	(3,208)	(10,402)
Income tax expense	—	—	—	—
Net income (loss) attributable to non-controlling interests	$—	$899	$329	$899
Net income (loss) attributable to AV Homes	$678	$(1,877)	$(3,537)	$(11,301)

We reclassified commission expense in the table above from "Homebuilding" to "Homebuilding Selling, General and Administrative." Below is a summary of the amounts incurred for the time periods presented:

	Three Months ended September 30		Nine Months ended September 30	
	2014	2013	2014	2013
Commission expense--Active Adult	$1,331	$525	$2,759	$1,284
Commission expense--Primary Residential	$1,450	$896	$2,912	$1,984

Data from closings for the active adult and primary residential homebuilding segments for the three and nine months ended September 30, 2014 and 2013 is summarized as follows:

For the three months ended September 30,	Number of Units	Revenues	Average Price Per Unit
2014			
Active adult communities	146	$37,783	$259
Primary residential	134	33,345	249
Total	280	$71,128	$254
2013			
Active adult communities	76	$17,304	$228
Primary residential	71	14,658	206
Total	147	$31,962	$217

For the nine months ended September 30,	Number of Units	Revenues	Average Price Per Unit
2014			
Active adult communities	303	$77,802	$257
Primary residential	268	67,353	251
Total	571	$145,155	$254
2013			
Active adult communities	149	$35,910	$241
Primary residential	161	36,330	226
Total	310	$72,240	$233

2014 Highlights

During the first nine months of 2014, we continued to execute our strategic and operational business plan through (i) the continued deployment of existing capital into land and lot acquisitions, as well as the acquisition of homebuilder operations, (ii) the development of existing land and lot positions, in addition to the construction of homes for sale, (iii) the increase in the number of homes sold and closed, (iv) the profitable sale of non-core asset positions, and (v) the successful completion of raising additional debt capital for continued growth and operational opportunities.

Three Months Ended September 30, 2014

Consolidated Results

Overall revenue increased by $51,743 or 148% to $86,641 during the three months ended September 30, 2014 compared to the three months ended September 30, 2013. This increase was comprised of homebuilding and amenity revenue which increased by $39,444 or 115% compared to the third quarter of 2013 and land sales which increased by $12,268. The increase in homebuilding and amenity revenue was driven by a 90% increase in units closed and a 17% increase in the average sales price for homes closed. During the quarter ended September 30, 2014, we completed the sale of a land position in Florida for $11,500. Land sales are highly variable from quarter to quarter and large fluctuations may occur. The gain on land sales during the three months ended September 30, 2014 was $4,270 compared to $579 during the same period in 2013. Homebuilding and amenity expenses increased by $37,675 or 115%, consistent with the increase in revenue.

Corporate general and administrative expenses increased by $131 to $4,016 for the three months ended September 30, 2014 compared to the same period in 2013. As a percentage of total revenue, general and administrative expenses improved to 5% for the three months ended September 30, 2014 compared to 11% for the same period in 2013. The decrease as a percent of revenue was driven by the significant increase in revenue, while containing our costs.

Interest expense increased to $2,841 for the three months ended September 30, 2014 compared to ($1,020) in the same period in 2013. The increase in interest expense is primarily attributable to the increase in qualifying debt related to the issuance of the 8.50% Notes in the second quarter of 2014, combined with a credit to interest expense taken in the third quarter of 2013 due to an increase in the amount of interest we capitalized to land under development and homes under construction.

Interest costs incurred, prior to capitalization, increased compared to the prior year to $6,716 for 2014 from $2,324 in the third quarter of 2013 due to the issuance of the 8.50% Notes.

Net income for the three months ended September 30, 2014 was $678 or $0.03 per share compared to a net loss of $1,877 or $0.86 per share for the three months ended September 30, 2013. The improvement in net income for the three months ended September 30, 2014 compared to the same period in 2013 was primarily due to the higher volume of closings, increase in average selling price, and increase in land sales, partially offset by the increase in interest expense.

Homebuilding Operations

Homebuilding revenue, which is revenue from home closings, increased $39,166 or 123% to $71,128 for the three months ended September 30, 2014 compared to the same period in 2013 due to a 90% increase in closings and a 17% increase in average sales price. In the active adult segment, revenues increased $20,479 or 118% over the prior period driven by a 92% increase in units closed due to higher absorption at our three existing active adult communities, predominantly in Florida, and a 14% increase in average price per unit due to the mix of homes sold and improved market conditions. The primary residential revenues increased $18,687 or 127% over the prior period driven by an 89% increase in units closed due to an increase in the number of communities in which we had closings from four to 16 and a 21% increase in the average price per unit due to a change in the mix of homes sold and improved market conditions.

