HOVNANIAN ENTERPRISES INC
Form 10-K
December 24, 2008

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K

ý ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended OCTOBER 31, 2008

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

Commission file number: 1-8551

Hovnanian Enterprises, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	22-1851059 (I.R.S. Employer Identification No.)
110 West Front Street, P.O. Box 500, Red Bank, N.J. (Address of Principal Executive Offices)	07701 (Zip Code)

732-747-7800
(Registrant's Telephone Number, Including Area Code)
Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	**Name of Each Exchange on Which Registered**
Class A Common Stock, $.01 par value per share	New York Stock Exchange
Preferred Stock Purchase Rights	New York Stock Exchange
Depositary Shares, each representing 1/1,000th of a share of 7.625% Series A Preferred Stock	NASDAQ Global Market

Securities registered pursuant to Section 12(g) of the Act:
Class B Common Stock, $.01 par value per share
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act of 1933. Yes o No ý

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No ý

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 ý No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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

Large Accelerated Filer o Accelerated Filer ý Non-Accelerated Filer o

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

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity as of April 30, 2008 (the last business day of the registrant's most recently completed second fiscal quarter) was $443,351,894.

As of the close of business on December 19, 2008, there were outstanding 62,227,673 shares of the Registrant's Class A Common Stock and 14,639,746 shares of its Class B Common Stock.

HOVNANIAN ENTERPRISES, INC.

DOCUMENTS INCORPORATED BY REFERENCE:

Part III Those portions of registrant's definitive proxy statement to be filed pursuant to Regulation 14A in connection with registrant's annual meeting of shareholders to be held on March 19, 2009 which are responsive to Part III, Items 10, 11, 12, 13 and 14.

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Part I

ITEM 1
BUSINESS

Business Overview

We design, construct, market and sell single-family detached homes, attached townhomes and condominiums, mid-rise and high-rise condominiums, urban infill and active adult homes in planned residential developments and are one of the nation's largest builders of residential homes. Founded in 1959 by Kevork Hovnanian, Hovnanian Enterprises, Inc. (the "Company", "we", "us" or "our") was incorporated in New Jersey in 1967 and reincorporated in Delaware in 1983. Since the incorporation of our predecessor company and including unconsolidated joint ventures, we have delivered in excess of 280,000 homes, including 11,281 homes in fiscal 2008. The Company consists of two distinct operations: homebuilding and financial services. Our homebuilding operations consist of six segments: Northeast, Mid-Atlantic, Midwest, Southeast, Southwest and West. Our financial services operations provide mortgage loans and title services to the customers of our homebuilding operations.

We are currently, excluding unconsolidated joint ventures, offering homes for sale in 284 communities in 44 markets in 18 states throughout the United States. We market and build homes for first-time buyers, first-time and second-time move-up buyers, luxury buyers, active adult buyers and empty nesters. We offer a variety of home styles at base prices ranging from $36,000 (low income housing) to $2,455,000 with an average sales price, including options, of $300,000 nationwide in fiscal 2008.

Our operations span all significant aspects of the home-buying process from design, construction and sale, to mortgage origination and title services.

The following is a summary of our growth history:

1959 Founded by Kevork Hovnanian as a New Jersey homebuilder.

1983 Completed initial public offering.

1986 Entered the North Carolina market through the investment in New Fortis Homes.

1992 Entered the greater Washington, D.C. market.

1994 Entered the Coastal Southern California market.

1998 Expanded in the greater Washington, D.C. market through the acquisition of P.C. Homes.

1999 Entered the Dallas, Texas market through our acquisition of Goodman Homes. Further diversified and strengthened our position as New Jersey's largest homebuilder through the acquisition of Matzel & Mumford.

2001 Continued expansion in the greater Washington D.C. and North Carolina markets through the acquisition of Washington Homes. This acquisition further strengthened our operations in each of these markets.

2002 Entered the Central Valley market in Northern California and Inland Empire region of Southern California through the acquisition of Forecast Homes.

2003 Expanded operations in Texas and entered the Houston market through the acquisition of Parkside Homes and Brighton Homes. Entered the greater Ohio market through our acquisition of Summit Homes and entered the greater metro Phoenix market through our acquisition of Great Western Homes.

2004 Entered the greater Tampa, Florida market through the acquisition of Windward Homes, and started operations in the Minneapolis/St. Paul, Minnesota market.

2005 Entered the Orlando, Florida market through our acquisition of Cambridge Homes and entered the greater Chicago, Illinois market and expanded our position in Florida and Minnesota through the acquisition of the operations of Town & Country Homes, which occurred concurrently with our entering into a joint venture with affiliates of Blackstone Real Estate Advisors to own and develop Town & Country's existing residential communities. We also entered the Fort Myers market through the acquisition of First Home Builders of Florida, and the Cleveland, Ohio market through the acquisition of Oster Homes.

2006 Entered the coastal markets of South Carolina and Georgia through the acquisition of Craftbuilt Homes.

Geographic Breakdown of Markets by Segment

Hovnanian markets and builds homes that are constructed in 23 of the nation's top 50 housing markets. We segregate our homebuilding operations geographically into the following six segments:

Northeast: New Jersey, New York, Pennsylvania

Mid-Atlantic: Delaware, Maryland, Virginia, West Virginia, Washington, D.C.

Midwest: Illinois, Kentucky, Minnesota, Ohio

Southeast: Florida, Georgia, North Carolina, South Carolina

Southwest: Arizona, Texas

West: California

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We employed approximately 2,816 full-time employees (which we refer to as associates) as of October 31, 2008.

Our Corporate offices are located at 110 West Front Street, P.O. Box 500, Red Bank, New Jersey 07701, our telephone number is (732)747-7800, and our Internet website address is www.khov.com. We make available through our website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to these reports filed or furnished pursuant to Section 13(d) or 15(d) of the Exchange Act as soon as reasonably practicable after they are filed with, or furnished to, the SEC. Copies of the Company's Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to these reports are available free of charge upon request.

Business Strategies

Due to the progressive weakening of demand in our homebuilding markets over the past few years, we have experienced declines in revenues and gross profit, sustained significant asset impairment charges and incurred losses in fiscal 2007 and 2008. Although we believe the long-term fundamentals which support housing demand, namely population growth and household formation, remain solid and the current negative conditions will moderate over time, the timing of a recovery in the housing market is unclear. Consequently, our primary focus while market conditions are weak is to strengthen our financial condition by reducing inventories of homes and land, controlling and reducing construction and overhead costs, maximizing cash flows, reducing outstanding debt and maintaining strong liquidity.

In addition to our current focus on maintaining strong liquidity, we will continue to focus on our historic key business strategies. We believe that these strategies separate us from our competitors in the residential homebuilding industry and the adoption, implementation, and adherence to these principles will continue to improve our business, lead to higher profitability for our shareholders and give us a clear advantage over our competitors.

Our market concentration strategy is a key factor that enables us to achieve powers and economies of scale and differentiate ourselves from most of our competitors. Our goal is to become a significant builder in each of the selected markets in which we operate.

We offer a broad product array to provide housing to a wide range of customers. Our customers consist of first-time buyers, first-time and second-time move-up buyers, luxury buyers, active adult buyers and empty nesters. Our diverse product array includes single family detached homes, attached townhomes and condominiums, mid-rise and high-rise condominiums, urban infill and active adult homes.

We are committed to customer satisfaction and quality in the homes that we build. We recognize that our future success rests in the ability to deliver quality homes to satisfied customers. We seek to expand our commitment to customer service through a variety of quality initiatives. In addition, our focus remains on attracting and developing quality associates. We use several leadership development and mentoring programs to identify key individuals and prepare them for positions of greater responsibility within our Company.

We focus on achieving high return on invested capital. Each new community, whether through organic growth or acquisition, is evaluated based on its ability to meet or exceed internal rate of return requirements. Our belief is that the best way to create lasting value for our shareholders is through a strong focus on return on invested capital. However, given current market conditions it has been difficult to find new land investments that meet or exceed these rate of return requirements. Therefore, we have focused on managing the balance sheet by selling through our currently owned inventory and conserving cash to be prepared to invest in new land when market conditions are right.

We utilize a risk averse land strategy. We attempt to acquire land with a minimum cash investment and negotiate takedown options, thereby limiting the financial exposure to the amounts invested in property and predevelopment costs. This policy significantly reduces our risk and generally allows us to obtain necessary development approvals before acquisition of the land.

We enter into homebuilding and land development joint ventures from time to time as a means of controlling lot positions, expanding our market opportunities, establishing strategic alliances, reducing our risk profile, leveraging our capital base and enhancing our returns on capital. Our homebuilding joint ventures are generally entered into with third party investors to develop land and construct homes that are sold directly to homebuyers. Our land development joint ventures include those with developers and other homebuilders as well as financial investors to develop finished lots for sale to the joint venture's members or other third parties. Our Hovnanian Land Investment Group ("HLIG"), a wholly owned subsidiary, identifies, acquires, and develops large land parcels for sale to our homebuilding operations or to other homebuilders. HLIG may acquire the property directly or via joint ventures.

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We manage our financial services operations to better serve all of our homebuyers. Our current mortgage financing and title service operations enhance our contact with customers and allow us to coordinate the homebuying experience from beginning to end.

Operating Policies and Procedures

We attempt to reduce the effect of certain risks inherent in the housing industry through the following policies and procedures:

Training Our training is designed to provide our associates with the knowledge, attitudes, skills and habits necessary to succeed at their jobs. Our Training Department regularly conducts training classes in sales, construction, administration, and managerial skills.

Land Acquisition, Planning and Development Before entering into a contract to acquire land, we complete extensive comparative studies and analyses which assist us in evaluating the economic feasibility of such land acquisition. We generally follow a policy of acquiring options to purchase land for future community developments.

> We typically acquire land for future development principally through the use of land options which need not be exercised before the completion of the regulatory approval process. We attempt to structure these options with flexible take down schedules rather than with an obligation to take down the entire parcel upon receiving regulatory approval. Additionally, we purchase improved lots in certain markets by acquiring a small number of improved lots with an option on additional lots. This allows us to minimize the economic costs and risks of carrying a large land inventory, while maintaining our ability to commence new developments during favorable market periods.

> Our option and purchase agreements are typically subject to numerous conditions, including, but not limited to, our ability to obtain necessary governmental approvals for the proposed community. Generally, the deposit on the agreement will be returned to us if all approvals are not obtained, although predevelopment costs may not be recoverable. By paying an additional, nonrefundable deposit, we have the right to extend a significant number of our options for varying periods of time. In most instances, we have the right to cancel any of our land option agreements by forfeiture of our deposit on the agreement. In fiscal 2008 and 2007, rather than purchase additional lots in underperforming communities, we took advantage of this right and walked-away from 15,370 lots and 18,157 lots, respectively, out of 31,834 total lots and 54,261 total lots, respectively, under option, resulting in a pretax charge of $114.1 million and $126.0 million, respectively.

Design Our residential communities are generally located in suburban areas easily accessible through public and personal transportation. Our communities are designed as neighborhoods that fit existing land characteristics. We strive to create diversity within the overall planned community by offering a mix of homes with differing architecture, textures and colors. Recreational amenities such as swimming pools, tennis courts, club houses, open areas and tot lots are frequently included.

Construction We design and supervise the development and building of our communities. Our homes are constructed according to standardized prototypes which are designed and engineered to provide innovative product design while attempting to minimize costs of construction. We generally employ subcontractors for the installation of site improvements and construction of homes. However, we employ general contractors to manage the construction of most mid-rise or high-rise buildings. Agreements with subcontractors are generally short term and provide for a fixed price for labor and materials. We rigorously control costs through the use of computerized monitoring systems.

Because of the risks involved in speculative building, our general policy is to construct an attached condominium or townhouse building only after signing contracts for the sale of at least 50% of the homes in that building. For our mid-rise and high-rise buildings our general policy is to begin building after signing contracts for the sale of at least 40% of the homes in that building. A majority of our single family detached homes are constructed after the signing of a sales contract and mortgage approval has been obtained. This limits the build-up of inventory of unsold homes and the costs of maintaining and carrying that inventory.

Materials and Subcontractors We attempt to maintain efficient operations by utilizing standardized materials available from a variety of sources. In addition, we generally contract with subcontractors to construct our homes. We have reduced construction and administrative costs by consolidating the number of vendors serving certain markets and by executing national purchasing contracts with select vendors. In most instances, we use general contractors for mid-rise and high-rise construction. In recent years, we have experienced no significant construction delays due to shortages of materials or labor, however, we cannot predict the extent to which shortages in necessary materials or labor may occur in the future.

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Marketing and Sales Our residential communities are sold principally through on-site sales offices. In order to respond to our customers' needs and trends in housing design, we rely upon our internal market research group to analyze information gathered from, among other sources, buyer profiles, exit interviews at model sites, focus groups and demographic data bases. We make use of newspaper, radio, television, internet advertisements, magazine, our website, billboard, video and direct mail advertising, special promotional events, illustrated brochures, and full-sized and scale model homes in our comprehensive marketing program. In addition, we have home design galleries in our New Jersey, Virginia, Maryland, Texas, North Carolina, Florida, Illinois, Ohio, and portions of our California markets, which offer a wide range of customer options to satisfy individual customer tastes. These galleries have increased option sales and profitability in these markets.

Customer Service and Quality Control In many of our markets, associates are responsible for customer service and pre-closing quality control inspections as well as responding to post-closing customer needs. Prior to closing, each home is inspected and any necessary completion work is undertaken by us. Our homes are enrolled in a standard limited warranty program which, in general, provides a homebuyer with a one-year warranty for the home's materials and workmanship, a two-year warranty for the home's heating, cooling, ventilating, electrical and plumbing systems and a ten-year warranty for major structural defects. All of the warranties contain standard exceptions, including, but not limited to, damage caused by the customer.

Customer Financing We sell our homes to customers who generally finance their purchases through mortgages. Our financial services segment provides our customers with competitive financing and coordinates and expedites the loan origination transaction through the steps of loan application, loan approval and closing and title services. We originate loans in New Jersey, New York, Pennsylvania, Delaware, Maryland, Washington, D.C., Virginia, West Virginia, North Carolina, South Carolina, Georgia, Texas, Arizona, Illinois, Ohio, Minnesota, Florida, and California. We believe that our ability to offer financing to customers on competitive terms as a part of the sales process is an important factor in completing sales.

During the year ended October 31, 2008, for the markets in which our mortgage subsidiaries originated loans, 9.0% of our homebuyers paid in cash and 74.9% of our non-cash homebuyers obtained mortgages from one of our mortgage banking subsidiaries. The loans we originated in fiscal 2008 were 35.5% FHA/VA, 7.7% Alt-A, 52.6% prime, 0.3% broker sub-prime, 1.8% broker non-subprime and 2.1% construction to permanent.

We customarily sell virtually all of the loans and loan servicing rights that we originate within a short period of time. Loans are sold either individually or against forward commitments to institutional investors, including banks, mortgage banking firms, and savings and loan associations.

Code of Ethics In almost 50 years of doing business, we have been committed to sustaining our shareholders' investment through conduct that is in accordance with the highest levels of integrity. Our Code of Ethics is a set of guidelines and policies that govern broad principles of ethical conduct and integrity embraced by our Company. Our Code of Ethics applies to our principal executive officer, principal financial officer, controller, and all other associates of our company, including our directors and other officers. The Company's Code of Ethics is available on the Company's website at www.khov.com under "Investor Relations/Governance/Code of Ethics".

Corporate Governance We also remain committed to our shareholders in fostering sound corporate governance principles. The Company's "Corporate Governance Guidelines" assist the Board of Directors of the Company (the "Board") in fulfilling its responsibilities related to corporate governance conduct. These guidelines serve as a framework, addressing the function, structure, and operations of the Board, for purposes of promoting consistency of the Board's role in overseeing the work of management.

Residential Development Activities

Our residential development activities include site planning and engineering, obtaining environmental and other regulatory approvals and constructing roads, sewer, water and drainage facilities, recreational facilities and other amenities and marketing and selling homes. These activities are performed by our associates, together with independent architects, consultants and contractors. Our associates also carry out long-term planning of communities. A residential development generally includes single family detached homes and/or a number of residential buildings containing from two to twenty-four individual homes per building, together with amenities such as club houses, swimming pools, tennis courts, tot lots and open areas. We also develop mid-rise and high-rise buildings including some that contain over 300 homes per building.

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Current base prices for our homes in contract backlog at October 31, 2008 range from $36,000 (low income housing) to $2,455,000 in the Northeast, from $135,000 to $1,404,000 in the Mid-Atlantic, from $80,000 to $667,000 in the Midwest, from $139,000 to $551,000 in the Southeast, from $88,000 to $727,000 in the Southwest, and from $136,000 to $1,159,000 in the West. Closings generally occur and are typically reflected in revenues within eighteen months of when sales contracts are signed.

Information on homes delivered by segment for the year ended October 31, 2008 is set forth below:

(Housing Revenue in Thousands)	**Housing Revenues**	**Homes Delivered**	**Average Price**
Northeast	$ 679,488	1,412	$ 481,224
Mid-Atlantic	509,009	1,248	407,860
Midwest	209,759	965	217,367
Southeast	624,106	2,572	242,654
Southwest	603,513	2,616	230,701
West	551,978	1,764	312,913
Consolidated Total	$ 3,177,853	10,577	$ 300,449
Unconsolidated Joint Ventures	262,605	704	373,018
Total Including Unconsolidated Joint Ventures	$ 3,440,458	11,281	$ 304,978

The value of our net sales contracts, excluding unconsolidated joint ventures, decreased 48.4% to $1.9 billion for the year ended October 31, 2008 from $3.6 billion for the year ended October 31, 2007. This decrease was the result of a net 40.5% decrease in the number of homes contracted to 6,546 in 2008 from 11,006 in 2007, as well as increased incentives or base price reductions as the homebuilding market weakened further in 2008.

Information on the value of net sales contracts by segment for the years ended October 31, 2008 and 2007 is set forth below:

(Value of Net Sales Contracts in Thousands)	**2008**	**2007**	**% Change**
Northeast	$ 381,401	$ 802,459	52.5%
Mid-Atlantic	313,405	677,581	53.8%
Midwest	106,887	248,744	57.0%
Southeast	132,245	312,070	57.6%
Southwest	518,565	758,340	31.6%
West	421,292	833,986	49.5%
Consolidated Total	$ 1,873,795	$ 3,633,180	48.4%

As the homebuilding market and the economy as a whole have continued to weaken this year, the number of homes contracted has decreased in all of our segments by 32% or more. In addition, these weaker conditions have resulted in lower average prices in all segments except the Southwest, where the average prices are up 1.4%. This combination of lower net contracts and lower average prices has resulted in 48.4% lower value of net sales contracts.

