SunGard VPM Inc.
Form 424B3
April 15, 2011
Table of Contents

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PROSPECTUS

SunGard Data Systems Inc.

Offers to Exchange

$900,000,000 principal amount of its 7 3/8% Senior Notes due 2018 and $700,000,000 principal amount of its 7 5/8% Senior Notes due 2020, each of which has been registered under the Securities Act of 1933, for any and all of its outstanding 7 3/8% Senior Notes due 2018 and 7 5/8% Senior Notes due 2020, respectively.

We are conducting the exchange offer in order to provide you with an opportunity to exchange your unregistered notes for freely tradable notes that have been registered under the Securities Act.

The Exchange Offer

We will exchange all outstanding notes that are validly tendered and not validly withdrawn for an equal principal amount of exchange notes that are freely tradable.

You may withdraw tenders of outstanding notes at any time prior to the expiration date of the exchange offer.

The exchange offer expires at 12:00 a.m. midnight, New York City time, on May 13, 2011, unless extended. We do not currently intend to extend the expiration date.

The exchange of outstanding notes for exchange notes in the exchange offer will not be a taxable event for U.S. federal income tax purposes.

The terms of the exchange notes to be issued in the exchange offer are substantially identical to the outstanding notes, except that the exchange notes will be freely tradable.

Results of the Exchange Offer

The exchange notes may be sold in the over-the-counter market, in negotiated transactions or through a combination of such methods. We do not plan to list the notes on a national market.

All untendered outstanding notes will continue to be subject to the restrictions on transfer set forth in the outstanding notes and in the indenture. In general, the outstanding notes may not be offered or sold, unless registered under the Securities Act, except pursuant to an exemption from, or in a transaction not subject to, the Securities Act and applicable state securities laws. Other than in connection with the exchange offer, we do not currently anticipate that we will register the outstanding notes under the Securities Act.

See Risk Factors beginning on page 17 for a discussion of certain risks that you should consider before participating in the exchange offer.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of the exchange notes to be distributed in the exchange offer or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.

Each broker-dealer that receives exchange notes for its own account pursuant to the exchange offer must acknowledge that it will deliver a prospectus in connection with any resale of such exchange notes. This prospectus, as it may be amended or supplemented from time to time, may be used by a broker-dealer in connection with resales of exchange notes received in exchange for outstanding notes where such outstanding notes were acquired as a result of market-making activities or other trading activities. See Plan of Distribution.

The date of this prospectus is April 15, 2011.

Table of Contents

You should rely only on the information contained in this prospectus. We have not authorized anyone to provide you with different information. The prospectus may be used only for the purposes for which it has been published and no person has been authorized to give any information not contained herein. If you receive any other information, you should not rely on it. We are not making an offer of these securities in any state where the offer is not permitted.

TABLE OF CONTENTS

	Page
Prospectus Summary	1
Summary Historical Consolidated Financial Data	14
Risk Factors	17
Forward-Looking Statements	31
Use of Proceeds	33
Cash and Capitalization	34
Selected Historical Consolidated Financial Information	36
Management s Discussion and Analysis of Financial Condition and Results of Operations	38
Business	64
Management	76
Security Ownership of Certain Beneficial Owners	104
Certain Relationships and Related Party Transactions	109
Director Independence	111
Description of Other Indebtedness	112
The Exchange Offer	118
Description of 2018 Notes	128
Description of 2020 Notes	187
Certain United States Federal Income Tax Consequences of the Exchange Offer	245
Certain ERISA Considerations	246
Plan of Distribution	247
Legal Matters	247
Experts	248
Where You Can Find More Information	248
Index to Consolidated Financial Statements	F-1

Table of Contents

PROSPECTUS SUMMARY

This summary highlights information contained elsewhere in this prospectus. This summary may not contain all of the information that may be important to you in making your investment decision. You should read the entire prospectus, including the financial data and related notes and section entitled Risk Factors, before making an investment decision. Unless the context otherwise indicates, as used in this prospectus, the terms SunGard, we, our, us, and the company and similar terms refer to SunGard Data Systems Inc. and its subsidiaries on a consolidated basis. Sc of the statements in this prospectus constitute forward-looking statements. See Forward Looking Statements.

Our Company

We are one of the world s leading software and technology services companies. We provide software and technology services to financial services, higher education and public sector organizations. We also provide disaster recovery services, managed services, information availability consulting services and business continuity management software. We serve more than 25,000 customers in more than 70 countries. Our high quality software solutions, excellent customer support and specialized technology services result in strong customer retention rates across all of our business segments and create long-term customer relationships. We believe that we are one of the most efficient operators of mission-critical IT solutions as a result of the economies of scale we derive from serving multiple customers on shared processing platforms.

We have four business segments: Financial Systems (FS), Higher Education (HE), Public Sector (PS) and Availability Services (AS).

FS provides mission-critical software and technology services to virtually every type of financial services institution, including buy-side and sell-side institutions, third-party administrators, wealth managers, retail banks, insurance companies, corporate treasuries and energy trading firms. Our broad range of complementary software solutions and associated technology services help financial services institutions automate the business processes associated with trading, managing portfolios and accounting for investment assets.

HE provides software and technology services primarily to colleges and universities as well as to school districts. Education institutions rely on our broad portfolio of solutions and technology services to improve the way they teach, learn, manage and connect with their constituents.

PS provides software and technology services designed to meet the specialized needs of local, state and federal governments, public safety and justice agencies, utilities and other public sector institutions as well as nonprofits.

AS provides disaster recovery services, managed services, information availability consulting services and business continuity management software to 10,000 customers in North America and Europe. With five million square feet of data center and operations space, AS assists IT organizations across virtually all industry and government sectors to prepare for and recover from emergencies by helping them minimize their computer downtime and optimize their uptime. Through direct sales and channel partners, AS helps organizations ensure their people and customers have uninterrupted access to the information systems they need in order to do business.

We were acquired in August 2005 in a leveraged buy-out (LBO) by a consortium of private equity investment funds associated with Bain Capital Partners, The Blackstone Group, Goldman, Sachs & Co., Kohlberg Kravis Roberts & Co., Providence Equity Partners, Silver Lake and TPG (Sponsors). As a result of the LBO, we are highly leveraged and our equity is not publicly traded.

Table of Contents

Our Sponsors continually evaluate various strategic alternatives with respect to the Company, including a potential spin-off of the AS business to our current equity holders. We expect that if we were to spin-off any business segment, that business segment would incur new debt and we would repay a portion of our existing indebtedness. Additionally, it is possible that along with any spin-off, we would receive cash proceeds from an issuance of equity of SunGard Capital Corp. (SCC) or SunGard Capital Corp. II (SCII), which together are collectively referred to as our Parent Companies. There can be no assurance that we will ultimately pursue any strategic alternatives with respect to any business segment, including AS, or an equity issuance or, if we do, what the structure or timing for any such transaction would be.

Our Strengths

Leading franchise, attractive industry dynamics and global expansion opportunities. We believe that our businesses have leading positions and strong customer relationships in industries with attractive growth prospects and significant opportunities for global expansion.

Leading industry positions. We believe that our FS business is a leader in the sectors in which it participates within the highly fragmented global market for financial services software and technology services. We believe that our HE and PS businesses are both leading providers of software and technology services to education institutions and the public sector, respectively, and that AS is the pioneer and a leading provider in the information availability services industry. We believe that our strong customer relationships in the highly fragmented software and technology services sectors that we serve help us to maintain leading positions. Our customers use our solutions to manage their most mission-critical business processes, which we believe results in high switching costs that promote the retention of our solutions, provide opportunities to sell additional software and technology services, and create barriers to entry for other vendors. We believe that these factors provide us with competitive advantages that should enhance our growth potential.

Attractive industry dynamics. We believe that over the long term each of our primary business segments has good growth potential. We believe that our FS business will benefit from several key industry dynamics: the general increase in IT spending associated with increasing compliance, regulatory and risk management requirements; the shift from internal to outsourced IT spending; and an increasing need of our customers for real time information. We anticipate that our HE business will benefit from key trends in education: investment in higher education as an essential driver of economic growth; the growing emphasis within education on performance management and data-driven decision making; the ongoing transformation of education by online and mobile technologies; and the global demand for both higher education and lifelong learning. We believe that our AS business will continue to benefit from the increasing criticality of IT availability to support day-to-day business operations and commerce. We believe that our strong relationships with our customers in the relatively fragmented software and processing sectors that we serve and our extensive experience and the significant total capital that we have invested in AS help us to maintain leading positions. We believe that these factors should provide us with competitive advantages and enhance our growth potential.

Global opportunities. We believe that our FS, HE and AS businesses will benefit from the growth in developing economies in Asia Pacific and Latin America. As financial services practices evolve and mature in these developing economies, we believe that local institutions will look to leading global software and technology services providers with deep domain expertise, a suite of proven software capabilities and a local presence to provide implementation and support. We believe that our largest customers that seek to expand their businesses around the world seek to enhance

Table of Contents

efficiency by scaling their software and processing platforms globally. We believe that our industry footprint, global delivery capabilities and suite of solutions will provide us a competitive advantage.

Highly attractive business model. We have substantial recurring revenue, maintain a diversified and stable customer base and generate significant operating cash flow.

Extensive portfolio of software and technology services across our businesses with substantial recurring revenue. With a large portfolio of proprietary products and services in each of our four business segments, we have a diversified and stable business. With the exception of our broker/dealer business, we believe that our FS revenue is more insulated from changes in trading and transaction volumes than the financial services industry at large because our FS customers generally pay us monthly fees that are based on metrics such as number of accounts, trades or transactions, users or number of hours of service. Our portfolio of solutions and the largely recurring nature of our revenue across all four of our segments have reduced volatility in our revenue and operating income. Moreover, our specialized technology services and customized solutions help support and automate our customers mission-critical business processes and help increase the level of efficiency for our customers, which we believe reduces customer defections to other vendors or to in-house solutions.

Diversified and stable customer base. Our base of more than 25,000 customers includes most of the world s largest financial services firms, a variety of other financial services firms, corporate and government treasury departments, energy companies, higher education institutions, school districts, local governments and not-for-profit organizations. Our AS business serves customers across virtually all industries. In addition, our track record of helping our customers improve their operational efficiency, achieve high levels of availability and address regulatory requirements results in stable, long-term customer relationships. Our revenue is highly diversified by customer and product. During each of the past three fiscal years, no single customer has accounted for more than 10% of total revenue. On average for the past three fiscal years, services revenue has been approximately 90% of total revenue. About 70% of services revenue is highly recurring as a result of multiyear contracts and is generated from (1) software-related services including software maintenance and support, processing and rentals and (2) recovery and managed services. The remaining services revenue includes (1) professional services, which are recurring in nature as a result of long-term customer relationships, and (2) broker/dealer fees, which are largely correlated with trading volumes.

Significant operating cash flow generation. We are able to generate significant operating cash flows because of our strong operating margins. Our strong and predictable cash flow allows us to meet our significant debt-service requirements and make discretionary investments to grow the business, both by investing in new products and services and through acquisitions.

Experienced management team with track record of success with proper incentives. Our management team has a long track record of operational excellence, has a proven ability to expand our business by adding new solutions through both internal development and the acquisition and integration of complementary businesses, and is highly committed to our Company s growth.

Long track record of operational excellence at a large scale. Our experienced management team has proven capabilities in both running a global business and managing numerous applications that are important to our customers. Under their leadership, our businesses have expanded into new geographic markets, invested in developing new solutions and enhancing our technology services, met stringent customer and industry requirements and successfully incorporated new acquisitions.

Table of Contents

Our FS solutions support over 14,000 customers and process over ten million transactions per day. In our HE business, more than 1,800 organizations including colleges, universities, campuses, foundations and state systems use our solutions to serve more than 14 million students worldwide. Our PS products are used by agencies that serve more than 115 million citizens in North America. Our AS business is the pioneer and a leading provider in the information availability services industry and has 10,000 customers.

Experienced management team with appropriate incentives. Our executive officers have on average more than 15 years of industry experience. As part of the LBO, many of our senior managers committed significant personal capital to our Company.

Our Business Strategy

We are focused on expanding our position not only as a leading provider of software and technology services for financial services, higher education and public sector organizations, but also as the provider of choice for a wide range of information availability services and managed services for IT departments in companies across virtually all industries. Our strategy is to leverage our extensive customer base, deep domain knowledge and understanding of how to apply technology to support mission-critical business processes to produce innovative products and services. In pursuing expansion of our business, we emphasize fiscal discipline, sustainable revenue growth, improving margins and significant operating cash flow generation. The following are key objectives of our growth strategy:

Expand our industry-leading franchise. We constantly enhance our product and service offerings across our portfolio of businesses, leverage our customer relationships, and look to acquire complementary businesses at attractive valuations.

Enhance our products and expand our technology services. We continually support, upgrade and enhance our products to incorporate new technologies, meet the needs of our customers for increased operational efficiency and comply with new industry regulations and requirements. Our strong base of recurring revenue drives high operating margins that allow us to reinvest in our products and technology services. In 2010 and 2009, product development expenses were 10% and 9%, respectively, of our revenue from software and processing solutions. We have invested in building a global services organization comprising more than 5,000 consultants and developers with deep domain expertise to help customers develop, deploy and operate software solutions wherever and however they do business. We believe that our ability to offer a broad range of technology services including advisory services, systems integration, application development and managed services will help increase customer satisfaction as well as our share of the total IT budget of our customers.

Innovate to provide new solutions. We continue to introduce innovative products and services in all four of our business segments. Since the LBO in 2005, we have been able to invest in strategic growth initiatives to balance short-term and long-term growth. These initiatives have included launching Infinity, a software-as-a-service (SaaS) initiative that offers financial services institutions a software development environment, business process management (BPM) platform and on-demand SaaS components. In our HE business, we launched Open Digital Campus, an open-source initiative that brings together our extensive user community in order to accelerate the availability of functionality. In our PS business, we launched ONESolution, a software suite that enables local government agencies to access information and share data through mobile computer, computer-aided dispatch and Internet technologies. In our AS business, we launched enterprise

Table of Contents

cloud computing, which will help customers tap into the efficiency and cost advantages of a fully managed cloud environment with enterprise-grade application availability and security. We believe that our focus on innovation will help us increase our penetration of new and existing market sectors.

Automate key financial services industry transaction and information flows. We help our FS customers automate their mission-critical business processes internally and between their counterparties and trading partners by providing a network and technology infrastructure. Our global transaction network helps financial services institutions address the connectivity challenges of trading new instruments and accessing new trading venues worldwide. Our financial management network helps corporations drive maximum value from working capital and reduce risk by automating their interactions with their trading partners, suppliers and banks. We believe that by continuing to link organizations across their business ecosystem we will help strengthen our position as a leading provider of mission-critical software and technology services to the financial services industry.

Deepen our customer relationships. We focus on developing mutually beneficial, long-term relationships with our customers. We look to maximize cross-selling opportunities, bundle solutions and maintain a high level of customer satisfaction. Our FS global account management program allows us to gain access to senior decision makers, maintain account control and better target potential cross-selling and new business opportunities.

Expand in emerging countries with high growth rates for software and technology services. We seek to grow our business in developing economies including China, India and Brazil, where there is growing demand for software and technology services from the sectors we serve. We have established our presence in these and other emerging countries by investing in local sales, marketing and support personnel, by customizing our products to meet the needs of the market and by acquiring businesses.

Acquire and integrate complementary businesses. We seek to acquire businesses that complement our existing product and technology service offerings, expand our footprint in new markets and strengthen our leadership positions, and that will provide us with a suitable return on investment. We have a highly disciplined program to identify, evaluate and integrate acquisitions. Before committing to an acquisition, we devote significant resources to due diligence and to developing post acquisition integration plans, including the identification and quantification of potential cost savings and synergies. Since 1986, we have successfully completed the acquisition of over 175 businesses. We believe that our acquisition program has contributed significantly to our long-term growth and success.

Focus on increasing recurring revenue and implementing operational improvements. We continue to focus on increasing our recurring revenue base and implementing incremental operational improvements.

Increase our recurring revenue base. We strive to generate a high level of recurring revenue and stable cash flow from operations. We charge customers monthly subscription fees under multiyear contracts and will continue to pursue these types of arrangements because they offer high levels of revenue stability and visibility. We seek to renew existing contracts with multiyear terms, add new services and capabilities that produce recurring revenues and shift our mix of new business from on-premise software to software-as-a-service based on a subscription model.

Implement incremental operational improvements. We continue to implement operational improvements to further increase revenue, reduce costs and improve cash flow from operations.

Table of Contents

These include expanding the global account management program within FS to include large regional institutions, capitalizing on our global services organization to offer a broader range of services to our customers, implementing new SaaS solutions to help accelerate time-to-market and serve new markets, and continuing to consolidate data centers within FS. Within AS, numerous initiatives are underway or have been recently completed that will streamline our direct sales model, increase the level of automation within the service delivery process, and maximize our return on investments in data center personnel and facility space.

SunGard Data Systems Inc. was incorporated under Delaware law in 1982. Our principal executive offices are located at 680 East Swedesford Road, Wayne, Pennsylvania 19087. Our telephone number is (484) 582-2000.

Table of Contents

The Exchange Offer

In this prospectus, the term outstanding 2018 notes refers to the 7 3/8% Senior Notes due 2018 and the term outstanding 2020 notes refers to the 7 5/8% Senior Notes due 2020, all of which are referred to collectively as the outstanding notes. The term 2018 exchange notes refers to the 7 3/8% Senior Notes due 2018 and the term 2020 exchange notes refers to the 7 5/8% Senior Notes due 2020, each as registered under the Securities Act of 1933, as amended (the Securities Act). The term exchange notes refers collectively to the 2018 exchange notes and the 2020 exchange notes. The term notes refers collectively to the outstanding notes and the exchange notes.

On November 16, 2010, SunGard Data Systems Inc. issued $900 million aggregate principal amount of 7 3/8% Senior Notes due 2018 and $700 million aggregate principal amount of 7 5/8% Senior Notes due 2020 in a private offering.

General

In connection with the private offering, SunGard Data Systems Inc. and the guarantors of the outstanding notes entered into a registration rights agreement with the initial purchasers in which they agreed, among other things, to deliver this prospectus to you and to complete the exchange offer within 360 days after the date of original issuance of the outstanding notes. You are entitled to exchange in the exchange offer your outstanding notes for exchange notes which are identical in all material respects to the outstanding notes except:

- the exchange notes have been registered under the Securities Act;
- the exchange notes are not entitled to any registration rights which are applicable to the outstanding notes under the registration rights agreement; and
- the additional interest provisions of the registration rights agreement are no longer applicable.

The Exchange Offer

SunGard is offering to exchange:

- $900 million aggregate principal amount of 7 3/8% Senior Notes due 2018 which have been registered under the Securities Act for any and all of its existing 7 3/8% Senior Notes due 2018;
- $700 million aggregate principal amount of 7 5/8% Senior Notes due 2020 which have been registered under the Securities Act for any and all of its existing 7 5/8% Senior Notes due 2020.

You may only exchange outstanding notes in a minimum denomination of $2,000 and integral multiples of $1,000 in excess of $2,000.

Resale

Based on an interpretation by the staff of the Securities and Exchange Commission (the SEC) set forth in no-action letters issued to third parties, we believe that the exchange notes issued pursuant to the exchange offer in exchange for outstanding notes may be offered for resale, resold and otherwise transferred by you (unless you are our affiliate

within the meaning of Rule 405 under the Securities Act)

Table of Contents

without compliance with the registration and prospectus delivery provisions of the Securities Act, provided that:

- you are acquiring the exchange notes in the ordinary course of your business; and
- you have not engaged in, do not intend to engage in, and have no arrangement or understanding with any person to participate in, a distribution of the exchange notes.