Gross margin from combined home closings decreased by 160 basis points to 17.7% from 19.3% for the three months ended September 30, 2014 compared to the same period in 2013. Gross margin from active adult homebuilding decreased by 70 basis points to 20.3% from 21.0% for the three months ended September 30, 2014 compared to the same period in 2013 primarily due to the change in the mix of homes sold. Gross margin from primary residential homebuilding decreased by 250 basis points to 14.7% from 17.2% for the three months ended September 30, 2014 compared to the same period in 2013 due primarily to the change in community mix between years and the negative 50 basis point effect of the amortization of fair value step-up included in the inventory acquired in the Royal Oak transaction. Capitalized interest included in cost of sales for the active adult and primary residential segments was $850 and $467, respectively, for the three months ended September 30, 2014 and was $396 and $307, respectively, for the same period in 2013.

Homebuilding selling, general and administrative expenses as a percentage of homebuilding revenue improved to 13.2% for the three months ended September 30, 2014 from 13.6% for the same period in 2013. Homebuilding selling, general and administrative expenses for the active adult segment as a percentage of homebuilding revenue improved to 11.1% for the three months ended September 30, 2014 compared to 13.8% for the three months ended September 30, 2013. Homebuilding selling, general and administrative expenses for the primary residential segment as a percentage of homebuilding revenue was 15.5% and 13.4% for the three month periods ended September 30, 2014 and 2013, respectively. Improvements in cost leverage from the increased revenue were more than offset by the costs incurred to start up new selling communities which are not yet generating revenue.

Amenity net loss for the three months ended September 30, 2014 improved to $9 compared to $401 for the three months ended September 30, 2013.

Nine Months Ended September 30, 2014

Consolidated Results

Overall revenue increased by $92,481 or 103% to $181,953 during the nine months ended September 30, 2014 compared to the nine months ended September 30, 2013. Homebuilding and amenity revenue increased by $73,192 or 92% to $152,612 compared to the nine months ended September 30, 2013. The increase in homebuilding and amenity revenue was driven by an 84% increase in units closed and a 9% increase in the average sales price for homes closed. Revenue from land sales increased by $19,612 or 205% during the nine months ended September 30, 2014 compared to the nine months ended September 30, 2013. This increase for the nine months ended September 30, 2014 compared to the nine months ended September 30, 2013 is primarily due to the sale of a multi-family property in Arizona to a related party for $13,850 for a gain of $2,315 in the first quarter of 2014 and the sale of a land position in Florida in the third quarter of 2014 for $11,500 and a gain of $3,334. The average gain on land sales during the nine months ended September 30, 2014 was approximately 28% compared to approximately 44% during the same period in 2013. Homebuilding and amenity expenses increased by $69,900 or 90%, consistent with the increase in revenue.

Corporate general and administrative expenses increased by $382 to $12,264 for the nine months ended September 30, 2014 compared to the same period in 2013. As a percentage of total revenue, general and administrative expenses improved to 7% for the nine months ended September 30, 2014 compared to 13% for the same period in 2013. The decrease as a percent of revenue was driven by the significant increase in revenue, while containing our costs.

Interest expense increased $437 or 17% for the nine months ended September 30, 2014 compared to the same period in 2013. The increase in interest expense is primarily attributable to the $200,000 issuance of 8.50% Notes on June 30, 2014, partially offset by an increase in capitalized interest caused by an expansion of inventory under development in 2014 as compared to 2013. Interest costs incurred, prior to capitalization, increased from the prior year to $11,403 for the nine months ended September 30, 2014 as compared to $6,974 for the same period in 2013.

Net loss for the nine months ended September 30, 2014 was $3,537 or $0.16 per share compared to $11,301 or $1.67 per share for the nine months ended September 30, 2013. The decrease in net loss for the nine months ended September 30, 2014 compared to the same period in 2013 was primarily due to leveraging our overhead cost base with a significant increase in revenues, a decrease in other real estate expenses, and an increase in the profits from the sale of assets held for sale.

Homebuilding Operations

Homebuilding revenue increased 101% from $72,240 to $145,155 for the nine months ended September 30, 2014 compared to the same period in 2013 due to an 84% increase in closings and a 9% increase in average sales price. In the active adult segment, revenues increased $41,892 or 117% over the prior period driven by a 103% increase in units closed due to higher absorption at our three existing active adult communities, predominantly in Florida, and a 6.6% increase in the average price per unit. The primary residential revenues increased $31,023 or 85% over the prior period due to a 66% increase in units closed due to an increase in the number of communities in which we had closings from four to 16 and an 11.1% increase in the average price per unit due to changes in the mix of homes closed.