The following table summarizes our active selling communities under development as of October 31, 2008. The contracted not delivered and remaining homes available in our active selling communities are included in the consolidated total home sites under the total residential real estate chart in Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations".

Active Selling Communities

	Communities	Approved Homes	Homes Delivered	Contracted Not Delivered(1)	Remaining Homes Available(2)
Northeast	31	7,965	5,269	495	2,201
Mid-Atlantic	48	10,231	5,568	385	4,278
Midwest	26	4,113	1,573	291	2,249
Southeast	32	10,079	7,180	163	2,736
Southwest	111	17,944	11,298	420	6,226
West	36	11,518	7,355	134	4,029
Total	284	61,850	38,243	1,888	21,719

(1) *Includes 139 home sites under option.*

(2) *Of the total remaining homes available, 1,596 were under construction or completed (including 321 models and sales offices), 9,897 were under option, and 229 were financed through purchase money mortgages.*

Backlog

At October 31, 2008 and October 31, 2007, including unconsolidated joint ventures, we had a backlog of signed contracts for 2,170 homes and 6,365 homes, respectively, with sales values aggregating $0.8 billion and $2.2 billion, respectively. The majority of our backlog at October 31, 2008 is expected to be completed and closed within the next twelve months. At November 30, 2008 and 2007, our backlog of signed contracts, including unconsolidated joint ventures, was 2,097 homes and 6,036 homes, respectively, with sales values aggregating $0.8 billion and $2.1 billion, respectively.

Sales of our homes typically are made pursuant to a standard sales contract that provides the customer with a statutorily mandated right of rescission for a period ranging up to 15 days after execution. This contract requires a nominal customer deposit at the time of signing. In addition, in the Northeast, Mid-Atlantic and some sections of the Southeast we typically obtain an additional 5% to 10% down payment due 30 to 60 days after signing. The contract may include a financing contingency, which permits the customers to cancel their obligation in the event mortgage financing at prevailing interest rates (including financing arranged or provided by us) is unobtainable within the period specified in the contract. This contingency period typically is four to eight weeks following the date of execution. As housing values decline in certain markets some customers cancel their contracts and forfeit their deposits. Cancellation rates are discussed further in Item 7 "Managements' Discussion and Analysis of Financial Condition and Results of Operation". Sales contracts are included in backlog once the sales contract is signed by the customer, which in some cases includes contracts that are in the rescission or cancellation periods. However, revenues from sales of homes are recognized in the Consolidated Statement of Operations, in accordance with generally accepted accounting principles, when title to the home is conveyed to the buyer, adequate initial and continuing investment have been received and there is no continued involvement.

Residential Land Inventory in Planning

It is our objective to control a supply of land, primarily through options, consistent with anticipated homebuilding requirements in each of our housing markets. Controlled land as of October 31, 2008, exclusive of communities under development described above under "Active Selling Communities" and excluding unconsolidated joint ventures, is summarized in the following table. The proposed developable home sites in communities under development are included in the 40,095 consolidated total home sites under the total residential real estate chart in Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations".

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Communities in Planning

(Dollars in Thousands)	Number of Proposed Communities	Proposed Developable Home Sites	Total Land Option Price	Book Value(2)
Northeast:				
Under Option(1)	26	4,478	$214,974	$ 58,477
Owned	18	1,801		314,299
Total	44	6,279		$372,776
Mid-Atlantic:				
Under Option(1)	5	290	$ 20,387	$ 4,790
Owned	5	1,353		25,391
Total	10	1,643		$ 30,181
Midwest:				
Under Option(1)	3	327	$ 9,634	$ 1,073
Owned	2	102		2,446
Total	5	429		$ 3,519
Southeast:				
Under Option(1)	9	998	$ 65,896	$ 3,377
Owned	11	583		21,335
Total	20	1,581		$ 24,712
Southwest:				
Under Option(1)	5	177	$ 11,098	$ 2,052
Owned	14	1,369		19,586
Total	19	1,546		$ 21,638
West:				
Under Option(1)	1	158	$ 4,740	$ 127
Owned	33	4,852		194,282
Total	34	5,010		$194,409
Totals:				
Under Option(1)	49	6,428	$326,729	$ 69,896
Owned	83	10,060		577,339
Combined Total	132	16,488		$647,235

(1) *Properties under option also include costs incurred on properties not under option but which are under evaluation. For properties under option, as of October 31, 2008, option fees and deposits aggregated approximately $13.3 million. As of October 31, 2008, we spent an additional $56.6 million in non-refundable predevelopment costs on such properties.*

(2) *The book value of $647.2 million is identified on the balance sheet as "Inventories land and land options held for future development or sale". The book value includes $1.3 million for specific performance options, $0.1 million for deposits on variable interest entity property and $1.7 million for other options reported under "Consolidated inventory not owned".*

We either option or acquire improved or unimproved home sites from land developers or other sellers. Under a typical agreement with the land developer, we purchase a minimal number of home sites. The balance of the home sites to be purchased is covered under an option agreement or a non-recourse purchase agreement. Due to the dwindling supply of improved lots in our segments, we have been increasing the percentage of optioned parcels of unimproved land for development as compared to owned land.

For additional financial information regarding our homebuilding segments, see Note 10 to the Consolidated Financial Statements.

Competition

Our homebuilding operations are highly competitive. We are among the top ten homebuilders in the United States in both homebuilding revenues and home deliveries. We compete with numerous real estate developers in each of the geographic areas in which we operate. Our competition ranges from small local builders to larger regional builders to publicly owned builders and developers, some of which have greater sales and financial resources than we do. Previously owned homes and the availability of rental housing provide additional competition. We compete primarily on the basis of reputation, price, location, design, quality, service and amenities.

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Regulation and Environmental Matters

We are subject to various local, state and federal statutes, ordinances, rules and regulations concerning zoning, building design, construction and similar matters, including local regulations which impose restrictive zoning and density requirements in order to limit the number of homes that can eventually be built within the boundaries of a particular locality. In addition, we are subject to registration and filing requirements in connection with the construction, advertisement and sale of our communities in certain states and localities in which we operate even if all necessary government approvals have been obtained. We may also be subject to periodic delays or may be precluded entirely from developing communities due to building moratoriums that could be implemented in the future in the states in which we operate. Generally, such moratoriums relate to insufficient water or sewerage facilities or inadequate road capacity.

In addition, some state and local governments in markets where we operate have approved, and others may approve, slow growth or no growth initiatives that could negatively impact the availability of land and building opportunities within those areas. Approval of these initiatives could adversely affect our ability to build and sell homes in the affected markets and/or could require the satisfaction of additional administrative and regulatory requirements, which could result in slowing the progress or increasing the costs of our homebuilding operations in these markets. Any such delays or costs could have a negative effect on our future revenues and earnings.

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

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

ITEM 1A
RISK FACTORS

You should carefully consider the following risks in addition to the other information included in this Form 10-K.

The homebuilding industry is significantly affected by changes in general and local economic conditions, real estate markets and weather conditions, which could affect our ability to build homes at prices our customers are willing or able to pay, could reduce profits that may not be recaptured, could result in cancellation of sales contracts and could affect our liquidity.

The homebuilding industry is cyclical, has from time to time experienced significant difficulties and is significantly affected by changes in general and local economic conditions such as:

- employment levels and job growth;
- availability of financing for home buyers;
- interest rates;
- foreclosure rates;
- inflation;
- adverse changes in tax laws;

- consumer confidence;
- housing demand; and
- population growth.

Turmoil in the financial markets could affect our liquidity. In addition, our cash balances are held at numerous financial institutions and may, at times, exceed insurable amounts. We believe we help to mitigate this risk by depositing our cash in major financial institutions and diversifying our investments. We also depend upon the lenders under our Revolving Credit Agreement to be able to perform under their commitments. If one or more of our lenders default on their funding obligations, the other lenders are not obligated to make up the shortfall, which would reduce our available liquidity. In addition, it may be difficult to find a bank willing to issue a letter of credit under our Revolving Credit Agreement in such a circumstance.

Weather conditions and natural disasters such as hurricanes, tornadoes, earthquakes, floods and fires can harm the local homebuilding business. Our business in Florida was adversely affected in late 2005 and into 2006 due to the impact of Hurricane Wilma on materials and labor availability and pricing. Conversely, Hurricane Ike, which hit Houston in September 2008, did not have an impact on materials and labor

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availability or pricing, but did impact the volume of home sales in subsequent weeks.

The difficulties described above could cause us to take longer and incur more costs to build our homes. We may not be able to recapture increased costs by raising prices in many cases because we fix our prices up to twelve months in advance of delivery by signing home sales contracts. In addition, some home buyers may cancel or not honor their home sales contracts altogether.

The homebuilding industry is undergoing a significant and sustained downturn which has, and could continue to, materially and adversely affect our business, liquidity and results of operations.

The homebuilding industry is now experiencing a significant and sustained downturn. An industry-wide softening of demand for new homes has resulted from a lack of consumer confidence, decreased housing affordability, decreased availability of mortgage financing, and large supplies of resale and new home inventories. In addition, an oversupply of alternatives to new homes, such as rental properties, resale homes and foreclosures, has depressed prices and reduced margins for the sale of new homes. Industry conditions had a material adverse effect on our business and results of operations during fiscal years 2008 and 2007. For example, we are continuing to experience significant declines in sales, significant reductions in our margins and higher cancellations. Further, we substantially increased our inventory through fiscal 2006, which required significant cash outlays and which has increased our price and margin exposure as we continue to work through this inventory. In addition, general economic conditions in the U.S. continue to weaken. Market volatility has been unprecedented and extraordinary in recent months, and the resulting economic turmoil may continue to exacerbate industry conditions or have other unforeseen consequences, leading to uncertainty about future conditions in the homebuilding industry. There can be no assurances that government responses to the disruptions in the financial markets will restore consumer confidence, stabilize the markets or increase liquidity and the availability of credit. Continuation or worsening of this downturn or general economic conditions would continue to have a material adverse effect on our business, liquidity and results of operations.

Leverage places burdens on our ability to comply with the terms of our indebtedness, may restrict our ability to operate, may prevent us from fulfilling our obligations and may adversely affect our financial condition.

We have a significant amount of debt. On a pro forma basis to give effect to the exchange offer (the "Exchange Offer") in which we issued $29.3 million aggregate principal amount of 18.0% Senior Secured Notes due 2017 in exchange for certain of our unsecured senior notes aggregating $71.4 million on December 3, 2008 (for more details about the Exchange Offer see Note 23 to the Consolidated Financial Statements):

- our debt, as of October 31, 2008, including the debt of the subsidiaries that guarantee our debt, would have been $2,472.9 million ($2,463.7 million net of discount);

- as of October 31, 2008, the aggregate outstanding face amount of letters of credit under our Revolving Credit Agreement would have been $197.5 million and we would have had no outstanding revolving loans (unchanged from the actual amount); and

- our debt service payments for the 12-month period ended October 31, 2008, which include interest incurred and mandatory principal payments on our corporate debt under the terms of our indentures (but which do not include principal and interest on non-recourse secured debt and debt of our financial subsidiaries), would have been approximately $168.4 million.

In addition, we had substantial contractual commitments and contingent obligations, including $632.5 million of performance bonds as of October 31, 2008. See Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations Contractual Obligations".

Our significant amount of debt could have important consequences. For example, it could:

- limit our ability to obtain future financing for working capital, capital expenditures, acquisitions, debt service requirements or other requirements;

- require us to dedicate a substantial portion of our cash flow from operations to the payment of our debt and reduce our ability to use our cash flow for other purposes;

- limit our flexibility in planning for, or reacting to, changes in our business;

- place us at a competitive disadvantage because we have more debt than some of our competitors; and

- make us more vulnerable to downturns in our business and general economic conditions.

Our ability to meet our debt service and other obligations will depend upon our future performance. We are engaged in businesses that are substantially affected by changes in economic cycles. Our revenues and earnings vary with the level of general economic activity in the markets we serve. Our businesses are also affected by customer sentiment and financial, political, business and other factors, many of which are beyond our control. The factors that affect our ability to generate cash can also affect our ability to raise additional funds for these purposes through the sale of equity securities, the refinancing of debt, or the sale of assets. Changes in prevailing interest rates may affect our ability to meet our debt service obligations, because borrowings under our Revolving Credit Agreement bear interest at floating rates. A higher interest rate on our debt service obligations could result in lower earnings.

Our business may not generate sufficient cash flow from operations and borrowings may not be available to us under our Revolving Credit Agreement in an amount sufficient to enable us to pay our indebtedness or to fund our other liquidity needs. Under the $300 million Revolving Credit Agreement, the amount available for revolving loans is limited to $100 million, with the remaining amounts available (subject to the borrowing base) for the issuance of letters of credit. We may need to refinance all or a portion of our debt on or before maturity, which we may not be able to do on favorable terms or at all.

Restrictive covenants in our debt instruments may restrict our ability to operate and if our financial performance worsens, we may not be able to maintain compliance with the financial covenants of our debt instruments.

The indentures governing our outstanding debt securities and our Revolving Credit Agreement impose restrictions on our operations and activities. The most significant restrictions relate to debt incurrence, sales of assets, cash distributions, including paying dividends on common and preferred stock, capital stock and debt repurchases, and investments by us and certain of our subsidiaries. The covenants in our Revolving Credit Agreement also include a borrowing base covenant and a covenant requiring either a minimum operating cash flow coverage ratio or minimum liquidity as of the last day of each fiscal quarter but do not contain any other financial covenants. Our level of home deliveries, amount of impairments and other financial performance factors negatively impacted the borrowing base and financial covenants under the Revolving Credit Agreement prior to its amendment in May 2008, and there can be no assurance that we will not violate the financial or other covenants under our debt instruments in the future or that the amount available under our Revolving Credit Agreement would not be reduced.

In addition, as a result of the restrictions in our indentures, which would require our fixed charge coverage ratio to be at least 2.0 to 1.0, we are currently restricted from paying dividends on our Series A Preferred Stock. If current market trends continue or worsen, we will continue to be restricted from paying dividends into fiscal 2009 and possibly beyond.

If we fail to comply with any of the restrictions or covenants of our debt instruments, and are unable to amend the instrument or obtain a waiver, or make timely payments on this debt and other material indebtedness, we could be precluded from incurring additional borrowings under our Revolving Credit Agreement and the trustees or the banks, as appropriate, could cause our debt to become due and payable prior to maturity. In such a situation, there can be no assurance that we would be able to obtain alternative financing. In addition, if we are in default of these agreements, we may be prohibited from drawing additional funds under the Revolving Credit Agreement, which could impair our ability to maintain sufficient working capital. Either situation could have a material adverse effect on the solvency of the Company.

The terms of our debt instruments allow us to incur additional indebtedness.

Under the terms of our indebtedness under our indentures and under the Revolving Credit Agreement, we have the ability, subject to our debt covenants, to incur additional amounts of debt. The incurrence of additional indebtedness could magnify the risks described above. In addition, certain obligations such as standby letters of credit and performance bonds issued in the ordinary course of business are not considered indebtedness under our indentures (and may be secured) and therefore are not subject to limits in our debt covenants.

We could be adversely affected by a negative change in our credit rating.

Our ability to access capital on favorable terms is a key factor in continuing to grow our business and operations in a profitable manner. On March 26, 2008, Moody's lowered our overall credit rating to B3 from B2 and maintained its negative outlook. On February 2, 2008, S&P lowered our credit rating to B- from B+ and maintained its negative outlook. On January 18, 2008, Fitch lowered the Company's issuer default rating to B- from BB- and placed the Company on negative rating outlook. These downgrades may make it more difficult and costly for us to access capital. A further downgrade by any of the principal credit agencies may exacerbate these difficulties.

Our business is seasonal in nature and our quarterly operating results can fluctuate.

Our quarterly operating results generally fluctuate by season. Historically, a large percentage of our agreements of sale have been entered into in the

winter and spring. The construction of a customer's home typically begins after signing the agreement of sale and can take 12 months or more to complete. Weather-related problems, typically in the late winter and early spring, can delay starts or closings and increase costs and thus reduce profitability. In addition, delays in opening communities could have an adverse impact on our sales and revenues. Due to these factors, our quarterly operating results may continue to fluctuate.

Our success depends on the availability of suitable undeveloped land and improved lots at acceptable prices.

Our success in developing land and in building and selling homes depends in part upon the continued availability of suitable undeveloped land and improved lots at acceptable prices. The availability of undeveloped land and improved lots for purchase at favorable prices depends on a number of factors outside of our control, including the risk of competitive over-bidding on land and lots and restrictive governmental regulation. Should suitable land opportunities become less available, the number of homes we may be able to build and sell would be reduced, which would reduce revenue and profits.

Raw material and labor shortages and price fluctuations could delay or increase the cost of home construction and adversely affect our operating results.

The homebuilding industry has from time to time experienced raw material and labor shortages. In particular, shortages and fluctuations in the price of lumber or in other important raw materials could result in delays in the start or completion of, or increase the cost of, developing one or more of our residential communities. In addition, we contract with subcontractors to construct our homes. Therefore, the timing and quality of our construction depends on the availability, skill and cost of our subcontractors. Delays or cost increases caused by shortages and price fluctuations could harm our operating results, the impact of which may be further affected depending on our ability to raise sales prices.

Changes in economic and market conditions could result in the sale of homes at a loss or holding land in inventory longer than planned, the cost of which can be significant.

Land inventory risk can be substantial for homebuilders. We must continuously seek and make acquisitions of land for expansion into new markets and for replacement and expansion of land inventory within our current markets. The market value of undeveloped land, buildable lots and housing inventories can fluctuate significantly as a result of changing economic and market conditions. In the event of significant changes in economic or market conditions, we may have to sell homes at a loss or hold land in inventory longer than planned. In the case of land options, we could choose not to exercise them, in which case we would write off the value of these options. Inventory carrying costs can be significant and can result in losses in a poorly performing project or market. The assessment of communities for indication of impairment is performed quarterly. While we consider available information to determine what we believe to be our best estimates as of the reporting period, these estimates are subject to change in future reporting periods as facts and circumstances change. See "Critical Accounting Policies." For example, during 2008 and 2007 we decided not to exercise many option contracts and walked away from land option deposits and predevelopment costs, which resulted in land option write-offs of $114.1 million and $126.0 million, respectively. Also, in 2008 and 2007, as a result of the slowing market, we recorded inventory impairment losses on owned property of $596.0 million and $331.8 million, respectively. If market conditions continue to worsen, additional inventory impairment losses and land option write-offs will likely be necessary.

Home prices and sales activities in the California, New Jersey, Texas, Virginia, Maryland, Florida and Arizona markets have a large impact on our profitability because we conduct a significant portion of our business in these markets.