If you are a broker-dealer and receive exchange notes for your own account in exchange for outstanding notes that you acquired as a result of market-making activities or other trading activities, you must acknowledge that you will deliver this prospectus in connection with any resale of the exchange notes. See Plan of Distribution.

Any holder of outstanding notes who:

- is our affiliate;
- does not acquire exchange notes in the ordinary course of its business; or
- tenders its outstanding notes in the exchange offer with the intention to participate, or for the purpose of participating, in a distribution of exchange notes cannot rely on the position of the staff of the SEC enunciated in Morgan Stanley & Co. Incorporated (available June 5, 1991) and *Exxon Capital Holdings Corporation* (available May 13, 1988), as interpreted in the SEC s letter to Shearman & Sterling, dated available July 2, 1993, or similar no-action letters and, in the absence of an exemption therefrom, must comply with the registration and prospectus delivery requirements of the Securities Act in connection with any resale of the exchange notes.

Expiration Date

The exchange offer will expire at 12:00 a.m. midnight, New York City time, on May 13, 2011, unless extended by SunGard Data Systems Inc. SunGard Data Systems Inc. does not currently intend to extend the expiration date.

Withdrawal

You may withdraw the tender of your outstanding notes at any time prior to the expiration of the exchange offer. SunGard Data Systems Inc. will return to you any of your outstanding notes that are not accepted for any reason for exchange, without expense to you, promptly after the expiration or termination of the exchange offer.

Conditions to the Exchange Offer

The exchange offer is subject to customary conditions, which SunGard Data Systems Inc. may waive. See The Exchange Offer Conditions to the Exchange Offer.

8

Table of Contents

Procedures for Tendering Outstanding Notes	If you wish to participate in the exchange offer, you must complete, sign and date the accompanying letter of transmittal, or a facsimile of such letter of transmittal, according to the instructions contained in this prospectus and the letter of transmittal. You must then mail or otherwise deliver the letter of transmittal, or a facsimile of such letter of transmittal, together with the outstanding notes and any other required documents, to the exchange agent at the address set forth on the cover page of the letter of transmittal.
	If you hold outstanding notes through The Depository Trust Company (DTC) and wish to participate in the exchange offer, you must comply with the Automated Tender Offer Program procedures of DTC by which you will agree to be bound by the letter of transmittal. By signing, or agreeing to be bound by, the letter of transmittal, you will represent to us that, among other things:
	you are not our affiliate within the meaning of Rule 405 under the Securities Act;
	you do not have an arrangement or understanding with any person or entity to participate in the distribution of the exchange notes;
	you are acquiring the exchange notes in the ordinary course of your business; and
	if you are a broker-dealer that will receive exchange notes for your own account in exchange for outstanding notes that were acquired as a result of market-making activities, that you will deliver a prospectus, as required by law, in connection with any resale of such exchange notes.
Special Procedures for Beneficial Owners	If you are a beneficial owner of outstanding notes that are registered in the name of a broker, dealer, commercial bank, trust company or other nominee, and you wish to tender those outstanding notes in the exchange offer, you should contact the registered holder promptly and instruct the registered holder to tender those outstanding notes on your behalf. If you wish to tender on your own behalf, you must, prior to completing and executing the letter of transmittal and delivering your outstanding notes, either make appropriate arrangements to register ownership of the outstanding notes in your name or obtain a properly completed bond power from the registered holder. The transfer of registered ownership may take considerable time and may not be able to be completed prior to the expiration date.
Guaranteed Delivery Procedures	If you wish to tender your outstanding notes and your outstanding notes are not immediately available or you cannot deliver your outstanding notes, the letter of transmittal or any other required documents, or you cannot comply with the procedures under DTC s

Table of Contents

	Automated Tender Offer Program for transfer of book-entry interests, prior to the expiration date, you must tender your outstanding notes according to the guaranteed delivery procedures set forth in this prospectus under The Exchange Offer Guaranteed Delivery Procedures.
Effect on Holders of Outstanding Notes	As a result of the making of, and upon acceptance for exchange of all validly tendered outstanding notes pursuant to the terms of the exchange offer, SunGard Data Systems Inc. and the guarantors of the notes will have fulfilled a covenant under the registration rights agreement. Accordingly, there will be no increase in the interest rate on the outstanding notes under the circumstances described in the registration rights agreement. If you do not tender your outstanding notes in the exchange offer, you will continue to be entitled to all the rights and limitations applicable to the outstanding notes as set forth in the indenture, except SunGard Data Systems Inc. and the guarantors of the notes will not have any further obligation to you to provide for the exchange and registration of the outstanding notes under the registration rights agreement. To the extent that outstanding notes are tendered and accepted in the exchange offer, the trading market for outstanding notes could be adversely affected.
Consequences of Failure to Exchange	All untendered outstanding notes will continue to be subject to the restrictions on transfer set forth in the outstanding notes and in the indenture. In general, the outstanding notes may not be offered or sold, unless registered under the Securities Act, except pursuant to an exemption from, or in a transaction not subject to, the Securities Act and applicable state securities laws. Other than in connection with the exchange offer, SunGard Data Systems Inc. and the guarantors of the notes do not currently anticipate that they will register the outstanding notes under the Securities Act.
United States Federal Income Tax Consequences	The exchange of outstanding notes in the exchange offer will not be a taxable event for United States federal income tax purposes. See Certain United States Federal Income Tax Consequences of the Exchange Offer.
Use of Proceeds	We will not receive any cash proceeds from the issuance of exchange notes in the exchange offer. See Use of Proceeds.
Exchange Agent	The Bank of New York Mellon is the exchange agent for the exchange offer. The addresses and telephone numbers of the exchange agent are set forth in the section captioned The Exchange Offer Exchange Agent.

Table of Contents

The Exchange Notes

The summary below describes the principal terms of the exchange notes. Certain of the terms and conditions described below are subject to important limitations and exceptions. The Description of 2018 Notes and Description of 2020 Notes sections of this prospectus contain more detailed descriptions of the terms and conditions of the outstanding notes and the exchange notes. The exchange notes will have terms identical in all material respects to the outstanding notes, except that the exchange notes will not contain terms with respect to transfer restrictions, registration rights and additional interest for failure to observe certain obligations in the registration rights agreement.

Issuer	SunGard Data Systems Inc.
Securities offered	$900.0 million aggregate principal amount of 7 $^{3}/8$% Senior Notes due 2018.
	$700.0 million aggregate principal amount of 7 $^{5}/8$% Senior Notes due 2020.
Maturity date	The 2018 exchange notes will mature on November 15, 2018.
	The 2020 exchange notes will mature on November 15, 2020.
Interest payment dates	May 15 and November 15, commencing May 15, 2011. Interest began accruing on November 16, 2010.
Optional redemption	At any time prior to November 15, 2013, we may redeem the 2018 exchange notes, in whole or in part, at a price equal to 100% of the principal amount of the 2018 exchange notes redeemed plus accrued and unpaid interest, if any, to the redemption date and a make-whole premium, as described under Description of 2018 Notes Optional Redemption.
	The 2018 exchange notes will be redeemable at our option, in whole or in part, at any time on or after November 15, 2013, at the redemption prices set forth in this prospectus, together with accrued and unpaid interest, if any, to the date of redemption.
	At any time prior to November 15, 2013, we may redeem up to 35% of the original principal amount of the 2018 exchange notes with the proceeds of certain equity offerings at a redemption price of 107.375% of the principal amount of the 2018 exchange notes, together with accrued and unpaid interest, if any, to the date of redemption.
	At any time prior to November 15, 2015, we may redeem the 2020 exchange notes, in whole or in part, at a price equal to 100% of the principal amount of the 2020 exchange notes redeemed plus accrued and unpaid interest, if any, to the redemption date and a make-whole premium, as described under Description of 2020 Notes Optional Redemption.

Table of Contents

The 2020 exchange notes will be redeemable at our option, in whole or in part, at any time on or after November 15, 2015, at the redemption prices set forth in this prospectus, together with accrued and unpaid interest, if any, to the date of redemption.

At any time prior to November 15, 2013, we may redeem up to 35% of the original principal amount of the 2020 exchange notes with the proceeds of certain equity offerings at a redemption price of 107.625% of the principal amount of the 2020 exchange notes, together with accrued and unpaid interest, if any, to the date of redemption.

Mandatory offers to purchase

The occurrence of a change of control will be a triggering event requiring us to offer to purchase from you all or a portion of your exchange notes at a price equal to 101% of their principal amount, together with accrued and unpaid interest, if any, to the date of purchase.

Certain asset dispositions will also require us to use the proceeds from those asset dispositions to make an offer to purchase the exchange notes at 100% of their principal amount, together with accrued and unpaid interest, if any, to the date of purchase if such proceeds are not otherwise used within a specified period to repay indebtedness (with a corresponding reduction in commitment, if applicable) or to invest in capital assets related to our business or capital stock of a restricted subsidiary (as defined under the headings Description of 2018 Notes and Description of 2020 Notes).

Guarantees

The exchange notes will be guaranteed, jointly and severally, fully and unconditionally on a senior unsecured basis by each of our wholly-owned domestic subsidiaries that guarantees our senior secured credit facilities. Under certain circumstances, subsidiary guarantors may be released from their guarantees without the consent of the holders of notes. See Description of 2018 Notes Guarantees and Description of 2020 Notes Guarantees.

Ranking

The exchange notes will be our senior unsecured obligations and will:

- rank senior in right of payment to our existing and future debt and other obligations that are, by their terms, expressly subordinated in right of payment to the exchange notes;

- rank equally in right of payment to all of our existing and future senior unsecured debt and other obligations that are not, by their terms, expressly subordinated in right of payment to the exchange notes; and

- be effectively subordinated to all of our existing and future secured debt, to the extent of the value of the assets securing such debt, and be structurally subordinated to all obligations of each of our subsidiaries that is not a guarantor of the exchange notes.

12

Table of Contents

Similarly, the note guarantees will be senior unsecured obligations of the guarantors and will:

- rank senior in right of payment to all of the applicable guarantor s existing and future debt and other obligations that are, by their terms, expressly subordinated in right of payment to the exchange notes;
- rank equally in right of payment to all of the applicable guarantor s existing and future senior unsecured debt and other obligations that are not, by their terms, expressly subordinated in right of payment to the exchange notes; and
- be effectively subordinated in right of payment to all of the applicable guarantor s existing and future secured debt, to the extent of the value of the assets securing such debt, and be structurally subordinated to all obligations of any subsidiary of a guarantor if that subsidiary is not also a guarantor of the exchange notes.

As of December 31, 2010, the exchange notes and related guarantees would have ranked effectively junior to approximately $4,632 million of senior secured indebtedness.

Absence of public market for the notes

The exchange notes will be freely transferable but will also be new securities for which there will not initially be an actively trading market. Accordingly, we cannot assure you as to the future liquidity of any market for the exchange notes. The initial purchasers in the private offering of the outstanding notes have advised us that they currently intend to make a market in the exchange notes. However, they are not obligated to make a market in the exchange notes and any such market-making may be discontinued by the initial purchasers in their discretion at any time without notice.

Risk Factors

You should carefully consider all the information in the prospectus prior to exchanging your outstanding notes. In particular, we urge you to carefully consider the factors set forth under the heading Risk Factors.

Table of Contents

SUMMARY HISTORICAL CONSOLIDATED FINANCIAL DATA

The following table sets forth summary historical consolidated financial and other data as of and for the periods indicated. The historical consolidated financial data for the annual periods ended December 31, 2008, 2009 and 2010 have been derived from SunGard s audited consolidated financial statements included elsewhere in this prospectus.

Our historical results are not necessarily indicative of our future performance. The summary of historical consolidated financial data should be read in conjunction with Selected Historical Consolidated Financial Data, Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and related notes appearing elsewhere in this prospectus.

	Year Ended December 31,		
(Dollars in millions)	**2008**	**2009**	**2010**
Consolidated statements of operations data:			
Revenue	$ 5,401	$ 5,332	$ 4,992
Costs and expenses:			
Cost of sales and direct operating	2,601	2,534	2,201
Sales, marketing and administration	1,113	1,088	1,141
Product development	309	348	370
Depreciation and amortization	274	288	291
Amortization of acquisition-related intangible assets	472	529	484
Goodwill impairment charges		1,126	237
Total operating costs and expenses	4,769	5,913	4,724
Income (loss) from operations	632	(581)	268
Interest income	17	7	2
Interest expense and amortization of deferred financing fees	(597)	(637)	(638)
Loss on extinguishment of debt			(58)
Other income (expense)	(93)	15	7
Loss before income taxes	(41)	(1,196)	(419)
Benefit from (provision for) income taxes	(51)	74	29
Loss from continuing operations	(92)	(1,122)	(390)
Income (loss) from discontinued operations	(150)	4	(180)
Net loss	$ (242)	$ (1,118)	$ (570)
Consolidated statements of cash flows data:			
Net cash provided by (used in):			
Operating activities	$ 385	$ 639	$ 721
Investing activities	(1,125)	(333)	(260)
Financing activities	1,319	(628)	(344)
Consolidated balance sheet data:			
Cash and cash equivalents	$ 965	$ 642	$ 778
Total assets	15,778	13,980	12,968
Total debt (including current portion of long-term debt)	$ 8,875	$ 8,315	$ 8,055
Total stockholders equity	3,063	2,067	1,607

Other financial data:			
EBITDA(1)	$ 1,285	$ 1,377	$ 1,229
Adjusted EBITDA(1)	$ 1,596	$ 1,484	$ 1,407
Capital expenditures(2)	$ 391	$ 323	$ 312

Table of Contents

(1) EBITDA, a non-GAAP measure, is defined as net income (loss) before interest, taxes, depreciation and amortization and goodwill impairment (EBITDA). Adjusted EBITDA is defined as EBITDA further adjusted to exclude unusual items and other adjustments permitted in calculating covenant compliance under the indentures and our senior secured credit facilities. Adjusted EBITDA is a non-GAAP measure used to determine our compliance with certain covenants contained in the indentures that will govern the notes offered hereby, the indentures governing our senior unsecured notes and our unsecured senior subordinated notes and in our senior secured credit facilities. EBITDA and Adjusted EBITDA have limitations as analytical tools and you should not consider them in isolation or as a substitute for an analysis of our results under GAAP, however, we believe that including supplementary information concerning Adjusted EBITDA is appropriate to provide additional information to investors to demonstrate compliance with our financing covenants.

Adjusted EBITDA does not represent net income (loss) or cash flow from operations as those terms are defined by GAAP and does not necessarily indicate whether cash flows will be sufficient to fund cash needs. While Adjusted EBITDA and similar measures are frequently used as measures of operations and the ability to meet debt service requirements, these terms are not necessarily comparable to other similarly titled captions of other companies due to the potential inconsistencies in the method of calculation. Adjusted EBITDA does not reflect the impact of earnings or charges resulting from matters that we may consider not to be indicative of SunGard s ongoing operations. In particular, the definition of Adjusted EBITDA in the indentures allows us to add back certain noncash, extraordinary or unusual charges that are deducted in calculating net income (loss). However, these are expenses that may recur, vary greatly and are difficult to predict. Further, SunGard s debt instruments require that Adjusted EBITDA be calculated for the most recent four fiscal quarters. As a result, the measure can be disproportionately affected by a particularly strong or weak quarter. Further, it may not be comparable to the measure for any subsequent four-quarter period or any complete fiscal year.

The following is a reconciliation of net loss, which is a GAAP measure of SunGard s operating results, to Adjusted EBITDA as defined in SunGard s debt agreements. The terms and related calculations are defined in the indentures.

	Year ended December 31,		
(Dollars in millions)	**2008**	**2009**	**2010**
Net loss from continuing operations	$ (92)	$ (1,122)	$ (390)
Interest expense, net	580	630	636
Taxes (benefit from)	51	(74)	(29)
Depreciation and amortization	746	817	775
Goodwill impairment charge		1,126	237
EBITDA	1,285	1,377	1,229
Purchase accounting adjustments(a)	35	17	13
Non-cash charges(b)	35	36	38
Restructuring and other charges(c)	66	41	50
Acquired EBITDA, net of disposed EBITDA(d)	57	4	7
Pro forma expense savings related to acquisitions(e)	17	4	2
Loss on extinguishment of debt and other(f)	76	5	68
Adjusted EBITDA Senior Secured Credit Facilities	1,571	1,484	1,407
Loss on sale of receivables(g)	25		
Adjusted EBITDA Senior Notes due 2015, 2018 and 2020 and Senior Subordinated Notes due 2015	$ 1,596	$ 1,484	$ 1,407

(a) Purchase accounting adjustments include the adjustment of deferred revenue and lease reserves to fair value at the dates of the LBO and subsequent acquisitions made by the Company and certain acquisition-related compensation expense.

(b) Non-cash charges include stock-based compensation and loss on the sale of assets.

(c) Restructuring and other charges include debt refinancing costs, severance and related payroll taxes, reserves to consolidate certain facilities, settlements with former owners of acquired companies and other expenses associated with acquisitions made by the Company.

Table of Contents

(d) Acquired EBITDA net of disposed EBITDA reflects the EBITDA impact of businesses that were acquired or disposed of during the period as if the acquisition or disposition occurred at the beginning of the period.

(e) Pro forma adjustments represent the full-year impact of savings resulting from post-acquisition integration activities.

(f) Loss on extinguishment of debt and other includes the loss on extinguishment of $1.6 billion of senior notes due 2013, gains or losses related to fluctuation of foreign currency exchange rates impacting the foreign-denominated debt, management fees paid to the Sponsors and franchise and similar taxes reported in operating expenses, partially offset by certain charges relating to the off-balance sheet accounts receivable securitization facility (terminated in December 2008).

(g) The loss on sale of receivables under the off-balance sheet accounts receivable securitization facility (terminated in December 2008) is added back in calculating Adjusted EBITDA for purposes of the indentures governing the senior notes due 2015, 2018 and 2020 and the senior subordinated notes due 2015 but is not added back in calculating Adjusted EBITDA for purposes of the senior secured credit facilities.

(2) Capital expenditures represent cash paid for property and equipment as well as software and other assets.

Table of Contents

RISK FACTORS

You should carefully consider the following risk factors and all other information contained in this prospectus before deciding whether to tender your outstanding notes in the exchange offer. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties that we are unaware of, or that we currently deem immaterial, also may become important factors that affect us.

If any of the following risks occur, our business, financial condition or results of operations could be materially and adversely affected. In that case, the trading price of the exchange notes could decline or we may not be able to make payments of interest and principal on the exchange notes, and you may lose some or all of your investment.

Risks Related to the Exchange Offer

There may be adverse consequences if you do not exchange your outstanding notes.

If you do not exchange your outstanding notes for exchange notes in the exchange offer, you will continue to be subject to restrictions on transfer of your outstanding notes as set forth in the offering circular distributed in connection with the private offering of the outstanding notes. In general, the outstanding notes may not be offered or sold unless they are registered or exempt from registration under the Securities Act and applicable state securities laws. Except as required by the registration rights agreement, we do not intend to register resales of the outstanding notes under the Securities Act. You should refer to Summary The Exchange Offer and The Exchange Offer for information about how to tender your outstanding notes.

The tender of outstanding notes under the exchange offer will reduce the outstanding amount of the outstanding notes, which may have an adverse effect upon, and increase the volatility of, the market prices of the outstanding notes due to a reduction in liquidity.

Risks Related to Our Indebtedness

Our substantial leverage could adversely affect our ability to raise additional capital to fund our operations, limit our ability to react to changes in the economy or our industry, expose us to interest rate risk to the extent of our variable rate debt and prevent us from meeting our debt obligations.

As a result of being acquired on August 11, 2005 by a consortium of private equity investment funds, we are highly leveraged and our debt service requirements are significant. As of December 31, 2010, our total indebtedness was $8.06 billion, and we had $796 million available for borrowing under our revolving credit facility, after giving effect to certain outstanding letters of credit.