Gross margin from combined home closings decreased by 200 basis points to 18.2% from 20.2% for the nine months ended September 30, 2014 compared to the same period in 2013. Gross margin from active adult homebuilding increased by 100 basis points to 20.6% from 19.6% for the nine months ended September 30, 2014 compared to the same period in 2013 due to improved market conditions. Gross margin from primary residential homebuilding decreased to 15.4% from 20.8% for the nine months ended September 30, 2014 and 2013 primarily due to the impact of the 2014 acquisition of Royal Oak which has lower gross margins. The Royal Oak gross margins were negatively impacted by 120 basis points due to the amortization of fair value step-up included in the inventory acquired in the Royal Oak transaction. Capitalized interest included in cost of sales for the active adult and primary residential segments was $1,842 and $776, respectively, for the nine months ended September 30, 2014 and was $849 and $705, respectively, for the same period in 2013.

Combined homebuilding selling, general and administrative expenses as a percentage of homebuilding revenue decreased to 15.4% for the nine months ended September 30, 2014 from 17.8% for the same period in 2013, primarily driven by increasing revenue while containing our costs, partially offset by costs incurred to start up new selling communities which are not yet generating revenue. Homebuilding selling, general and administrative expenses for the active adult segment as a percentage of homebuilding revenue improved to 15.0% for the nine months ended September 30, 2014 compared to 21.3% for the same period in 2013 due to increased revenue, while containing our costs. Homebuilding selling, general and administrative expenses for the primary residential segment as a percentage of homebuilding revenue was 15.8% and 14.3% for the nine months ended September 30, 2014 and 2013, respectively. Overall improvements in cost leverage from the increased revenue were more than offset by the costs incurred to start up new selling communities which are not yet generating revenue.

Amenity net income (loss) for the nine months ended September 30, 2014 improved to $104 from ($920) for the nine months ended September 30, 2013.

Data from contracts signed for the active adult and primary residential homebuilding segments for the three and nine months ended September 30, 2014 and 2013 is summarized as follows:

For the three months ended September 30,	Gross Number of Contracts Signed	Cancellations	Contracts Signed, Net of Cancellations	Dollar Value	Average Price Per Unit
2014					
Active adult communities	115	(17)	98	$25,118	$256
Primary residential	206	(34)	172	42,021	$244
Total	321	(51)	270	$67,139	$249
2013					
Active adult communities	93	(14)	79	$19,670	$249
Primary residential	49	(24)	25	6,536	$261
Total	142	(38)	104	$26,206	$252
For the nine months ended September 30,					
2014					
Active adult communities	398	(43)	355	$93,469	$263
Primary residential	455	(59)	396	102,556	$259
Total	853	(102)	751	$196,025	$261
2013					
Active adult communities	292	(39)	253	$60,353	$239
Primary residential	173	(68)	105	25,769	$245
Total	465	(107)	358	$86,122	$241

The total number of net housing contracts signed during the three months ended September 30, 2014 compared to the same period in 2013 increased by 166 or 160%. The dollar value of housing contracts signed increased by $40,933 or 156%. The increase in units and value were driven by improvements in both the active adult and primary residential segments. The number of net housing contracts signed for the active adult segment during the three months ended September 30, 2014 increased by 19 or 24%, while the dollar value of housing contracts signed increased by $5,448 or 28%. The number of net housing contracts signed for the primary residential segment during the three months ended September 30, 2014 increased by 147 or 588%, while the dollar value of housing contracts signed increased by $35,466 or 543%. The increase reflects an increase in the number of selling communities from eight to 18 as well as improved market conditions for both of our homebuilding segments.

The cancellation rate for the three months ended September 30, 2014 decreased to 16% from 27% for the three months ended September 30, 2013. The cancellation rate in the primary residential segment decreased to 17% in the third quarter of 2014 from 49% in the third quarter of 2013 driven by higher cancellation rates in our Florida communities in 2013, which was primarily attributable to customer mortgage qualification issues. The cancellation rate within the active adult segment remained consistent at 15% for the three months ended September 30, 2014 and 2013.