We presently conduct a significant portion of our business in the California, New Jersey, Texas, Virginia, Maryland, Florida and Arizona markets. Home prices and sales activities in these markets, and in most of the other markets in which we operate, have declined from time to time, particularly as a result of slow economic growth. In particular, Arizona, California, Florida, New Jersey, Virginia and Maryland have declined significantly since the end of 2006. Furthermore, precarious economic and budget situations at the state government level may adversely affect the market for our homes in those affected areas. If home prices and sales activity decline in one or more of the markets in which we operate, our costs may not decline at all or at the same rate and profits may be reduced.

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Because almost all of our customers require mortgage financing, increases in interest rates or the decreased availability of mortgage financing could impair the affordability of our homes, lower demand for our products, limit our marketing effectiveness, and limit our ability to fully realize our backlog.

Virtually all of our customers finance their acquisitions through lenders providing mortgage financing. Increases in interest rates or decreases in availability of mortgage financing could lower demand for new homes because of the increased monthly mortgage costs to potential home buyers. Even if potential customers do not need financing, changes in interest rates and mortgage availability could make it harder for them to sell their existing homes to potential buyers who need financing. This could prevent or limit our ability to attract new customers as well as our ability to fully realize our backlog because our sales contracts generally include a financing contingency. Financing contingencies permit the customer to cancel his obligation in the event mortgage financing at prevailing interest rates, including financing arranged or provided by us, is unobtainable within the period specified in the contract. This contingency period is typically four to eight weeks following the date of execution of the sales contract.

Over the last several quarters, many lenders have significantly tightened their underwriting standards, and many subprime and other alternative mortgage products are no longer being made available in the marketplace. If these trends continue and mortgage loans continue to be difficult to obtain, the ability and willingness of prospective buyers to finance home purchases or to sell their existing homes will be adversely affected, which will adversely affect our operating results.

In addition, we believe that the availability of mortgage financing, including FNMA, FHLMC and FHA / VA financing, is an important factor in marketing many of our homes. Any limitations or restrictions on the availability of those types of financing could reduce our sales.

We conduct certain of our operations through unconsolidated joint ventures with independent third parties in which we do not have a controlling interest. These investments involve risks and are highly illiquid.

We currently operate through a number of unconsolidated homebuilding and land development joint ventures with independent third parties in which we do not have a controlling interest. At October 31, 2008, we had invested an aggregate of $71.1 million in these joint ventures, which had borrowings outstanding of approximately $320.2 million. In addition, as part of our strategy, we intend to continue to evaluate additional joint venture opportunities.

These investments involve risks and are highly illiquid. There are a limited number of sources willing to provide acquisition, development and construction financing to land development and homebuilding joint ventures, and as market conditions become more challenging, it may be difficult or impossible to obtain financing for our joint ventures on commercially reasonable terms. In addition, we lack a controlling interest in these joint ventures and therefore are usually unable to require that our joint ventures sell assets or return invested capital, make additional capital contributions or take any other action without the vote of at least one of our venture partners. Therefore, absent partner agreement, we will be unable to liquidate our joint venture investments to generate cash.

Homebuilders are subject to a number of federal, local, state and foreign laws and regulations concerning the development of land, the home building, sales and customer financing processes and protection of the environment, which can cause us to incur delays and costs associated with compliance and which can prohibit or restrict our activity in some regions or areas.

We are subject to extensive and complex regulations that affect the development and home building, sales and customer financing processes, including zoning, density, building standards and mortgage financing. These regulations often provide broad discretion to the administering governmental authorities. This can delay or increase the cost of development or homebuilding. In addition, some state and local governments in markets where we operate have approved, and others may approve, slow growth or no growth initiatives that could negatively impact the availability of land and building opportunities within those areas. Approval of these initiatives could adversely affect our ability to build and sell homes in the affected markets and/or could require the satisfaction of additional administrative and regulatory requirements, which could result in slowing the progress or increasing the costs of our homebuilding operations in these markets. Any such delays or costs could have a negative effect on our future revenues and earnings.

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

For example, during 2005, we received two requests for information pursuant to Section 308 of the Clean

Water Act from Region 3 of the Environmental Protection Agency (the "EPA"). These requests sought information concerning storm water discharge practices in connection with completed, ongoing and planned homebuilding projects by subsidiaries in the states and district that comprise EPA Region 3. We also received a notice of violations for one project in Pennsylvania and requests for sampling plan implementation in two projects in Pennsylvania. We have subsequently received notification from the EPA alleging violations of storm water discharge practices at other locations and requesting related information. We provided the EPA with information in response to its requests. The Department of Justice ("DOJ") is also involved in the review of these practices and enforcement with respect to them. We are engaged in discussions with the DOJ and EPA regarding a resolution of these matters. We cannot predict whether those discussions will result in a resolution, or what any resolution of these matters ultimately will require of us.

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

Product liability litigation and warranty claims that arise in the ordinary course of business may be costly.

As a homebuilder, we are subject to construction defect and home warranty claims arising in the ordinary course of business. Such claims are common in the homebuilding industry and can be costly. In addition, the amount and scope of coverage offered by insurance companies is currently limited, and this coverage may be further restricted and become more costly. If we are not able to obtain adequate insurance against such claims, we may experience losses that could hurt our financial results. Our financial results could also be adversely affected if we were to experience an unusually high number of claims or unusually severe claims.

We compete on several levels with homebuilders that may have greater sales and financial resources, which could hurt future earnings.

We compete not only for home buyers but also for desirable properties, financing, raw materials and skilled labor often within larger subdivisions designed, planned and developed by other homebuilders. Our competitors include other local, regional and national homebuilders, some of which have greater sales and financial resources.

The competitive conditions in the homebuilding industry together with current market conditions have, and could continue to, result in:

- difficulty in acquiring suitable land at acceptable prices;
- increased selling incentives;
- lower sales; or
- delays in construction.

Any of these problems could increase costs and/or lower profit margins.

We may have difficulty in obtaining the additional financing required to operate and develop our business.

Our operations require significant amounts of cash, and we may be required to seek additional capital, whether from sales of equity or borrowing additional money, for the future growth and development of our business. The terms or availability of additional capital is uncertain. Moreover, the indentures for our outstanding debt securities and our Revolving Credit Agreement contain provisions that restrict the debt we may incur and the equity we may issue in the future. If we are not successful in obtaining sufficient capital, it could reduce our sales and may hinder our future growth and results of operations. In addition, pledging substantially all of our assets to support the Revolving Credit Agreement, the $11^1/_2$% Senior Secured Notes due 2013 and the 18.0% Senior Secured Notes due 2017 issued in the Exchange Offer may make it more difficult to raise additional financing in the future.

Also, our mortgage business currently operates with working capital from a Mortgage Master Repurchase Agreement that comes due in July 2009. We believe we will be able to extend the Master Repurchase Agreement beyond its expiration date, but there can be no assurance of such extension.

Our future growth may include additional acquisitions of companies that may not be successfully integrated and may not achieve expected benefits.

Acquisitions of companies have contributed to our historical growth and may again be a component of our growth strategy in the future. In April 2006, we acquired Craftbuilt Homes. In the future, we may acquire other businesses, some of which may be significant. As a result of acquisitions of companies, we may need to seek additional financing and integrate product lines, dispersed operations and distinct corporate cultures. These integration efforts may not succeed or may distract our management from operating our existing business. Additionally, we may not be able to enhance our earnings as a result of acquisitions. Our failure to successfully identify and manage future acquisitions could harm our operating results.

Our controlling stockholders are able to exercise significant influence over us.

Kevork S. Hovnanian, the Chairman of our Board of Directors, and Ara K. Hovnanian, our President and Chief Executive Officer, have voting control, through personal holdings and family-owned entities, of Class A and Class B common stock that enables them to cast approximately 72.3% of the votes that may be cast by the holders of our outstanding Class A and Class B common stock combined. Their combined stock ownership enables them to exert significant control over us, including power to control the election of our Board of Directors and to approve matters presented to our stockholders. This concentration of ownership may also make some transactions, including mergers or other changes in control, more difficult or impossible without their support. Also, because of their combined voting power, circumstances may occur in which their interests could be in conflict with the interests of other stakeholders.

Our net operating loss carryforwards could be substantially limited if we experience an ownership change as defined in the Internal Revenue Code.

Based on recent impairments and our current financial performance, we generated a net operating loss carryforward of $404.8 million for the year ending October 31, 2008, and we may generate net operating loss carryforwards in future years.

Section 382 of the Internal Revenue Code contains rules that limit the ability of a company that undergoes an ownership change, which is generally any change in ownership of more than 50% of its stock over a three-year period, to utilize its net operating loss carryforwards and certain built-in losses recognized in years after the ownership change. These rules generally operate by focusing on ownership changes among stockholders owning directly or indirectly 5% or more of the stock of a company and any change in ownership arising from a new issuance of stock by the company.

If we undergo an ownership change for purposes of Section 382 as a result of future transactions involving our common stock, including purchases or sales of stock between 5% shareholders, our ability to use our net operating loss carryforwards and to recognize certain built-in losses would be subject to the limitations of Section 382. Depending on the resulting limitation, a significant portion of our net operating loss carryforwards could expire before we would be able to use them. Our inability to utilize our net operating loss carryforwards could have a negative impact on our financial position and results of operations.

In August 2008, we announced that our Board of Directors adopted a shareholder rights plan designed to preserve shareholder value and the value of certain tax assets primarily associated with net loss carryforwards and built in losses under Section 382 of the Internal Revenue Code. See Note 3 to the Consolidated Financial Statements for further details about the shareholder rights plan.

Utility shortages and outages or rate fluctuations could have an adverse effect on our operations.

In prior years, the areas in which we operate in California have experienced power shortages, including periods without electrical power, as well as significant fluctuations in utility costs. We may incur additional costs and may not be able to complete construction on a timely basis if such power shortages/outages and utility rate fluctuations continue. Furthermore, power shortages and outages, such as the blackout that occurred in 2003 in the Northeast, and rate fluctuations may adversely affect the regional economies in which we operate, which may reduce demand for our homes. Our operations may be adversely affected if further rate fluctuations and/or power shortages and outages occur in California, the Northeast or in our other markets.

Geopolitical risks and market disruption could adversely affect our operating results and financial condition.

Geopolitical events, such as the aftermath of the war with Iraq and the continuing involvement in Iraq, may have a substantial impact on the economy and the housing market. The terrorist attacks on the World Trade Center and the Pentagon on September 11, 2001 had an impact on our business and the occurrence of similar events in the future cannot be ruled out. The war and the continuing involvement in Iraq and Afghanistan, terrorism and related geopolitical risks have created many economic and political uncertainties, some of which may have additional material adverse effects on the U.S. economy, and our customers and, in turn, our results of operations and financial condition.

ITEM 1B
UNRESOLVED STAFF COMMENTS

None.

ITEM 2
PROPERTIES

We own a 69,000 square foot office complex located in the Northeast that serves as our corporate headquarters. We own 215,000 square feet of office and warehouse space throughout the Midwest. We lease approximately 868,000 square feet of space for our segments located in the Northeast, Mid-Atlantic, Midwest, Southeast, Southwest and West.

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ITEM 3
LEGAL PROCEEDINGS

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

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

In March 2005, we received two requests for information pursuant to Section 308 of the Clean Water Act from Region 3 of the Environmental Protection Agency (the "EPA"). These requests sought information concerning storm water discharge practices in connection with completed, ongoing and planned homebuilding projects by subsidiaries in the states and district that comprise EPA Region 3. We also received a notice of violations for one project in Pennsylvania and requests for sampling plan implementation in two projects in Pennsylvania. We have subsequently received notification from the EPA alleging violations of storm water discharge practices at other locations and requesting related information. We provided the EPA with information in response to its requests. The Department of Justice ("DOJ") is also involved in the review of these practices and enforcement with respect to them. We are engaged in discussions with the DOJ and EPA regarding a resolution of these matters. We cannot predict whether those discussions will result in a resolution, or what any resolution of these matters ultimately will require of us.

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

The Company is also involved in the following litigation in different parts of the country:

The Company, Chief Executive Officer and President Ara K. Hovnanian, Executive Vice President and Chief Financial Officer J. Larry Sorsby and a former officer of a Company subsidiary have been named as defendants in a purported class action. The original complaint, which only named Mr. Sorsby as a defendant, was filed on September 14, 2007 in the United States District Court for the Central District of California, captioned *Herbert Mankofsky v. J. Larry Sorsby,* and names only Mr. Sorsby as a defendant. On January 31, 2008, the court appointed Herbert Mankofsky as Lead Plaintiff. On February 19, 2008, the action was transferred to the United States District Court for the District of New Jersey. On March 10, 2008, plaintiff filed an amended complaint, captioned *In re Hovnanian Enterprises, Inc. Securities Litigation*, alleging, among other things, that the defendants violated federal securities laws by making false and misleading statements regarding the Company's business and future prospects in connection with the Company's acquisition of First Home Builders of Florida. The Company filed a Motion to Dismiss the amended complaint on July 14, 2008. On September 11, 2008, plaintiff filed his opposition to the Motion to Dismiss. The Company filed its reply brief on October 28, 2008. The Motion to Dismiss is now fully briefed and is pending before the court.

The Company has been named as a defendant in a purported class action suit filed May 30, 2007 in the United States District Court for the Eastern District of Pennsylvania*, Mark W. Mellar, et al., v. Hovnanian Enterprises, Inc., et al.*, asserting that the Company's sales of homes along with the financing of home purchases and the provision of title insurance by affiliated companies violated the Real Estate Settlement Procedures Act. Plaintiffs seek to represent a class of persons who purchased a home from the Company, who received a mortgage loan via a subsidiary of the Company and/or who bought title insurance from a company affiliated with the Company, and are seeking damages (including treble damages), declaratory and injunctive relief, and attorney's fees and costs. The Company's Motion to Dismiss the complaint was denied by the Court on March 4, 2008 without prejudice. The case was settled in October 2008 (with the Stipulation of Dismissal filed with the Court on November 5, 2008) and the terms of the settlement had no material impact on the Company.

A subsidiary of the Company has been named as a defendant in a purported class action suit filed on May 30, 2007 in the United States District Court for the Middle District of Florida, *Randolph Sewell, et al., v. D'Allesandro & Woodyard, et al.*, alleging violations of the federal securities acts, among other allegations, in connection with the sale of some of the subsidiary's homes in Fort Myers, Florida. Plaintiffs filed an amended complaint on October 19, 2007. Plaintiffs sought to represent a class of certain home purchasers in southwestern Florida and sought damages, rescission of certain purchase agreements, restitution of out-of-pocket expenses, and attorneys' fees and costs. The Company's subsidiary filed a Motion to Dismiss the amended complaint on December 14, 2007. Following oral argument on the motion in September 2008, the court dismissed the amended complaint with leave for plaintiffs to amend. Plaintiffs filed a second amended complaint on October 31, 2008. Plaintiffs seek to represent a class of certain home purchasers in southwestern Florida and seek damages, rescission of certain purchase agreements, restitution of out-of-pocket expenses, and attorneys' fees and costs.

On April 4, 2008, K. Hovnanian Enterprises, Inc. ("K. Hovnanian"), a wholly-owned subsidiary of the Company, initiated arbitration proceedings against GMAC Model Home Finance, LLC ("GMAC") to resolve a dispute arising under a Model Purchase, Construction Management and Rental Agreement dated October 4, 2001 (the "Agreement"). The Company is the guarantor of K. Hovnanian's obligations under the Agreement. On March 31, 2008, GMAC advised K. Hovnanian that it was terminating all model home leases and intended to take possession of all model homes at issue based on the claim that K. Hovnanian had defaulted under the Agreement. In its arbitration demand, K. Hovnanian disputes the existence of any default and claims that GMAC has materially breached the Agreement by failing to fund certain construction costs. On April 25, 2008, GMAC asserted counterclaims against K. Hovnanian and the Company alleging that K. Hovnanian defaulted and that all leases were terminated. On September 4, 2008, parties entered into a settlement and release agreement resolving all disputes between them arising under the Agreement. The terms of the settlement had no material impact on the Company.

ITEM 4
SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

During the fourth quarter of the fiscal year ended October 31, 2008, no matters were submitted to a vote of security holders. See Note 23 to the Consolidated Financial Statements for a discussion of the matters submitted to a vote of security holders during the first quarter of fiscal 2009.

EXECUTIVE OFFICERS OF THE REGISTRANT

Information on executive officers of the registrant is incorporated herein from Part III, Item 10.

Part II

ITEM 5
MARKET FOR THE REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our Class A Common Stock is traded on the New York Stock Exchange and was held by 597 stockholders of record at December 19, 2008. There is no established public trading market for our Class B Common Stock, which was held by 284 stockholders of record at December 19, 2008. In order to trade Class B Common Stock, the shares must be converted into Class A Common Stock on a one-for-one basis. The high and low sales prices for our Class A Common Stock were as follows for each fiscal quarter during the years ended October 31, 2008 and 2007:

	Oct. 31, 2008		**Oct. 31, 2007**	
Quarter	**High**	**Low**	**High**	**Low**
First	$10.45	$4.80	$38.01	$27.81
Second	$12.41	$8.09	$36.98	$22.85
Third	$11.87	$4.64	$25.95	$13.24
Fourth	$ 9.05	$3.38	$16.22	$ 9.99

Certain debt instruments to which we are a party contain restrictions on the payment of cash dividends. As a result of the most restrictive of these provisions, we are not currently able to pay any cash dividends. We have never paid a cash dividend to common stockholders.

Issuer Purchases of Equity Securities

In July 2001, our Board of Directors authorized a stock repurchase program to purchase up to 4 million shares of Class A Common Stock (adjusted for a 2 for 1 stock dividend on March 5, 2004). No shares of our Class A Common Stock or Class B Common Stock were purchased by or on behalf of Hovnanian Enterprises or any affiliated purchaser during the fiscal fourth quarter of 2008 (excluding purchases by certain members of the Hovnanian family, which have been previously reported in filings with the Securities and Exchange Commission). The maximum number of shares that may yet be purchased under the Company's plans or programs is 0.6 million.

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ITEM 6
SELECTED CONSOLIDATED FINANCIAL DATA

The following table sets forth selected consolidated financial data and should be read in conjunction with the financial statements included elsewhere in this Form 10-K. Per common share data and weighted average number of common shares outstanding reflect all stock splits. The selected consolidated financial data should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our Consolidated Financial Statements and Notes thereto included elsewhere in this Form 10-K.

