

CALIFORNIA COASTAL COMMUNITIES INC
Form 10-K
March 26, 2009

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549
FORM 10-K

(Mark
One)

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

For the fiscal year ended December 31, 2008

OR

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

For the transition period from _____ to _____
Commission file number: 0-17189

CALIFORNIA COASTAL COMMUNITIES, INC.

(Exact name of registrant as specified in its charter)

Delaware **02-0426634**
(State or other jurisdiction of (I.R.S. Employer Identification No.)
incorporation or organization)

6 Executive Circle, Suite 250 **92614**
Irvine, California (Zip Code)
(Address of principal executive offices)
Registrant's telephone number, including area code: **(949) 250-7700**

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, par value \$.05 per share	NASDAQ Global Market

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Ruleb 405 of the Securities Act. YES NO

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. YES NO

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

Large accelerated
filer

Accelerated
filer

Non-accelerated
filer

Smaller reporting
company

(Do not check if a
smaller reporting
company)

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

The aggregate market value of the voting stock held by non-affiliates of the registrant (shares of common stock held by each executive officer and director and by each person who, as of such date, may be deemed to have beneficially owned more than 5% of the outstanding voting stock have been excluded in that such persons may be deemed to be affiliates of the registrant under certain circumstances) was \$12,351,668 as of June 30, 2008 (the last business day of the registrant's most recently completed second fiscal quarter) based upon 3,233,421 shares of common stock held by such non-affiliates and the \$3.82 closing price of the registrant's common stock on the NASDAQ Stock Market LLC reported for June 30, 2008.

The number of shares of Common Stock outstanding as of March 16, 2009 was 10,995,902.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Proxy Statement for the 2009 Annual Meeting of Stockholders are incorporated by reference into Part III of this Annual Report on Form 10-K.

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FOR THE YEAR ENDED DECEMBER 31, 2008

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PART I

Item 1. Business

Overview of California Coastal Communities, Inc. and Recent Industry Events.

We are a residential land development and homebuilding company with properties owned or controlled primarily in Orange County, California and also in two other Southern California counties (Los Angeles and Riverside). Our primary asset is a 356-home luxury coastal community known as Brightwater. Our principal activities include:

obtaining zoning and other entitlements for land we own;

improving the land for residential development; and

designing, constructing and selling single-family homes in Southern California.

Once our residential land is entitled, we may build homes, sell unimproved land to other developers or homebuilders, sell improved land to homebuilders, or participate in joint ventures with other developers, investors or homebuilders to finance and construct infrastructure and homes. The majority of our homes are designed to appeal to move-up homebuyers and are generally offered for sale in advance of their construction.

During 2008, the financial crisis and economic recession further exacerbated the existing downturn in the homebuilding market and resulted in additional downward pressure on home sales and asset values. Based on statistics from the Mortgage Bankers Association, processed foreclosures reached approximately 1.4 million in the last quarter of 2008 as compared to an average of about 500,000 per quarter during 2000-2007. These record-high foreclosure rates intensified competition for homebuyers in an already saturated marketplace with the influx of existing homes inventory, coupled with the reduced availability of mortgage financing resulting from the turmoil in the financial industry. Concern about the state of the economy and the job market further deteriorated consumer confidence, as unemployment rates rose in almost all of the metropolitan areas tracked by the U.S. Department of Labor, ending 2008 with a national average of 6.5% as compared to 4.5% in the prior year. The unemployment rate in California reached 8.7% at the end of 2008 compared with 5.9% in the prior year. We believe that the tepid demand we are experiencing reflects homebuyers' reluctance to make a purchasing decision until they are comfortable that home price declines are near bottom and economic conditions have stabilized. We believe the current conditions could continue, and potentially worsen during 2009 and perhaps beyond, and we expect that our operations will remain depressed until the homebuilding industry and economy as a whole begin to rebound.

During the year, we successfully modified the terms for our term loan and revolving loan which are secured by our Brightwater project and completed a sale-leaseback transaction for 17 Brightwater model homes for \$22.5 million in cash plus future consideration, which has provided us with greater operating flexibility. In view of the continuing significant economic downturn in the housing market, we currently expect that during the next 12 months our new home construction will be limited primarily to our 356-home Brightwater project located on the Bolsa Chica mesa in Huntington Beach, California; and that our operations in other markets will focus on the sale of standing inventory and resolution of certain existing project loans.