The total number of net housing contracts signed during the nine months ended September 30, 2014 compared to the same period in 2013 increased by 393 or 110%. The dollar value of housing contracts signed increased by $109,903 or 128%. The increase in units and value were driven by improvements in both the active adult and primary residential segments. The number of net housing contracts signed for the active adult segment during the nine months ended September 30, 2014 increased by 102 or 40%, while the dollar value of housing contracts signed increased by $33,116 or 55%. The number of net housing contracts signed for the primary residential segment during the nine months ended September 30, 2014 increased by 291 or 277%, while the dollar value of housing contracts signed increased by $76,787 or 298%. The increase reflects an increase in the number of selling communities from eight to 18 as well as improved market conditions for both of our homebuilding segments.

During the nine months ended September 30, 2014, cancellations of previously signed contracts totaled 102 compared to 107 during the nine months ended September 30, 2013. As a percentage of the gross number of contracts signed, this represents 12% and 23% for the nine months ended September 30, 2014 and 2013, respectively. The 2013 cancellation rate was higher due to one primary residential community in Florida, which closed out in 2013, that experienced higher than normal rates.

The cancellation rate for the nine months ended September 30, 2014 decreased to 12% from 23% for the nine months ended September 30, 2013. The cancellation rate in the primary residential segment decreased to 13% in the first nine months of 2014 from 39% in the first nine months of 2013 driven by higher cancellation rates in our Florida communities in 2013 and was primarily attributable to customer mortgage qualification issues. The cancellation rate for the active adult segment decreased to 11% from 13% for the nine months ended September 30, 2014 and 2013, respectively.
Backlog for the active adult and primary residential homebuilding segments as of September 30, 2014 and 2013 is summarized as follows:

As of September 30	Number of Backlog Units	Dollar Volume	Average Price Per Unit
2014			
Active adult communities	179	$48,074	$269
Primary residential	291	72,862	$250
Total	470	$120,936	$257
2013			
Active adult communities	167	$41,401	$248
Primary residential	66	16,837	$255
Total	233	$58,238	$250

The backlog of housing contracts as of September 30, 2014 compared to September 30, 2013 increased by 237 or 102%, and the dollar value of backlog increased by $62,698 or 108%. The increase in units of backlog were driven by both the active adult and primary residential sectors. The backlog of housing contracts in the active adult segment as of September 30, 2014 compared to September 30, 2013 increased by 12 or 7%, and the dollar value increased by $6,673 or 16%. The backlog of housing contracts in the primary residential segment as of September 30, 2014 compared to September 30, 2013 increased by 225 or 341%, and the dollar value increased by $56,025 or 333%, driven by the increase in selling communities from eight to 18.
As of September 30, 2014, our inventory of unsold (speculative) homes, both completed and under construction, was 244 units, as compared to 60 units as of December 31, 2013. The increase in speculative homes is due to increased community count, an expanded number of floor plans, the increase in pace of sales, and the improved housing environment compared to the prior year. As of September 30, 2014, approximately 36% of unsold homes were completed compared to approximately 22% as of December 31, 2013.

The following is a breakdown of our land holdings as of September 30, 2014:

			Remaining Lots				
	Total Lots (1)	Closed Lots (2)	Developed	Partially Developed	Raw	Total Remaining Lots	Total Acres (3)
Principal Communities							
Active Adult Communities							
Florida							
Solivita	10,387	3,860	578	563	5,386	6,527	
Vitalia at Tradition	1,144	242	122	349	431	902	
	11,531	4,102	700	912	5,817	7,429	—

Arizona

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CantaMia	1,696	271	155	196	1,074	1,425	
Eastmark	905	—	—	288	617	905	
	2,601	271	155	484	1,691	2,330	
North Carolina							
Bethpage	658	—	—	166	492	658	
Total Active Adult Communities	14,790	4,373	855	1,562	8,000	10,417	—
Primary Residential Communities							
Florida	5,853	1,732	1,549	1,213	1,359	4,121	
Arizona	1,224	165	449	212	398	1,059	
North Carolina	496	—	61	55	380	496	
Total Primary Residential Communities	7,573	1,897	2,059	1,480	2,137	5,676	
Total Principal Communities	22,363	6,270	2,914	3,042	10,137	16,093	
Commercial & Industrial	—	—	—	—	—	—	1,613
Not Actively Building or Developing							
Platted Scattered Lots	4,578	3,545	514	488	31	1,033	
Unplatted Scattered Mixed-Use Raw Land	—	—	—	—	—	—	5,451
Total Not Actively Building or Developing	4,578	3,545	514	488	31	1,033	5,451
Land Held for Sale							
Platted Residential	236	—	125	—	—	125	
Unplatted Residential, Commerical or Industrial	—	—	—	—	—	—	175
Total Land Held for Sale	236	—	125	—	—	125	175
Grand Total	27,177	9,815	3,553	3,530	10,168	17,251	7,239

(1) Estimated planned lots/units are based on historical densities for our land. New projects may ultimately be developed into more or less than the number of lots/units stated.
(2) Closed lots are only shown for communities where we are actively building.
(3) Acres are reflected as gross acres and are not intended to represent net developable acres.