	Year Ended				
Summary Consolidated Statements of Operations Data (In Thousands, Except Per Share Data)	**October 31, 2008**	**October 31, 2007**	**October 31, 2006**	**October 31, 2005**	**October 31, 2004**
Revenues	$ 3,308,111	$ 4,798,921	$ 6,148,235	$ 5,348,417	$ 4,153,890
Expenses	4,439,559	5,417,664	5,930,514	4,602,871	3,608,909
(Loss) income from unconsolidated joint ventures	(36,600)	(28,223)	15,385	35,039	4,791
(Loss) income before income taxes	(1,168,048)	(646,966)	233,106	780,585	549,772
State and Federal income tax (benefit)/provision	(43,458)	(19,847)	83,573	308,738	201,091
Net (loss) income	(1,124,590)	(627,119)	149,533	471,847	348,681
Less: preferred stock dividends		10,674	10,675	2,758	
Net (loss) income available to common stockholders	$(1,124,590)	$ (637,793)	$ 138,858	$ 469,089	$ 348,681
Per share data:					
Basic:					
(Loss) income per common share	$ (16.04)	$ (10.11)	$ 2.21	$ 7.51	$ 5.63
Weighted average number of common shares outstanding	70,131	63,079	62,822	62,490	61,892
Assuming dilution:					
(Loss) income per common share	$ (16.04)	$ (10.11)	$ 2.14	$ 7.16	$ 5.35
Weighted average number of common shares outstanding	70,131	63,079	64,838	65,549	65,133

Summary Consolidated Balance Sheet Data (In Thousands)	**October 31, 2008**	**October 31, 2007**	**October 31, 2006**	**October 31, 2005**	**October 31, 2004**
Total assets	$ 3,637,322	$ 4,540,548	$ 5,480,035	$ 4,726,138	$ 3,156,267
Mortgages, term loans, revolving credit agreements, and notes payable	$ 107,913	$ 410,298	$ 319,943	$ 271,868	$ 354,055
Senior secured notes, senior notes, and senior subordinated notes	$ 2,505,805	$ 1,910,600	$ 2,049,778	$ 1,498,739	$ 902,737
Stockholders' equity	$ 330,264	$ 1,321,803	$ 1,942,163	$ 1,791,357	$ 1,192,394

Ratios of Earnings to Fixed Charges and Earnings to Combined Fixed Charges and Preferred Stock Dividends

For purposes of computing the ratio of earnings to fixed charges and the ratio of earnings to combined fixed charges and preferred stock dividends, earnings consist of earnings from continuing operations before income taxes and income or loss from equity investees, plus fixed charges and distributed income of equity investees, less interest capitalized. Fixed charges consist of all interest incurred plus the amortization of debt issuance costs and bond discounts. Combined fixed charges and preferred stock dividends consist of fixed charges and preferred stock dividends declared. The fourth quarter of 2005 was the first period we declared and paid preferred stock dividends and, due to covenant restrictions, we have been prohibited from paying dividends beginning with the first quarter of fiscal 2008.

The following table sets forth the ratios of earnings to fixed charges and the ratios of earnings to combined fixed charges and preferred stock dividends for each of the periods indicated:

	Years Ended October 31,				
	2008	2007	2006	2005	2004
Ratio of earnings to fixed charges	(a)	(a)	2.0	7.8	6.3
Ratio of earnings to combined fixed charges and preferred stock dividends	(b)	(b)	1.8	7.5	6.3

(a)
Earnings for the years ended October 31, 2008 and 2007 were insufficient to cover fixed charges for such period by $1,138.5 million and $667.5 million, respectively.

(b)
Earnings for the years ended October 31, 2008 and 2007 were insufficient to cover fixed charges and preferred stock dividends for such period by $1,138.5 million and $678.6 million, respectively.

ITEM 7
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Beginning during the second half of our fiscal year ended October 31, 2006 and continuing through today, the U. S. housing market has been impacted by a lack of consumer confidence, increasing home foreclosure rates and large supplies of resale and new home inventories. The result has been weakened demand for new homes, slower sales, higher than normal cancellation rates, and increased price discounts and other sales incentives to attract homebuyers. Additionally, the availability of certain mortgage financing products became more constrained starting in February 2007 when the mortgage industry began to more closely scrutinize sub-prime, Alt-A, and other non-prime mortgage products. The combination of these homebuilding industry and related mortgage financing developments resulted in significant decreases in our revenues and gross margins during 2008 and 2007 compared with prior years. Additionally, we incurred total land-related charges of $710.1 million and $457.8 million for the years ended October 31, 2008 and 2007, respectively. These charges resulted from the write-off of deposit and preacquisition costs of $114.1 million and $126.0 million, respectively, related to land we no longer plan to pursue and impairments on owned inventory of $596.0 million and $331.8 million for the fiscal years ended October 31, 2008 and 2007. In addition to land related charges, the continued weakening of the market resulted in impairments of our intangible assets and goodwill of $35.4 million and $135.2 million during fiscal 2008 and 2007, respectively.

We have exposure to additional impairments of our inventories, which, as of October 31, 2008, have a book value of $2.2 billion, net of $719.0 million of impairments recorded on 181 of our communities. We also have $161.7 million invested in 16,464 lots under option, including cash and letters of credit deposits of $69.9 million as of October 31, 2008. We will record a write-off for the amounts associated with an option if we determine it is probable we will not exercise it. As of October 31, 2008, we have total investments in, and advances to, unconsolidated joint ventures of $71.1 million. Each of our joint ventures assesses its inventory and other long-lived assets for impairment in accordance with U.S. GAAP, which has resulted in reductions in our investment in joint ventures of $72.2 million from our second half of fiscal 2006 through October 31, 2008. We still have exposure to future write-downs of our investment in unconsolidated joint ventures if conditions continue to deteriorate in the markets that our joint ventures operate. With respect to goodwill and intangibles, there is no remaining risk of further exposure to impairments because both goodwill and definite life intangibles have been fully written off as of October 31, 2008.

We continue to operate our business with the expectation that difficult market conditions will continue to impact us for at least the near term. We have adjusted our approach to land acquisition and construction practices and continue to shorten our land pipeline, reduce production volumes, and balance home price and profitability with sales pace. We are delaying and cancelling planned land purchases and renegotiating land prices and have significantly reduced our total number of controlled lots owned and under option. Additionally, we are significantly reducing the number of speculative homes put into production. While we will continue to purchase select land positions where it makes strategic and economic sense to do so, we currently anticipate minimal investment in new land parcels in fiscal 2009. We have also closely evaluated and made reductions in selling, general and administrative expenses, including corporate general and administrative expenses, reducing these expenses $165.3 million from $625.2 million in fiscal 2007 to $459.9 million in fiscal 2008 due in large part to a 59% reduction head count from our peak in June 2006. Given the persistence of these difficult market conditions, improving the efficiency of our selling, general and administrative expenses will continue to be a significant area of focus. We believe that these measures will help to strengthen our market position and allow us to take advantage of opportunities that will develop in the future.

Critical Accounting Policies

Management believes that the following critical accounting policies affect its more significant judgments and estimates used in the preparation of its consolidated financial statements:

Business Combinations When we make an acquisition of another company, we use the purchase method of accounting in accordance with the Statement of Financial Accounting Standards (SFAS) No. 141 "Business Combinations" ("SFAS 141"). Under SFAS 141, we record as our cost the estimated fair value of the acquired assets less liabilities assumed. Any difference between the cost of an acquired company and the sum of the fair values of tangible and intangible assets less liabilities is recorded as goodwill. The reported income of an acquired company includes the operations of the acquired company from the date of acquisition.

Income Recognition from Home and Land Sales We are primarily engaged in the development, construction, marketing and sale of residential single-family and multi-family homes where the planned construction cycle is less than 12 months. For these homes, in accordance with SFAS No. 66, "Accounting for Sales of Real Estate" ("SFAS 66"), revenue is recognized when title is conveyed to the buyer, adequate initial and continuing investments have been received and there is no continued involvement. In situations where the buyer's financing is originated by our mortgage subsidiary and the buyer has not made an adequate initial or continuing investment as prescribed by SFAS 66, the profit on such sales is deferred until the sale of the related mortgage loan to a third-party investor has been completed.

Additionally, in certain markets, we sell lots to customers, transferring title, collecting proceeds, and entering into contracts to build homes on these lots. In these cases, we do not recognize the revenue from the lot sale until we deliver the completed home and have no continued involvement related to that home. The cash received on the lot is recorded as a component of inventory until the revenue is recognized.

Income Recognition from High-Rise/Mid-Rise Projects We are developing several high-rise/mid-rise buildings that will take more than 12 months to complete. If these buildings qualify, revenues and costs are recognized using the percentage of completion method of accounting in accordance with SFAS 66. Under the percentage of completion method, revenues and costs are to be recognized when construction is beyond the preliminary stage, the buyer is committed to the extent of having a sufficient initial and continuing investment that the buyer cannot require to be refunded except for non-delivery of the home, sufficient homes in the building have been sold to ensure that the property will not be converted to rental property, the sales prices are collectible and the aggregate sales proceeds and the total cost of the building can be reasonably estimated. We currently do not have any buildings that meet these criteria; therefore the revenues from delivering homes in high-rise/mid-rise buildings are recognized when title is conveyed to the buyer, adequate initial and continuing involvement have been received and there is no continued involvement with respect to that home.

Income Recognition from Mortgage Loans Our Financial Services segment originates mortgages, primarily for our homebuilding customers. We use mandatory mortgage-backed securities ("MBS") forward commitments and investor commitments to hedge our mortgage-related interest rate exposure on agency and government loans. These instruments involve, to varying degrees, elements of credit and interest rate risk. Credit risk associated with MBS forward commitments and loan sales transactions is managed by limiting our counterparties to investment banks, federally regulated bank affiliates and other investors meeting our credit standards. Our risk, in the event of default by the purchaser, is the difference between the contract price and fair value of the MBS forward commitments. In an effort to reduce our exposure to the marketability and disposal of non-agency and non-governmental loans, including Alt-A (FICO scores below 680 and depending on credit criteria) and sub-prime loans (FICO scores below 580 and depending on credit criteria), we require our Financial Services segment to either presell or broker all of these loans, on an individual loan basis as soon as they are committed to by the customer. However, because of the recent tightening by mortgage lenders, our origination of Alt-A and sub-prime loans has declined to only 7.6% and 0.3%, respectively, of the total loans we originated during fiscal 2008, as compared to 27.3% and 3.7%, respectively, for the same period last year. In addition, of the $87.5 million of mortgage loans held for sale as of October 31, 2008, none were Alt-A or sub-prime loans. There were, however, $3.2 million of mortgage loans held for investment at October 31, 2008, which represent loans that cannot currently be sold at reasonable terms in the secondary mortgage market. As Alt-A and sub-prime originations declined, we have seen an increase in our level of Federal Housing Administration and Veterans Administration ("FHA/VA") loan origination. For the twelve months ended October 31, 2008 and 2007, FHA/VA loans represented 35.5% and 6.5%, respectively, of our total loans. Profits and losses relating to the sale of mortgage loans are recognized when legal control passes to the buyer of the mortgage and the sales price is collected.

Interest Income Recognition for Mortgage Loans Receivable and Recognition of Related Deferred Fees and Costs Interest income is recognized as earned for each mortgage loan during the period from the loan closing date to the sale date when legal control passes to the buyer, and the sale price is collected. All fees related to the origination of mortgage loans and direct loan origination costs are deferred and recorded as either (a) an adjustment to the related mortgage loans upon the closing of a loan or (b) recognized as a deferred asset or deferred revenue while the loan is in process. These fees and costs include loan origination fees, loan discount, and salaries and wages. Such deferred fees and costs relating to the closed loans are recognized over the life of the loans as an adjustment of yield or taken into operations upon sale of the loan to a permanent investor.

Inventories Inventories consist of land, land development, home construction costs, capitalized interest and construction overhead and are stated at cost, net of impairment losses, if any. Construction costs are accumulated during the period of construction and charged to cost of sales under specific identification methods. Land, land development and common facility costs are allocated based on buildable acres to product types within each community, then charged to cost of sales equally based upon the number of homes to be constructed in each product type.

We report inventories in our consolidated balance sheets at the lower of cost or fair value. Our inventories consist of the following three components: (1) Sold and unsold homes and lots under development, which includes all construction, land, and land development costs related to started homes and land under development in our active communities; (2) Land and land options held for future development or sale, which includes all costs related to land in our communities in planning; and (3) Consolidated inventory not owned, which includes all cost related to specific performance options, variable interest entities, and other options, which consists primarily of our GMAC model homes and inventory related to structured lot options.

As a result of the declining homebuilding market, we have decided to mothball (or stop development on) certain communities where we determine the current performance does not justify further investment at this time. When we decide to mothball a community, the inventory is reclassified from Sold and unsold homes and lots under development to Land and land options held for future development or sale. As of October 31, 2008, the book value associated with the 54 mothballed communities was $550.4 million, net of an impairment balance of $290.1 million. We continually review communities to determine if mothballing is appropriate.

The recoverability of inventories and other long-lived assets are assessed in accordance with the provisions of Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 requires long-lived assets, including inventories, held for development to be evaluated for impairment based on undiscounted future cash flows of the assets at the lowest level for which there are identifiable cash flows. As such, we evaluate inventories for impairment at the individual community level, the lowest level of discrete cash flows that we measure.

We evaluate inventories of communities under development and held for future development for impairment when indicators of potential impairment are present. Indicators of impairment include, but are not limited to, decreases in local housing market values, decreases in gross margins or sales absorption rates, decreases in net sales prices (base sales price net of sales incentives), or actual or projected operating or cash flow losses. The assessment of communities for indication of impairment is performed quarterly, primarily by completing detailed budgets for all of our communities and identifying those communities with a projected operating loss for any projected fiscal year or for the entire projected community life. For those communities with projected losses, we estimate remaining undiscounted future cash flows and compare those to the carrying value of the community, to determine if the carrying value of the asset is recoverable.

The projected operating profits, losses or cash flows of each community can be significantly impacted by our estimates of the following:

- future base selling prices;
- future home sales incentives;
- future home construction and land development costs; and
- future sales absorption pace and cancellation rates.

These estimates are dependent upon specific market conditions for each community. While we consider available information to determine what we believe to be our best estimates as of the end of a quarterly reporting period, these estimates are subject to change in future reporting periods as facts and circumstances change. Local market-specific conditions that may impact our estimates for a community include:

- the intensity of competition within a market, including publicly available home sales prices and home sales incentives offered by our competitors;
- the current sales absorption pace for both our communities and competitor communities;
- community specific attributes, such as location, availability of lots in the market, desirability and uniqueness of our community, and the size and style of homes currently being offered;

- potential for alternative product offerings to respond to local market conditions;
- changes by management in the sales strategy of the community; and
- current local market economic and demographic conditions and related trends and forecasts.

These and other local market-specific conditions that may be present are considered by management in preparing projection assumptions for each community. The sales objectives can differ between our communities, even within a given market. For example, facts and circumstances in a given community may lead us to price our homes with the objective of yielding a higher sales absorption pace, while facts and circumstances in another community may lead us to price our homes to minimize deterioration in our gross margins, although it may result in a slower sales absorption pace. In addition, the key assumptions included in our estimate of future undiscounted cash flows may be interrelated. For example, a decrease in estimated base sales price or an increase in homes sales incentives may result in a corresponding increase in sales absorption pace. Additionally, a decrease in the average sales price of homes to be sold and closed in future reporting periods for one community that has not been generating what management believes to be an adequate sales absorption pace may impact the estimated cash flow assumptions of a nearby community. Changes in our key assumptions, including estimated construction and development costs, absorption pace and selling strategies, could materially impact future cash flow and fair value estimates. Due to the number of possible scenarios that would result from various changes in these factors, we do not believe it is possible to develop a sensitivity analysis with a level of precision that would be meaningful to an investor.

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If the undiscounted cash flows are more than the carrying value of the community, then the carrying amount is recoverable, and no impairment adjustment is required. However, if the undiscounted cash flows are less than the carrying amount, then the community is deemed impaired and is written-down to its fair value. We determine the estimated fair value of each community by determining the present value of the estimated future cash flows at a discount rate commensurate with the risk of the respective community. Our discount rates used for the impairments recorded to date range from 13.5% to 17.0%. The estimated future cash flow assumptions are the same for both our recoverability and fair value assessments. Should the estimates or expectations used in determining estimated cash flows or fair value decrease or differ from current estimates in the future, we may be required to recognize additional impairments related to current and future communities. The impairment of a community is allocated to each lot on a straight line basis.

Inventories held for sale, which are land parcels where we have decided not to build homes, are a very small portion of our total inventories, and are reported at the lower of carrying amount or fair value less costs to sell. In determining whether land held for sale is impaired, management considers, among other things, prices for land in recent comparable sale transactions, market analysis studies, which include the estimated price a willing buyer would pay for the land (other than in a forced liquidation sale) and recent bona fide offers received from outside third parties, if available.

From time to time, we write-off deposits and approval, engineering and capitalized interest costs when we decide not to exercise options to buy land in various locations or when we redesign communities and/or abandon certain engineering costs. In deciding not to exercise a land option, we take into consideration changes in market conditions, the timing of required land takedowns, the willingness of land sellers to modify terms of the land option contract (including timing of land takedowns), and the availability and best use of our capital, among other factors. The write-off is recorded in the period it is deemed probable that the optioned property will not be acquired. In certain instances, we have been able to recover deposits and other preacquisition costs which were previously written off. These recoveries are generally not significant in comparison to the total costs written off.

The impairment of communities under development and held for future development and inventories held for sale, and the charge for land option write-offs, are reflected on the Consolidated Statement of Operations in a separate line entitled "Homebuilding Inventory impairment loss and land option write-offs". See also the "Results of Operations" below and Note 13 to the Consolidated Financial Statements for inventory impairment and write-off amounts by segment.

Insurance Deductible Reserves For homes delivered in fiscal 2008 and 2007, our deductible is $20 million per occurrence with an aggregate $20 million for liability claims and an aggregate $21.5 million for construction defect claims under our general liability insurance. Our worker's compensation insurance deductible is $0.5 million per occurrence in fiscal 2008 and fiscal 2007. Reserves have been established based upon actuarial analysis of estimated losses for fiscal 2008 and fiscal 2007. We engage a third party actuary that uses our historical warranty data to estimate our unpaid claims, claim adjustment expenses and incurred but not reported claims reserves for the risks that we are assuming under the general liability and workers compensation programs. The estimates include provisions for inflation, claims handling and legal fees. These estimates are subject to a high degree of variability due to uncertainties such as trends in construction defect claims relative to our markets and the types of products we build, claim settlement patterns, insurance industry practices and legal interpretations, among others. Because of the high degree of judgment required in determining these estimated liability amounts, actual future costs could differ significantly from our currently estimated amounts.

Interest In accordance with SFAS 34, "Capitalization of Interest Cost", interest incurred is first capitalized to properties under development during the land development and home construction period and expensed along with the associated cost of sales as the related inventories are sold. Interest incurred in excess of interest capitalized because qualifying assets for interest capitalization are less than debt, or interest incurred on borrowings directly related to properties not under development are expensed immediately in "Other interest".