During 2009, our primary goals will be to:

continue selling and delivering homes at Brightwater;

continue evaluating potential alternatives regarding our capital structure including, but not limited to, various strategies for restructuring our debt and raising additional capital;

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continue reducing standing inventories and thereby maximize deliveries and revenues at our other homebuilding projects in Los Angeles and Riverside counties; and

pursue consensual resolution of loan defaults on nonperforming inland development projects.

There can be no assurance that we will accomplish, in whole or in part, all or any of these strategic goals or any other strategic goals or opportunities that we may pursue.

Our total revenues for the years ended December 31, 2008, 2007, and 2006 were \$46.0 million, \$47.0 million, and \$95.7 million, respectively. For the years ended December 31, 2008, 2007, and 2006 we delivered 55, 77, and 147, homes, respectively. Our total assets as of December 31, 2008 and 2007 were \$312.5 million and \$367.6 million, respectively, with Brightwater constituting \$238.5 million (76% of total assets) and \$219.9 million (60% of total assets), respectively. Our homebuilding subsidiary, Hearthside Homes, Inc., has delivered over 2,100 homes to families throughout Southern California since its formation in 1994.

Prior to obtaining the Coastal Development Permit for our Brightwater project in December 2005, we historically maintained a minimal amount of leverage. In September 2006, we obtained \$225 million of debt financing, as described below in Notes 6 and 7 to the Consolidated Financial Statements, which provided \$100 million for Brightwater construction and \$125 million to fund a \$12.50 per share special dividend paid to our stockholders in September 2006, as described in Note 13 to the Consolidated Financial Statements. As of December 31, 2008, we had \$243.2 million of debt against \$55.5 million of book equity.

We were formed in 1988 and our executive offices are located at 6 Executive Circle, Suite 250, Irvine, California 92614. Our website address is <http://www.californiacoastalcommunities.com> and our telephone number is (949) 250-7700. Through our website we make available our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to these reports filed or furnished pursuant to Section 13(d) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonably practicable after they are filed with, or furnished to, the Securities and Exchange Commission. Copies of our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to these reports are available free of charge upon request. In addition, at our website: <http://www.californiacoastalcommunities.com>, we post copies of our Securities and Exchange Commission filings and press releases, as well as current versions of our code of ethics, audit committee charter and nominating committee charter.

Our Current and Future Homesites

We currently have on-going Southern California homebuilding projects in:

Orange County in the Huntington Beach area;

Riverside County in the City of Corona and in the City of Beaumont; and

Northern Los Angeles County in the City of Lancaster.

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The following chart describes our current projects, their location and our lot and standing home inventories as of December 31, 2008:

Project	Location	Models(a)	Backlog	Standing Inventory	Remaining Lots	Total Lot Inventory
<u>Brightwater in Orange County:</u>						
The Trails	Huntington Beach	4	1	2	44	51
The Sands	Huntington Beach	4	1	1	62	68
The Cliffs	Huntington Beach	4	1	1	95	101
The Breakers	Huntington Beach	5	4	2	93	104
<i>Subtotal Orange County</i>		17	7	6	294	324
<u>Inland Empire/Lancaster:</u>						
Hearthside Lane	Corona	5		2	134	141
Woodhaven	Beaumont	4	1	4	62	71
Las Colinas	Lancaster			2	54	56
Other unimproved lots	Lancaster				73	73
<i>Subtotal Inland Empire/Lancaster</i>		9	1	8	323	341
<i>Total All Projects</i>		26	8	14	617	665

(a)

While we sold our 17 Brightwater models to an independent third-party investor on December 31, 2008, the transaction is accounted for as a financing and therefore those homes are included in our home inventories.

As of December 31, 2008, we had standing inventory of 14 homes, including six homes at Brightwater and eight homes at our inland projects. During the year ended December 31, 2008, net new orders decreased to 58 homes compared with 65 homes during 2007, primarily due to reduced sales activity at our inland communities. Cancellations as a percentage of new orders were 27% during the year ended December 31, 2008 (19% at Brightwater and 33% at our inland projects), compared with approximately 30% during 2007. Backlog as of December 31, 2008 increased to eight homes compared with five homes as of December 31, 2007 primarily due to sales activity at our Brightwater project.