In accordance with 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. During 2008, we established a valuation allowance against our deferred tax assets. Our cumulative loss position over the evaluation period and the uncertain and volatile

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market conditions provided significant evidence supporting the need for a valuation allowance. During the three and nine months ended September 30, 2014, we recognized a decrease of $909 and an increase of $753, respectively, in the valuation allowance. As of September 30, 2014, our deferred tax asset valuation allowance was $130,985. In future periods, the allowance could be reduced based on sufficient evidence indicating that it is more likely than not that a portion of our deferred tax assets will be realized.

Liquidity and Capital Resources

Our primary business activities are capital intensive in nature. Significant capital resources are required to finance planned active adult and primary residential communities, homebuilding construction in process, community infrastructure, selling expenses, new projects and working capital needs, including funding of debt service requirements, operating deficits and the carrying costs of land.

Cash Flows

As of September 30, 2014, our cash and cash equivalents totaled $181,845 compared to $144,727 as of December 31, 2013. As of September 30, 2014 and December 31, 2013, total consolidated indebtedness was $299,981 and $105,402, respectively. The increase in cash and debt balances at September 30, 2014 are due to issuance of the $200,000 8.50% Notes in the second quarter of 2014. Additionally, as of September 30, 2014, we had $12,774 in restricted cash, which is comprised primarily of $11,985 on deposit as an interest reserve to comply with the terms of our Senior Secured Credit Facility, as compared to $3,956 in restricted cash as of December 31, 2013. We were in compliance with all debt covenants as of September 30, 2014 and December 31, 2013.

Our operating cash flows fluctuate relative to the status of development within existing communities, expenditures for land, new developments and other real estate activities, sales of various homebuilding product lines within those communities and other developments and to fund operating deficits.

For the nine months ended September 30, 2014, net cash used in operating activities was $82,597. The operating cash outflow was primarily due to an increase in restricted cash of $8,818 related to a covenant requirement in our credit facility and the increase in land and other inventories of $111,226. Using portions of the proceeds from our equity issuance in June 2013 and our newly issued senior notes, we purchased land and lots for the expansion of our primary residential segment and increased the number of homes under construction commensurate with the increase in our home sales. These outflows were partially offset by cash inflow of $19,537 from assets held for sale and an increase in accounts payable, estimated development liability and accrued and other liabilities of $14,168 as a result of the increase in the number of homes under construction. Net cash used by investing activities amounted to $62,684 primarily due to the purchase of Royal Oak. Net cash provided by financing activities was $184,858 primarily due to the issuance of the $200,000 8.50% Notes in the second quarter of 2014, partially offset by $9,220 of debt issue costs related to the senior secured credit facility and 8.50% Notes, as well as the repayment of $5,402 of the 4.50% Notes.

For the nine months ended September 30, 2013, net cash used in operating activities was $31,095. The operating cash outflow was primarily due to the net loss of $10,402 and the increase in land and other inventories of $32,071 primarily related to the increase in the number of homes under construction commensurate with the increase in our home sales. These outflows were partially offset by an increase of $5,298 in accounts payables, estimated development liability and accrued and other liabilities as a result of the increase in the number of homes under construction, and $2,310 of customer deposits and deferred revenues. Net cash used in investing activities amounted to $955, primarily due to investments in property and equipment. Net cash provided by financing activities of $128,402 was primarily attributable to the TPG Investment in common and preferred stock.

Off Balance Sheet Arrangements

Performance bonds, issued by third party entities, are used primarily to guarantee our performance to construct improvements in our various communities. As of September 30, 2014, we had outstanding performance bonds of approximately $29,405. The amount of outstanding performance bonds could fluctuate depending on the level of development activity. We do not believe that it is likely any of these outstanding performance bonds will be drawn upon.

Other

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Assuming that no significant adverse changes occur in our business, we anticipate the aggregate cash on hand, cash flow generated through homebuilding and related operations, sales of commercial and industrial and other land, and the revolving line of credit will provide sufficient liquidity to fund our business for 2014.