Land Options Costs are capitalized when incurred and either included as part of the purchase price when the land is acquired or charged to operations when we determine we will not exercise the option. In accordance with Financial Accounting Standards Board ("FASB") Interpretation No. 46R ("FIN 46R") "Consolidation of Variable Interest Entities", an interpretation of Accounting Research Bulletin No. 51, SFAS No. 49 "Accounting for Product Financing Arrangements" ("SFAS 49"), SFAS No. 98 "Accounting for Leases" ("SFAS 98"), and Emerging Issues Task Force ("EITF") No. 97-10 "The Effects of Lessee Involvement in Asset Construction" ("EITF 97-10"), we record on the Consolidated Balance Sheets specific performance options, options with variable interest entities and other options under "Consolidated inventory not owned" with the offset to "Liabilities from inventory not owned" and "Minority interest from inventory not owned".

Unconsolidated Homebuilding and Land Development Joint Ventures Investments in unconsolidated homebuilding and land development joint ventures are accounted for under the equity method of accounting. Under the equity method, we recognize our proportionate share of earnings and losses earned by the joint venture upon the delivery of lots or homes to third parties. Our ownership interest in joint ventures varies but is generally less than or equal to 50%. In determining whether or not we must consolidate joint ventures where we are the managing member of the joint venture, we consider the guidance in EITF 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights" ("EITF 04-5"), in assessing whether the other partners have specific rights to overcome the presumption of control by us as the manager of the joint venture. In most cases, the presumption is overcome because the joint venture agreements require that both partners agree on establishing the operating and capital decisions of the partnership, including budgets, in the ordinary course of business. In accordance with Accounting Principles Board Opinion 18 ("APB 18"), we assess our investments in unconsolidated joint ventures for recoverability, and if it is determined that a loss in value of the investment is other than temporary, we write-down the investment to the recoverable value. We evaluate our equity investments for recoverability based on the joint venture's projected cash flows. In fiscal 2008, we wrote-down certain joint venture investments by $11.3 million, based on this recoverability analysis.

Intangible Assets The intangible assets recorded on our October 31, 2007 balance sheet are goodwill, which has an indefinite life, and definite life intangibles, including trade names, architectural designs, distribution processes, and contractual agreements resulting from our acquisitions. We no longer amortize goodwill but instead assess it periodically for impairment. We performed such assessments utilizing a fair value approach as of October 31, 2008. If the fair value of the applicable business unit is less than the carrying amount of that business unit, the goodwill of that business unit is considered impaired. The amount of the impairment is determined as the excess of the book value of the goodwill over the implied fair value of the goodwill, and the implied fair value of the goodwill is determined in the same manner as the amount of goodwill recognized in a business combination is determined. That is, the fair value of the business unit is allocated to all of the assets and liabilities of that business unit as if the business unit had been acquired in a business combination. The excess of the fair value of the business unit over the amounts assigned to its assets and liabilities is the implied fair value of goodwill. The estimates used in the determination of the estimated cash flows and fair value of a business unit are based on factors known to us at the time such estimates are made and our expectations of future operations and economic conditions. Should the estimates or expectations used in determining estimated cash flows or fair value decrease or differ from current estimates in the future, we may be required to recognize additional impairments. This was the case in fiscal 2008, whereby we wrote-off the remaining $32.7 million of goodwill balance based upon present value cash flow analyses, bringing the balance to zero at October 31, 2008. The goodwill impairment charge was included in "Goodwill and intangible amortization and impairment" on the Consolidated Statements of Operations.

We also assess definite life intangibles for impairment whenever events or changes indicate that their carrying amount may not be recoverable. An intangible impairment is recorded when events and circumstances indicate the undiscounted future cash flows generated from the business unit with the intangible asset are less than the net assets of the business unit. The impairment loss is the lesser of the difference between the net assets of the business unit and the discounted future cash flows generated from the applicable business unit, which approximates fair value and the intangible asset balance. The estimates used in the determination of the estimated cash flows and fair value of a business unit are based on factors known to us at the time such estimates are made and our expectations of future operations and economic conditions. Should the estimates or expectations used in determining estimated cash flows or fair value decrease or differ from current estimates in the future, we may be required to recognize additional impairments. This was the case in fiscal 2008, whereby we wrote off $2.7 million of intangible assets carrying amount, bringing the balance to zero at October 31, 2008. In fiscal 2007, we determined that the intangible assets associated with our Fort Myers, California, Tampa, Orlando, Canton and Building Products operations were impaired and wrote them off for a total reduction of $162.2 million, of which $135.2 million was included in "Goodwill and intangible amortization and impairment" on the Consolidated Statement of Operations and $27.0 million was included in "Accounts payable and other liabilities" on the Consolidated Balance Sheets. The intangible impairment charge is included in "Goodwill and intangible amortization and impairment" on the Consolidated Statements of Operations.

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Post-Development Completion and Warranty Costs In those instances where a development is substantially completed and sold and we have additional construction work to be incurred, an estimated liability is provided to cover the cost of such work. In addition, we accrue warranty costs as part of cost of sales for repair costs under $5,000 per occurrence to homes, community amenities and land development infrastructure. In addition, we accrue for warranty costs over $5,000 per occurrence as part of our general liability insurance deductible expensed as selling, general and administrative costs. As previously stated, the deductible for our general liability insurance for homes delivered in fiscal 2008 and 2007 is $20 million per occurrence with an aggregate $20 million for liability claims, and an aggregate $21.5 million for construction defect claims. Both of these liabilities are recorded in "Accounts payable and other liabilities" on the Consolidated Balance Sheets.

Deferred Income Taxes Deferred income taxes or income tax benefits are provided for temporary differences between amounts recorded for financial reporting and for income tax purposes. If, for some reason, the combination of future years income (or loss) combined with the reversal of the timing differences results in a loss, such losses can be carried back to prior years or carried forward to future years to recover the deferred tax assets. In accordance with SFAS No. 109, "Accounting for Income Taxes" ("SFAS 109"), we evaluate our deferred tax assets quarterly to determine if valuation allowances are required. SFAS 109 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. See Total Taxes below under Results of Operations for further discussion of the valuation allowances.

Recent Accounting Pronouncements

See Note 3 to the Consolidated Financial Statements included elsewhere in this Form 10-K.

Capital Resources and Liquidity

Our operations consist primarily of residential housing development and sales in the Northeast (New Jersey, New York, Pennsylvania), the Midwest (Illinois, Kentucky, Minnesota, Ohio), the Mid-Atlantic (Delaware, Maryland, Virginia, West Virginia, Washington D. C.), the Southeast (Florida, Georgia, North Carolina, South Carolina), the Southwest (Arizona, Texas) and the West (California). In addition, we provide financial services to our homebuilding customers.

Our cash uses during the twelve months ended October 31, 2008 and 2007 were for operating expenses, construction, state income taxes, and interest. We provided for our cash requirements from available cash on hand, housing and land sales, the issuance of $600 million of senior secured second lien notes ("Senior Secured Notes"), the issuance of 14 million shares of Class A Common Stock, the revolving credit facility, financial service revenues, a federal tax refund and other revenues. We believe that these sources of cash are sufficient to finance our working capital requirements and other needs, despite continued declines in total revenues and a reduction in the availability under our revolving credit facility. For fiscal 2009, we are focused on maximizing cash flow, even at the expense of lower gross margins, by limiting investments in new communities and delaying further investment in current communities thereby reducing our inventory as we continue to build and deliver homes from our current communities. In addition, we anticipate receiving a federal tax refund in fiscal 2009 of $145.2 million. We may also enter into land sale agreements or joint ventures to generate cash from our existing balance sheet.

On December 3, 2008, we issued $29.3 million of 18% Senior Secured Notes in exchange for $71.4 million of our unsecured senior notes. On May 27, 2008, we issued $600 million of $11^{1}/_{2}$% Senior Secured Notes, and the Amendment to the Seventh Amended and Restated Credit Agreement, which reduced the aggregate amount of commitments from $900 million to $300 million, became effective. Availability under the Amended Credit Agreement equals the lesser of $300 million and the amount available pursuant to the borrowing base and the sub-limit for revolving loans is $100 million. The Amended Credit Agreement eliminated all but one of the financial maintenance covenants, which requires that as of the last day of each fiscal quarter either (1) the ratio of our adjusted operating cash flow to fixed charges exceed 1.50 to 1.00 or (2) our liquidity, as defined in the Amended Credit Agreement, equals or exceeds $100 million. Because of our $838.2 million of homebuilding cash at October 31, 2008 and our expectations of cash flows in fiscal 2009, we believe we will be in compliance with this new covenant through 2009.

Our net (loss) income historically does not approximate cash flow from operating activities. The difference between net (loss) income and cash flow from operating activities is primarily caused by changes in inventory levels together with changes in receivables, prepaid and other assets, interest and other accrued liabilities, deferred income taxes, accounts payable, mortgage loans and liabilities, and non-cash charges relating to depreciation, amortization of computer software costs, amortization of definite life intangibles, stock compensation awards and impairment losses for inventory, definite life intangibles and goodwill. When we are expanding our operations, which was the case in fiscal 2006, inventory levels, prepaids and other assets increase causing cash flow from operating activities to decrease. Certain liabilities also increase as operations expand and partially offset the negative effect on cash flow from operations caused by the increase in inventory levels, prepaids and other assets. Similarly, as our mortgage operations expand, net income from these operations increase, but for cash flow purposes are offset by the net change in mortgage assets and liabilities. The opposite is true as our investment in new land purchases and development of new communities decrease, which is what has been happening since the last half of fiscal 2007 allowing us to generate positive cash flow from operations during this period. Looking forward, given the continued deterioration in the housing market, it will become more difficult to generate positive cash flow. However, we will continue to make adjustments to our structure and our business plans in order to maximize our liquidity.

On July 3, 2001, our Board of Directors authorized a stock repurchase program to purchase up to 4 million shares of Class A Common Stock. As of October 31, 2008, 3.4 million shares of Class A Common Stock have been purchased under this program (See Part II, Item 5 for information on equity purchases). On March 5, 2004, our Board of Directors authorized a 2-for-1 stock split in the form of a 100% stock dividend. All share information reflects this stock dividend.

On July 12, 2005, we issued 5,600 shares of 7.625% Series A Preferred Stock, with a liquidation preference of $25,000. Dividends on the Series A Preferred Stock are not cumulative and are paid at an annual rate of 7.625%. The Series A Preferred Stock is not convertible into the Company's common stock and is redeemable in whole or in part at our option at the liquidation preference of the shares beginning on the fifth anniversary of their issuance. The Series A Preferred Stock is traded as depositary shares, with each depositary share representing 1/1000th of a share of Series A Preferred Stock. The depositary shares are listed on the Nasdaq Global Market under the symbol "HOVNP". In each of fiscal year 2007 and 2006, we paid $10.7 million of dividends on the Series A Preferred Stock. In fiscal 2008, we did not make any dividend payments as a result of covenant restrictions in the indentures governing our Senior Secured, Senior and Senior Subordinated Notes discussed below. We anticipate that we will continue to be restricted from paying dividends into fiscal 2009 and potentially beyond.

On May 14, 2008, we issued 14,000,000 shares of Class A Common Stock for net proceeds of $125.9 million.

On May 16, 2008, we entered into Amendment No. 1 (the "Amendment") to the Seventh Amended and Restated Credit Agreement (as amended, the "Amended Credit Agreement"). On May 27, 2008, in conjunction with the consummation of the issuance of $600 million of 11$^{1}/_{2}$% Senior Secured Notes due 2013, the Amendment became effective. The Amendment decreased the aggregate amount of commitments under the Amended Credit Agreement from $900 million to $300 million. The maturity date of the facility remains May 31, 2011. Availability under the Amended Credit Agreement equals the lesser of $300 million and the amount available pursuant to the borrowing base and the sub-limit for revolving loans is $100 million. Borrowings under the Amended Credit Agreement bear interest at a rate equal, at the Company's option, to (1) one, two, three or six month LIBOR, plus 4.50%, (2) a base rate equal to the greater of PNC Bank, National Association's prime rate and the federal funds effective rate plus 0.50%, plus 2.75% or (3) an index rate based on daily LIBOR, plus 4.625%. In addition to paying interest on outstanding principal under the revolving facility, the Company is required to pay an unused fee equal to 0.55% per annum on the daily average unused portion of the revolving facility. The Company will also pay a letter of credit fee of 4.50% per annum on the average outstanding face amount of letters of credit issued under the revolving facility. Notwithstanding the foregoing, the interest rate and fees payable under the revolving facility may not be less than the applicable interest rates and fees that would have been payable pursuant to the revolving facility that was in effect prior to March 7, 2008, the date of the Amended Credit Agreement. Borrowings under the Amended Credit Agreement may be used for general corporate purposes and working capital. A portion of the proceeds of the issuance of 11$^{1}/_{2}$% Senior Secured Notes due 2013 were used to repay the outstanding balance of $325.0 million at May 27, 2008 under the Amended Credit Agreement. As of October 31, 2008, there was zero drawn under the Amended Credit Agreement, excluding letters of credit totaling $197.5 million. As of October 31, 2007, there was $206.8 million drawn under the Revolving Credit Agreement then in effect, excluding letters of credit totaling $306.4 million.

We and each of our subsidiaries are guarantors under the Amended Credit Agreement, except for K. Hovnanian Enterprises, Inc. ("K. Hovnanian"), the borrower, certain of our financial services subsidiaries and joint ventures. All obligations under the Amended Credit Agreement, and the guarantees of those obligations, are secured, subject to permitted liens and other exceptions, by a first-priority lien on substantially all of the assets owned by us, K. Hovnanian and the guarantors.

The Amended Credit Agreement has covenants that restrict, among other things, the ability of the Company and certain of its subsidiaries, including K.

Hovnanian, to incur additional indebtedness, pay dividends on, and make distributions with respect to, common and preferred stock and repurchase capital stock, make other restricted payments, make investments, dispose of assets, incur liens, consolidate, merge, sell or otherwise transfer all or substantially all of its assets and enter into certain transactions with affiliates. The Amended Credit Agreement also contains a covenant that requires that as of the last day of each fiscal quarter either (1) the ratio of our adjusted operating cash flow to fixed charges exceed 1.50 to 1.00 or (2) our liquidity, as defined in the Amended Credit Agreement, equals or exceeds $100 million. However, the Amended Credit Agreement does not contain any other financial maintenance covenants. The Amended Credit Agreement contains events of default which would permit the lenders to accelerate the loans if not cured within applicable grace periods, including the failure to make timely payments under the Amended Credit Agreement or other material indebtedness, the failure to satisfy covenants, the failure of the documents granting security for the obligations under the Amended Credit Agreement to be in full force and effect and specified events of bankruptcy and insolvency. As of October 31, 2008, we were in compliance with the covenants under the Amended Credit Agreement.

Our wholly-owned mortgage banking subsidiary originates mortgage loans, primarily from the sale of our homes. Such mortgage loans and related servicing rights are sold in the secondary mortgage market within a short period of time. Our secured Master Repurchase Agreement, which was amended on July 7, 2008, with a group of banks is a short-term borrowing facility that provides up to $151 million through July 6, 2009. Interest is payable monthly at LIBOR plus 1.50% (4.08% at October 31, 2008). The loan is secured by the mortgages held for sale and is repaid when we sell the underlying mortgage loans to permanent investors. We also had a commercial paper facility which provided for up to $200 million through April 25, 2008 with interest payable monthly at LIBOR plus 0.40%. On November 28, 2007, we paid the outstanding balance in full and terminated the commercial paper facility. We believe that we will be able to extend the Master Repurchase Agreement beyond its expiration date, but there can be no assurance of such extension. As of October 31, 2008, the aggregate principal amount of all borrowings under the Master Repurchase Agreement was $84.8 million. The Master Repurchase Agreement requires K. Hovnanian American Mortgage, LLC to satisfy and maintain specified financial ratios and other financial condition tests. As of October 31, 2008, we were in compliance with the covenants of the Master Repurchase Agreement.

On May 27, 2008, K. Hovnanian issued $600 million ($594.4 million net of discount) of $11\frac{1}{2}\%$ Senior Secured Notes due 2013. The notes are secured, subject to permitted liens and other exceptions, by a second-priority lien on substantially all of the assets owned by us, K. Hovnanian and the guarantors to the extent such assets secure obligations under the Amended Credit Agreement. The notes are redeemable in whole or in part at our option at 102% of principal commencing November 1, 2010, 101% of principal commencing May 1, 2011 and 100% of principal commencing May 1, 2012. In addition, we may redeem up to 35% of the aggregate principal amount of the notes before May 1, 2011 with the net cash proceeds from certain equity offerings at 111.50% of principal. A portion of the net proceeds of the issuance were used to repay the outstanding balance under the Amended Credit Agreement.

At October 31, 2008, we had $600 million of outstanding Senior Secured Notes due 2013 ($594.7 million net of discount). We also had $1,515.0 million of outstanding senior notes ($1,511.1 million, net of discount), comprised of $100 million 8% Senior Notes due 2012, $215 million $6\frac{1}{2}\%$ Senior Notes due 2014, $150 million $6\frac{3}{8}\%$ Senior Notes due 2014, $200 million $6\frac{1}{4}\%$ Senior Notes due 2015, $300 million $6\frac{1}{4}\%$ Senior Notes due 2016, $300 million $7\frac{1}{2}\%$ Senior Notes due 2016 and $250 million $8\frac{5}{8}\%$ Senior Notes due 2017. In addition, we had $400.0 million of outstanding senior subordinated notes, comprised of $150 million $8\frac{7}{8}\%$ Senior Subordinated Notes due 2012, $150 million $7\frac{3}{4}\%$ Senior Subordinated Notes due 2013 and $100 million 6% Senior Subordinated Notes due 2010.

On December 3, 2008 we issued $29.3 million of 18.0% Senior Secured Notes due 2017 in exchange for $71.4 million of our unsecured senior notes as follows: $0.5 million aggregate principal amount of the 8% Senior Notes due 2012, $12.0 million aggregate principal amount of the $6\frac{1}{2}\%$ Senior Notes due 2014, $1.1 million aggregate principal amount of the $6\frac{3}{8}\%$ Senior Notes due 2014, $3.3 million aggregate principal amount of the $6\frac{1}{4}\%$ Senior Notes due 2015, $24.8 million aggregate principal amount of the $7\frac{1}{2}\%$ Senior Notes due 2016, $28.7 million aggregate principal amount of the $6\frac{1}{4}\%$ Senior Notes due 2016 and $1.0 million aggregate principal amount of the $8\frac{5}{8}\%$ Senior Notes due 2017. The notes are secured, subject to permitted liens and other exceptions, by a third-priority lien on substantially all of the assets owned by us, K. Hovnanian and the guarantors to the extent such assets secure obligations under the Amended Credit Agreement and the $11\frac{1}{2}\%$ Senior Secured Notes due 2013. The notes are redeemable in whole or in part at our option at 102% of principal commencing May 1, 2011, 101% of principal commencing November 1, 2011 and 100% of principal commencing November 1, 2012. In addition, we may redeem up to 35% of the aggregate principal amount of the notes before May 1, 2011 with the net cash proceeds from certain equity offerings at 118.0% of principal.