Brightwater at Bolsa Chica

Brightwater is our coastal Orange County residential community, located on the 110-acre Bolsa Chica mesa in the City of Huntington Beach, approximately 35 miles south of downtown Los Angeles. Brightwater was recently annexed into the City of Huntington Beach. Brightwater offers a broad mix of home choices averaging 2,860 square feet and ranging in size from 1,710 square feet to 4,339 square feet. Located near Pacific Coast Highway and overlooking the Pacific Ocean, Huntington Harbor and the recently restored 1,300-acre Bolsa Chica Wetlands, 62 of the 356 homes at Brightwater will have unobstructed ocean and/or wetlands views.

Brightwater is the largest property in our portfolio, representing approximately 91% of our real estate inventories as of December 31, 2008. This project is located on one of the last large undeveloped coastal properties in Southern California. Brightwater is bordered on the north and east by residential development in the City of Huntington Beach and Huntington Harbor, to the south by open space and the 1,300-acre Bolsa Chica wetlands, and to the west by 120 acres of publicly-owned conservation land and open space on the lower bench of the Bolsa Chica mesa, Pacific Coast Highway, Bolsa Chica State Beach, and the Pacific Ocean. Brightwater also has 37 acres of open space and conservation area.

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We completed construction of eight model homes at The Trails and The Sands neighborhoods in July 2007 and held a grand opening in August 2007 and delivered the first nine homes in December 2007. We delivered 12 and nine homes at The Trails and The Sands during the years ended December 31, 2008 and 2007, respectively, and generated \$12.3 million and \$11.0 million in revenue, respectively. We generated gross operating margins of 28.6% and 33.6% for The Trails and The Sands during 2008 and 2007, respectively. Homes at The Trails and The Sands are presently being offered at prices ranging from \$798,000 to \$1.1 million. As of March 16, 2009, two homes are in escrow at The Trails and The Sands.

During January 2008, we completed construction of nine additional model homes for The Cliffs and The Breakers and in February 2008 began selling homes to buyers who previously registered on our priority list. We held a grand opening for these neighborhoods on March 15, 2008. These homes are larger than The Trails and The Sands, ranging from 2,724 to 4,339 square feet. We began delivering homes at The Cliffs and The Breakers during the third quarter of 2008 and delivered 11 of these homes during the year ended December 31, 2008. We generated \$21.0 million in revenue and generated gross operating margins of 35.1% for The Cliffs and The Breakers in 2008. Homes at The Cliffs and The Breakers are presently being offered at prices ranging from \$1.5 to \$3.3 million for 2,724 to 4,339 square foot homes. As of March 16, 2009, four homes are in escrow at The Cliffs and The Breakers.

Key facts and assumptions regarding the Brightwater development project include the following:

Brightwater is expected to consist of 356 homes, including 106 homes at The Breakers, 109 homes at The Cliffs, 79 homes at The Sands and 62 homes at The Trails.

There are 62 homes at Brightwater which will have unobstructed views of the Pacific Ocean and/or the Bolsa Chica wetlands, including 35 homes at The Breakers, 25 homes at The Cliffs and two homes at The Sands.

Build-out of production homes, which is subject to market conditions, is currently expected to take approximately four years and be completed in 2012.

Costs to improve the lots from their raw condition to finished lots, including County permits, City annexation fees and school fees, approximate \$200,000 per lot.

The direct costs (excluding indirect costs such as supervision, overhead, sales and marketing, warranty, insurance, etc.) of building homes at Brightwater are currently expected to range from approximately \$125 to \$145 per square foot.

Indirect costs are expected to approximate 6% of sales revenues.

Based on current sales price and cost projections, the various Brightwater products are currently expected to generate gross margins of approximately 25% to 35% due to our low carrying value in Brightwater. Gross margins for the larger homes at The Cliffs and The Breakers are currently expected to approximate 32% to 36%, while gross margins at The Trails and The Sands are currently expected to approximate 25% to 29%.