Our high degree of leverage could have important consequences, including:

- making it more difficult for us to make payments on our debt obligations;

- increasing our vulnerability to general economic and industry conditions;

- requiring a substantial portion of cash flow from operations to be dedicated to the payment of principal and interest on our indebtedness, therefore reducing our ability to use our cash flow to fund our operations, capital expenditures and future business opportunities;

- exposing us to the risk of increased interest rates as certain of our borrowings, including borrowings under our senior secured credit facilities, are at variable rates of interest;

- restricting us from making strategic acquisitions or causing us to make non-strategic divestitures;

limiting our ability to obtain additional financing for working capital, capital expenditures, product development, debt service requirements, acquisitions and general corporate or other purposes; and

Table of Contents

- limiting our ability to adjust to changing market conditions and placing us at a competitive disadvantage compared to our competitors who are less highly leveraged.

We and our subsidiaries may be able to incur substantial additional indebtedness in the future, subject to the restrictions contained in our senior secured credit agreement, the indentures that govern the exchange notes, our senior notes due 2015 and senior subordinated notes due 2015. If new indebtedness is added to our current debt levels, the related risks that we now face could be exacerbated. Additionally, if we were to divest any material operations in the future, our leverage could increase and our ability to service our remaining debt could be negatively impacted.

Our debt agreements contain restrictions that limit our flexibility in operating our business.

Our senior secured credit agreement and the indentures governing our senior notes due 2015, the senior subordinated notes due 2015 and the exchange notes contain various covenants that limit our ability to engage in specified types of transactions. These covenants limit our and our restricted subsidiaries ability to, among other things:

- incur additional indebtedness or issue certain preferred shares;
- pay dividends on, repurchase or make distributions in respect of our capital stock or make other restricted payments;
- make certain investments;
- sell certain assets;
- create liens;
- consolidate, merge, sell or otherwise dispose of all or substantially all of our assets; and
- enter into certain transactions with our affiliates.

In addition, under the senior secured credit agreement, we are required to satisfy and maintain specified financial ratios and other financial condition tests. Our ability to meet those financial ratios and tests can be affected by events beyond our control, and we may not be able to meet those ratios and tests. A breach of any of these covenants could result in a default under the senior secured credit agreement. Upon an event of default under the senior secured credit agreement, the lenders could elect to declare all amounts outstanding to be immediately due and payable and terminate all commitments to extend further credit.

If we were unable to repay those amounts, the lenders under the senior secured credit agreement could proceed against the collateral granted to them to secure that indebtedness. We have pledged a significant portion of our assets as collateral under the senior secured credit agreement and the senior secured notes due 2014, to the extent required by the indenture governing those notes. If the lenders under the senior secured credit agreement accelerate the repayment of borrowings, we may not have sufficient assets to repay the senior secured credit facilities and the senior secured notes due 2014, as well as our unsecured indebtedness.

Risks Related to Our Business

Our business depends largely on the economy and financial markets, and a slowdown or downturn in the economy or financial markets could adversely affect our business and results of operations.

When there is a slowdown or downturn in the economy, a drop in stock market levels or trading volumes, or an event that disrupts the financial markets, our business and financial results may suffer for a number of reasons. Customers may react to worsening conditions by reducing their capital expenditures in general or by specifically reducing their IT spending. In addition, customers may curtail or discontinue trading

Table of Contents

operations, delay or cancel IT projects, or seek to lower their costs by renegotiating vendor contracts. Also, customers with excess IT resources may choose to take their information availability solutions in-house rather than obtain those solutions from us. Moreover, competitors may respond to market conditions by lowering prices and attempting to lure away our customers to lower cost solutions. If any of these circumstances remain in effect for an extended period of time, there could be a material adverse effect on our financial results. Because our financial performance tends to lag behind fluctuations in the economy, our recovery from any particular downturn in the economy may not occur until after economic conditions have generally improved.

Our business depends to a significant degree on the financial services industry, and a weakening of, or further consolidation in, or new regulations affecting, the financial services industry could adversely affect our business and results of operations.

Because our customer base is concentrated in the financial services industry, our business is largely dependent on the health of that industry. When there is a general downturn in the financial services industry, or if our customers in that industry experience financial or business problems, our business and financial results may suffer. If financial services firms continue to consolidate, there could be a material adverse effect on our business and financial results. When a customer merges with a firm using its own solution or another vendor s solution, it could decide to consolidate on a non-SunGard system, which could have an adverse effect on our financial results.

To the extent new regulations adopted negatively impact the business, operations or financial condition of our customers, our business and financial results could be adversely affected. We could be required to invest a significant amount of time and resources to comply with additional regulations or to modify the manner in which we provide products and services to our customers; and such regulations could limit how much we can charge for our services. We may not be able to update our existing products and services, or develop new ones at all or in a timely manner, to satisfy our customers needs. Any of these events, if realized, could have a material adverse effect on our business and financial results.

Our acquisition program is an important element of our strategy but, because of the uncertainties involved, this program may not be successful and we may not be able to successfully integrate and manage acquired businesses.

Part of our growth strategy is to pursue additional acquisitions in the future. There can be no assurance that our acquisition program will continue to be successful. In addition, we may finance any future acquisition with debt, which would increase our overall levels of indebtedness and related interest costs. If we are unable to successfully integrate and manage acquired businesses, then our business and financial results may suffer. It is possible that the businesses we have acquired and businesses that we acquire in the future may perform worse than expected, be subject to an adverse litigation outcome or prove to be more difficult to integrate and manage than expected. If that happens, there may be a material adverse effect on our business and financial results for a number of reasons, including:

- we may have to devote unanticipated financial and management resources to acquired businesses;
- we may not be able to realize expected operating efficiencies or product integration benefits from our acquisitions;
- we may have to write off goodwill or other intangible assets; and
- we may incur unforeseen obligations or liabilities (including assumed liabilities not fully indemnified by the seller) in connection with acquisitions.

Table of Contents

If we are unable to identify suitable acquisition candidates and successfully complete acquisitions, our growth may be adversely affected.

Our growth has depended in part on our ability to acquire similar or complementary businesses on favorable terms. This growth strategy is subject to a number of risks that could adversely affect our business and financial results, including:

- we may not be able to find suitable businesses to acquire at affordable valuations or on other acceptable terms;
- we may face competition for acquisitions from other potential acquirers, some of whom may have greater resources than us or may be less highly leveraged, or from the possibility of an acquisition target pursuing an initial public offering of its stock;
- we may have to incur additional debt to finance future acquisitions as we have done in the past and no assurance can be given as to whether, and on what terms, such additional debt will be available; and
- we may find it more difficult or costly to complete acquisitions due to changes in accounting, tax, securities or other regulations.

Catastrophic events may disrupt or otherwise adversely affect the markets in which we operate, our business and our profitability.

Our business may be adversely affected by a war, terrorist attack, natural disaster or other catastrophe. A catastrophic event could have a direct negative impact on us or an indirect impact on us by, for example, affecting our customers, the financial markets or the overall economy. The potential for a direct impact is due primarily to our significant investment in our infrastructure. Although we maintain redundant facilities and have contingency plans in place to protect against both man-made and natural threats, it is impossible to fully anticipate and protect against all potential catastrophes. Despite our preparations, a security breach, criminal act, military action, power or communication failure, flood, severe storm or the like could lead to service interruptions and data losses for customers, disruptions to our operations, or damage to our important facilities. The same disasters or circumstances that may lead to our customers requiring access to our availability services may negatively impact our own ability to provide such services. Our three largest availability services facilities are particularly important, and a major disruption at one or more of those facilities could disrupt or otherwise impair our ability to provide services to our availability services customers. If any of these events happen, we may be exposed to unexpected liability, our customers may leave, our reputation may be tarnished, and there could be a material adverse effect on our business and financial results.

Our application service provider systems may be subject to disruptions that could adversely affect our reputation and our business.

Our application service provider systems maintain and process confidential data on behalf of our customers, some of which is critical to their business operations. For example, our global trading and position, risk and operations systems maintain account and trading information for our customers and their clients, and our wealth management and insurance systems maintain investor account information for retirement plans, insurance policies and mutual funds. There is no guarantee that the systems and procedures that we maintain to protect against unauthorized access to such information are adequate to protect against all security breaches. If our application service provider systems are disrupted or fail for any reason, or if our systems or facilities are infiltrated or damaged by unauthorized persons, our customers could experience data loss, financial loss, harm to reputation and significant business interruption. If that happens, we may be exposed to unexpected liability, our customers may leave, our reputation may be tarnished, and there could be a material adverse effect on our business and financial results.

Table of Contents

Because the sales cycle for our software is typically lengthy and unpredictable, our results may fluctuate from period to period.

Our operating results may fluctuate from period to period and be difficult to predict in a particular period due to the timing and magnitude of software sales. We offer a number of our software solutions on a license basis, which means that the customer has the right to run the software on its own computers. The customer usually makes a significant up-front payment to license software, which we generally recognize as revenue when the license contract is signed and the software is delivered. The size of the up-front payment often depends on a number of factors that are different for each customer, such as the number of customer locations, users or accounts. As a result, the sales cycle for a software license may be lengthy and take unexpected turns. Thus, it is difficult to predict when software sales will occur or how much revenue they will generate. Since there are few incremental costs associated with software sales, our operating results may fluctuate from quarter to quarter and year to year due to the timing and magnitude of software sales.

Rapid changes in technology and our customers businesses could adversely affect our business and financial results.

Our business may suffer if we do not successfully adapt our products and services to changes in technology and changes in our customers businesses. These changes can occur rapidly and at unpredictable intervals and we may not be able to respond adequately. If we do not successfully update and integrate our products and services to adapt to these changes, or if we do not successfully develop new products and services needed by our customers to keep pace with these changes, then our business and financial results may suffer. Our ability to keep up with technology and business changes is subject to a number of risks and we may find it difficult or costly to, among other things:

- update our products and services and to develop new products fast enough to meet our customers needs;
- make some features of our products and services work effectively and securely over the Internet;
- integrate more of our FS solutions;
- update our products and services to keep pace with business, regulatory and other developments in the financial services industry, where many of our customers operate; and
- update our services to keep pace with advancements in hardware, software and telecommunications technology.

Some technological changes, such as advancements that have facilitated the ability of our AS customers to develop their own internal solutions, may render some of our products and services less valuable or eventually obsolete. In addition, because of ongoing, rapid technological changes, the useful lives of some technology assets have become shorter and customers are therefore replacing these assets more often. As a result, our customers are increasingly expressing a preference for contracts with shorter terms, which could make our revenue less predictable in the future.

Customers taking their information availability solutions in-house may continue to create pressure on our organic revenue growth rate.

Our AS solutions allow customers to leverage our significant infrastructure and take advantage of our experience, technology expertise, resource management capabilities and vendor neutrality. Technological advances in recent years have significantly reduced the cost and the complexity of developing in-house solutions. Some customers, especially among the very largest having significant IT resources, prefer to develop and maintain their own in-house availability solutions, which can result in a loss of revenue from those customers. If this trend continues or worsens, there will be continued pressure on our organic revenue growth rate.

Table of Contents

The trend toward information availability solutions utilizing more single customer dedicated resources likely will lower our overall operating margin rate over time.

In the information availability services industry, especially among our more sophisticated customers, there is an increasing preference for solutions that utilize some level of dedicated resources, such as blended advanced recovery services and managed services. The primary reason for this trend is that adding dedicated resources, although more costly, provides greater control, reduces data loss and facilitates quicker responses to business interruptions. Advanced recovery services often result in greater use of dedicated resources with a modest decrease in operating margin rate. Managed services require significant dedicated resources and, therefore, have an appropriately lower operating margin rate.

Our brokerage operations are highly regulated and are riskier than our other businesses.

Organizations like the Securities and Exchange Commission, Financial Services Authority and Financial Industry Regulatory Authority can, among other things, fine, censure, issue cease-and-desist orders and suspend or expel a broker/dealer or any of its officers or employees for failures to comply with the many laws and regulations that govern brokerage operations. Our ability to comply with these laws and regulations is largely dependent on our establishment, maintenance and enforcement of an effective brokerage compliance program. Our failure to establish, maintain and enforce proper brokerage compliance procedures, even if unintentional, could subject us to significant losses, lead to disciplinary or other actions, and tarnish our reputation. Regulations affecting the brokerage industry, in particular with respect to active traders, may change, which could adversely affect our financial results.

We are exposed to certain risks relating to the execution and clearance services provided by our brokerage operations to retail customers, institutional clients (including hedge funds and other broker/dealers), and proprietary traders. These risks include, but are not limited to, customers failing to pay for securities commitments in the marketplace, trading errors, the inability or failure to settle trades, and trade execution or clearance systems failures. In our other businesses, we generally can disclaim liability for trading losses that may be caused by our software, but in our brokerage operations, we cannot limit our liability for trading losses even when we are not at fault. As a result we may suffer losses that are disproportionate to the relatively modest profit contributions of this business.

We could lose revenue due to fiscal funding or termination for convenience clauses in certain customer contracts, especially in our HE and PS businesses.

Certain of our customer contracts, particularly those with governments, institutions of higher education and school districts, may be partly or completely terminated by the customer due to budget cuts or sometimes for any reason at all. These types of clauses are often called fiscal funding or termination for convenience clauses. If a customer exercises one of these clauses, the customer would be obligated to pay for the services we performed up to the date of exercise, but would not have to pay for any further services. In addition, governments, institutions of higher education and school districts may require contract terms that differ from our standard terms. While we have not been materially affected by exercises of these clauses or other unusual terms in the past, we may be in the future. If customers that collectively represent a substantial portion of our revenue were to invoke the fiscal funding or termination for convenience clauses of their contracts, our future business and results of operations could be adversely affected.

If we fail to comply with government regulations in connection with our business or providing technology services to certain financial institutions, our business and results of operations may be adversely affected.

Because we act as a third-party service provider to financial institutions and provide mission-critical applications for many financial institutions that are regulated by one or more member agencies of the Federal Financial Institutions Examination Council (FFIEC), we are subject to examination by the member agencies of the FFIEC. More specifically, we are a Multi-Regional Data Processing Servicer of the FFIEC because we

Table of Contents

provide mission critical applications for financial institutions from several data centers located in different geographic regions. As a result, the FFIEC conducts periodic reviews of certain of our operations in order to identify existing or potential risks associated with our operations that could adversely affect the financial institutions to whom we provide services, evaluate our risk management systems and controls, and determine our compliance with applicable laws that affect the services we provide to financial institutions. In addition to examining areas such as our management of technology, data integrity, information confidentiality and service availability, the reviews also assess our financial stability. Our incurrence of significant debt in connection with the LBO increases the risk of an FFIEC agency review determining that our financial stability has been weakened. A sufficiently unfavorable review from the FFIEC could result in our financial institution customers not being allowed to use our technology services, which could have a material adverse effect on our business and financial condition.

If we fail to comply with any regulations applicable to our business, we may be exposed to unexpected liability and/or governmental proceedings, our customers may leave, our reputation may be tarnished, and there could be a material adverse effect on our business and financial results. In addition, the future enactment of more restrictive laws or rules on the federal or state level, or, with respect to our international operations, in foreign jurisdictions on the national, provincial, state or other level, could have an adverse impact on business and financial results.

If we are unable to retain or attract customers, our business and financial results will be adversely affected.

If we are unable to keep existing customers satisfied, sell additional products and services to existing customers or attract new customers, then our business and financial results may suffer. A variety of factors could affect our ability to successfully retain and attract customers, including the level of demand for our products and services, the level of customer spending for information technology, the level of competition from customers that develop their own solutions internally and from other vendors, the quality of our customer service, our ability to update our products and develop new products and services needed by customers, and our ability to integrate and manage acquired businesses. Further, the markets in which we operate are highly competitive and we may not be able to compete effectively. Our services revenue, which has been largely recurring in nature, comes from the sale of our products and services under fixed-term contracts. We do not have a unilateral right to extend these contracts when they expire. Revenue from our broker/dealer businesses is not subject to minimum or ongoing contractual commitments on the part of brokerage customers. If customers cancel or refuse to renew their contracts, or if customers reduce the usage levels or asset values under their contracts, there could be a material adverse effect on our business and financial results.

If we fail to retain key employees, our business may be harmed.

Our success depends on the skill, experience and dedication of our employees. If we are unable to retain and attract sufficiently experienced and capable personnel, especially in product development, sales and management, our business and financial results may suffer. For example, if we are unable to retain and attract a sufficient number of skilled technical personnel, our ability to develop high quality products and provide high quality customer service may be impaired. Experienced and capable personnel in the technology industry remain in high demand, and there is continual competition for their talents. When talented employees leave, we may have difficulty replacing them, and our business may suffer. There can be no assurance that we will be able to successfully retain and attract the personnel that we need.

We are subject to the risks of doing business internationally.

A portion of our revenue is generated outside the United States, primarily from customers located in Europe. Over the past few years we have expanded our operations in India and acquired businesses in China and Singapore in an effort to increase our presence throughout Asia Pacific. Because we sell our services outside the

Table of Contents

United States, our business is subject to risks associated with doing business internationally. Accordingly, our business and financial results could be adversely affected due to a variety of factors, including:

- changes in a specific country s or region s political and cultural climate or economic condition;
- unexpected or unfavorable changes in foreign laws and regulatory requirements;
- difficulty of effective enforcement of contractual provisions in local jurisdictions;
- inadequate intellectual property protection in foreign countries;
- trade-protection measures, import or export licensing requirements such as Export Administration Regulations promulgated by the U.S. Department of Commerce and fines, penalties or suspension or revocation of export privileges;
- the effects of applicable foreign tax law and potentially adverse tax law changes;
- significant adverse changes in foreign currency exchange rates;
- longer accounts receivable cycles;
- managing a geographically dispersed workforce; and
- difficulties associated with repatriating cash in a tax-efficient manner.

In foreign countries, particularly in those with developing economies, certain business practices may exist that are prohibited by laws and regulations applicable to us, such as the U.S. Foreign Corrupt Practices Act. Although our policies and procedures require compliance with these laws and are designed to facilitate compliance with these laws, our employees, contractors and agents may take actions in violation of applicable laws or our policies. Any such violation, even if prohibited by our policies, could have a material adverse effect on our business and reputation.

The private equity firms that acquired the Company control us and may have conflicts of interest with us.

Investment funds associated with or designated by the Sponsors indirectly own, through their ownership in the Parent Companies, a substantial portion of our capital stock. As a result, the Sponsors have control over our decisions to enter into any corporate transaction regardless of whether noteholders believe that any such transaction is in their own best interests. For example, the Sponsors could cause us to make acquisitions or pay dividends that increase the amount of indebtedness that is secured or that is senior to our senior subordinated notes or to sell assets.

Additionally, the Sponsors are in the business of making investments in companies and may from time to time acquire and hold interests in businesses that compete directly or indirectly with us. One or more of the Sponsors may also pursue acquisition opportunities that may be complementary to our business and, as a result, those acquisition opportunities may not be available to us. So long as investment funds associated with or designated by the Sponsors continue to indirectly own a significant amount of the outstanding shares of our common stock, even if such amount is less than 50%, the Sponsors will continue to be able to strongly influence or effectively control our decisions.

If we are unable to protect our proprietary technologies and defend infringement claims, we could lose one of our competitive advantages and our business could be adversely affected.