We and each of our subsidiaries are guarantors of the Senior Secured, Senior and Senior Subordinated Notes, except for K. Hovnanian, the issuer of the notes, certain of our financial services subsidiaries and joint ventures. The indentures governing the Senior Secured, Senior and Senior Subordinated Notes contain restrictive covenants that limit, among other things, the ability of Hovnanian and certain of its subsidiaries, including K. Hovnanian, the issuer of the Senior Secured, Senior and Senior Subordinated Notes, to incur additional indebtedness, pay dividends and make distributions on common and preferred stock, repurchase senior and senior subordinated notes (with respect to the senior secured notes indenture), make other restricted payments, make investments, sell certain assets, incur liens, consolidate, merge, sell or otherwise dispose of all or substantially all of its assets and enter into certain transactions with affiliates. If our consolidated fixed charge coverage ratio, as defined in the indentures governing our Senior Secured, Senior and Senior Subordinated Notes, is less than 2.0 to 1.0, we are restricted from making certain payments, including dividends, and from incurring indebtedness other than certain permitted indebtedness, refinancing indebtedness and non-recourse indebtedness. As a result of this restriction, we are currently restricted from paying dividends on our 7.625% Series A Preferred Stock. If current market trends continue or worsen, we will continue to be restricted from paying dividends into fiscal 2009 and possibly future years. The restriction on making preferred dividend payments under our bond indentures will not affect our compliance with any of the covenants contained in the Amended Credit Agreement and will not permit the lenders under the Amended Credit Agreement to accelerate the loans. The indentures also contain events of default which would permit the holders of the Senior Secured, Senior and Senior Subordinated Notes to declare those notes to be immediately due and payable if not cured within applicable grace periods, including the failure to make timely payments on the notes or other material indebtedness, the failure to satisfy covenants and specified events of bankruptcy and insolvency and, with respect to the indenture governing the senior secured notes, the failure of the documents granting security for the senior secured notes to be in full force and effect and the failure of the liens on any material portion of the collateral securing the senior secured notes to be valid and perfected. As of October 31, 2008, we were in compliance with the covenants of the indentures governing our outstanding notes. Under the terms of the indentures, we have the right to make certain redemptions and, depending on market conditions and covenant restrictions, may do so from time to time. We may also make debt purchases and/or exchanges through open market purchases, private transactions or otherwise from time to time depending on market conditions and covenant restrictions.

Total inventory decreased $1.3 billion, excluding inventory not owned, during the fiscal year ended October 31, 2008. This decrease excluded the decrease in consolidated inventory not owned of $107.3 million consisting of specific performance options, options with variable interest entities, and other options that were added to our balance sheet in accordance with SFAS 49, SFAS 98, and EITF 97-10, and variable interest entities in accordance with FIN 46R. See "Notes to Consolidated Financial Statements" Note 19 for additional information on FIN 46R. Total inventory decreased in the Northeast $203.9 million, in the Mid-Atlantic $189.8 million, in the Midwest $29.6 million, in the Southeast $166.8 million, in the Southwest $138.4 million, and in the West $523.4 million. These decreases were due to decisions to delay or terminate new communities, as well as slow spending in current communities and due to inventory impairments recorded in these segments. Substantially all homes under construction or completed and included in inventory at October 31, 2008 are expected to be closed during the next 12 months. Most inventory completed or under development was/is partially financed through our line of credit, preferred stock and senior secured, senior and senior subordinated indebtedness.

Despite the decrease in total inventory, our inventory representing "Land and land options held for future development or sale" on the Consolidated Balance Sheets increased by $197.9 million compared to October 31, 2007. The increase is due to "Sold and unsold home and lots under development inventory" being reclassified to "Land and land options held for future development or sale inventory" when we decide to mothball (or stop development on) a community. We mothball communities when we determine the current performance does not justify further investment at this time. That is, we believe we will generate higher returns if we avoid spending money to improve land today and save the raw land until such times as the markets improve. As of October 31, 2008, we have mothballed land in 54 communities. The book value associated with these 54 communities at October 31, 2008 was $550.4 million, net of an impairment balance of $290.1 million. We continually review communities to determine if mothballing is appropriate.

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We usually option property for development prior to acquisition. By optioning property, we are only subject to the loss of the cost of the option and predevelopment costs if we choose not to exercise the option. As a result, our commitment for major land acquisitions is reduced. Inventory impairment losses, which include inventory that has been written-off or written-down, increased $252.3 million for the fiscal year ended October 31, 2008, compared to the prior year. During the fiscal year 2008, we incurred $596.0 million in write-downs primarily attributable to impairments as a result of a continued decline in sales pace, sales price and general market conditions, as well as increased cancellation rates. In addition, we wrote-off costs in the amount of $114.1 million during the fiscal year ended October 31, 2008.

The following table summarizes home sites included in our total residential real estate. The decrease in total home sites available in 2008 compared to 2007 is partially attributable to terminating certain option agreements, as discussed herein.

	Total Home Sites	Contracted Not Delivered	Remaining Home Sites Available
October 31, 2008:			
Northeast	8,975	495	8,480
Mid-Atlantic	6,306	385	5,921
Midwest	2,969	291	2,678
Southeast	4,480	163	4,317
Southwest	8,192	420	7,772
West	9,173	134	9,039
Consolidated total	40,095	1,888	38,207
Unconsolidated joint ventures	3,256	261	2,995
Total including unconsolidated joint ventures	43,351	2,149	41,202
Owned	23,439	1,557	21,882
Optioned	16,464	139	16,325
Construction to permanent financing lots	192	192	
Consolidated total	40,095	1,888	38,207
Lots controlled by unconsolidated joint ventures	3,256	261	2,995
Total including unconsolidated joint ventures	43,351	2,149	41,202
October 31, 2007:			
Northeast	12,923	967	11,956
Mid-Atlantic	12,627	753	11,874
Midwest	4,062	759	3,303
Southeast	13,578	2,151	11,427
Southwest	13,936	751	13,185
West	9,797	547	9,250
Consolidated total	66,923	5,928	60,995
Unconsolidated joint ventures	4,326	425	3,901
Total including unconsolidated joint ventures	71,249	6,353	64,896

Owned	28,680	3,327	25,353
Optioned	36,104	462	35,642
Construction to permanent financing lots	2,139	2,139	
Consolidated total	66,923	5,928	60,995
Lots controlled by unconsolidated joint ventures	4,326	425	3,901
Total including unconsolidated joint ventures	71,249	6,353	64,896

The following table summarizes our started or completed unsold homes and models, excluding unconsolidated joint ventures, in active and substantially completed communities:

	October 31, 2008			**October 31, 2007**		
	Unsold Homes	**Models**	**Total**	**Unsold Homes**	**Models**	**Total**
Northeast	186	33	219	301	49	350
Mid-Atlantic	182	19	201	318	3	321
Midwest	70	27	97	125	28	153
Southeast	181	20	201	386	24	410
Southwest	566	125	691	787	91	878
West	90	97	187	473	237	710
Total	1,275	321	1,596	2,390	432	2,822
Started or completed unsold homes and models per active selling communities(1)	4.5	1.1	5.6	5.5	1.0	6.5

(1)
Active selling communities were 284 at October 31, 2008 and 431 at October 31, 2007.

The decrease in total unsold homes compared to the prior year is primarily due to an effort to sell inventoried homes during fiscal 2008. In some instances, this required giving additional incentives to homebuyers on completed unsold homes.

Investments in and advances to unconsolidated joint ventures decreased $105.3 million during the fiscal year ended October 31, 2008. A significant portion of the decrease is the result of consolidating a previously unconsolidated land development joint venture in our West segment, when our partner in the joint venture decided to terminate its investment. There was no debt associated with this joint venture and no further financial obligations required from us. However, we will be responsible for property taxes on the land previously owned by the joint venture going forward. Upon consolidating, no additional funds were invested in this land, as we had already invested the money in the lots via our investment in the joint venture. We decided not to walk away from the land investment of the joint venture because we believe we will be able to recover a portion of the original basis, whether or not developed. Because of the consolidation, we now own

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the lots outright and they are included in our consolidated lot count. This resulted in reclassing $61.5 million investment in this joint venture to inventory. This inventory was subsequently impaired by $41.1 million in the fourth quarter of 2008 and we have mothballed the community for the time being. Also contributing to the decrease in investments in and advances to unconsolidated joint ventures are distributions received from joint ventures and losses incurred by joint ventures, primarily related to inventory impairments and land option and walk away costs during fiscal 2008, partially offset by increases resulting from joint venture income not distributed and additional investments in joint ventures. As of October 31, 2008, we have investments in ten homebuilding joint ventures and seven land development joint ventures. Other than guarantees limited only to completion of development, environmental indemnification and standard indemnification for fraud and misrepresentation including voluntary bankruptcy, we have no guarantees associated with unconsolidated joint ventures.

Receivables, deposits and notes decreased $31.1 million to $78.8 million at October 31, 2008. The decrease is primarily due to the receipt of cash of $20.2 million from insurance carriers related to outstanding warranty claims, as well as the return of refundable deposits as we complete communities and the required land development.

Property, plant and equipment decreased $14.0 million primarily due to depreciation and disposals, which were not offset by additions during the period as we elected to reduce our investment in new property, plant and equipment in the current market environment.

Prepaid expenses and other assets are as follows as of:

(In Thousands)	October 31, 2008	October 31, 2007	Dollar Change
Prepaid insurance	$ 8,262	$ 6,769	$ 1,493
Prepaid project costs	82,394	110,439	(28,045)
Senior residential rental properties	7,321	7,694	(373)
Other prepaids	49,167	20,995	28,172
Other assets	9,451	28,135	(18,684)
Total	$ 156,595	$ 174,032	$ (17,437)

Prepaid insurance increased slightly due to the timing of payments for insurance premium costs. These costs are amortized over the life of the associated insurance policy. Prepaid project costs decreased for homes delivered and have not been replenished, as we have reduced the number of active selling communities given the current homebuilding environment. Prepaid project costs consist of community specific expenditures that are used over the life of the community. Such prepaids are expensed as homes are delivered. Other prepaids increased primarily as a result of fees paid in connection with the issuance of the $600 million 11$^1/_2$% senior secured notes due 2013 in May 2008. This increase was partially offset by a decrease for bank fees paid in connection with the entering into the Seventh Amended and Restated Credit Agreement in March 2008, which normally would be amortized over the loan period. Because we amended and reduced the aggregate commitment of the facility effective May 27, 2008, we wrote off a significant portion of these bank fees in the third quarter of fiscal 2008. Other assets decreased because there were significant distributions in the first quarter from our executive deferred compensation plan. These distributions also resulted in a corresponding decrease in accrued compensation discussed below under Accounts payable and other liabilities.

At October 31, 2007, we had $32.7 million of goodwill. This amount resulted from Company acquisitions prior to fiscal 2002. As required by SFAS 142, Goodwill and Other Intangible Assets ("SFAS 142"), we performed an annual assessment of this goodwill for impairment, and despite years of significant income generation in the markets with goodwill, primarily Texas in the Southwest segment and the Mid-Atlantic segment, the current financial projections of these markets has resulted in a full impairment of existing goodwill. As such, as of October 31, 2008, the goodwill balance is zero. The impairment was written off in the line "Goodwill and intangible amortization and impairment" on the Consolidated Statement of Operations.

Definite life intangibles decreased $4.2 million to zero at October 31, 2008. The decrease was the result of amortization during the twelve months of $1.5 million, and the write-off of $2.7 million for impaired intangible assets. In fiscal 2008, we determined that the remaining intangible assets in our Mid-Atlantic and Southeast segments were impaired, and wrote off the assets accordingly.

Financial Services - Mortgage loans held for sale or investment consist primarily of residential mortgages receivable held for sale of which $87.5 million and $177.0 million at October 31, 2008 and October 31, 2007, respectively, were being temporarily warehoused and awaiting sale in the secondary mortgage market. Also included are residential mortgages receivable held for investment of $3.2 million and $5.6 million at October 31, 2008 and October 31, 2007, which represent loans that cannot currently be sold at reasonable terms in the secondary mortgage market. We may incur risk with respect to mortgages that are delinquent, but only to the extent the losses are not covered by mortgage insurance or resale value of the house. Historically, we have incurred minimal credit losses. We have reserves for potential losses on mortgages we currently hold. The decrease in the receivable from October 31, 2007 is directly related to

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a decrease in the amount of loans financed at October 31, 2008 as compared to October 31, 2007.

Income taxes receivable decreased $67.6 million from October 31, 2007 to $126.8 million. The decrease is primarily due to the receipt of our federal tax refund for fiscal year 2007 during the third quarter of fiscal 2008 of $94.7 million, offset by the current tax receivable which can be carried back to 2006. The recoverability of the tax asset is limited to the use of loss carrybacks to 2006 and existing deferred tax liabilities. See Total Taxes later in Item 7 for further discussion of the valuation allowances recorded during fiscal 2008.

Accounts payable and other liabilities are as follows as of:

(In Thousands)	October 31, 2008	October 31, 2007	Dollar Change
Accounts payable	$ 167,407	$ 170,091	$ (2,684)
Reserves	133,423	131,790	1,633
Accrued expenses	59,394	97,753	(38,359)
Accrued compensation	27,211	53,767	(26,556)
Other liabilities	33,260	62,021	(28,761)
Total	$ 420,695	$ 515,422	$ (94,727)

The decrease in accounts payable was primarily due to the lower volume of deliveries in the fourth quarter of 2008 compared to the prior year. The decrease in accrued expenses is primarily due to payments made for land options with letters of credit that were terminated and accrued in the fourth quarter of fiscal 2007. The decrease in accrued compensation was primarily due to the significant distributions in the first quarter from our executive deferred compensation plan as well as lower bonus accruals at October 31, 2008 compared to October 31, 2007. The decrease in other liabilities is primarily related to accrued costs paid for resolution of matter with respect to our Fort Myers operations, and the final scheduled payment associated with a 2005 acquisition, offset by an increase in deferred revenue on GMAC model homes.

Nonrecourse Land Mortgages decreased $8.6 million from October 31, 2007 to $0.8 million at October 31, 2008. The decrease is primarily due to purchase money mortgages for a property in our Mid-Atlantic segment that were paid during fiscal 2008.

Customer deposits decreased $36.5 million from October 31, 2007 to $28.7 million at October 31, 2008. The decrease is primarily due to the reduction in the number of homes in backlog from 5,938 at October 31, 2007 to 1,907 at October 31, 2008.

Mortgage warehouse line of credit under our secured Master Repurchase Agreement decreased $86.3 million from $171.1 million at October 31, 2007 to $84.8 million at October 31, 2008. The decrease is directly correlated to the decrease in mortgage loans held for sale from October 31, 2007 to October 31, 2008.

Liabilities from inventory not owned and Minority interest from inventory not owned decreased $54.9 million and $37.4 million, respectively, from $189.9 million and $62.2 million, respectively, at October 31, 2007 to $135.1 million and $24.9 million at October 31, 2008, respectively. These decreases are directly correlated to the decrease in "Consolidated inventory not owned" on the Consolidated Balance Sheets, which is discussed above.

Accrued interest increased $28.5 million from $43.9 million at October 31, 2007 to $72.5 million at October 31, 2008. The increase is primarily due to interest on our new $600 million Senior Secured Notes due 2013.

Results of Operations

Total Revenues

Compared to the same prior period, revenues increased (decreased) as follows:

Year Ended

(Dollars in Thousands)	**October 31, 2008**	**October 31, 2007**	**October 31, 2006**
Homebuilding:			
Sale of homes	$(1,403,522)	$(1,322,012)	$ 725,732
Land sales	(50,179)	(32,434)	52,130
Other revenues	(13,137)	18,539	4,729
Financial services	(23,972)	(13,407)	17,227
Total change	$(1,490,810)	$(1,349,314)	$ 799,818
Total revenues percent change	(31.1)%	(22.0)%	15.0%

Homebuilding

Compared to the same prior period, housing revenues decreased $1,403.5 million, or 30.6%, for the year ended October 31, 2008, decreased $1,322.0 million, or 22.4%, for the year ended October 31, 2007, and increased $725.7 million or 14.0%, for the year ended October 31, 2006. Increases in 2006 were the result of both organic growth and acquisition of other homebuilders. Decreased revenue in 2007 and 2008 are primarily due to weakening market conditions and increased competition in most of our markets. Housing revenues are recorded at the time when title is conveyed to the buyer, adequate cash payment has been received and there is no continued involvement. Land sales are ancillary to our residential homebuilding operations and are expected to continue in the future but may significantly fluctuate up or down. For further details on land sales and other revenues, see the section titled "Land Sales and Other Revenues" below.

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Information on homes delivered by segment is set forth below:

	Year Ended		
(Housing Revenue in Thousands)	**October 31, 2008**	**October 31, 2007**	**October 31, 2006**
Northeast:			
Housing revenues	$ 679,488	$ 935,476	$ 992,713
Homes delivered	1,412	1,999	2,188
Average price	$ 481,224	$ 467,972	$ 453,708
Mid-Atlantic:			
Housing revenues	$ 509,009	$ 885,599	$ 980,691
Homes delivered	1,248	1,926	1,984
Average price	$ 407,860	$ 459,813	$ 494,300
Midwest:			
Housing revenues	$ 209,759	$ 226,804	$ 173,699
Homes delivered	965	1,043	855
Average price	$ 217,367	$ 217,453	$ 203,157
Southeast(1):			
Housing revenues	$ 624,106	$ 745,240	$ 1,243,501
Homes delivered	2,572	2,771	5,074
Average price	$ 242,654	$ 268,943	$ 245,073
Southwest:			
Housing revenues	$ 603,513	$ 828,574	$ 925,918
Homes delivered	2,616	3,643	4,252
Average price	$ 230,701	$ 227,443	$ 217,761
West:			
Housing revenues	$ 551,978	$ 959,682	$ 1,586,865
Homes delivered	1,764	2,182	3,587
Average price	$ 312,913	$ 439,818	$ 442,393
Consolidated total:			
Housing revenues	$ 3,177,853	$ 4,581,375	$ 5,903,387
Homes delivered	10,577	13,564	17,940
Average price	$ 300,449	$ 337,760	$ 329,063
Unconsolidated joint ventures:			
Housing revenues	$ 262,605	$ 535,051	$ 868,222
Homes delivered	704	1,364	2,261
Average price	$ 373,018	$ 392,266	$ 383,999
Total including unconsolidated joint ventures:			
Housing revenues	$ 3,440,458	$ 5,116,426	$ 6,771,609
Homes delivered	11,281	14,928	20,201
Average price	$ 304,978	$ 342,740	$ 335,212

(1) *Southeast includes deliveries from our acquisition of CraftBuilt Homes on April 17, 2006.*

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The decrease in housing revenues during the year ended October 31, 2008 was primarily due to weakening market conditions in most of our markets. Housing revenues in 2008 decreased in all of our homebuilding segments combined by 30.6%, and average sales prices decreased 11.0%. In our homebuilding segments, homes delivered decreased 29.4%, 35.2%, 7.5%, 7.2%, 28.2% and 19.2% in the Northeast, Mid-Atlantic, Midwest, Southeast, Southwest and West, respectively.