Critical Accounting Policies

There were no material changes in AV Homes' critical accounting policies during the nine months ended September 30, 2014. For additional information regarding AV Homes' critical accounting policies, refer to Item 7. Management's Discussion and Analysis in our Annual Report on Form 10-K for the year ended December 31, 2013.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There were no material changes in AV Homes' market risk during the nine months ended September 30, 2014. For additional information regarding AV Homes' market risk, refer to Item 7A. Quantitative and Qualitative Disclosures About Market Risk in our Annual Report on Form 10-K for the year ended December 31, 2013.

Special notes concerning forward-looking statements

Certain statements discussed in Item 2 (“Management’s Discussion and Analysis of Financial Condition and Results of Operations”) and elsewhere in this Form 10-Q constitute “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements involve known and unknown risks, uncertainties and other important factors that could cause the actual results, performance or achievements of results to differ materially from any future results, performance or achievements expressed or implied by such forward-looking statements. Such risks, uncertainties and other important factors include, among others: the stability of certain financial markets; disruption of the credit markets and reduced availability and more stringent financing requirements for commercial and residential mortgages of all types; the number of investor and speculator resale homes for sale and homes in foreclosure in our communities and in the geographic areas in which we develop and sell homes; the increased level of unemployment; the decline in net worth and/or of income of potential buyers; the decline in consumer confidence; the failure to successfully implement our business strategy (including our intentions to focus primarily on the development of active adult communities in the future); shifts in demographic trends affecting demand for active adult and primary housing; the level of immigration and migration into the areas in which we conduct real estate activities; our access to financing; construction defect and home warranty claims; changes in, or the failure or inability to comply with, government regulations; the failure to successfully integrate acquisitions into our business, including our acquisition of Royal Oak Homes, LLC and other factors as are described in our Annual Report on Form 10-K for the year ended December 31, 2013. Readers are cautioned not to place undue reliance on any forward-looking statements contained herein, which reflect management’s opinions only as of the date hereof.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), as of the end of the period covered by this quarterly report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this quarterly report.

Internal Control Over Financial Reporting

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we have determined that, during the fiscal quarter ended September 30, 2014, there were no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. Other Information

ITEM 1A. RISK FACTORS (Dollars in thousands)

Our business, financial condition, results of operations, cash flows and prospects, and the prevailing market price and performance of our common stock, may be adversely affected by a number of factors, including the matters discussed below. Certain statements and information set forth in this Quarterly Report on Form 10-Q, as well as other written or oral statements made from time to time by us or by our authorized officers on our behalf, constitute “forward-looking statements” within the meaning of the Federal Private Securities Litigation Reform Act of 1995. We intend for our forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. Forward-looking statements in this document speak only as of the date of this Quarterly Report on Form 10-Q and we undertake no duty or obligation to update or revise our forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law. Although we believe that the expectations, plans, intentions and projections reflected in our forward-looking statements are reasonable, such statements are subject to risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements.

There have not been any material changes to the risk factors discussed in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2013. However, the below risks and uncertainties related to our recent issuance of 8.5% Notes and our entry into the Credit Agreement should be considered by stockholders and potential investors in addition to the risk factors contained within our 10-K for the year ended December 31, 2013.

We may not be able to generate sufficient cash to service all of our indebtedness, including the notes, and may be forced to take other actions to satisfy our obligations under our indebtedness, which may not be successful.

Our ability to make scheduled payments on or refinance our debt obligations, including the notes offered hereby, depends on our financial condition and operating performance, which are subject to prevailing economic and competitive conditions and to certain financial, business, legislative, regulatory and other factors beyond our control. We may be unable to maintain a level of cash flows from operating activities sufficient to permit us to pay the principal, premium, if any, and interest on our indebtedness, including the notes.

If our cash flows and capital resources are insufficient to fund our debt service obligations, we could face substantial liquidity problems and could be forced to reduce or delay investments and capital expenditures or to dispose of material assets or operations, seek additional debt or equity capital or restructure or refinance our indebtedness, including the notes. We may not be able to effect any such alternative measures, if necessary, on commercially reasonable terms or at all and, even if successful, those alternative actions may not allow us to meet our scheduled debt service obligations. The credit agreement governing the revolving credit facility and the indenture that will govern the notes will restrict our ability to dispose of assets and use the proceeds from those dispositions and may also restrict our ability to raise debt or equity capital to be used to repay other indebtedness when it becomes due. We may not be able to consummate those dispositions or to obtain proceeds in an amount sufficient to meet any debt service obligations then due.

Our inability to generate sufficient cash flows to satisfy our debt obligations, or to refinance our indebtedness on commercially reasonable terms or at all, would materially and adversely affect our financial position and results of operations and our ability to satisfy our obligations under the 7.5% Notes, the 7.5% Exchange Notes and the 8.5% Notes (collectively, the "Notes").