Our success depends in part on our ability to protect our proprietary products and services and to defend against infringement claims. If we are unable to do so, our business and financial results may suffer. To protect our proprietary technology, we rely upon a combination of copyright, patent, trademark and trade secret law, confidentiality restrictions in contracts with employees, customers and others, software security measures, and

Table of Contents

registered copyrights and patents. Despite our efforts to protect the proprietary technology, unauthorized persons may be able to copy, reverse engineer or otherwise use some of our technology. It also is possible that others will develop and market similar or better technology to compete with us. Furthermore, existing patent, copyright and trade secret laws may afford only limited protection, and the laws of certain countries do not protect proprietary technology as well as United States law. For these reasons, we may have difficulty protecting our proprietary technology against unauthorized copying or use. If any of these events happens, there could be a material adverse effect on the value of our proprietary technology and on our business and financial results. In addition, litigation may be necessary to protect our proprietary technology. This type of litigation is often costly and time-consuming, with no assurance of success.

We may be sued for violating the intellectual property rights of others.

The software industry is characterized by the existence of a large number of trade secrets, copyrights and the rapid issuance of patents, as well as frequent litigation based on allegations of infringement or other violations of intellectual property rights. We may unknowingly violate the intellectual property rights of others. Some of our competitors or other third parties may have been more aggressive than us in applying for or obtaining patent protection for innovative proprietary technologies both in the United States and internationally. In addition, we use a limited amount of open source software in our products and may use more open source software in the future. Because open source software is developed by numerous independent parties over whom we exercise no supervision or control, allegations of infringement for using open source software are possible. Although we monitor our use and our suppliers use of open source software to avoid subjecting our products to conditions we do not intend, the terms of many open source licenses have not been interpreted by United States or other courts, and there is a risk that these licenses could be construed in a manner that could impose unanticipated conditions or restrictions on our ability to commercialize our products.

As a result of all of these factors, there can be no assurance that in the future third parties will not assert infringement claims against us and preclude us from using a technology in our products or require us to enter into royalty and licensing arrangements on terms that are not favorable to us, or force us to engage in costly infringement litigation, which could result in us paying monetary damages or being forced to redesign our products to avoid infringement. Additionally, our licenses and service agreements with our customers generally provide that we will defend and indemnify them for claims against them relating to our alleged infringement of the intellectual property rights of third parties with respect to our products or services. We might have to defend or indemnify our customers to the extent they are subject to these types of claims. Any of these claims may be difficult and costly to defend and may lead to unfavorable judgments or settlements, which could have a material adverse effect on our reputation, business and financial results. For these reasons, we may find it difficult or costly to add or retain important features in our products and services.

At present, we are vigorously defending a number of patent infringement cases. While we do not believe we have a potential liability for damages or royalties from any known current legal proceedings or claims related to the infringement of patent or other intellectual property rights that would individually or in the aggregate materially adversely affect our financial condition and operating results, the results of such legal proceedings cannot be predicted with certainty. Should we fail to prevail in any of the matters related to infringement of patent or other intellectual property rights of others or should several of these matters be resolved against us in the same reporting period, it could have a material adverse effect on our business and financial results.

Defects, design errors or security flaws in our products could harm our reputation and expose us to potential liability.

Most of our products are very complex software systems that are regularly updated. No matter how careful the design and development, complex software often contains errors and defects when first introduced and when major new updates or enhancements are released. If errors or defects are discovered in our current or

Table of Contents

future products, we may no Nevada market and an unusual level of lot closings in fiscal 2001. The increase in average sales price is due to the closing of a higher number of units in the higher-priced California market in fiscal 2002. The decrease in the Company s backlog from 512 units at February 28, 2001 to 194 units at February 28, 2002 is also primarily due to a decrease in selling projects in certain of the Company s markets and to a lesser extent, the reduction in backlog units in Nevada in connection with the Company s exit from that market. The number of actively selling projects (not including the Managed Projects) has decreased from 26 at February 28, 2001 to 22 at February 28, 2002, which affected both backlog and net new orders. The

Table of Contents

Company anticipates opening between 18 and 24 new communities over the next fiscal year in the following markets:

Market	Approximate Number of New Projects	Approximate Number of Lots
California	6-8	589-648
Texas	4-6	273-759
Arizona	5-6	511-699
Colorado	3-4	608-758
Total	18-24	1,981-2,864

Certain of these projects contain lots which may ultimately be sold to other builders. The Company expects a net increase in selling projects of between 11 and 18 projects during fiscal 2003, due to the close out of between 6 and 7 currently selling projects.

The Company s gross margin decreased from 25.1% in fiscal 2001 to 24.2% in fiscal 2002, due to a change in the mix of closings to certain higher volume, lower-margin projects and the close out of certain less profitable projects. The gross margin, including unconsolidated joint ventures, decreased from 25.0% in fiscal 2001 to 23.8% in fiscal 2002.

Selling, general and administrative expense of $36.3 million for fiscal 2002 decreased $2.3 million or 6.0% as compared to fiscal 2001 due primarily to a lower level of sales activity. As a percentage of revenue, selling, general and administrative expense increased from 10.6% in fiscal 2001 to 12.2% in fiscal 2002. The increased percentage was primarily due to lower volume of revenue in fiscal 2002.

Income from unconsolidated joint ventures increased from a loss of $874,000 in fiscal 2001 to income of $746,000 in fiscal 2002, due to the establishment of certain reserves in connection with the wind down in fiscal 2001 of some of the older joint ventures, and the benefit of certain newer joint ventures generating profits in fiscal 2002.

Interest and other income decreased from $1.9 million in fiscal 2001 to $1.4 million in fiscal 2002 and consists primarily of the results of operations of the Company s mortgage broker operations, as well as certain financing and other transactions.

Minority interest of $5.6 million in fiscal 2001 and $159,000 in fiscal 2002 primarily represents the share of income from CPH LLC and CPH Newport Coast, LLC attributable to CHF, until the Company acquired the remaining minority interest in CPH LLC on May 31, 2001.

Interest incurred was $14.8 million in fiscal 2002, as compared to $25.7 million in fiscal 2001, while interest expensed was $28.9 million in fiscal 2002 as compared to $35.7 million in fiscal 2001. Due both to selling out of older projects with higher capitalized interest and the Company s substantially reduced borrowing costs, the Company expects interest incurred and interest expensed to continue to drop in future periods. Substantially all interest costs are initially capitalized to real estate projects and are recognized as interest expense as homes and land are sold.

The Company recorded a provision for income taxes of $2.8 million in fiscal 2002, as compared to $1.8 million in fiscal 2001. The effective tax rate was reduced from the statutory rate in fiscal 2002 due to the impact of amortizing negative goodwill, and in fiscal 2001 primarily through the reversal of the Company s previously established valuation allowance. The valuation allowance was reduced to zero at February 28, 2001, and the Company expects its effective tax rate to approximate 40 percent in future years.

Fiscal 2001 (Year Ended February 28, 2001) Compared to Fiscal 2000 (Year Ended February 29, 2000)

The Company reported income from operations of $18.1 million in fiscal 2001, as compared to income from operations of $9.8 million in fiscal 2000. The Company reported net income of $12.2 million, or $0.88 per share, in fiscal 2001, as compared to net income of $6.2 million, or $0.44 per share, in fiscal 2000. Net income

Table of Contents

for fiscal 2001 included an extraordinary gain of $1.5 million, or $0.11 per share, as compared to $1.0 million, or $0.07 per share, in fiscal 2000, as a result of the retirement of debt at less than face value.

On a consolidated basis, sales of homes and land increased from $290.8 million in fiscal 2000 to $363.7 million in fiscal 2001. Home and lot closings increased from 1,978 in fiscal 2000 to 2,153 in fiscal 2001. Sales of homes and land including unconsolidated joint ventures were $426.4 million for fiscal 2001 compared to $319.1 million for fiscal 2000. The increase was due to an increase in total unit closings from 2,006 for fiscal 2000 to 2,199 in fiscal 2001 and an increase in average sales price. Home closings declined slightly from 1,296 in fiscal 2000 to 1,209 in fiscal 2001, including 28 and 46 homes, respectively, closed in unconsolidated joint ventures. The average home sales price increased from $233,000 in fiscal 2000 to $315,000 in fiscal 2001.

The increase in total unit closings was due primarily to increased activity in the Company s Colorado market and to a few significant lot sales. The increase in average sales price was due to the closing of a higher number of units in the higher-priced California market in fiscal 2001. The Company s actual gross margin increased from 20.5% in fiscal 2000 to 25.1% in fiscal 2001, due to a change in the mix of closings to certain higher-margin projects. The gross margin including unconsolidated joint ventures increased from 20.2% in fiscal 2000 to 25.0% in fiscal 2001.

As a percentage of revenue, selling, general and administrative expense remained stable at 10.6% in both fiscal 2000 and fiscal 2001. Selling, general and administrative expense of $38.6 million for fiscal 2001 increased $7.8 million or 25.3% as compared to fiscal 2000 due to a higher level of sales activity.

Income from unconsolidated joint ventures decreased from $1.7 million fiscal 2000 to a loss of $874,000 in fiscal 2001, due to the establishment of certain reserves in connection with the wind down of some of the older joint ventures, as well as the fact that the profits from the newer joint ventures were being allocated primarily to cover preferred return on partner s capital during fiscal 2001.

Interest and other income increased from $1.5 million in fiscal 2000 to $1.9 million in fiscal 2001 and consists primarily of the results of operations of the Company s mortgage broker operations, as well as certain financing and other transactions.

Minority interest of $2.8 million in fiscal 2000 and $5.6 million in fiscal 2001 primarily represents the share of income from CPH LLC and CPH Newport Coast, LLC attributable to CHF.

Interest incurred was $25.7 million in fiscal 2001, as compared to $24.5 million in fiscal 2000, while interest expensed was $35.7 million in fiscal 2001 as compared to $22.1 million in fiscal 2000. Substantially all interest costs are initially capitalized to real estate projects and are recognized as interest expense as homes and land are sold. As presented in the consolidated statements of operations, income from unconsolidated joint ventures for fiscal 2000 excludes the recognition of approximately $519,000 in interest previously capitalized to the lots contributed to MPE. Such interest costs are included in interest expense.

The Company recorded a provision for income taxes of $1.8 million in fiscal 2001, as compared to $1.7 million in fiscal 2000. The effective tax rate in both years was reduced from the statutory rate by the use of available loss carryforwards. Such loss carryforwards have now been substantially fully utilized.

Liquidity and Capital Resources

The Company s principal cash requirements are for the acquisition, development, construction, marketing and overhead of its projects. When building inventory, the Company uses substantial amounts of cash that are generally obtained from borrowings, available cash flow from operations and partners contributions to joint ventures.

At the current time, all material financing transactions and arrangements are incurred either by CPH LLC or by certain project-specific entities. During the third quarter of fiscal 2002, CPH LLC entered into a senior unsecured revolving credit facility (the Senior Facility) with several participant banks. The facility has a maximum commitment of $125 million and a two year revolving term. Proceeds from this facility were used to pay down CPH LLC s existing facilities and retire the remaining Senior Notes during the quarter

ending November 30, 2001, as discussed below. The new credit facility has substantially more favorable pricing than the Senior Notes which have been retired.

As of February 28, 2002, the Company has in place several credit facilities, including the Senior Facility, totaling $181 million (the Facilities) with various bank lenders (the Banks), of which approximately $109 million was outstanding. The Facilities other than the Senior Facility are secured by liens on various completed or under construction homes and lots held by CPH LLC, CPH Newport Coast, LLC and CPH Yucaipa I, LLC, all of which are wholly-owned subsidiaries. Pursuant to the Facilities, the Company and the wholly-owned subsidiaries are subject to certain covenants, which require, among other things, the maintenance of a consolidated liabilities to net worth ratio, minimum liquidity, minimum net worth and loss limitations, all as defined in the documents that evidence the Facilities. At February 28, 2002, the Company and the wholly-owned subsidiaries were in compliance with these covenants. The Facilities also define certain events that constitute events of default. As of February 28, 2002, no such event had occurred. Commitment fees are payable annually on some of the Facilities.

Homebuilding activity is being financed out of CPH LLC cash, bank financing, and the existing joint ventures, including joint ventures with institutional investors. In addition, development work undertaken in certain of the Company s joint ventures is financed through various non-recourse lending arrangements. The Company anticipates that it will continue to utilize both third party financing and joint ventures to cover financing needs in excess of internally generated cash flow.

Management expects that cash flow generated from operations and from bank financing will be sufficient to cover the debt service and to fund CPH LLC s current development and homebuilding activities for the reasonably foreseeable future, and expects that capital commitments from its joint venture partners and other bank facilities will provide sufficient financing for the operation of its joint ventures.

Interest Rates and Inflation

The long-term impact of inflation on the Company is manifested in increased land prices, land development, construction and overhead costs balanced by increased sales prices. The Company generally contracts for land significantly before development and sales efforts begin and, accordingly, to the extent land acquisition costs are fixed, increases or decreases in the sales prices of homes, land and other real estate properties may affect the Company s profits. Since the sales prices of homes are fixed at the time of sale and the Company generally sells its homes prior to commencement of construction, any inflation of construction costs in excess of those anticipated may result in lower gross margins. The Company generally attempts to minimize that effect by entering into fixed-price contracts with its subcontractors and material suppliers for specified periods of time, which generally do not exceed one year.

Housing demand, in general, is adversely affected by increases in interest costs, as well as materials and other costs. Interest rates, the length of time that land remains in inventory and the proportion of inventory that is financed affect the Company s interest costs. If the Company is unable to duplicate its past ability to raise sales prices enough to compensate for higher costs, or if mortgage interest rates increase significantly, affecting prospective buyers ability to adequately finance a home purchase, the Company s homebuilding revenues, gross margins and net income would be adversely affected. Increases in sales prices, whether the result of inflation or demand, may affect the ability of prospective buyers to afford a new home.

Critical Accounting Policies

The Company s financial statements have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and costs and expenses during the reporting period. Management evaluates its estimates and judgments, including those which impact its most critical accounting policies on an ongoing basis. Management bases its estimates and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances, within the framework of current accounting literature. Actual results may differ from these estimates under different assumptions or

Table of Contents

conditions. Management believes that the following accounting policies are among the most important to accurately report the Company s financial condition and results of operations and require among the most subjective or complicated judgments, which are subject to uncertainty and the potential for change in subsequent accounting periods:

Revenue Recognition, Real Estate Projects and Cost of Sales

A sale is recorded and profit is recognized when a sale is consummated, the buyer s initial and continuing investments are adequate, any receivables are not subject to future subordination, and the usual risks and rewards of ownership have been transferred to the buyer in accordance with the provisions of Statement of Financial Accounting Standards (SFAS) No. 66, Accounting for Sales of Real Estate. When it is determined that the earnings process is not complete, profit is deferred for recognition in future periods. Examples of such circumstances would be if the Company sells and leases back a model home, or if the Company takes a buyer s home in trade. The profit recorded by the Company is based on the calculation of cost of sales which is dependent on the Company s allocation of costs, including a provision for estimated future warranty costs, as discussed below.

Real estate projects are carried at cost, net of impairment losses, if any. Real estate projects consist primarily of raw land, lots under development, houses under construction and completed houses. All direct and indirect land costs, offsite and onsite improvements and applicable interest and other carrying charges are capitalized to real estate projects during periods when the project is under development. Land, offsite costs and all other common costs, including projected indirect construction costs and carrying costs, are typically allocated to lots benefited within a project based upon relative sales values before construction. Onsite direct construction costs are allocated to the individual homes based upon the relative sales value of the homes. The estimation process involved in determining relative sales values is inherently uncertain because it involves estimates of current market values for land parcels before construction as well as future sales values of individual homes. The Company s estimates of future sales values are supported by the Company s budgeting process. Any estimate of future sales values is inherently uncertain because it requires estimates of current market conditions as well as future market events and conditions. The impact of applying the relative sales value method can be significant in the case where certain lots in a project are expected to command high premiums for views, lot size or other desirable attributes, in comparison with other lots within the same project. Additionally, in determining the allocation of costs to a particular land parcel or individual home, the Company relies on project budgets that are based on a variety of assumptions, including assumptions about construction schedules and future costs to be incurred. It is possible that actual results could differ from budgeted amounts for various reasons, including construction delays, increases in costs which have not yet been committed, or unforeseen issues encountered during construction that fall outside the scope of contracts obtained. While the actual results for a particular construction project are accurately reported over time, a variance between the budget and actual costs could result in the understatement or overstatement of costs and a related impact on gross margins in a specific reporting period. To reduce the potential for such distortion, the Company has set forth procedures which have been applied by the Company on a consistent basis, including assessing and revising project budgets on a monthly basis, obtaining, where possible, commitments from subcontractors and vendors for future costs to be incurred, reviewing the adequacy of warranty accruals and historical warranty claims experience, and utilizing the most recent information available to estimate costs. Management believes that the Company s policies provide for reasonably dependable estimates to be used in the calculation and reporting of costs. The Company relieves its accumulated real estate projects through cost of sales and interest expense for the cost of homes sold.

Impairment of Real Estate Projects

SFAS No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of, requires impairment losses to be recorded on assets to be held and used by the Company when indicators of impairments are present and the undiscounted cash flows estimated to be generated by those assets are less than the carrying amount of assets. The estimation process used in determining the undiscounted cash flows of the assets is inherently uncertain because it involves estimates of future revenues

Table of Contents

and costs. As described more fully above, estimates of revenues and costs are supported by the Company s budgeting process. When an impairment loss is required for assets to be held and used by the Company, the related assets are adjusted to their estimated fair value. Management reviews all real estate projects for impairment on an ongoing basis.

Fair value represents the amount at which an asset could be bought or sold in a current transaction between willing parties, that is, other than a forced or liquidation sale. The estimation process involved in determining if assets have been impaired and in the determination of fair value is inherently uncertain because it requires estimates of current market yields as well as future events and conditions. Such future events and conditions include economic and market conditions, as well as the availability of suitable financing to fund development and construction activities. The realization of the Company s real estate projects is dependent upon future uncertain events and conditions and, accordingly, the actual timing and amounts realized by the Company may be materially different from their estimated fair values.

Joint Ventures

The Company has historically entered into joint ventures with financial partners in which the joint venture partner typically provides the majority of the capital and/or financing required for the project. The Company has utilized joint ventures in order to increase the ability of the Company to control real property and to diversify the Company s sources of financing. The Company expects to continue to utilize joint ventures in the future on a selective basis, taking into account other available sources of financing, project risk and the potential return to the Company.

At the current time, the Company s typical investment in most of its joint ventures consists of a percentage of the total capital required (typically ten percent or less) and after substantial completion of the project and after payment of all project expenses, return of invested capital together with a preferred return the Company participates in the profits of the project. The Company typically does not provide any financial or other credit enhancements in connection with these joint venture investments but sometimes provides operational agreements that it will complete construction. The Company accounts for these joint ventures on the equity method when the Company s ownership is less than 50 percent, and on a consolidated basis when the Company s ownership exceeds 50 percent.

Management Fees

In connection with the joint ventures discussed above, the Company typically charges a management fee to the joint venture, representing reimbursement for overhead expenditures made by the Company on behalf of the joint venture project. These fees are typically based on a percentage of revenue within the joint venture and are collected over the life of the project. This reimbursement is included in the Company s income statement as an offset to selling, general and administrative expense and is disclosed in Note 11 of the Notes to Consolidated Financial Statements. For unconsolidated joint ventures and Managed Projects, such amounts are recognized currently, and for consolidated joint ventures and subsidiaries, a portion of the fee related to homes which have not closed is deferred.

Related Party Transactions

The Company has in place formal systems to identify, track and report related party transactions. The Company feels that all significant related party transactions have been properly accounted for and adequately disclosed. See Item 13 and Note 11 of the Notes to Consolidated Financial Statements for a description of the Company s transactions with related parties.