Unaudited quarterly housing revenues and net sales contracts by segment, excluding unconsolidated joint ventures, for the years ending October 31, 2008, 2007 and 2006 are set forth below:

	Quarter Ended			
(In Thousands)	October 31, 2008	July 31, 2008	April 30, 2008	January 31, 2008
Housing revenues:				
Northeast	$ 181,158	$ 169,394	$ 168,590	$ 160,346
Mid-Atlantic	133,121	115,836	134,494	125,558
Midwest	57,084	51,003	55,092	46,580
Southeast	51,979	69,763	109,182	393,182
Southwest	153,710	141,970	143,649	164,184
West	100,609	144,724	144,677	161,968
Consolidated total	$ 677,661	$ 692,690	$ 755,684	$ 1,051,818
Sales contracts (net of cancellations):				
Northeast	$ 66,381	$ 90,953	$ 140,651	$ 83,416
Mid-Atlantic	50,477	82,437	107,067	73,424
Midwest	18,866	26,261	43,023	18,737
Southeast	13,314	32,364	44,144	42,423
Southwest	103,626	121,223	169,331	124,385
West	66,032	97,294	142,561	115,405
Consolidated total	$ 318,696	$ 450,532	$ 646,777	$ 457,790

	Quarter Ended			
(In Thousands)	October 31, 2007	July 31, 2007	April 30, 2007	January 31, 2007
Housing revenues:				
Northeast	$ 298,039	$ 238,299	$ 185,852	$ 213,286
Mid-Atlantic	258,178	215,363	189,370	222,688
Midwest	81,138	65,563	41,524	38,579
Southeast	155,560	164,111	207,844	217,725
Southwest	255,670	196,681	200,053	176,170
West	259,634	199,209	233,371	267,468
Consolidated total	$ 1,308,219	$ 1,079,226	$ 1,058,014	$ 1,135,916
Sales contracts (net of cancellations):				
Northeast	$ 218,424	$ 206,103	$ 202,884	$ 175,048
Mid-Atlantic	119,188	126,269	239,485	192,639
Midwest	71,678	52,386	68,735	55,945
Southeast	76,451	88,253	107,345	40,021
Southwest	168,440	201,579	222,119	166,202

West	165,023	145,295	248,815	274,853
Consolidated total	$ 819,204	$ 819,885	$ 1,089,383	$ 904,708

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	Quarter Ended			
(In Thousands)	**October 31, 2006**	**July 31, 2006**	**April 30, 2006**	**January 31, 2006**
Housing revenues:				
Northeast	$ 358,355	$ 234,231	$ 203,828	$ 196,299
Mid-Atlantic	309,148	222,653	251,012	197,878
Midwest	63,353	52,019	29,124	29,203
Southeast	267,762	394,759	311,202	269,778
Southwest	290,159	220,211	232,289	183,259
West	389,039	375,953	452,093	369,780
Consolidated total	$ 1,677,816	$ 1,499,826	$ 1,479,548	$ 1,246,197
Sales contracts (net of cancellations):				
Northeast	$ 178,882	$ 209,478	$ 225,355	$ 195,021
Mid-Atlantic	149,168	190,855	309,773	187,374
Midwest	61,748	43,396	52,226	29,380
Southeast	142,701	179,897	189,762	314,027
Southwest	212,366	199,492	265,790	170,704
West	235,475	271,904	343,303	257,151
Consolidated total	$ 980,340	$ 1,095,022	$ 1,386,209	$ 1,153,657

Our reported level of sales contracts (net of cancellations) has been impacted by a slow down in sales and an increase in our cancellation rates over the past two years, due to weakening market conditions and tighter mortgage loan underwriting criteria. Cancellation rates represent the number of cancelled contracts in the quarter divided by the number of gross sales contracts executed in the quarter. For comparison, the following are historical cancellation rates, excluding unconsolidated joint ventures. The more recent spike in the fourth quarter of fiscal 2008 cancellation rate, we believe, is partially due to the significant financial market turmoil that began in mid-September 2008:

Quarter	**2008**	**2007**	**2006**	**2005**	**2004**
First	38%	36%	30%	27%	23%
Second	29%	32%	32%	21%	19%
Third	32%	35%	33%	24%	20%
Fourth	42%	40%	35%	25%	24%

Another common and meaningful way to analyze our cancellation trends is to compare the number of contract cancellations as a percentage of beginning backlog. The following table provides this historical comparison, excluding unconsolidated joint ventures.

Quarter	**2008**	**2007**	**2006**	**2005**	**2004**
First	16%	17%	11%	15%	14%
Second	24%	19%	15%	17%	18%
Third	20%	18%	14%	15%	13%
Fourth	30%	26%	16%	12%	15%

Historically, most cancellations occur within the legal rescission period, which varies by state but is generally less than two weeks. Cancellations also occur as a result of a buyer's failure to qualify for a mortgage, which generally occurs during the first few weeks after signing. However, in 2008 and 2007, we have experienced a higher than normal number of cancellations later in the construction process. These cancellations are related primarily to falling prices, sometimes due to new discounts offered by us or other builders, leading the buyer to lose confidence in their contract price and due to tighter mortgage underwriting criteria leading to some customer's inability to be approved for a mortgage loan. In some cases, the buyer will walk away from a significant nonrefundable deposit that we recognize as other revenues. We expect that cancellation rates will return to a more normal level at some point as prices stabilize, but it is difficult to predict when this will occur, and the timing will vary by market.

An important indicator of our future results is recently signed contracts and our home contract backlog for future deliveries. Our consolidated contract backlog, excluding unconsolidated joint ventures, using base

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sales prices by segment is set forth below:

(Dollars In Thousands)	October 31, 2008	October 31, 2007	October 31, 2006
Northeast:			
Total contract backlog	$ 215,604	$ 503,445	$ 591,849
Number of homes	497	975	1,218
Mid-Atlantic:			
Total contract backlog	$ 165,871	$ 358,778	$ 562,670
Number of homes	385	753	1,134
Midwest:			
Total contract backlog	$ 61,108	$ 153,171	$ 117,148
Number of homes	291	759	668
Southeast:			
Total contract backlog	$ 45,657	$ 614,575	$ 1,093,299
Number of homes	163	2,151	3,813
Southwest:			
Total contract backlog	$ 100,305	$ 174,206	$ 224,482
Number of homes	420	751	999
West:			
Total contract backlog	$ 57,642	$ 205,716	$ 334,102
Number of homes	151	549	664
Totals:			
Total consolidated contract backlog	$ 646,187	$ 2,009,891	$ 2,923,550
Number of homes	1,907	5,938	8,496

The decline in our backlog from October 31, 2007 to October 31, 2008 is a direct result of a falloff in our contract pace. Our net contracts for the full year of fiscal 2008, excluding unconsolidated joint ventures, declined 40.5% compared to fiscal 2007. In the month of November 2008, excluding unconsolidated joint ventures, we signed an additional 284 net contracts amounting to $63.4 million in contract value.

Cost of sales includes expenses for consolidated housing and land and lot sales, including inventory impairment loss and land option write-offs (defined as "land charges" in the schedules below). A breakout of such expenses for consolidated housing sales and housing gross margin is set forth below:

	Year Ended		
(Dollars In Thousands)	October 31, 2008	October 31, 2007	October 31, 2006
Sale of homes	$3,177,853	$ 4,581,375	$ 5,903,387
Cost of sales, excluding interest expense	2,965,886	3,890,474	4,538,795
Homebuilding gross margin, before cost of	211,967	690,901	1,364,592

sales interest expense and land charges			
Cost of sales interest expense, excluding land sales interest expense	136,439	130,825	106,892
Homebuilding gross margin, after cost of sales interest expense, before land charges	75,528	560,076	1,257,700
Land charges	710,120	457,773	336,204
Homebuilding gross margin, after cost of sales interest expense and land charges	$ (634,592)	$ 102,303	$ 921,496
Gross margin percentage, before cost of sales interest expense and land charges	6.7%	15.1%	23.1%
Gross margin percentage, after cost of sales interest expense, before land charges	2.4%	12.2%	21.3%
Gross margin percentage after cost of sales interest expense and land charges	(20.0)%	2.2%	15.6%

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Cost of sales expenses as a percentage of consolidated home sales revenues are presented below:

	Year Ended		
	October 31, 2008	October 31, 2007	October 31, 2006
Sale of homes	100%	100.0%	100.0%
Cost of sales, excluding interest:			
Housing, land and development costs	82.1%	74.3%	68.6%
Commissions	2.7%	2.8%	2.5%
Financing concessions	1.7%	1.4%	1.0%
Overheads	6.8%	6.4%	4.8%
Total cost of sales, before interest expense and land charges	93.3%	84.9%	76.9%
Gross margin percentage, before cost of sales interest expense and land charges	6.7%	15.1%	23.1%
Cost of sales interest	4.3%	2.9%	1.8%
Gross margin percentage, after cost of sales interest expense and before land charges	2.4%	12.2%	21.3%

We sell a variety of home types in various communities, each yielding a different gross margin. As a result, depending on the mix of communities delivering homes, consolidated gross margin may fluctuate up or down. Total homebuilding gross margins, before interest expense and land impairment and option write off charges decreased to 6.7% for the year ended October 31, 2008 compared to 15.1% for the same period last year. Continued declines in percentages in fiscal 2008 are primarily the result of decreased sales prices and increased buyer concessions. The declining pace of sales in our markets in 2006, 2007 and 2008 has led to intense competition in many of our specific community locations. In order to maintain a reasonable pace of absorption, we have increased incentives, reduced lot location premiums, as well as lowered some base prices, all of which have impacted our margins significantly. In addition, homes for which contracts have been cancelled have typically been resold at a lower price, resulting in a further decline in margins. As discussed in "Homebuilding Results by Segment" below, certain of our segments experienced increases in average selling prices for the year ended October 31, 2008 compared to 2007. It should be noted however, that these increases are primarily the result of geographic and community mix of our deliveries, rather than an ability to increase home prices.

Reflected as inventory impairment loss and land option write-offs in cost of sales ("land charges"), we have written-off or written-down certain inventories totaling $710.1 million, $457.8 million, and $336.2 million during the years ended October 31, 2008, 2007, and 2006, respectively, to their estimated fair value. See "Notes to Consolidated Financial Statements Note 13" for an additional discussion. During the years ended October 31, 2008, 2007, and 2006, we wrote-off residential land options and approval and engineering costs amounting to $114.1 million, $126.0 million, and $159.1 million, respectively, which are included in the total write-offs mentioned above. When a community is redesigned, abandoned engineering cost are written-off. Option and approval and engineering costs are written-off when a community's proforma profitability does not produce adequate returns on the investment commensurate with the risk and we cancel the option. Such write-offs were located in all of our segments. The impairments amounting to $596.0 million, $331.8 million and $177.1 million for the years ending October 31, 2008, 2007 and 2006, respectively, were incurred because of recent changes in the value of land in many of our markets and a change in the market strategy to liquidate a particular property or lower sales prices.

Below is a break-down of our lot option walk-aways and impairments by segment for fiscal 2008. In 2008, in total, we walked away from 48.3% of all the lots we controlled under option contracts. The remaining 51.7% of our option lots are in communities that remain economically feasible, including a substantial number that were successfully renegotiated over the past year. The largest concentration of lots we walked away from was in the Mid-Atlantic and Southeast segments.

The following table represents lot option walk-aways by segment for the year ended October 31, 2008:

(In Millions)	Dollar Amount of Walk Away	Number of Walk-Away Lots	% of Walk-Away Lots	Total Option Lots at October 31, 2008(1)	Walk-Away Lots as a % of Total Lots
Northeast	$ 20.7	2,155	14.0%	7,069	30.5%
Mid-Atlantic	45.6	5,017	32.6%	8,183	61.3%
Midwest	0.7	257	1.7%	2,537	10.1%
Southeast	32.2	5,833	38.0%	7,169	81.4%
Southwest	10.4	1,689	11.0%	5,321	31.7%
West	4.5	419	2.7%	1,555	26.9%
Total	$ 114.1	15,370	100.0%	31,834	48.3%

(1) *Includes lots optioned that the Company walked-away from in the year ended October 31, 2008.*

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The following table represents impairments by segment for the year ended October 31, 2008:

(In Millions)	Dollar Amount of Impairment	% of Impairments	Pre-Impairment Value	% of Pre-Impairment Value
Northeast	$ 43.5	7.3%	$ 208.2	20.9%
Mid-Atlantic	38.1	6.4%	155.3	24.5%
Midwest	7.7	1.3%	32.3	23.8%
Southeast	53.4	9.0%	160.5	33.3%
Southwest	81.1	13.6%	212.8	38.1%
West	372.2	62.4%	1,018.2	36.6%
Total	$ 596.0	100.0%	$ 1,787.3	33.3%

Homebuilding selling, general, and administrative expenses decreased to $377.1 million for the year ended October 31, 2008, and decreased to $539.4 million for the year ended October 31, 2007 from $593.9 million for the year ended October 31, 2006. The decrease in expenses in 2008 and 2007 is the result of a reduction of personnel in order to better manage our overhead during the current market decline, partially offset by severance costs associated with involuntary terminations that occured during the year and decreases in incentive compensation, that were based on profitability. Also adding to the decrease is the reduction in the number of open for sale communities of 284 in fiscal 2008 from 431 in fiscal 2007.

Land Sales and Other Revenues

Land sales and other revenues consist primarily of land and lot sales. A breakout of land and lot sales is set forth below:

	Year Ended		
(In Thousands)	October 31, 2008	October 31, 2007	October 31, 2006
Land and lot sales	$57,776	$ 107,955	$ 140,389
Cost of sales, excluding interest	45,016	87,179	94,286
Land and lot sales gross margin, excluding interest	12,760	20,776	46,103
Land sales interest expense	9,522	1,132	1,437
Land and lot sales gross margin, including interest	$ 3,238	$ 19,644	$ 44,666

Land sales are ancillary to our residential homebuilding operations and are expected to continue in the future but may significantly fluctuate up or down. Profits from land sales for the year ended October 31, 2008 were less than for the year ended October 31, 2007. Although we budget land sales, they are often dependent upon receiving approvals and entitlements, the timing of which can be uncertain. As a result, projecting the amount and timing of land sales is difficult.

Other revenues decreased $13.1 million for the year ended October 31, 2008 compared to the year ended October 31, 2007. Other revenues include income from contract cancellations, where the deposit has been forfeited due to contract terms, interest income, cash discounts and miscellaneous one-time receipts. For fiscal 2007, Other revenues also included $19.1 million related to the termination of our Credit Agreement and Agreement for Letter of Credit with Citicorp USA, Inc. which was the primary reason for the decrease from fiscal 2008 to 2007. This is also the cause of the $18.5 million increase in Other revenue for the year ended October 31, 2007 when compared to the year ended October 31, 2006.

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Homebuilding Operations by Segment

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

Segment Analysis (Dollars in Thousands, except average sales price)

	Years Ended October 31,				
	2008	Variance 2008 Compared to 2007	2007	Variance 2007 Compared to 2006	2006
Northeast					
Homebuilding revenue	$ 704,723	$ (254,110)	$ 958,833	$ (59,151)	$ 1,017,984
(Loss) income before income taxes	$ (114,416)	$ (95,599)	$ (18,817)	$ (98,914)	$ 80,097
Homes delivered	1,412	(587)	1,999	(189)	2,188
Average sales price	$ 481,224	$ 13,252	$ 467,972	$ 14,264	$ 453,708
Contract cancellation rate	30%	4%	26%	4%	22%
Mid-Atlantic					
Homebuilding revenue	$ 513,719	$ (399,994)	$ 913,713	$ (120,760)	$ 1,034,473
(Loss) income before income taxes	$ (142,249)	$ (217,073)	$ 74,824	$ (81,106)	$ 155,930
Homes delivered	1,248	(678)	1,926	(58)	1,984
Average sales price	$ 407,860	$ (51,953)	$ 459,813	$ (34,487)	$ 494,300
Contract cancellation rate	42%	1%	41%	4%	37%
Midwest					
Homebuilding revenue	$ 211,587	$ (16,288)	$ 227,875	$ 55,935	$ 171,940
(Loss) before income taxes	$ (37,415)	$ 42,792	$ (80,207)	$ (20,112)	$ (60,095)
Homes delivered	965	(78)	1,043	188	855
Average sales price	$ 217,367	$ (86)	$ 217,453	$ 14,296	$ 203,157
Contract cancellation rate	34%	7%	27%	(2)%	29%
Southeast					
Homebuilding revenue	$ 632,050	$ (146,454)	$ 778,504	$ (482,835)	$ 1,261,339
(Loss) before income taxes	$ (146,406)	122,096	$ (268,502)	$ (266,980)	$ (1,522)
Homes delivered	2,572	(199)	2,771	(2,303)	5,074
Average sales price	$ 242,654	$ (26,289)	$ 268,943	$ 23,870	$ 245,073
Contract cancellation rate	49%	(3)%	52%	15%	37%
Southwest					
Homebuilding revenue	$ 610,045	$ (231,020)	$ 841,065	$ (88,789)	$ 929,854
(Loss) income before income taxes	$ (101,470)	$ (127,181)	$ 25,711	$ (49,972)	$ 75,683
Homes delivered	2,616	(1,027)	3,643	(609)	4,252
Average sales price	$ 230,701	$ 3,258	$ 227,443	$ 9,682	$ 217,761
Contract cancellation rate	30%	0%	30%	3%	27%
West					
Homebuilding revenue	$ 577,228	$ (405,904)	$ 983,132	$ (657,937)	$ 1,641,069
(Loss) income before income taxes	$ (524,701)	$ (187,487)	$ (337,214)	$ (386,333)	$ 49,119
Homes delivered	1,764	(418)	2,182	(1,405)	3,587
Average sales price	$ 312,913	$ (126,905)	$ 439,818	$ (2,575)	$ 442,393
Contract cancellation rate	31%	(8)%	39%	1%	38%

Homebuilding Results by Segment

Northeast Homebuilding revenues decreased 26.5% in 2008 compared to 2007 primarily due to a 29.4% decrease in homes delivered offset by a 2.8% increase in average selling price as the mix of communities that had deliveries in 2008 was different than 2007. Loss before income taxes increased $95.6 million to a loss of $114.4 million, which is mainly due to a significant reduction in gross margin percentage before interest expense as the markets in this segment have become much more competitive and a $7.8 million increase in inventory impairment loss and land option write-offs in 2008.