If we cannot make scheduled payments on our debt, we will be in default and holders of the notes could declare all outstanding principal and interest to be due and payable, the lenders under the revolving credit facility could terminate their commitments to loan money, the lenders could foreclose against the assets securing their borrowings and we could be forced into bankruptcy or liquidation.

Despite our current level of indebtedness, we and our subsidiaries may still be able to incur substantially more debt. This could further exacerbate the risks to our financial condition described above.

We and our subsidiaries may be able to incur significant additional indebtedness in the future. Although the indentures related to our Notes contain and the credit agreement governing our revolving credit facility contains restrictions on the incurrence of additional indebtedness, these restrictions are subject to a number of qualifications and exceptions, and the additional indebtedness incurred in compliance with these restrictions could be substantial. These restrictions also will not prevent us from incurring obligations that do not constitute indebtedness. If new debt is added to our current debt levels, the related risks that we face could intensify.

The terms of the credit agreement governing our revolving credit facility and the indentures governing the Notes will restrict our current and future operations, particularly our ability to respond to changes or to take certain actions.

The indentures governing the Notes contain and the credit agreement governing our revolving credit facility contains a number of restrictive covenants that impose significant operating and financial restrictions on us and may limit our ability to engage in acts that may be in our long-term best interest, including restrictions on our ability to:

- incur additional indebtedness and guarantee indebtedness;
- pay dividends or make other distributions or repurchase or redeem our capital stock;
- prepay, redeem or repurchase certain debt;
- issue certain preferred stock or similar equity securities;
- make loans and investments;
- sell assets;
- incur liens;
- enter into transactions with affiliates;
- alter the businesses we conduct;
- enter into agreements restricting our subsidiaries' ability to pay dividends; and
- consolidate, merge or sell all or substantially all of our assets.

In addition, the restrictive covenants in the credit agreement governing our revolving credit facility require us to maintain specified financial ratios and satisfy other financial condition tests. Our ability to meet those financial ratios and tests can be affected by events beyond our control, and we may be unable to meet them.

A breach of the covenants or restrictions under the indentures governing the Notes or under the credit agreement governing our revolving credit facility could result in an event of default under the applicable indebtedness. Such a default may allow the creditors to accelerate the related debt and may result in the acceleration of any other debt to which a cross-acceleration or cross-default provision applies. In addition, an event of default under the credit agreement governing our revolving credit facility would permit the lenders under our revolving credit facility to terminate all commitments to extend further credit under that facility. Furthermore, if we were unable to repay the amounts due and payable under our revolving credit facility, those lenders could proceed against the collateral granted to them to secure that indebtedness. In the event our lenders or Noteholders accelerate the repayment of our borrowings, we and our subsidiaries may not have sufficient assets to repay that indebtedness. As a result of these restrictions, we may be:

- limited in how we conduct our business;

- unable to raise additional debt or equity financing to operate during general economic or business downturns; or
- unable to compete effectively or to take advantage of new business opportunities.

These restrictions may affect our ability to grow in accordance with our strategy. In addition, our financial results, our substantial indebtedness and our credit ratings could adversely affect the availability and terms of our financing.

Our variable rate indebtedness subjects us to interest rate risk, which could cause our debt service obligations to increase significantly.

Borrowings under our revolving credit facility are at variable rates of interest and expose us to interest rate risk. If interest rates were to increase, our debt service obligations on the variable rate indebtedness would increase even though the amount borrowed remained the same, and our net income and cash flows, including cash available for servicing our indebtedness, will correspondingly decrease. Assuming all loans are fully drawn, each quarter point change in interest rates would result in a $0.2 million change in annual interest expense on our indebtedness under our revolving credit facility. In the future, we may enter into interest rate swaps that involve the exchange of floating for fixed rate interest payments in order to reduce interest rate volatility. However, we may not maintain interest rate swaps with respect to all of our variable rate indebtedness, and any swaps we enter into may not fully mitigate our interest rate risk.

A major health and safety incident relating to our business could be costly in terms of potential liabilities and reputational damage.

Building sites are inherently dangerous, and operating in the homebuilding industry poses certain inherent health and safety risks. Due to health and safety regulatory requirements and the number of projects we work on, health and safety performance is critical to the success of all areas of our business. Any failure in health and safety performance may result in penalties for non-compliance with relevant regulatory requirements, and a failure that results in a major or significant health and safety incident is likely to be costly in terms of potential liabilities incurred as a result. Such a failure could generate significant negative publicity and have a corresponding impact on our reputation, our relationships with relevant regulatory agencies or governmental authorities, and our ability to sell homes, which, in turn, could have a material adverse effect on our business, financial condition and operating results.