The estimation process involved in the determination of value is inherently uncertain because it requires estimates as to future events and market conditions. This estimation process assumes our ability to complete development and disposition of our real estate inventories in the ordinary course of business based on management's present plans and intentions. Economic, market, and environmental conditions may affect our development and marketing plans. The development of Brightwater depends upon various factors. Accordingly, the amount ultimately realized from the Brightwater project may differ materially from our current estimates and the project's carrying value.

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Oxnard Land Development - Unconsolidated Joint Venture - Full Impairment Charges

We are evaluating the feasibility of continuing the entitlement project for 168 acres of land adjacent to the City of Oxnard in Ventura County, California through a joint venture that our Hearthside Homes, Inc. homebuilding subsidiary entered into in October 2003 with a major financial partner.

The joint venture is attempting to renegotiate the land purchase option contracts to reflect current economic conditions and expectations for a prolonged period required for the Oxnard housing market to recover to a level that would support the land purchase price stipulated in the option agreements. If the land sellers do not agree to revised terms for the option agreements that are acceptable to the joint venture, it will not exercise further extension options which would have the effect of abandoning the project. Given the uncertainty over the ultimate outcome of these negotiations, we have taken impairment charges for our entire \$4.6 million investment in the project.

As of December 31, 2008, our aggregate capital contributions were \$2.5 million and our total investment in the Oxnard joint venture was \$3.3 million. In addition, as of December 31, 2008, we have incurred capitalized overhead costs of approximately \$800,000 for the project which are unreimbursed by the venture, bringing our total investment in the project to \$4.1 million. As of December 31, 2008, the non-managing member's aggregate capital contributions to the joint venture were \$6.5 million.

During the year ended December 31, 2008, we recorded an investment loss of \$4.6 million related to our investment in the joint venture which reflects our \$3.3 million investment in the venture, \$800,000 of unreimbursed project costs, and \$500,000 of deferred capital contributions that are payable to the non-managing member upon dissolution of the joint venture. The resulting loss allocation upon closing out the venture will be 66% to the non-managing member and 34% to us.

Homebuilding

Our homebuilding operations include active projects in the Huntington Beach, the Inland Empire (Beaumont), and Lancaster areas of Southern California. We delivered 55 homes during 2008, compared with 77 deliveries in 2007. We acquired no single-family residential lots during 2008, 2007 or 2006 and we have no contracts to acquire land or lots.

During 2008, we saw continued price depreciation and an excess supply of homes available for sale in the Inland Empire and Lancaster markets. Therefore, we have reduced sales prices and offered incentives for all of our homes in these markets in order to reduce our standing inventory and remain competitive during this continuing significant economic downturn in the housing market. The price reductions and additional incentives have resulted in significantly reduced gross profits for Inland Empire and Lancaster home sales. In addition, during the third quarter of 2008 we began selling the existing model homes at our Las Colinas project in Lancaster and will defer any further development of that project.

We recorded non-cash asset impairment charges of \$35.0 million for our inland projects during 2008, compared with \$32.0 million of asset impairment charges recorded during 2007. The impairment charges reflect our expectations about home prices, sales pace, sales and marketing costs, infrastructure and homebuilding costs and financing costs for our inland projects. The impairment charges were calculated based on market conditions and assumptions made by management that reflected current conditions at the time such impairment charges were determined, which may differ materially from actual results if market conditions change. As required by Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," ("SFAS 144"), we will reevaluate the expected cash flows from our homebuilding projects to determine whether any additional impairment exists should events or circumstances change.

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In view of the continuing downturn in the housing market, we currently expect that, during the next 12 months, our new home construction will primarily be at our 356-home Brightwater project in Huntington Beach; and that our operations in other markets will involve the sale of standing inventory, with limited or no new construction. In some inland markets, we may determine to sell additional existing model homes and re-open the projects when the market demonstrates improved sales levels. Our management has concluded that this strategy is necessary under the prevailing market conditions and may allow us to market the inland properties at some future time when market conditions may have improved.