Homebuilding revenues decreased 5.8% in 2007 compared to 2006 primarily due to an 8.6% decrease in homes delivered offset by a 3.1% increase in average selling price as the mix of communities that had deliveries in 2007 was different than 2006. Income before income taxes decreased $98.9 million to a loss of $18.8 million, which was mainly due to a significant reduction in gross margin percentage before interest expense as the markets in this segment have become much more competitive.

Mid-Atlantic Homebuilding revenues decreased 43.8% in 2008 compared to 2007 primarily due to a 35.2% decrease in homes delivered and a 11.3% decrease in average selling price due to increased incentives and the mix of communities delivered in 2008 was different than 2007. Income before income taxes decreased $217.1 million to a loss of $142.2 million, which $64.3 million is from the increase in inventory impairment loss and land option write-offs in 2008. Additionally, there was a $15.1 million goodwill impairment charge recorded in 2008. The segment also had a significant reduction in gross margin percentage before interest expense as the markets in this segment have become much more competitive.

Homebuilding revenues decreased 11.7% in 2007 compared to 2006 primarily due to a 2.9% decrease in homes delivered and a 7.0% decrease in average selling price due to increased incentives and the mix of communities delivered in 2007 was different than 2006. Income before income taxes was down $81.1 million to $74.8 million, which is mainly due to a significant reduction in gross margin percentage before interest expense as the markets in this segment have become much more competitive.

Midwest Homebuilding revenues decreased 7.1% in 2008 compared to 2007 primarily due to a 7.5% decrease in homes delivered, while average selling prices remained flat. The decreases in deliveries was the result of a more competitive and slowing housing market. The segment loss before income taxes decreased $42.8 million to a loss of $37.4 million. This was due to only $8.4 million of inventory impairment loss and land option write-offs in 2008, compared to $28.1 million in 2007 and no intangible impairment in 2008 compared to $14.6 million in 2007.

Homebuilding revenues increased 32.5% in 2007 compared to 2006 primarily due to a 22% increase in homes delivered and a 7.0% increase in average selling price. The increases in deliveries and average selling price were the result of organic growth in this segment in Cleveland. Despite the growth in revenues, the segment loss before income taxes increased $20.1 million to a loss of $80.2 million. This was due to a $14.6 million intangible impairments and a sizable reduction in gross margin percentage before interest expense.

Southeast Homebuilding revenues decreased 18.8% in 2008 compared to 2007 primarily due to a 7.2% decrease in homes delivered and a 9.8% decrease in average selling price. The primary reason for the decrease in deliveries and average selling price is the continuing declining market conditions in Florida and in the mix of communities delivering homes. The loss before income taxes decreased $122.1 million to a loss of $146.4 million, due mainly to $85.6 million of inventory impairment losses and land option write-offs in 2008 compared to $113.3 million in 2007 and $2.4 million of intangible impairments in 2008 compared to $108.6 million in 2007.

Homebuilding revenues decreased 38.3% in 2007 compared to 2006 primarily due to a 45.4% decrease in homes delivered, partially offset by a 9.7% increase in average selling price. The primary reason for the decrease in deliveries is the continuing declining market conditions in Florida. The average price increase is due to the change in the mix of communities delivering homes. The loss before income taxes increased $267.0 million to a loss of $268.5 million, due mainly to a $7.3 million increase in inventory impairment loss and land option write-offs in 2007 and $108.6 million of intangibles impairments, as well as a significant reduction in gross margin percentage before interest expense as the markets in this segment have become much more competitive.

Southwest Homebuilding revenues decreased 27.5% in 2008 compared to 2007 primarily due to a 28.2% decrease in homes delivered offset by 1.4% increase in average selling price. The reduction of deliveries resulted from a decline in the activity in the Arizona market, as that market has been impacted by tighter mortgage lending requirements, thus eliminating certain potential homebuyers. The increase in average selling price is due to the mix of communities that had deliveries in 2008 compared to 2007. Income before income taxes decreased $127.2 million to a loss of $101.5 million in 2008 mainly due to a $75.5 million increase in inventory impairment losses and land option write-offs in 2008, a goodwill impairment of $14.9 million and a significant reduction in gross margin percentage before interest expense.

Homebuilding revenues decreased 9.5% in 2007 compared to 2006 primarily due to a 14.3% decrease in homes delivered offset by 4.4% increase in average selling price. The reduction of deliveries resulted from a decline in the activity in the Arizona market, as that market has been impacted by tighter mortgage lending requirements, thus eliminating certain potential homebuyers. The increase in average selling price is due to the mix of communities that had deliveries in 2007 compared to 2006. Income before income taxes decreased $50.0 million to $25.7 million in 2007 mainly due to a $15.4 million increase in land charges in 2007 and a reduction in gross margin percentage before interest expense.

West Homebuilding revenues decreased 41.3% in 2008 compared to 2007 primarily due to a 19.2% decrease in homes delivered and a 28.9% decrease in average selling price. This reduced revenue was further

compounded by a significant reduction in gross margin percentage before interest expense. The decrease in deliveries and the reduced gross margin was the result of the more competitive and slowing housing market in California throughout 2007 and more so in 2008. As a result of the above and a $152.1 million increase in inventory impairment losses and land option write-offs in 2008, loss before income taxes increased $187.5 million to a loss of $524.7 million in 2008.

Homebuilding revenues decreased 40.1% in 2007 compared to 2006 primarily due to a 39.2% decrease in homes delivered and a 0.6% decrease in average selling price. This reduced revenue was further compounded by a significant reduction in gross margin percentage before interest expense. The decrease in deliveries and the reduced gross margin was the result of the more competitive and slowing housing market in California throughout 2007. As a result of the above and a $123.2 million increase in inventory impairment losses and land option write-offs in 2007, income before income taxes decreased $386.3 million to a loss of $337.2 million in 2007.

Financial Services

Financial services consist primarily of originating mortgages from our homebuyers, selling such mortgages in the secondary market, and title insurance activities. During the years ended October 31, 2008, October 31, 2007, and October 31, 2006, financial services provided a $16.7 million, $27.9 million, and $31.0 million pretax profit, respectively. In 2008 financial services revenue decreased $24.0 million to $52.2 million due to a decrease in the number of mortgage settlements and a decrease in the average loan amount. Revenues from October 31, 2006 to October 31, 2007 decreased $13.4 million to $76.2 million consistent with our reduction in deliveries. In the market areas served by our wholly-owned mortgage banking subsidiaries, approximately 75%, 71%, and 63% of our non-cash homebuyers obtained mortgages originated by these subsidiaries during the years ended October 31, 2008, 2007, and 2006, respectively. Servicing rights on new mortgages originated by us will be sold as the loans are closed.

Corporate General and Administrative

Corporate general and administrative expenses include the operations at our headquarters in Red Bank, New Jersey. These expenses include our executive offices, information services, human resources, corporate accounting, training, treasury, process redesign, internal audit, construction services, and administration of insurance, quality, and safety. Corporate general and administrative expenses declined $3.0 million for the year ended October 31, 2008 compared to the year ended October 31, 2007 and $10.9 million for the year ended October 31, 2007 compared to the year ended October 31, 2006. The reduction in expenses is due to personnel reductions, reduced bonuses and other overhead cost savings.

Other Interest

Other interest increased $20.6 million to $30.4 million for the year ended October 31, 2008. In 2007, other interest increased $6.2 million to $9.8 million for the year ended October 31, 2007. Beginning in the third quarter of fiscal 2008, our assets that qualify for interest capitalization (inventory under development) no longer exceeded our debt, and therefore a portion of interest not covered by qualifying assets must be directly expensed. The increase for 2007, from 2006, is due to the interest on completed homes in backlog in Fort Myers, unsold homes in completed high rise communities and interest on land in planning being expensed as incurred. The interest related to Fort Myers was capitalized during construction, but in 2007 many of the homes were complete. When we incur interest on completed homes, it is expensed as it no longer qualifies for capitalization.

Other Operations

Other operations consist primarily of miscellaneous residential housing operations expenses, senior rental residential property operations, earnout payments from homebuilding company acquisitions, minority interest relating to consolidated joint ventures, and corporate owned life insurance. Other operations increased $5.0 million to $9.8 million for the year ended October 31, 2008 and decreased $40.4 million to $4.8 million for the year ended October 31, 2007. The increase in other operations from October 31, 2007 to October 31, 2008, is attributed to the $2.1 million in legal and settlement costs in 2008, related to cases dismissed in Item 3, Legal Proceedings, as well as an increase in rent expense from a new commercial rental property. The decrease from October 31, 2006 to October 31, 2007 is primarily due to decreased accrued earnout obligations, resulting from two earnout agreements ending and lower profits in fiscal 2007, compared to the prior year. Other operations was further decreased by reduced profits from a consolidated joint venture that has finished delivering the homes in its community.

Goodwill and Intangible Amortization and Impairments

We amortized our definite life intangibles over their expected useful life, ranging from one to four years. In fiscal 2008, this expense includes the impairment of the remaining $2.7 million balance of definite life intangibles and $32.7 million of goodwill. Goodwill and Intangible amortization and impairments decreased $125.2 million for the year ended October 31, 2008, when compared to the same period last year. The decrease for the year ended October 31, 2008 was primarily the result of reduced intangible amortization in 2008 as a result of the extensive write-offs during the fourth quarter of 2007, partially offset by the impairments recorded in 2008. The amortization expense increased $107.3 million to $162.1 million for the year ended October 31, 2007. This increase is primarily due the impairment of intangible assets of $135.2 million previously discussed, as well as additional amortization from our 2006 acquisitions.

(Loss) Income From Unconsolidated Joint Ventures

(Loss) income from unconsolidated joint ventures consists of our share of the losses or earnings of the joint venture. The loss increased $8.4 million to a loss of $36.6 million for the year ended October 31, 2008. Our share of operations decreased $43.6 million to a loss of $28.2 million for the year ended October 31, 2007. The increase in the loss in 2008 is mainly due to our share of the losses from operations on our unconsolidated joint ventures, as well as the write-off of the investment we had in two of our homebuilding joint ventures, as the recoverability of these investments have been deemed unlikely. The loss in 2007 is primarily related to our share of the losses from inventory impairments, land-option and walk-away costs, and the write-off of the intangibles from our joint venture with Blackstone Real Estate Advisors.

Total Taxes

Total tax provision (benefit) as a percentage of the loss before taxes was 3.7% for the twelve months ended October 31, 2008. The rate was significantly below the statutory tax rate, because we recorded an additional $409.6 million charge to our current and deferred tax asset valuation allowance in the twelve months ended October 31, 2008, as discussed further below.

Deferred federal and state income tax assets primarily represent the deferred tax benefits arising from temporary differences between book and tax income which will be recognized in future years as an offset against future taxable income. If, for some reason, the combination of future years income (or loss) combined with the reversal of the timing differences results in a loss, such losses can be carried back to prior years or carried forward to future years to recover the deferred tax assets. In accordance with SFAS No. 109, "Accounting for Income Taxes" ("SFAS 109"), we evaluate our deferred tax assets quarterly to determine if valuation allowances are required. SFAS 109 requires that companies assess whether valuation allowances should be established based on the consideration of all available evidence using a "more likely than not" standard. Given the continued downturn in the homebuilding industry during 2007 and 2008, resulting in additional inventory and intangible impairments, we are now in a three-year cumulative loss position. According to SFAS 109, a three-year cumulative loss is significant negative evidence in considering whether deferred tax assets are realizable and also precludes relying on projections of future taxable income to support the recovery of deferred tax assets. Therefore, during the fourth quarter of 2007, we recorded a valuation allowance of $265.9 million against our deferred tax assets. Our valuation allowance for current and deferred taxes increased $409.6 million during the twelve months ended October 31, 2008, to $675.5 million at October 31, 2008. Our deferred tax assets at October 31, 2007 and October 31, 2008, for which there is no valuation allowance, relate to amounts that can be realized through future reversals of existing taxable temporary differences or through carrybacks to the 2005 and 2006 years.

Off-Balance Sheet Financing

In the ordinary course of business, we enter into land and lot option purchase contracts in order to procure land or lots for the construction of homes. Lot option contracts enable us to control significant lot positions with a minimal capital investment and substantially reduce the risks associated with land ownership and development. At October 31, 2008, we had $69.9 million in option deposits in cash and letters of credit to purchase land and lots with a total purchase price of $862.8 million. Our liability is generally limited to forfeiture of the nonrefundable deposits, letters of credit and other nonrefundable amounts incurred. We have no material third party guarantees. However, $9.4 million of the $862.8 million in land and lot option purchase contracts contain specific performance clauses which require us to purchase the land or lots upon satisfaction of certain requirements by both the sellers and the Company. Therefore, this specific performance obligation of $9.4 million, which is the purchase price for these lots net of cash deposits already paid, is recorded on the balance sheet in Liabilities from inventory not owned.

Pursuant to FASB Interpretation No. 46 (FIN 46R), "Consolidation of Variable Interest Entities" ("VIE"), we consolidated $77.0 million of inventory not owned at October 31, 2008, representing the fair value of the optioned property. Additionally, to reflect the fair value of the inventory consolidated under FIN 46R, we eliminated $8.3 million of its related cash deposits for lot option contracts, which are included in Consolidated inventory not owned. Since we do not own an equity interest in any of the unaffiliated variable interest entities that we must consolidate pursuant to FIN 46R, we generally have little or no control or influence over the operations of these entities or their owners. When our requests for financial information are denied by the land sellers, certain assumptions about the assets and liabilities of such entities are required. In most cases, the fair value of the assets of the consolidated entities have been based on the

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remaining contractual purchase price of the land or lots we are purchasing. In these cases, it is assumed that the entities have no debt obligations and the only asset recorded is the land or lots we have the option to buy with a related offset to minority interest for the assumed third party investment in the variable interest entity. At October 31, 2008, the balance reported in Minority interest from inventory not owned was $24.9 million. At October 31, 2008, we had cash deposits and letters of credit totaling $8.7 million, representing our current maximum exposure associated with the consolidation of lot option contracts. Creditors of these VIEs, if any, have no recourse against us. In addition, see Note 19 to the Consolidated Financial Statements for disclosure related to our investment in unconsolidated joint ventures.

Contractual Obligations

The following summarizes our aggregate contractual commitments at October 31, 2008:

	Payments Due by Period				
(In Thousands)	**Total**	**Less than 1 year**	**1-3 years**	**3-5 years**	**More than 5 years**
Long term debt(1)	$3,635,738	$209,104	$507,209	$1,556,340	$1,363,085
Operating leases	78,493	18,942	27,169	16,534	15,848
Purchase obligations(2)	11,226	10,089	1,137		
Total	$3,725,457	$238,135	$535,515	$1,572,874	$1,378,933

(1) *Represents our Senior Secured, Senior and Senior Subordinated Notes, Other Notes Payable and related interest payments for the life of the debt of $1,097.1 million. Interest on variable rate obligations is based on rates effective as of October 31, 2008. See Note 23 to the Consolidated Financial Statements for a discussion of the exchange offer completed in December 2008.*

(2) Represents obligations under option contracts with specific performance provisions, net of cash deposits.

We had outstanding letters of credit and performance bonds of approximately $197.5 million and $632.5 million, respectively, at October 31, 2008 related principally to our obligations to local governments to construct roads and other improvements in various developments. We do not believe that any such letters of credit or bonds are likely to be drawn upon.

Inflation

Inflation has a long-term effect, because increasing costs of land, materials, and labor result in increasing sale prices of our homes. In general, these price increases have been commensurate with the general rate of inflation in our housing markets and have not had a significant adverse effect on the sale of our homes. A significant risk faced by the housing industry generally is that rising house construction costs, including land and interest costs, will substantially outpace increases in the income of potential purchasers. Recently in the more highly regulated markets that have seen significant home price appreciation, customer affordability has become a concern. Our broad product array insulates us to some extent, but customer affordability of our homes is something we monitor closely.

Inflation has a lesser short-term effect, because we generally negotiate fixed price contracts with many, but not all, of our subcontractors and material suppliers for the construction of our homes. These prices usually are applicable for a specified number of residential buildings or for a time period of between three to twelve months. Construction costs for residential buildings represent approximately 59.3% of our homebuilding cost of sales.

Mergers and Acquisitions

On April 17, 2006, we acquired for cash the assets of CraftBuilt Homes, a privately held homebuilder headquartered in Bluffton, South Carolina. The acquisition expands our operations into the coastal markets of South Carolina and Georgia. CraftBuilt Homes designs, markets and sells single family detached homes. Due to its close proximity to Hilton Head, CraftBuilt Homes focuses on first-time, move-up, empty-nester and retiree homebuyers. This acquisition is being accounted for as a purchase with the results of its operations included in our consolidated financial statements as of the date of the acquisition.

In connection with the CraftBuilt Homes acquisition, we have definite life intangible assets equal to the excess purchase price over fair value of net tangible assets of $4.5 million in aggregate. During the fourth quarter of 2008, we determined that these assets were impaired and wrote off the remaining asset balance of $2.7 million. Prior to the impairment, we were amortizing the definite life intangibles over their estimated lives.

On May 1, 2006, we acquired through the issuance of 175,936 shares of Class A common stock substantially all of the assets of two mechanical contracting businesses. These acquisitions were accounted for as purchases with the results of their operations included in our consolidated financial statements as of the date of acquisition.

In connection with the two mechanical contracting business acquisitions, we recorded definite life intangible assets equal to the excess purchase price over fair value of net tangible assets of $4.0 million in aggregate. During the fourth quarter of fiscal 2007, we

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determined that these intangible assets were impaired and wrote off the remaining asset balance of $2.8 million. Prior to the impairment, we were amortizing the definite life intangibles over their estimated lives.

All fiscal 2006 acquisitions provide for other payments to be made, generally dependant upon achievement of certain future operating and return objectives, however, we do not expect to make any future payments based on our forecasts for these businesses.

Safe Harbor Statement

All statements in this Form 10-K that are not historical facts should be considered as "Forward-Looking Statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements involve known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Although we believe that our plans, intentions and expectations reflected in, or suggested by such forward-looking statements are reasonable, we can give no assurance that such pla