We may incur additional healthcare costs arising from federal healthcare reform legislation and our compliance therewith.

In March 2010, the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 (the “Healthcare Reform Legislation”) were signed into law in the United States. The Healthcare Reform Legislation increases the level of regulatory complexity for companies that offer health and welfare benefits to their employees. Due to the breadth and complexity of the Healthcare Reform Legislation and the staggered implementation, the uncertain timing of the regulations and limited interpretive guidance, it is difficult to predict the overall impact of the healthcare reform legislation on our business over the coming years. Possible adverse effects include increased healthcare costs, which could adversely affect our business, financial condition and results of operations.

ITEM 6. EXHIBITS

3.1	*	Certificate of Incorporation, as amended and restated May 28, 1998 (filed as Exhibit 3(a) to Form 10-Q for the quarter ended June 30, 1998 (File No. 1-7395), and incorporated herein by reference).
3.2	*	Certificate of Amendment of Restated Certificate of Incorporation, dated May 26, 2000 (filed as Exhibit 3(a) to Form 10-Q for the quarter ended June 30, 2000 (File No. 1-7395), and incorporated herein by reference).
3.3	*	Amended and Restated By-Laws (filed as Exhibit 3.2 to Form 8-K filed on April 11, 2014 (File No. 1-7395), and incorporated herein by reference).
3.4	*	Certificate of Designation of Series B Junior Participating Preferred Stock of AV Homes, Inc. (filed as Exhibit 3.2 to Form 8-K filed on June 20, 2013 (File No. 1-7395), and incorporated herein by reference).
4.1	*	Indenture, dated March 30, 2004, between Avatar Holdings Inc. and JPMorgan Chase Bank, in respect of 4.50% Convertible Senior Notes due 2024 (filed as Exhibit 4.1 to Form 10-Q for the quarter ended March 31, 2004 (File No. 0-7616), and incorporated herein by reference).
4.2	*	Indenture, dated February 4, 2011, between Avatar Holdings Inc. and Wilmington Trust FSB, as Trustee (filed as Exhibit 4.1 to Form 8-K dated February 4, 2011, and incorporated herein by reference).
4.3	*	First Supplemental Indenture, dated as of February 4, 2011, between Avatar Holdings Inc., and Wilmington Trust FSB, as Trustee (filed as Exhibit 4.2 to Form 8-K dated February 4, 2011, and incorporated herein by reference).
4.4	*	Rights Agreement, dated as of June 19, 2013, by and between AV Homes, Inc. and Computershare Shareowner Services LLC, as Rights Agent (filed as Exhibit 4.1 to Form 8-K filed on June 20, 2013 (File No. 1-7395), and incorporated herein by reference).
4.5	*	Indenture, dated June 30, 2014, by and among AV Homes, Inc., certain subsidiaries of AV Homes, Inc., Wilmington Trust, National Association, as Trustee (filed as Exhibit 4.1 to Form 8-K dated July 1, 2014 (File No. 1-7395), and incorporated herein by reference).
4.6	*	Registration Rights Agreement, dated June 30, 2014, by and among AV Homes, Inc., certain subsidiaries of AV Homes, Inc., and J.P. Morgan Securities LLC (filed as Exhibit 4.2 to Form 8-K dated July 1, 2014 (File No. 1-7395), and incorporated herein by reference).
31.1		Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
31.2		Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
32.1		Certification of Chief Executive Officer required by 18 U.S.C. Section 1350 (as adopted by Section 906 of the Sarbanes-Oxley Act of 2002) (furnished herewith).
32.2		Certification of Principal Financial Officer required by 18 U.S.C. Section 1350 (as adopted by Section 906 of the Sarbanes-Oxley Act of 2002) (furnished herewith).
101.INS		XBRL Instance Document.
101.SCH		XBRL Taxonomy Extension Schema.
101.CAL		XBRL Taxonomy Extension Calculation Linkbase.
101.DEF		XBRL Taxonomy Extension Definition Linkbase.
101.LAB		XBRL Taxonomy Extension Label Linkbase.
101.PRE		XBRL Taxonomy Extension Presentation Linkbase.

* These exhibits are incorporated by reference and are on file with the Securities and Exchange Commission.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

			AV HOMES, INC.
Date:	October 31, 2014	By:	/s/ Roger A. Cregg Roger A. Cregg President and Chief Executive Officer (Principal Executive Officer)
Date:	October 31, 2014	By:	/s/ Michael S. Burnett Michael S. Burnett Executive Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)