New Accounting Pronouncements

In June 2001, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 141, Business Combinations (SFAS 141). This Statement addresses financial accounting and reporting for business combinations and supersedes APB Opinion No. 16, Business Combinations, and FASB Statement No. 38, Accounting for Preacquisition Contingencies of Purchased

Table of Contents

Enterprises. All business combinations in the scope of this Statement are to be accounted for using one method, the purchase method. The Company will adopt SFAS 141 for any business combinations initiated after June 30, 2001. Also in June 2001, the FASB issued Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets (SFAS 142). SFAS 142 addresses financial accounting and reporting for acquired goodwill and other intangible assets and supersedes APB Opinion No. 17, Intangible Assets. This pronouncement addresses, among other things, how goodwill and other intangible assets should be accounted for after they have been initially recognized in the financial statements. Goodwill will no longer be amortized but will be assessed at least annually for impairment using a fair value methodology. The Company will adopt this statement for all goodwill and other intangible assets acquired after June 30, 2001 and for all existing goodwill and other intangible assets beginning March 1, 2002. Upon adoption of this standard on March 1, 2002, the Company is required to accrete the remaining balance of negative goodwill through a cumulative effect of change in accounting principle, which will increase net income in fiscal 2003 by approximately $5.4 million, or approximately $0.37 per diluted share. Other than the accretion of the remaining negative goodwill, the Company does not anticipate that the adoption of SFAS 142 will have a significant effect on the Company s financial position or results of operations.

In August 2001, the FASB issued Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets (SFAS 144). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. SFAS 144 supersedes SFAS No. 121, which is discussed above, and the accounting and reporting provisions of APB Opinion No. 30, Reporting the Results of Operations Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions, for the disposal of a segment of a business (as previously defined in that Opinion). The provisions of SFAS 144 are effective for financial statements issued for fiscal years beginning after December 15, 2001, with early application encouraged and generally are to be applied prospectively. The Company does not expect the adoption of SFAS 144 to have a material impact on the Company s financial position or results of operations.

Item 7A. ***Quantitative and Qualitative Disclosures about Market Risk***

The Company is exposed to market risks related to fluctuations in interest rates on its debt. Under the new credit facility, the Company utilized interest rate swaps in order to fix the interest rate on $75 million of its variable rate debt. The Company has not used forward or option contracts on foreign currencies or commodities, or other types of derivative financial instruments. The purpose of the following analysis is to provide a framework to understand the Company s sensitivity to hypothetical changes in interest rates as of February 28, 2002. Many of the statements contained in this section are forward looking and should be read in conjunction with the Company s disclosures under the heading Forward-Looking Statements.

The Company uses debt financing primarily for the purpose of acquiring and developing land and constructing and selling homes. Historically, the Company has made short-term borrowings under its revolving credit facilities to fund these expenditures. In addition, the Company has previously issued $100 million in fixed rate debt to provide longer-term financing. During fiscal 2002, the Company repurchased the remaining balance of Senior Notes.

For fixed rate debt, changes in interest rates generally affect the fair market value of the debt instrument, but not the Company s earnings or cash flows. Conversely, for variable rate debt, changes in interest rates generally do not impact fair market value of the debt instrument, but do affect the Company s future earnings and cash flows. The Company does not have an obligation to prepay fixed rate debt prior to maturity, and as a result, interest rate risk and changes in fair market value should not have a significant impact on such debt until the Company would be required to refinance such debt. Based on the amount of variable rate debt outstanding at February 28, 2002, and holding the variable rate debt balance constant, each one-percentage point increase in interest rates would result in an increase in interest incurred for the coming year of approximately $300,000, including the impact of the interest rate swaps and discussed above.

The table below details the principal amount and the average interest rates for debt for each category based upon the expected maturity dates. The carrying value of the Company s variable rate debt approximates

Table of Contents

fair value due to the frequency of repricing of this debt. The Company s fixed rate debt consists of various purchase money trust deed notes and other notes.

	Expected Maturity Date			
	Year Ending February 28,			
	2003	2004	Total	Fair Value
	(Dollars in thousands)			
Liabilities:				
Fixed rate debt	$ 7,596	$	$ 7,596	$ 7,677
Average interest rate	13.34%		13.34%	
Variable rate debt	$12,218	$96,451	$108,669	$108,669
Average interest rate	5.26%	4.21%	4.33%	

The Company does not believe that the future market rate risks related to the above securities will have a material adverse impact on the Company s financial position, results of operations or liquidity.

Table of Contents

Item 8. ***Financial Statements and Supplementary Data***

	Page
Capital Pacific Holdings, Inc.	
Report of Independent Auditors	25
Report of Independent Public Accountants	26
Consolidated Balance Sheets as of February 28, 2001 and 2002	27
Consolidated Statements of Income for the years ended February 29, 2000 and February 28, 2001 and 2002	28
Consolidated Statements of Stockholders Equity for the years ended February 29, 2000 and February 28, 2001 and 2002	29
Consolidated Statements of Cash Flows for the years ended February 29, 2000 and February 28, 2001 and 2002	30
Notes to Consolidated Financial Statements	32
Grand Coto Estates, L.P.	
Report of Independent Auditors	48
Balance Sheets as of December 31, 2000 (unaudited) and 2001 (unaudited)	49
Statements of Operations for the years ended December 31, 1999, 2000 (unaudited) and 2001 (unaudited)	50
Statements of Partners Capital (Deficit) for the years ended December 31, 1999, 2000 (unaudited) and 2001 (unaudited)	51
Statements of Cash Flows for the years ended December 31, 1999, 2000 (unaudited) and 2001 (unaudited)	52
Notes to Financial Statements	53
M.P.E. Partners, L.P.	
Report of Independent Auditors	55
Balance Sheets as of December 31, 2000 (unaudited) and 2001 (unaudited)	56
Statements of Operations for the years ended December 31, 1999, 2000 (unaudited) and 2001 (unaudited)	57
Statements of Partners Capital (Deficit) for the years ended December 31, 1999, 2000 (unaudited) and 2001 (unaudited)	58
Statements of Cash Flows for the years ended December 31, 1999, 2000 (unaudited) and 2001 (unaudited)	59
Notes to Financial Statements	60

Table of Contents

REPORT OF INDEPENDENT AUDITORS

To the Board of Directors and Stockholders

of Capital Pacific Holdings, Inc.:

We have audited the accompanying consolidated balance sheet of Capital Pacific Holdings, Inc. and subsidiaries as of February 28, 2002, and the related consolidated statements of income, stockholders equity and cash flows for the year ended February 28, 2002. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, based on our audits, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Capital Pacific Holdings, Inc. and subsidiaries as of February 28, 2002, and the consolidated results of their operations and their cash flows for the year ended February 28, 2002, in conformity with accounting principles generally accepted in the United States.

Irvine, California
May 15, 2002

Table of Contents

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Board of Directors and Stockholders

of Capital Pacific Holdings, Inc.:

We have audited the accompanying consolidated balance sheet of Capital Pacific Holdings, Inc. (a Delaware corporation) and subsidiaries as of February 28, 2001, and the related consolidated statements of income, stockholders equity and cash flows for the two years in the period ended February 28, 2001. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of certain Joint Ventures for the year ended February 29, 2000 (Notes 1 and 4), the investments in which are reflected in the accompanying financial statements using the equity method of accounting. The equity in the net income of these Joint Ventures was $1,197,000 for the year ended February 29, 2000. Those financial statements were audited by other auditors whose report has been furnished to us and our opinion, insofar as it relates to the amounts included for those entities, is based on the report of the other auditors.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of Capital Pacific Holdings, Inc. and subsidiaries as of February 28, 2001, and the results of their operations and their cash flows for the two years in the period ended February 28, 2001, in conformity with accounting principles generally accepted in the United States.

Orange County, California

May 16, 2001

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In thousands, except share data)

	February 28, 2001	February 28, 2002
ASSETS		
Cash and cash equivalents	$ 7,552	$ 5,080
Restricted cash	781	365
Accounts and notes receivable	25,082	14,537
Real estate projects	259,873	203,685
Property and equipment		971
Investment in and advances to unconsolidated joint ventures	5,273	8,549
Prepaid expenses and other assets	10,851	17,008
Total assets	$ 309,412	$ 250,195
LIABILITIES AND STOCKHOLDERS EQUITY		
Accounts payable and accrued liabilities	$ 46,684	$ 35,369
Notes payable	110,223	116,265
Senior unsecured notes payable	55,592	
Total liabilities	212,499	151,634
Negative goodwill	6,390	5,447
Minority interest	7,743	
Stockholders equity:		
Common stock, par value $0.10 per share; 60,000,000 shares authorized; 16,230,000 shares issued; 13,767,311 and 14,878,711 shares outstanding, respectively	1,500	1,623
Additional paid-in capital	211,888	216,853
Accumulated deficit	(127,054)	(120,762)
Treasury stock	(3,554)	(4,080)
Accumulated other comprehensive income (loss)		(520)
Total stockholders equity	82,780	93,114
Total liabilities and stockholders equity	$ 309,412	$ 250,195

See accompanying notes to financial statements.

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(In thousands, except per share data)

	For the Years Ended		
	February 29, 2000	February 28, 2001	February 28, 2002
Sales of homes and land	$290,791	$363,743	$298,701
Cost of sales	231,273	272,332	226,373
Gross margin	59,518	91,411	72,328
Income (loss) from unconsolidated joint ventures	1,730	(874)	746
Selling, general and administrative expenses	(30,813)	(38,615)	(36,301)
Interest expense	(22,141)	(35,707)	(28,932)
Interest and other income, net	1,513	1,927	1,367
Income from operations	9,807	18,142	9,208
Minority interest	(2,835)	(5,628)	(159)
Income before provision for income taxes and extraordinary item	6,972	12,514	9,049
Provision for income taxes	1,745	1,786	2,757
Income before extraordinary item	5,227	10,728	6,292
Extraordinary item gain on debt retired at less than face value, net of minority interest and taxes	955	1,461	
Net income	$ 6,182	$ 12,189	$ 6,292
Earnings per common share basic and diluted:			
Income before extraordinary item	$ 0.37	$ 0.77	$ 0.43
Extraordinary item	0.07	0.11	
Net income	$ 0.44	$ 0.88	$ 0.43
Weighted average common shares basic	13,923	13,773	14,620
Weighted average common shares diluted	14,014	13,896	14,795

See accompanying notes to financial statements.

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

For the Three Years Ended February 28, 2002
(In thousands, except shares)

	Common Stock		Additional Paid-In	Accumulated	Treasury	Accumulated Other Comprehensive	
	Shares	Amount	Capital	Deficit	Stock	Income (Loss)	Total
Balance, February 28, 1999	14,027,911	$1,500	$211,888	$(145,425)	$(2,609)	$	$65,354
Repurchase of common stock	(212,000)				(650)		(650)
Net income				6,182			6,182
Balance, February 29, 2000	13,815,911	1,500	211,888	(139,243)	(3,259)		70,886
Repurchase of common stock and warrants	(48,600)				(295)		(295)
Net income				12,189			12,189
Balance, February 28, 2001	13,767,311	1,500	211,888	(127,054)	(3,554)		82,780
Issuance of non-voting common stock	1,235,000	123	4,965				5,088
Repurchase of common stock and warrants	(123,600)				(526)		(526)
Net income				6,292			6,292
Other comprehensive income (loss):							
Interest rate swap						(520)	(520)
Balance, February 28, 2002	14,878,711	$1,623	$216,853	$(120,762)	$(4,080)	$(520)	$93,114

See accompanying notes to financial statements.

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	For the Years Ended		
	February 29, 2000	**February 28, 2001**	**February 28, 2002**
Operating Activities:			
Net income	$ 6,182	$ 12,189	$ 6,292
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Gain on retirement of senior unsecured notes payable	(955)	(1,461)	
Gain on sale of building		(1,040)	
Depreciation and amortization	1,897	1,458	138
Accretion of deferred gain			(707)
Accretion of negative goodwill			(1,336)
Changes in operating assets and liabilities:			
(Increase) decrease in accounts and notes receivable	(10,329)	(2,301)	10,545
(Increase) decrease in real estate projects	(21,164)	18,695	56,188
(Increase) decrease in prepaid expenses and other assets	2,020	(2,689)	(5,741)
Increase (decrease) in accounts payable and accrued liabilities	1,394	(1,517)	(13,189)
(Income) loss from unconsolidated joint ventures, including interest expense	(1,211)	874	(746)
Minority interest	3,424	5,628	159
Net cash provided by (used in) operating activities	(18,742)	29,836	51,603
Investing Activities:			
Proceeds from sale of building		3,500	
Purchases of property and equipment	(1,039)	(1,410)	(1,469)
Cash distributed with Divested Joint Ventures		(3,983)	
Decrease (increase) in investments in and advances to unconsolidated joint ventures	9,133	5,162	(2,530)
Net cash provided by (used in) investing activities	8,094	3,269	(3,999)
Financing Activities:			
Proceeds from notes payable	306,169	417,072	495,507
Principal payments of notes payable	(271,849)	(431,409)	(489,465)
Capital contributions (distributions) to minority interest, net	106	(660)	
Retirement of senior unsecured notes payable	(9,521)	(29,650)	(55,592)
Repurchase of common stock and warrants	(650)	(295)	(526)
Net cash provided by (used in) financing activities	24,255	(44,942)	(50,076)
Net increase (decrease) in cash and cash equivalents	13,607	(11,837)	(2,472)
Cash and cash equivalents, beginning of year	5,782	19,389	7,552
Cash and cash equivalents, end of year	$ 19,389	$ 7,552	$ 5,080
Supplemental Disclosure of Cash and Non-Cash Activities:			

Cash paid during the year for interest, all capitalized to real estate projects	$ 25,450	$ 27,614	$ 14,798
Cash paid during the year for income taxes	$	$ 1,771	$ 6,491

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)

Non-Cash Activities:

During fiscal 2001, the Company consummated an Exchange Transaction with CHF (see Note 1) which was an entirely non-cash transaction, other than the distribution to the Company of cash balances held by the Divested Joint Ventures. The transaction resulted in the elimination of a substantial portion of the Company s minority interest and certain other accounts as summarized below:

Assets and liabilities held by Divested Joint Ventures exchanged by the Company:

Cash	$ (3,983)
Accounts receivable	(81)
Real estate projects	(3,929)
Property and equipment	(3,038)
Prepaid expenses and other assets	(213)
Accounts payable and accrued liabilities	103
Notes payable	1,249
	$ (9,892)
Summary of amounts recorded as a result of the Exchange Transaction:	
Minority interest acquired	$31,685
Assets exchanged:	
Divested Joint Ventures	(9,892)
Investment in unconsolidated joint ventures	(4,070)
	17,723
Deferred income taxes and accrued expenses recorded	(4,805)
Adjustment of remaining property and equipment to zero	(2,994)
Deferred gain recorded	(3,534)
Negative goodwill recorded	(6,390)
	$

During fiscal 2002, the Company issued 1,235,000 shares of non-voting common stock to CHF in return for CHF s remaining 7% interest in CPH LLC in connection with the Exchange Transaction described in Note 1 to the financial statements. As a result CPH, Inc. owned 100% of CPH LLC. Below is a summary of amounts recorded as a result of this transaction:

Minority interest acquired	$ 7,902
Issuance of non-voting common stock	(5,088)
Deferred income taxes and accrued expenses recorded	(2,061)
Adjustment of remaining property and equipment to zero	(360)
Negative goodwill recorded	(393)
	$

See accompanying notes to financial statements.

31

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Company Organization, Operations and Summary of Significant Accounting Policies

Company Organization and Operations

Capital Pacific Holdings, Inc. (CPH, Inc.), together with its subsidiaries, (the Company) conducts business principally under the names Capital Pacific Homes and, in Texas, Clark Wilson Homes.

In fiscal year 1998, CPH, Inc. consummated an equity and restructuring transaction whereby CPH, Inc. and certain of its subsidiaries transferred to a newly formed entity, Capital Pacific Holdings, LLC (CPH LLC), substantially all of their respective assets and CPH LLC assumed all the liabilities of CPH, Inc. and its subsidiaries. An unaffiliated investment company, California Housing Finance, L.P. (CHF) then acquired a 32.07% minority interest in CPH LLC as a result of a cash investment of $30 million in CPH LLC. From fiscal 1998 through fiscal 2001, CPH, Inc. expanded its operating strategy to encompass the acquisition and development of commercial and mixed-use projects, as well as ownership of existing commercial properties, primarily through 0.7% capital investments in limited liability companies, with approximately 99% of the capital for these projects being provided by CHF. CPH, Inc. and CHF had contingent profits interests (after repayment of debt, the costs of the project, invested capital and preferred return, typically 12%) of approximately 30% to CPH, Inc. and 70% to CHF.

Effective February 23, 2001, CPH, Inc. and CHF consummated an interest exchange transaction (the Exchange Transaction), whereby CPH, Inc. exchanged its 0.7% capital interests and contingent profit interest in the majority of the joint ventures capitalized by CHF, including certain entities which were previously consolidated, (the Divested Joint Ventures) for approximately 78% of CHF s interest in CPH LLC and all of CHF s interests in certain residential joint ventures. At February 28, 2001 and during the three month period ended May 31, 2001, CPH, Inc. had a 93% interest in CPH LLC (as compared to 67.03% formerly), which had at February 28, 2001 total capital of $109.5 million, and CHF held a 7% minority interest (as compared to 32.07% formerly). As a result of the first portion of the Exchange Transaction, CPH Inc. s interest in total capital of CPH LLC increased by 37% equal to $27.7 million. CPH, Inc. and CHF both had an option to convert CHF s remaining 7% interest in CPH LLC into 1,235,000 shares of non-voting Common Stock of CPH, Inc. at the equivalent of approximately $6.40 per share. This option was exercised by CPH, Inc. on May 31, 2001, thus, as of this date, CPH, Inc. owned 100% of CPH LLC, and obtained an additional increment of CPH LLC s total capital of $7.9 million. In addition, Capital Pacific Homes, Inc., a wholly-owned subsidiary of CPH, Inc., has entered into construction, management and marketing agreements relating to certain of the Divested Joint Ventures with residential components, (the Managed Projects), whereby CPH, Inc. is compensated for performing such services through a management fee arrangement including reimbursement of all project costs. As a result of the Exchange Transaction, CPH, Inc. has no further exposure to the economic or entitlement risks associated with the Divested Joint Ventures and the Managed Projects, including no obligation to provide any capital.

The Exchange Transaction was accounted for as the simultaneous acquisition of CHF s minority interest in CPH LLC and certain other residential joint ventures and the disposition of the Company s interest in the Divested Joint Ventures. All of the investments received were investments in real estate housing developments. A substantial portion of the investments conveyed represented investments in similar real estate. For these exchanges of real estate assets for real estate assets, the Company recorded such amounts based upon their historical cost in accordance with EITF 98-8 and APB 29. The remaining investments conveyed were investments in various types of real estate developments, which were intended to be held for operation, and thus required fair value accounting. Only one of these entities (CPH Newport Office Building, LLC) had a fair value that was measurably different from its historical cost that resulted in a gain, which has been deferred, as discussed below.

The Company performed a preliminary allocation of the fair value of CPH LLC as of the consummation date in accordance with APB 16. As such, the acquired assets and assumed liabilities were allocated a portion

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

of the purchase price (which was determined to be the historical cost of the assets conveyed by the Company) equal to their estimated fair values, which approximated historical cost. As a result, no gain was initially recognized, the remaining balance of the Company s property and equipment was adjusted to zero at February 28, 2001, and again at May 31, 2001, and the balance of the transaction was recorded initially as negative goodwill. During fiscal 2002, the Company finalized its purchase price allocation with respect to the Exchange Transaction, whereby approximately $3.5 million of the amount previously assigned to negative goodwill was assigned to a gain on the disposition of one of the Divested Joint Ventures. Due to continuing involvement in the form of both consulting and lease arrangements between the Company and this Divested Joint Venture, this gain is being deferred and amortized over its expected life of five years. The Company s consolidated balance sheet at February 28, 2001 reflects a reclassification of this deferred gain which is included in accounts payable and accrued liabilities. Negative goodwill in the amount of $6.8 million represents a portion of the positive difference between the Company s basis in the assets acquired in the Exchange Transaction as compared to the assets which were divested. Both negative goodwill and the deferred gain are being accreted over five years, which accretion is included as a reduction in selling, general and administrative expenses. As further discussed below, due to a recently promulgated change in accounting principles, the remaining $5.4 million in unaccreted negative goodwill as of February 28, 2002 will increase net income in the first quarter of fiscal 2003 through a cumulative effect of change in accounting principle. The remaining $2.8 million of the deferred gain will continue to be accreted over the four years of its remaining expected life. The positive difference in book value immediately prior to the transaction between the ownership interests received by CPH, Inc. and the interests given by CPH, Inc. totaled $20.5 million.

Assets under management, including assets owned by unconsolidated joint ventures and Managed Projects, totaled $475 million at February 28, 2002 in 50 residential projects. At February 28, 2002, CPH LLC, which is now 100% owned by the Company, had $212 million in assets and a net worth of $109.5 million. The Company and its subsidiaries perform their respective management functions for CPH LLC and the Managed Projects pursuant to management agreements, which include provisions for the reimbursement of Company and subsidiary costs and a management fee. CPH LLC, the Managed Projects and certain other project-specific entities indemnify CPH, Inc. and its subsidiaries against liabilities arising from the projects owned by such entities. The Company maintains certain licenses and other assets as is necessary to fulfill its obligations as managing member and under management agreements.

References to the Company are, unless the context indicates otherwise, also references to CPH LLC and the joint venture entities and its other subsidiaries. At the current time, all material financing transactions and arrangements are incurred either by CPH LLC or by the project-specific entities.

The Company is a regional builder and developer with operations throughout selected metropolitan areas of California, Texas, Arizona and Colorado and, until recently, Nevada. The Company s principal business activities are to build and sell single-family homes. The Company s single-family homes are targeted to entry-level, move-up and luxury buyers.

Approximately 43, 27, 11, 13 and 6 percent of the Company s total revenues derived from the sale of homes and lots were in California, Texas, Arizona, Colorado and Nevada, respectively, for the year ended February 28, 2002.

The Company s business, and the markets which it serves in California, Texas, Arizona and Colorado are affected by local, national and world economic conditions and events, in particular by the level of mortgage interest rates, consumer confidence and real estate prices. The Company cannot predict whether mortgage interest rates will be at levels attractive to prospective homebuyers. If interest rates increase, in particular mortgage interest rates, the Company s operating results could be adversely impacted.

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Accounting Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingencies at the dates of the financial statements and the reported amounts of revenues and expenses during the reported periods. Significant estimates include projected revenues and costs of projects, which impact the allocation of costs to homes sold. Actual results could differ from estimated amounts.

Principles of Consolidation and Minority Interest in Joint Ventures

The consolidated financial statements include the accounts of the Company and wholly-owned subsidiaries and certain majority-owned joint ventures, as well as the accounts of CPH LLC, including the capital accounts of CPH LLC, which as of May 31, 2001 is 100% owned by the Company, totaling $109.5 million at February 28, 2002. All other investments (See Note 4) are accounted for under the equity method. All significant intercompany balances and transactions have been eliminated in consolidation.

Property and Equipment

Property and equipment are recorded at cost and are depreciated over their estimated useful lives of three to thirty years using the straight-line method. During fiscal 2001, a building with a book value of $2,460,000 was sold, resulting in a gain of $1,040,000. In addition, a building with a book value of $3,038,000 was exchanged as part of the Exchange Transaction. As a result of the Exchange Transaction, the remaining balance of $2,994,000 in property and equipment was adjusted to zero at February 28, 2001 and again at May 31, 2001 in the amount $360,000.

Real Estate Projects

All direct and indirect land costs, offsite and onsite improvements and applicable interest and carrying charges are capitalized to real estate projects under development. Capitalized costs are expensed as real estate is sold; direct marketing costs are expensed in the period incurred. Land and land development costs are accumulated by project and are allocated to individual phases using the relative sales value method.

The Company follows Statement of Financial Accounting Standards (SFAS) No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of. SFAS No. 121 requires long-lived assets that are expected to be held and used in operations are to be carried at the lower of cost or, if impaired, the fair value of the asset, rather than the net realizable value. Long-lived assets to be disposed of should be reported at the lower of carrying amount or fair value less cost to sell. For purposes of applying SFAS No. 121, real estate under development is considered to be held for use whereas finished units are considered assets to be disposed of. In evaluating long-lived assets held for use, a review for impairment loss is triggered if the sum of the expected future cash flows (undiscounted and without interest charges) is less than the carrying amount of the asset. Various assumptions and estimates are used to determine fair value in determining the amount of any impairment loss including, among others, estimated costs of construction, development and direct marketing, sales absorption rates, anticipated sales prices and carrying costs. The estimates used to determine any impairment adjustment can change materially in the near term as the economy in the Company s key areas changes.

Negative Goodwill

Negative goodwill recorded as a result of the Exchange Transaction was being accreted over five years. During fiscal 2002, the Company recorded accretion of $1.3 million which was included as a reduction in selling, general and administrative expenses. Due to a recently promulgated change in accounting principles,

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

the remaining balance of negative goodwill of $5.4 million at February 28, 2002 will increase income in the first quarter of fiscal 2003 through a cumulative effect of change in accounting principle.

Revenue Recognition

The Company s revenue recognition policy for the sales of homes and land follows the provisions of SFAS No. 66, Accounting for Sales of Real Estate, which specify minimum down payment requirements, financing terms and certain other requirements for sales of real estate.

Income from sales of homes and land is recognized when title has passed, the buyer has met minimum down payment requirements and the terms of any notes received by the Company satisfy continuing investment requirements. At the time of sale, accumulated costs are relieved from real estate projects and charged to cost of sales and interest expense on a relative sales value basis.

The Company recognizes fees paid to its wholly-owned mortgage brokerage operation from third-party lenders concurrent with the closing on the sale of the residential unit. Such fees are classified in Interest and other income, net in the Company s consolidated statements of income.

Warranty Costs

Estimated future warranty costs are accrued and charged to cost of sales for each home concurrent with the recognition of revenue upon satisfaction of the requirements of SFAS No. 66.

Income Taxes

The Company accounts for income taxes in accordance with SFAS No. 109, Accounting for Income Taxes, which requires the liability method of accounting for income taxes.

Statements of Cash Flows

For purposes of the consolidated statements of cash flows, short-term investments which have a maturity of 90 days or less from the date of purchase are considered cash equivalents.

Stock Options

The Company accounts for equity-based compensation under SFAS No. 123, Accounting for Stock-Based Compensation. Under SFAS No. 123, companies have the option to implement a fair value-based accounting method or continue to account for employee stock options and stock purchase plans using the intrinsic value based method of accounting as prescribed by Accounting Principles Board (APB) Opinion No. 25 Accounting for Stock Issued to Employees. Entities electing to remain under APB Opinion No. 25 must make pro forma disclosures of net income or loss and earnings per share as if the fair value based method of accounting defined in SFAS No. 123 had been applied. The Company has adopted the disclosure requirements of SFAS No. 123 and will continue accounting for stock options under APB Opinion No. 25.

Earnings Per Common Share

The Company follows the provisions of SFAS No. 128, Earnings Per Share. This statement requires the presentation of both basic and diluted earnings per common share for financial statement purposes. Basic earnings per common share is computed by dividing income available to common stockholders by the weighted average number of common shares outstanding. Diluted earnings per common share includes the effect of the potential shares outstanding, including dilutive securities using the treasury stock method. The

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

table below reconciles the components of the basic earnings per common share calculation to diluted earnings per common share (in thousands, except per share data):

	Year Ended February 29, 2000			Year Ended February 28, 2001			Year Ended February 28, 2002		
	Income	Shares	EPS	Income	Shares	EPS	Income	Shares	EPS
Basic Earnings Per Share:									
Income available to common stockholders before extraordinary item	$5,227	13,923	$0.37	$10,728	13,773	$0.77	$6,292	14,620	$0.43
Effect of Dilutive Securities:									
Warrants								51	
Stock options		91			123			124	
Diluted Earnings Per Share before extraordinary item	$5,227	14,014	$0.37	$10,728	13,896	$0.77	$6,292	14,795	$0.43

Comprehensive Income

The Company follows the provisions of SFAS No. 130, Reporting Comprehensive Income. SFAS No. 130 requires that the Company (a) classify items of other comprehensive income by their nature in a financial statement and (b) display the accumulated balance of other comprehensive income separately from retained earnings and additional paid-in capital in the equity section of the balance sheet (See Note 10).

Segment Reporting

Effective February 28, 1999, the Company adopted SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information. Under the provisions of SFAS No. 131, the Company s operations are conducted primarily under one segment, homebuilding, at this time.

New Accounting Pronouncements

In June 2001, the Financial Accounting Standards Board (FASB) issued SFAS No. 141, Business Combinations . This Statement addresses financial accounting and reporting for business combinations and supersedes APB Opinion No. 16, Business Combinations, and SFAS No. 38, Accounting for Preacquisition Contingencies of Purchased Enterprises. All business combinations in the scope of this Statement are to be accounted for using one method, the purchase method. The Company will adopt SFAS 141 for any business combinations initiated after June 30, 2001.

Also in June 2001, the FASB issued SFAS No. 142, Goodwill and Other Intangible Assets . SFAS 142 addresses financial accounting and reporting for acquired goodwill and other intangible assets and supersedes APB Opinion No. 17, Intangible Assets. This pronouncement addresses, among other things, how goodwill and other intangible assets should be accounted for after they have been initially recognized in the financial statements. Goodwill will no longer be amortized but will be assessed at least annually for impairment using a fair value methodology. The Company will adopt this statement for all goodwill and other intangible assets acquired after June 30, 2001 and for all existing goodwill and other intangible assets beginning March 1, 2002. Upon adoption of this standard on March 1, 2002 the Company is required to accrete the remaining balance of negative goodwill through a cumulative effect of change in accounting principle, which will increase net income in fiscal 2003 by approximately $5.4 million, or approximately $0.37 per diluted share. Other than the accretion of the remaining negative goodwill, the Company does not anticipate that the adoption of SFAS 142 will have a significant effect on the Company s financial position or results of operations.

36

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In August 2001, the FASB issued SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets . SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. SFAS 144 supersedes SFAS 121 and the accounting and reporting provisions of APB Opinion No. 30, Reporting the Results of Operations Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions, for the disposal of a segment of a business (as previously defined in that Opinion). The provisions of SFAS 144 are effective for financial statements issued for fiscal years beginning after December 15, 2001, with early application encouraged and generally are to be applied prospectively. The Company does not expect the adoption of SFAS 144 to have a material impact on the Company s financial position or results of operations.

Reclassifications

Certain reclassifications have been made to certain prior year amounts in order to conform with the current year presentation.

2. Restricted Cash

The Company has restricted cash totaling $781,000 and $365,000 as of February 28, 2001 and 2002, respectively. Restricted cash primarily consists of deposits to various municipalities, banks, and utilities to guarantee future performance of development obligations.

3. Real Estate Projects

Real estate projects consist of the following at February 28, 2001 and 2002 (in thousands):

	2001	2002
Land and improvements under construction	$229,207	$157,471
Completed residential homes	12,678	24,967
Completed model homes	17,988	21,247
	$259,873	$203,685

Total interest costs incurred during the years ended February 29, 2000, February 28, 2001 and February 28, 2002 were $24,465,000, $25,696,000 and $14,798,000 respectively, all of which was initially capitalized to real estate projects.

37

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

4. Investments in and Advances to Unconsolidated Joint Ventures

The Company is a general partner or a direct or indirect managing member and has a 50 percent or less ownership in 13 unconsolidated joint ventures at February 28, 2002. The Company s net investment in and advances to unconsolidated joint ventures are as follows at February 28, 2001 and 2002 (in thousands):

	Capital Interest	February 28, 2001	February 28, 2002
Unconsolidated Joint Ventures:			
JMP Canyon Estates, L.P.	10%	$ 162	$ 112
JMP Harbor View, L.P.	10%	609	318
Grand Coto Estates, L.P.	10%	231	546
M.P.E. Partners, L.P.	10%	983	989
LB/L CPH Providence, LLC	10%	715	1,065
LB/L CPH Longmont, LLC	10%	1,087	1,004
LB/L CPH Laguna Street, LLC	10%		946
CPH Daily Ranch, L.P.	10%		3,103
CPH Banning-Lewis Ranch, LLC			200
Other	Various		266
		3,787	8,549
Divested Joint Ventures		1,486	
		$5,273	$8,549

The Company s ownership interests in the unconsolidated joint ventures vary. Generally, the Company receives a portion of earnings although a preferred return on invested capital is provided. Typically, the majority of capital is provided by capital partners. The Company is typically a general partner or managing member in each of the above entities and is the managing entity pursuant to terms in each venture s agreement. In the case of Divested Joint Ventures which are now Managed Projects, the Company or its subsidiary manages the development of the project under a management contract which typically provides for the payment of a fee to compensate the Company for overhead expenditures as well as reimbursement of all direct project costs. The Company s carrying amount in each of the unconsolidated joint ventures (and the Divested Joint Ventures prior to the Exchange Transaction) equals the underlying equity in the joint venture, and there are generally no significant amounts of undistributed earnings. The Company provides for income taxes currently on its share of distributed and undistributed earnings and losses from the investments.

The Company uses the equity method of accounting for its investments in the unconsolidated 50 or less percent-owned joint ventures. The accounting policies of the entities are substantially the same as those of the Company.

Following is summarized, combined financial information for the unconsolidated joint ventures at February 28, 2001 and 2002 (in thousands). The balance sheet information at both dates does not include the Divested Joint Ventures, but the income statement information for the years ended February 29, 2000 and

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

February 28, 2001 does reflect the results of the Divested Joint Ventures because the Company held an ownership interest in those entities for all of fiscal 2000 and substantially all of fiscal 2001:

	2001	2002
Assets		
Cash	$ 512	$ 1,163
Real estate projects	14,620	94,818
Other assets	611	1,275
	$15,743	$97,256

	2001	2002
Liabilities and Equity		
Accounts payable and other liabilities	$ 1,962	$ 2,752
Due to the Company	2,205	3,066
Notes payable	1,878	5,539
	6,045	11,357
Equity		
The Company	1,278	5,260
Others	8,420	80,639
	9,698	85,899
	$15,743	$97,256

	2000	2001	2002
Income Statement			
Sales of homes and land	$28,274	$62,704	$14,989
Interest and other income, net	16,296	16,214	2,146
	44,570	78,918	17,135
Costs and expenses	33,428	63,505	14,201
Net income	$11,142	$15,413	$ 2,934

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

5. Notes Payable

Notes payable at February 28, 2001 and 2002, are summarized as follows (in thousands):

	2001	2002
Senior unsecured revolving credit facility, bearing interest varying from LIBOR to prime, as selected by the Company, plus applicable margins	$	$ 90,658
Notes payable to banks, including interest varying from prime plus one quarter percent to LIBOR plus four and one quarter percent, maturing between July 31, 2002 and November 30, 2003, secured by certain real estate projects on a non-recourse basis	88,272	18,011
Notes payable to banks, including interest at prime, secured by certain real estate projects on a recourse basis, refinanced during the quarter via the revolving credit facility	16,158	
Other	5,793	7,596
	$110,223	$116,265

During the third quarter of fiscal 2002, CPH LLC entered into a senior unsecured revolving credit facility with several participant banks. The facility has a maximum commitment of $125 million and a two year revolving term. At the option of the Company, borrowings under the agreement bear interest at LIBOR plus applicable margin (4.10 percent at February 28, 2002) or at prime plus applicable margin (5.00 percent at February 28, 2002). Proceeds from this facility were used to pay down certain of CPH LLC s existing facilities and retire the remaining $55.6 million of Senior Notes at face value. In addition, the Company fixed the interest rate on $50 million and $25 million of borrowings at 5.68% and 5.62%, respectively, until September 2003 through interest rate swap agreements with a bank.

At the current time, all material financing transactions and arrangements are incurred either by CPH LLC or by certain project-specific entities. As of February 28, 2002, CPH LLC has in place several credit facilities with contingent availabilities totaling $181 million (the Facilities) with various bank lenders (the Banks), of which $109 million was outstanding. The Facilities are secured by liens on various completed or under construction homes and lots held by CPH LLC and CPH Newport Coast, LLC and CPH Yucaipa I, LLC, which are wholly-owned subsidiaries. Pursuant to the Facilities, CPH LLC and the wholly-owned subsidiaries are subject to certain covenants, which require, among other things, the maintenance of a consolidated liabilities to net worth ratio, minimum liquidity, minimum net worth and loss limitations, all as defined in the documents that evidence the Facilities. At February 28, 2002, CPH LLC and the wholly-owned subsidiaries were in compliance with these covenants. The Facilities also define certain events that constitute events of default. As of February 28, 2002, no such event had occurred. Commitment fees are payable annually on some of the Facilities.

Homebuilding activity is being financed out of CPH LLC cash, bank financing, and the existing joint ventures, including joint ventures with institutional investors, including CHF. In addition, activity undertaken in certain of the Company s joint ventures is financed through various non-recourse lending arrangements. The Company anticipates that it will continue to utilize both third party financing and joint ventures to cover financing needs in excess of internally generated cash flow.

During the years ended February 29, 2000, February 28, 2001 and February 28, 2002, the highest month-end balance on notes payable was $126 million, $205 million and $168 million, respectively, and the weighted average outstanding balance was $111 million, $124 million and $124 million, respectively. The weighted average interest rates on notes payable during the years ended February 29, 2000, February 28, 2001 and February 28, 2002, were 9.0 percent, 10.0 percent and 6.2 percent, respectively. The weighted average interest

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

rates on notes payable at February 29, 2000, February 28, 2001 and February 28, 2002, were 9.7 percent, 8.4 percent and 5.1 percent, respectively.

The aggregate scheduled principal maturities of notes payable are as follows (in thousands):

Fiscal Years Ending:	As of February 28, 2002
2003	$ 19,814
2004	96,451
Total	$116,265

6. Senior Unsecured Notes Payable; Warrants

In May, 1994, the Company issued $100 million principal amount of its 12 3/4 percent Senior Notes due May 1, 2002 (the Notes). In connection with the issuance of the Notes, the Company issued 790,000 warrants to purchase the Company s common stock at a price of $3.30 per share, all of which are fully exercisable until May 1, 2002. Interest is due and payable on May 1 and November 1 of each year. The obligations associated with the Notes were transferred to CPH LLC. Effective May 1, 2001, the Notes became redeemable at the option of CPH LLC at par, plus accrued interest.

During fiscal 2000 and 2001, the Company repurchased $11.6 and $32.8 million of the Notes (face value), respectively, resulting in an extraordinary gain of $955,000 and $1,461,000, respectively. During the third quarter of fiscal 2002, the Company redeemed at face value the remaining $55.6 million of Senior Notes utilizing the proceeds of CPH LLC s senior unsecured revolving credit facility obtained after the closing of the Exchange Transaction.

At February 28, 2001, unamortized bond issuance cost was $650,000, net of accumulated amortization of $5.2 million, which was being amortized over the term of the Notes utilizing the effective interest rate method. The balance of the unamortized bond issuance cost was fully amortized during fiscal 2002.

7. Income Taxes

The provision for income taxes consists of the following for the years ended February 29, 2000, February 28, 2001 and February 28, 2002 (in thousands):

	2000	2001	2002
Current			
Federal	$ 745	$ 2,996	$ 6,237
State	700	865	1,317
	1,445	3,861	7,554
Deferred	300	(2,075)	(4,797)
Provision for income taxes	$1,745	$ 1,786	$ 2,757

41

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The deferred income tax provision (benefit) at February 29, 2000, February 28, 2001 and February 28, 2002 results from the following temporary differences between financial and tax reporting (in thousands):

	2000	2001	2002
Accrued expenses	$ 22	$ (921)	$ (2,362)
Construction period expenses	197	569	(548)
Depreciation	(40)	(78)	(126)
Built-in losses	722	1,159	46
Net operating loss carryforward	(823)	1,950	
Real estate projects			(2,399)
Property and equipment			498
Other		135	94
Increase (decrease) in valuation allowance	222	(4,889)	
	$ 300	$ (2,075)	$ (4,797)

The components of the Company s deferred income tax asset as of February 28, 2001 and February 28, 2002 are as follows:

	2001	2002
Accrued expenses	$ 975	$ 3,337
Construction period expenses	1,878	2,426
Depreciation	14	140
Built-in losses	2,367	2,321
Real estate projects	(5,701)	(5,308)
Property and equipment	1,197	843
Other	(41)	(93)
	$ 689	$ 3,666

A reconciliation of the income tax provision computed at the federal statutory rate and the income tax provision for financial reporting purposes for the years ended February 29, 2000, February 28, 2001 and February 28, 2002, are as follows:

	2000	2001	2002
Income taxes at statutory rate	34%	34%	35%
State income taxes, net of federal tax benefit	3	6	3
Franchise tax liability	2	3	2
Income tax accrued on Exchange Transaction		10	
Reversal of valuation allowance		(39)	
Accretion of negative goodwill			(8)
Utilization of loss carryforwards	(14)		
Other			(2)
	25%	14%	30%

42

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

8. Stockholders Equity

In fiscal 1998, the Company announced a stock repurchase program whereby up to 1,000,000 shares of the Company s outstanding common stock may be repurchased by CPH, Inc. or CPH LLC. As of February 28, 2002, 661,800 shares had been repurchased and held under this program. In addition, as of February 28, 2002, the Company has repurchased 373,511 of the warrants originally issued in connection with the issuance of the Senior Notes.

In connection with the Exchange Transaction, the Company issued 1,235,000 shares of non-voting Common Stock to CHF. These shares are identical in all respects to the voting Common Stock of the Company with the exception of voting privileges.

9. Stock Option Plan

Effective February 28, 1995, the Board of Directors of the Company approved the 1995 Stock Incentive Plan (the 1995 Plan). The 1995 Plan permits a committee designated by the Board of Directors to make awards to key employees and directors of the Company and its subsidiaries. Subject to various restrictions, awards could be in the form of stock options, restricted or unrestricted stock, stock appreciation rights or a combination of the above. The maximum number of shares or share equivalents that may be awarded under the 1995 Plan is 1,500,000.

Options are granted to purchase shares at prices equal to the fair market value of the shares at the date of grant. The options vest over a one to five year period and are exercisable at various dates over one to 10 year periods. When the options are exercised, the proceeds will be credited to equity along with the related income tax benefits, if any.

The following is a summary of the transactions relating to the Company s stock option plan for the years ended February 29, 2000, February 28, 2001 and February 28, 2002:

	Fiscal 2000		Fiscal 2001		Fiscal 2002	
	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price
Options outstanding, beginning of year	256,000	$2.75	463,000	$2.28	600,500	$2.37
Granted	250,000	1.88	250,000	2.50		
Exercised						
Canceled	(43,000)	2.75	(112,500)	2.39	(274,334)	2.43
Options outstanding, end of year	463,000	$2.28	600,500	$2.37	326,166	$2.32
Options exercisable at end of year	71,000		171,499		225,668	
Options available for future grant	1,037,000		899,500		1,173,834	

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following information is provided pursuant to the requirements of SFAS No. 123. The fair value of each option granted during the years ended February 29, 2000 and February 28, 2001, is estimated using the Black-Scholes option-pricing model on the date of grant using the following weighted average assumptions:

	Fiscal 2000	Fiscal 2001
Dividend yield	0%	0%
Expected volatility	56.5%	25.8%
Risk-free interest rate	6.12%	5.88%
Expected life	5 years	5 years

The 108,000, 134,833 and 83,333 options granted in fiscal 1999, 2000 and 2001, respectively, which remain outstanding as of February 28, 2002 have exercise prices of $2.75, $1.875 and $2.50, respectively, and a remaining contractual life of 6.92, 7.58 and 8.59 years, respectively. As of February 28, 2002, 225,668 of these options are exercisable. The per share fair value of all options granted during fiscal 2000 and 2001 was $1.03 and $0.87, respectively. No stock options were granted during fiscal 2002.

During the years ended February 29, 2000, February 28, 2001 and February 28, 2002, no compensation expense was recognized related to the stock options granted, however, had compensation expense been determined consistent with SFAS No. 123 for the Company s stock option grants for its stock-based compensation plan, the Company s income before extraordinary item and diluted earnings per common share for the years ended February 29, 2000, February 28, 2001 and February 28, 2002 would approximate the pro forma amounts below (Dollars in thousands, except per share amounts):

	Fiscal 2000		Fiscal 2001		Fiscal 2002	
	As Reported	Pro Forma	As Reported	Pro Forma	As Reported	Pro Forma
Income before extraordinary item	$5,227	$5,144	$10,728	$10,638	$6,292	$6,164
Diluted earnings per common share before extraordinary item	$ 0.37	$ 0.37	$ 0.77	$ 0.77	$ 0.43	$ 0.42

The effects of applying SFAS No. 123 in this pro forma disclosure are not indicative of future amounts.

10. Comprehensive Income and Implementation of SFAS No. 133

Effective March 1, 2001, the Company adopted SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities , as amended. SFAS 133 establishes accounting and reporting standards for derivative instruments and for hedging activities by requiring that all derivatives be recognized in the balance sheet and measured at fair value. The Company s policy is to designate at a derivative s inception the specific assets, liabilities, or future commitments being hedged and monitor the derivative to determine if it remains an effective hedge.

The Company has various interest rate swap agreements which effectively fix the variable interest rate on a notional amount of $75 million of the senior unsecured revolving credit facility related to its homebuilding operations. The swap agreements have been designated as cash flow hedges and, accordingly, are reflected at their fair value in the consolidated balance sheet at February 28, 2002. The unrealized loss, as of February 28, 2002, of $520,000 is recorded in stockholders equity as accumulated other comprehensive loss.

Amounts to be received or paid as a result of the swap agreements are recognized as adjustments to interest incurred on the related debt instruments. The Company believes that there will be no ineffectiveness related to the interest rate swaps and therefore no portion of the accumulated other comprehensive loss would be reclassified into future earnings. The net effect on the Company s operating results is that interest on the variable-rate debt being hedged is recorded and paid based on fixed interest rates.

44

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

11. Related Party Transactions

In fiscal 2000, the Company contributed cash totaling $3,278,000 to unconsolidated joint ventures. In fiscal 2001, the Company contributed cash totaling $1,244,000 to unconsolidated joint ventures. In fiscal 2002, the Company contributed cash totaling $4,039,000 to unconsolidated joint ventures.

The Company has made reimbursable advances to unconsolidated joint ventures (including the Divested Joint Ventures) for construction and other expenditures. The balance of advances at February 29, 2000, February 28, 2001 and February 28, 2002 was $10,588,000, $3,725,000 and $3,220,000, respectively. These amounts are included in investment in and advances to unconsolidated joint ventures in the accompanying consolidated balance sheets. During fiscal 2000 and fiscal 2001, the Company charged interest totaling $1,422,000 and $338,000, respectively, to the joint ventures based on these advances.

During fiscal 2000, 2001 and 2002, the Company recognized $12,446,000, $12,092,000 and $4,330,000, respectively, in construction overhead reimbursements from unconsolidated joint ventures (including the Divested Joint Ventures). Amounts are received pursuant to terms of the joint venture agreements, which generally specify a fixed payment per month over the anticipated period of development. Such amounts are included in selling, general and administrative expenses as a reimbursement of costs incurred in the accompanying income statements. As a result of the Exchange Transaction, the amount of overhead incurred, as well as the corresponding reimbursements, will decrease in the future years with respect to the Divested Joint Ventures.

Included in accounts receivable at February 28, 2001 and February 28, 2002 is $1,805,000 and $270,000, respectively, of amounts owed from the Company s various unconsolidated joint ventures to the Company s wholly-owned subsidiary, Newport Design Center, Inc. for goods and services rendered.

Effective February 23, 2001, CPH, Inc. and CHF consummated the Exchange Transaction, as further described in Note 1 above, whereby CPH, Inc. exchanged its 0.7% capital interests and contingent profit interest in the majority of the joint ventures capitalized by CHF including the Divested Joint Ventures for all of CHF s interest in CPH LLC and all of CHF s interests in certain residential joint ventures. As a result of the Exchange Transaction, as further described in Note 1 above, CPH, Inc. s interest in total capital of CPH LLC increased by 48% or $35.6 million. As a result of the Exchange Transaction, as further described in Note 1 above, CPH, Inc. has no further exposure to the economic or entitlement risks associated with the Divested Joint Ventures and the Managed Projects, including no obligation to provide any capital.

Under the Exchange Transaction, the Company transferred its interests in the Divested Projects to Makallon, LLC (Makallon), which is beneficially owned by CHF and by a former director and officer of the Company, who is a relative of the Chairman of the Board of the Company. In connection with the Exchange Transaction, Capital Pacific Homes, Inc., a wholly-owned subsidiary of CPH, Inc., has entered into construction, management and marketing agreements with Makallon relating to the Managed Projects whereby CPH, Inc. will be compensated for performing such services through a management fee arrangement. In addition, the Company has entered into a lease agreement with Makallon for office space in one building owned by a certain joint venture controlled by Makallon. The original term of the lease is three years with the opportunity for multiple extensions at the Company s option. During fiscal 2002 the Company paid Makallon approximately $400,000 for rent. As described above, in consideration for the assets given up in the Exchange Transaction, CPH, Inc. received a substantial increase to its equity in the homebuilding operations of CPH LLC and several other homebuilding joint ventures.

During fiscal 2000 approximately $193,000 was paid to a company partially owned by a relative of the Chairman of the Board for services rendered in connection with website design and maintenance and the development of a virtual reality tour of certain of the Company s model homes.

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

An officer of the Company purchased a home from the Company in fiscal 2001 for $1,450,000. During fiscal 2002, two different officers of the Company purchased homes from one of the Managed Projects for $1,451,000 and $976,000, respectively.

12. Commitments and Contingencies

General

Approximately $47,352,000 and $42,301,000 of performance bonds which have been issued on behalf of both CPH LLC and certain joint ventures, by which the Company has been indemnified, were outstanding at February 28, 2001 and February 28, 2002, respectively. The estimated cost to complete the development work related to the performance bonds is $33,147,000 and $13,267,000 at February 28, 2001 and February 28, 2002, respectively. The beneficiaries of these bonds are certain municipalities. Additionally, at February 28, 2002, CPH LLC has an outstanding letter of credit with a bank in the amount of $1,488,000.

CPH LLC has entered into agreements to lease certain office equipment and facilities under operating leases which expire at various dates through fiscal year 2007. The facility leases generally provide that CPH LLC shall pay property taxes, insurance and other items. Minimum payments under noncancelable leases at February 28, 2002, are as follows (in thousands):

Fiscal Years Ending:	
2003	$1,566
2004	1,172
2005	550
2006	222
2007	88
Total	$3,598

Total rent expense was $769,000, $1,153,000 and $1,366,000 for the years ended February 29, 2000, February 28, 2001 and February 28, 2002, respectively.

As discussed in Notes 1 and 4, CPH LLC is a general partner in certain joint venture partnerships. As a general partner, CPH LLC is liable for all debts of the partnerships without limitation to the respective partnership interest.

Dividends

No dividends were declared or paid for the years ended February 29, 2000, February 28, 2001 and February 28, 2002.

Legal Proceedings

The Company is involved in routine claims and litigation arising in the ordinary course of its business. A former senior executive officer of the Company has filed a suit styled in part as a shareholder derivative suit which the Company considers to be without merit challenging the Exchange Transaction (described in Note 1). The Company intends to vigorously defend its interests regarding this litigation, including pursuing all available counterclaims and appeals. The legal responsibility and financial impact with respect to pending claims and litigation cannot be presently ascertained.

Table of Contents

CAPITAL PACIFIC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

13. Disclosures About Fair Value of Financial Instruments

The following methods and assumptions were used to estimate the fair value of each class of financial instrument for which it is practicable to estimate:

Cash and Equivalents The carrying amount is a reasonable estimate of fair value. These assets primarily consist of short-term investments and demand deposits.

Notes Payable to Banks These notes payable mature in two to three years. The rates of interest paid on the notes approximate the current rates available for secured real estate financing with similar terms and maturities.

Senior Unsecured Notes Payable Due 2002 This issue was not publicly traded on a major exchange. Consequently, the fair value of this issue at February 28, 2001 is based on the repurchase closest to the year ended February 28, 2001. These Notes were redeemed during fiscal 2002.

Interest Rate Swaps These instruments are accounted for in accordance with SFAS 133 and are marked to market at each reporting period.

The estimated fair values of the Company s financial instruments are as follows (in thousands):

	At February 28, 2001		At February 28, 2002	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial Assets:				
Cash and equivalents	$ 7,552	$ 7,552	$ 5,080	$ 5,080
Financial Liabilities:				
Notes payable	110,223	110,223	116,265	116,346
Senior unsecured notes payable	55,592	51,978		
Interest rate swaps			520	520

14. Unaudited Summarized Quarterly Financial Data

Summarized quarterly financial data for the years ended February 28, 2001 and February 28, 2002 is as follows (in thousands except per share data):

	Quarter				
	First	Second	Third	Fourth	Total
2001:					
Sales of homes and land	$65,034	$96,215	$84,583	$117,911	$363,743
Gross margin	14,388	22,893	21,438	32,692	91,411
Net income	$ 2,289	$ 2,544	$ 1,830	$ 5,526	$ 12,189
Earnings per common share basic and diluted	$ 0.17	$ 0.18	$ 0.13	$ 0.40	$ 0.88

2002:					
Sales of homes and land	$77,494	$81,206	$60,209	$ 79,792	$298,701
Gross margin	19,612	20,199	14,135	18,382	72,328
Net income	$ 1,430	$ 1,215	$ 872	$ 2,775	$ 6,292
Earnings per common share basic and diluted	$ 0.10	$ 0.08	$ 0.06	$ 0.19	$ 0.43

Table of Contents

REPORT OF INDEPENDENT AUDITORS

To the Partners

Grand Coto Estates, L.P.

We have audited the accompanying statements of operations, partners capital (deficit) and cash flows of Grand Coto Estates, L.P., a California limited partnership (the Partnership), for the year ended December 31, 1999. These financial statements are the responsibility of the Partnership s management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the results of operations and cash flows of Grand Coto Estates, L.P. for the year ended December 31, 1999, in conformity with accounting principles generally accepted in the United States.

Irvine, California
January 28, 2000

Table of Contents

GRAND COTO ESTATES, L.P.

(a California limited partnership)

BALANCE SHEETS

December 31, 2000 and 2001

	2000	2001
	(Unaudited)	(Unaudited)
ASSETS		
Cash	$ 51,213	$ 36,722
Other assets	48,445	360,544
	$ 99,658	$ 397,266
LIABILITIES AND PARTNERS DEFICIT		
Accounts payable and accrued liabilities	$ 55,160	$ 582,480
Due to general partner	836,207	1,023,262
	891,367	1,605,742
Commitments and contingencies (Note 4)		
Partners deficit	(791,709)	(1,208,476)
	$ 99,658	$ 397,266

See accompanying notes to financial statements.

Table of Contents

GRAND COTO ESTATES, L.P.

(a California limited partnership)

STATEMENTS OF OPERATIONS

For the Years Ended December 31, 1999, 2000 and 2001

	1999	2000	2001
		(Unaudited)	(Unaudited)
Sales	$37,557,500	$ 2,991	$
Cost of sales	28,116,357	(259,449)	413,887
Gross profit	9,441,143	262,440	(413,887)
Other expenses (income):			
Selling and marketing	2,650,480	4,800	4,010
Other income	(18,032)		(1,130)
Net income (loss)	$ 6,808,695	$ 257,640	$(416,767)

See accompanying notes to financial statements.

Table of Contents

GRAND COTO ESTATES, L.P.

(a California limited partnership)

STATEMENTS OF PARTNERS CAPITAL (DEFICIT)

For the Years Ended December 31, 1999, 2000 and 2001

	IHP Investment Fund I, L.P.	Capital Pacific Holdings, LLC	Total
Balance December 31, 1998	15,350,982	1,455,136	16,806,118
Contributions from partners	7,688,262	2,801,787	10,490,049
Distributions to partners	(27,318,352)	(7,916,505)	(35,234,857)
Net income	3,686,647	3,122,048	6,808,695
Balance December 31, 1999	(592,461)	(537,534)	(1,129,995)
Contributions from partners	67,602	67,602	135,204
Distributions to partners		(54,558)	(54,558)
Net income	128,820	128,820	257,640
Balance December 31, 2000 (unaudited)	$ (396,039)	$ (395,670)	$ (791,709)
Net loss	(208,383)	(208,384)	(416,767)
Balance December 31, 2001 (unaudited)	$ (604,422)	$ (604,054)	$ (1,208,476)

See accompanying notes to financial statements.

Table of Contents

GRAND COTO ESTATES, L.P.

(a California limited partnership)

STATEMENTS OF CASH FLOWS

For the Years Ended December 31, 1999, 2000 and 2001

	1999	2000	2001
		(Unaudited)	(Unaudited)
Operating Activities			
Net income (loss)	$ 6,808,695	$ 257,640	$ (416,767)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities			
Changes in operating assets and liabilities			
Real estate inventories	20,164,994		
Due from general partner	56,467		
Other assets	(33,386)	58,435	(312,099)
Accounts payable and accrued liabilities	(2,651,401)	(1,242,017)	527,320
Due to general partner	176,493	659,714	187,055
Net cash provided by (used in) operating activities	24,521,862	(266,228)	(14,491)
Financing Activities			
Capital contributions from partner	10,490,049	135,204	
Capital distributions to partners	(35,234,857)	(54,558)	
Net cash (used in) provided by financing activities	(24,744,808)	80,646	
Net decrease in cash	(222,946)	(185,582)	(14,491)
Cash beginning of year	459,741	236,795	51,213
Cash end of year	$ 236,795	$ 51,213	$ 36,722

See accompanying notes to financial statements.

52

Table of Contents

GRAND COTO ESTATES, L.P.

(a California limited partnership)

NOTES TO FINANCIAL STATEMENTS

December 31, 1999

1. Organization and Summary of Significant Accounting Policies

Organization

Grand Coto Estates, L.P., a California limited partnership (the Partnership), was formed on October 30, 1996 in accordance with the provisions of the laws of the State of California for the purpose of developing and selling 93 single-family homes in Coto de Caza, California (the Project). The general partner, Peters Ranchland Company, Inc. (Peters), and the limited partner, IHP Investment Fund I, L.P. (IHP), each owned a 50% interest in the Partnership at inception. On October 1, 1997, Peters transferred its interest in the Partnership to Capital Pacific Holdings, LLC (CPH).

The Partnership Agreement provides that cash flows, as defined, are distributed to the partners first, in the amount of the adjusted GAAP profit component (as defined) from the sale of each home, in accordance with their percentage interests; second, in satisfaction of unpaid preferred returns; third, for payment of partners capital contributions; fourth, in accordance with their percentage interests.

Net income is allocated to the partners in the following order of priority: first, to recover any net losses allocated previously; second, to the extent of and in proportion to the amount by which cash flow distributed in satisfaction of preferred returns and the adjusted GAAP profit component (as defined in the partnership agreement) exceeds previously allocated net income; thereafter, in accordance with their percentage interests. Net losses are allocated first, to the general partner up to $2,076,921 plus all previously allocated net income; second, to the limited partner until the limited partner s capital account is reduced to zero; any remaining losses are allocated to the general partner.

Certain distributions reflected in the statement of partners capital were not in accordance with the provisions of the partnership agreement and it is management s and the partners intent to cumulatively adjust future contributions and distributions of the Partnership to reflect the provisions of the partnership agreement.

The partnership agreement provides, among other things, that the partners shall be entitled to receive a preferred return on contributed capital computed using an interest rate equal to prime plus 2%.

Use of Estimates

The preparation of the Partnership s financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of December 31, 1999 and revenues and expenses in the period ended December 31, 1999. Actual results could materially differ from those estimates in the near term.

Real Estate Inventories

Real estate inventories include direct and indirect land costs, offsite costs and onsite improvement costs, project commitment fees and builder overhead fees which are capitalized to the real estate project. Selling and marketing costs are expensed as incurred.

The Partnership complies with the provisions of Statement of Financial Accounting Standards No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of (SFAS No. 121). SFAS No. 121 requires the Partnership to review the Project whenever events or changes in circumstances indicate that the cost basis of such assets may not be recoverable. If the cost basis of the Project is greater than the projected future net cash flows from the Project, an impairment loss is recognized. Impairment losses are calculated as the difference between the Project s cost basis and its estimated fair value, net of disposal costs on completed units, if any. No impairment losses were recorded in December 31, 1999,

Table of Contents

GRAND COTO ESTATES, L.P.
(a California limited partnership)

NOTES TO FINANCIAL STATEMENTS (Continued)

accordingly, the Project was carried at its historical cost basis. The Partnership sold all of its remaining homes in 1999, therefore, there is no inventory balance as of December 31, 1999.

Sales and Profit Recognition

Sales are recorded and profit is recognized when title has passed to a buyer who has met down payment and continuing investment criteria and substantially all of the risks and rewards of ownership have been transferred to the buyer. At the time of sale, accumulated costs are relieved from real estate inventories by a method that approximates relative sales value and are charged to cost of sales.

Income Taxes

The Partnership is not a taxable entity and the results of its operations are included in the tax returns of the partners. Accordingly, no provision for income taxes is reflected in the accompanying financial statements.

2. Real Estate Inventories

During 1999, the Project s remaining 45 homes were sold. At December 31, 1999, included in accounts payable and accrued liabilities is $1,155,219 of estimated costs to complete the development of the Project and $141,958 of warranty cost reserves.

3. Related Party Transactions

The partnership agreement provides that a total of $1,579,199 be paid to the general partner in monthly installments for builder overhead fees. If, after all of the homes in the Project are sold, actual sales prices (as defined) are less than budgeted sales prices, the general partner shall be liable to the Partnership for all overhead fees received in excess of 3% of actual gross sales prices (as defined). If actual sales prices are greater than budgeted sales prices, the general partner shall be entitled to receive from the Partnership an amount equal to 3% of actual gross sales prices less overhead fees already received. An additional $394,154 of builder overhead fees was incurred by the Partnership as actual sale prices were greater than budget.

The following fees were paid to the partners and capitalized to the Project during the year ended December 31, 1999:

Commitment fees paid to IHP	$
Builder overhead fees paid to CPH	218,920
	$218,920

4. Commitments and Contingencies

The Partnership s commitments and contingencies include the usual obligations incurred by real estate developers in the normal course of business. In the opinion of management, these matters will not have a material effect on the Partnership s financial position.

In the jurisdiction in which the Partnership develops and constructs the Project, community facilities district bonds are issued by government instrumentalities to finance major infrastructure and other improvements. As a land owner benefited by these improvements, the Partnership is responsible for the assessments on its land until the property is sold to buyers. When homes within the Project are sold, the buyers assume the responsibility for the related assessment.

Table of Contents

REPORT OF INDEPENDENT AUDITORS

To the Partners

M.P.E. Partners, L.P.

We have audited the accompanying statements of operations, partners capital (deficit) and cash flows of M.P.E. Partners, L.P., a California limited partnership (the Partnership), for the year ended December 31, 1999. These financial statements are the responsibility of the Partnership s management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the results of operations and cash flows of M.P.E. Partners, L.P. for the year ended December 31, 1999, in conformity with accounting principles generally accepted in the United States.

Irvine, California
January 28, 2000

Table of Contents

M.P.E. PARTNERS, L.P.

(a California limited partnership)

BALANCE SHEETS

December 31, 2000 and 2001

	2000	2001
	(Unaudited)	(Unaudited)
ASSETS		
Cash	$ 323,102	$ 232,466
	$ 323,102	$ 232,466
LIABILITIES AND PARTNERS DEFICIT		
Accounts payable and accrued liabilities	$ 542,621	$ 127,898
Due to partners	471,683	323,290
	1,014,304	451,188
Commitments and contingencies (Note 4)		
Partners deficit	(691,202)	(218,722)
	$ 323,102	$ 232,466

See accompanying notes to financial statements.

Table of Contents

M.P.E. PARTNERS, L.P.

(a California limited partnership)

STATEMENTS OF OPERATIONS

For the Years Ended December 31, 1999, 2000 and 2001

	1999	2000	2001
		(Unaudited)	(Unaudited)
Sales	$24,345,000	$	$
Cost of sales	19,039,542		(478,095)
Gross profit	5,305,458		478,095
Other expenses:			
Selling and marketing	2,701,810	1,600	5,615
Other	17,045		
Net income (loss)	$ 2,586,603	$(1,600)	$ 472,480

See accompanying notes to financial statements.

Table of Contents

M.P.E. PARTNERS, L.P.

(a California limited partnership)

STATEMENTS OF PARTNERS CAPITAL (DEFICIT)

For the Years Ended December 31, 1999, 2000 and 2001

	IHP Investment Fund I, L.P.	Capital Pacific Holdings, LLC	Total
Balance December 31, 1998	11,908,276	1,917,752	13,826,028
Contributions from partner	6,149,660		6,149,660
Distributions to partners	(21,609,165)	(1,700,445)	(23,309,610)
Net income	1,677,956	908,647	2,586,603
Balance December 31, 1999	(1,873,273)	1,125,954	(747,319)
Contributions from partner	57,717		57,717
Net loss	(1,494)	(106)	(1,600)
Balance December 31, 2000 (unaudited)	$ (1,817,050)	$ 1,125,848	$ (691,202)
Net income (loss)	915,272	(442,790)	472,480
Balance December 31, 2001 (unaudited)	$ (901,778)	$ 683,058	$ (218,722)

See accompanying notes to financial statements.

58

Table of Contents

M.P.E. PARTNERS, L.P.

(a California limited partnership)

STATEMENTS OF CASH FLOWS

For the Years Ended December 31, 1999, 2000 and 2001

	1999	2000	2001
		(Unaudited)	(Unaudited)
Operating Activities			
Net income (loss)	$ 2,586,603	$ (1,600)	$ 472,480
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities			
Changes in operating assets and liabilities			
Receivables and other assets	275,698	2,846	
Real estate inventories	16,102,348		
Accounts payable and accrued liabilities	(2,042,853)	(280,767)	(414,723)
Due to partners	346,797	15,748	(148,393)
Net cash provided by (used in) operating activities	17,268,593	(263,773)	(90,636)
Financing Activities			
Capital contributions from partners	6,149,660	57,717	
Capital distributions to partners	(23,309,610)		
Net cash (used in) provided by financing activities	(17,159,950)	57,717	
Net increase (decrease) in cash	108,643	(206,056)	(90,636)
Cash beginning of period	420,515	529,158	323,102
Cash end of period	$ 529,158	$ 323,102	$ 232,466

See accompanying notes to financial statements.

Table of Contents

M.P.E. PARTNERS, L.P.

(a California limited partnership)

NOTES TO FINANCIAL STATEMENTS

December 31, 1999

1. Organization and Summary of Significant Accounting Policies

Organization

M.P.E. Partners, L.P., a California limited partnership (the Partnership), was formed on March 14, 1997 (inception) in accordance with the provisions of the laws of the State of California for the purpose of developing and selling 51 single-family homes in Tarzana, California (the Project). The general partner, Peters Ranchland Company, Inc. (Peters), and the limited partner, IHP Investment Fund I, L.P. (IHP), each owned a 50% interest in the Partnership at inception. On October 1, 1997, Peters transferred its interest in the Partnership to Capital Pacific Holdings, LLC (CPH).

The partnership agreement provides that cash flows, as defined, are distributed to the partners first, in the amount of the adjusted GAAP profit component (as defined) from the sale of each home, in accordance with their percentage interests; second, in satisfaction of unpaid preferred returns; third, for payment of partners capital contributions in accordance with their percentage interests; any remaining cash flows are distributed to the partners in accordance with their percentage interests.

Net income is allocated to the partners in the following order of priority: first, to recover any net losses allocated previously; second, to the extent of and in proportion to the amount by which cash flow distributed in satisfaction of preferred returns and the adjusted GAAP profit component (as defined in the partnership agreement) distributed from the sale of each home exceeds previously allocated profits; third, to the extent other cash flows distributed, as defined, exceed previously allocated net income; thereafter, in accordance with their percentage interests. Net losses are allocated first, to the general partner up to $4,063,045 plus all previously allocated net income; second, to the limited partner until the limited partner s capital account is reduced to zero; any remaining losses are allocated to the general partner.

Certain distributions reflected in the statement of partners capital were not in accordance with the provisions of the partnership agreement and it is management s and the partners intent to cumulatively adjust future contributions and distributions of the Partnership to reflect the provisions of the partnership agreement.

The partnership agreement provides, among other things, that the partners shall be entitled to receive a preferred return on contributed capital computed at the rate of prime plus 1%. As of December 31, 1999, the Partnership has unpaid preferred returns of $0 on IHP s capital contributions, and $307,434 on CPH s capital contributions.

Use of Estimates

The preparation of the Partnership s financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of December 31, 1999 and revenues and expenses for the year ended December 31, 1999. Actual results could materially differ from those estimates in the near term.

Real Estate Inventories

Real estate inventories include direct and indirect land costs, offsite costs and onsite improvement costs, project commitment fees and builder overhead fees which are capitalized to the Project. Selling and marketing costs are expensed as incurred.

The Partnership complies with the provisions of Statement of Financial Accounting Standards No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of (SFAS

Table of Contents

M.P.E. PARTNERS, L.P.
(a California limited partnership)

NOTES TO FINANCIAL STATEMENTS (Continued)

No. 121). SFAS No. 121 requires the Partnership to review the Project whenever events or changes in circumstances indicate that the cost basis of the Project may not be recoverable. If the cost basis of the Project is greater than the projected future net cash flows from the Project, an impairment loss is recognized. Impairment losses are calculated as the difference between the Project s cost basis and its estimated fair value, net of disposal costs on completed units, if any. No impairment losses were recorded in 1999. Accordingly, the Project was carried at its historical cost basis. The Partnership sold all of its remaining homes in 1999, therefore, there is no inventory balance at December 31, 1999.

Sales and Profit Recognition

Sales are recorded and profit is recognized when title has passed to a buyer who has met down payment and continuing investment criteria, and substantially all of the risks and rewards of ownership have been transferred to the buyer. At the time of sale, accumulated costs are relieved from real estate inventories by a method that approximates relative sales value and are charged to cost of sales.

Income Taxes

The Partnership is not a taxable entity and the results of its operations are included in the tax returns of the partners. Accordingly, no provision for income taxes is reflected in the accompanying financial statements.

2. Real Estate Inventories

During 1999, the Project s remaining 20 homes were sold. At December 31, 1999, included in accounts payable and accrued liabilities is $552,475 of estimated costs to complete the development of the Project and $270,913 of warranty cost reserves.

3. Related Party Transactions

The Partnership acquired the Project on April 11, 1997 from a related party, Capital Pacific Holdings, Inc. and two other affiliates (collectively, CPH, Inc.), for $12,392,547, utilizing IHP s initial cash contribution.

CPH, Inc. incurred certain costs in connection with the development of the Partnership s models and sales office. In accordance with the Partnership Agreement, $2,710,000 was credited to CPH s capital account relating to these development costs.

The partnership agreement provides that a total of $1,623,655 be paid to the general partner in monthly installments for builder overhead fees. If, after all of the homes in the Project are sold, actual sales prices (as defined) are less than budgeted sales prices, the general partner shall be liable to the Partnership for all overhead fees received in excess of 3% of actual gross sales prices (as defined). If actual sales prices are greater than budgeted sales prices, the general partner shall be entitled to receive from the Partnership an amount equal to 3% of actual gross sales prices less overhead fees already received. An additional $126,725 of builder overhead fees was incurred by the Partnership as actual sale prices were greater than budget.

Table of Contents

M.P.E. PARTNERS, L.P.
(a California limited partnership)

NOTES TO FINANCIAL STATEMENTS (Continued)

The following fees were paid to the partners and capitalized to the Project during the year ended December 31, 1999:

Commitment fees paid to IHP	$
Builder overhead fees paid to CPH	267,913
	$ 267,913

The amounts due to the partners as of December 31, 1999 consist of amounts due to CPH for the payment of builder overhead fees and development fees.

4. Commitments and Contingencies

The Partnership s commitments and contingencies include the usual obligations incurred by real estate developers in the normal course of business. In the opinion of management, these matters will not have a material effect on the Partnership s financial position.

62

Table of Contents

Item 9. ***Changes in and Disagreements with Accountants on Accounting and Financial Disclosure***

On April 4, 2002 the Company filed a report on Form 8-K, regarding a change in the Registrant s certifying accountant from Arthur Andersen LLP (Andersen) to Ernst & Young LLP.

The Report of Independent Public Accountants of Andersen on the consolidated financial statements of Capital Pacific Holdings as of February 28, 2001 and February 29, 2000 and for each of the three years in the period ended February 28, 2001 contained no adverse opinions or disclaimers of opinion, nor were such reports qualified as to uncertainty, audit scope or accounting principles. During such periods and through March 29, 2002, (i) there were no disagreements with Andersen on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedures, which disagreements if not resolved to its satisfaction would have caused it to make reference in connection with its report to the subject matter of the disagreement, and (ii) Andersen has not advised the registrant of any reportable events as defined in paragraph (A) through (D) of Regulation S-K Item 304(a)(1)(v).

PART III

Item 10. ***Directors and Executive Officers of the Registrant***

The information required by Item 10 is incorporated by reference to the Company s definitive proxy statement to be filed with the Commission no later than June 28, 2002 (the Proxy Statement).

Item 11. ***Executive Compensation***

The information required by Item 11 is incorporated by reference to the Company s definitive Proxy Statement.

Item 12. ***Security Ownership of Certain Beneficial Owners and Management***

The information required by Item 12 is incorporated by reference to the Company s definitive Proxy Statement.

Item 13. ***Certain Relationships and Related Transactions***

The information required by Item 13 is incorporated by reference to the Company s definitive Proxy Statement.

PART IV

Item 14. ***Exhibits, Financial Statements, Schedules and Reports on Form 8-K***

(a) *Documents filed as part of this report:*

1. *Financial Statements.* The following Financial Statements, together with the Notes thereto and Reports of Independent Auditors and Public Accountants thereon, are included in Part II, Item 8 of this report.

Capital Pacific Holdings, Inc.
Report of Independent Auditors
Report of Independent Public Accountants

Consolidated Balance Sheets as of February 28, 2001 and 2002
Consolidated Statements of Income for the years ended February 29, 2000 and February 28, 2001 and 2002
Consolidated Statements of Stockholders Equity for the years ended February 29, 2000 and February 28, 2001 and 2002

Consolidated Statements of Cash Flows for the years ended February 29, 2000 and February 28, 2001 and 2002
Notes to Consolidated Financial Statements

Grand Coto Estates, L.P.
Report of Independent Auditors
Balance Sheets as of December 31, 2000 (unaudited) and 2001 (unaudited)
Statements of Operations for the years ended December 31, 1999, 2000 (unaudited) and 2001 (unaudited)
Statements of Partners Capital (Deficit) for the years ended December 31, 1999, 2000 (unaudited) and 2001 (unaudited)
Statements of Cash Flows for the years ended December 31, 1999, 2000 (unaudited) and 2001 (unaudited)
Notes to Financial Statements

M.P.E. PARTNERS, L.P.
Report of Independent Auditors
Balance Sheets as of December 31, 2000 (unaudited) and 2001 (unaudited)
Statements of Operations for the years ended December 31, 1999, 2000 (unaudited) and 2001 (unaudited)
Statements of Partners Capital (Deficit) for the years ended December 31, 1999, 2000 (unaudited) and 2001 (unaudited)
Statements of Cash Flows for the years ended December 31, 1999, 2000 (unaudited) and 2001 (unaudited)
Notes to Financial Statements

2. *Exhibits*

Exhibit Number	Description
3.1	Third Restated Certificate of Incorporation of the Registrant.*
3.2	Second Amended and Restated Bylaws of the Registrant. (Incorporated by reference to Exhibit 3.4 of the Registrant s Annual Report on Form 10-K for the fiscal year ended February 28, 1998).
4.1	See the Articles of Incorporation and Bylaws of the Registrant (Exhibits 3.1 3.2).
10.1	Capital Pacific Holdings, Inc. Stock Incentive Agreement (Non-Qualified). (Incorporated by reference to Exhibit 10.7 of the Registrant s Annual Report on Form 10-K for the fiscal year ended February 28, 1999).
21.1	Subsidiaries of the Registrant.*
23.1	Consent of Ernst & Young LLP.*
23.2	Consent of Arthur Andersen LLP.*

* Previously filed

(b) *Reports on Form 8-K*

A report on Form 8-K was filed on March 9, 2001, regarding the Interest Exchange Agreement between the Registrant and California Housing Finance, L.P.

A report on Form 8-K was filed on April 4, 2002, regarding a change in the Registrant s certifying accountant from Arthur Andersen LLP to Ernst & Young LLP.

Table of Contents

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned; thereunto duly authorized, in the City of Newport Beach, State of California, on May 29, 2002.

CAPITAL PACIFIC HOLDINGS, INC.

By /s/ HADI MAKARECHIAN

Hadi Makarechian
Chairman of the Board,
Chief Executive Officer and President

Date: May 29, 2002

KNOW ALL MEN BY THESE PRESENTS that each person whose signature appears below constitutes and appoints Hadi Makarechian and Steven O. Spelman, Jr., and each of them, his true and lawful attorneys-in-fact and agents, with full power of substitution and resubstitution, for each person and in such person s name, place and stead, in any and all capacities, to sign any and all amendments to this report on Form 10-K, and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents full power and authority to do and perform each and every act and thing requisite and necessary to be done in connection therewith, as fully and to all intents and purposes as such person might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, or their substitute or substitutes, may lawfully do or cause to be done by virtue of the powers herein granted.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons in the capacities and on the dates indicated.

Signature	Title	Date
/s/ HADI MAKARECHIAN Hadi Makarechian	Chairman of the Board, Chief Executive Officer and President	May 29, 2002
/s/ STEVEN O. SPELMAN, JR. Steven O. Spelman, Jr.	Chief Financial Officer and Corporate Secretary	May 29, 2002
/s/ KARLHEINZ M. KAISER Karlheinz M. Kaiser	Director	May 29, 2002
/s/ ALLAN L. ACREE Allan L. Acree	Director	May 29, 2002
/s/ WILLIAM J. HADAWAY William J. Hadaway	Director	May 29, 2002

Table of Contents

EXHIBIT INDEX

Exhibit Number	Description	Sequential Page Number
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* Previously filed