Our homebuilding projects are described below:

	Location	Land Acquisition	Commenced Construction	Commenced Sales	Deliveries		
					2008	2007	2006
<u>Brightwater</u>							
The Trails	Huntington Beach	1970	2006	2007(a)	6	5	
The Sands	Huntington Beach	1970	2006	2007(a)	6	4	
The Cliffs	Huntington Beach	1970	2006	2008(b)	6		
The Breakers	Huntington Beach	1970	2006	2008(b)	5		
<i>Total Brightwater</i>					23	9	
<u>Inland Empire/Lancaster</u>							
Completed Projects	Various	n/a	n/a	n/a	6	21	
Chandler Ranch	North Corona	2004	2005	2005	4	21	58
Alisal at Ontario	Ontario	2005	2005	2006	8	9	9
Woodhaven	Beaumont	2005	2005	2006	6	10	15
Hearthside Lane	Corona	2005	2005	2007	7	3	
Alisal at Lancaster	Lancaster	2004	2004	2005	1	7	41
Las Colinas	Lancaster	2005	2006	2006	6	12	3
Future Community	Lancaster	2005	(c)	(c)			
<i>Total Inland Empire/Lancaster</i>					32	68	147
<i>Total Deliveries</i>					55	77	147

(a) Commenced in August 2007.

(b) Commenced in February 2008.

(c) To be determined subject to market conditions.

Huntington Beach. We completed construction of the first eight model homes for The Trails and The Sands products which range from 1,710 to 2,160 square feet during July 2007 and opened for sales in August 2007. We completed construction of nine model homes for The Cliffs and The Breakers in January 2008 and began selling homes to homebuyers who previously registered on our priority list in February 2008. We held a grand opening for The Cliffs and The Breakers on March 15, 2008. We delivered nine homes at an average price of \$1.2 million, or \$609 per square foot during 2007 and 23 homes during 2008, at an average price of \$1.4 million, or approximately \$564 per square foot. We delivered three additional homes at an average price of \$2.1 million through March 16, 2009. As of March 16, 2009, six Brightwater homes (including four homes with wetland and ocean views) are in escrow at an average price of \$2.1 million, or approximately \$690 per square foot, and 18 additional homes are completed or under construction and have been released for sale.

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Corona. We acquired 83 lots in North Corona known as Chandler Ranch in May 2004. Following construction of infrastructure, during April 2005 we began construction of homes averaging 3,160 square feet. We opened for sales during the third quarter of 2005 and delivered 58 homes during 2006

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at an average price of \$600,000. We delivered 21 homes during 2007 at an average price of \$511,000 and the final four homes during 2008 at an average price of \$434,000.

During April 2005, we acquired 151 additional lots in Corona known as Hearthside Lane. Following construction of infrastructure, construction of five model homes averaging 3,600 square feet on lots of approximately 7,200 square feet began during the fourth quarter of 2006. These models were completed during April 2007, and we opened for sales during the second quarter of 2007. We delivered three homes at an average price of \$545,000 during 2007 and seven homes at an average price of \$454,000 during 2008. As of March 16, 2009, five model homes and two production homes are completed and available for sale.

The subsidiary which owns the Hearthside Lane property is currently in default on the \$29.2 million project loan which matured in January 2009. The loan is non-recourse to California Coastal Communities, Inc.; however, the subsidiary's parent, Hearthside Homes, Inc. guaranteed payment of the debt. As of December 31, 2008, Hearthside Homes had a negative net worth of approximately \$64.0 million. On December 22, 2008, the lender, IndyMac Federal Bank, sold the loan to a third party investor. The sale of the loan did not alter any of the terms and conditions of the loan. In January 2009, the Hearthside Homes subsidiary received a notice of event of default from the new lender. Hearthside Homes' subsidiary is attempting to negotiate a consensual resolution of the loan default with the new lender which will involve turning over the property securing the loan to the lender. During the third quarter of 2008, we reduced the carrying value of the Hearthside Lane real estate project to its estimated fair value at that time of \$8.6 million. As of December 31, 2008, following delivery of an additional home, the carrying value of the project was \$8.2 million. If the Hearthside Lane property is transferred to the lender in full settlement of the loan, without further recourse or obligation, we will recognize a substantial gain as a result of debt cancellation. However, there can be no assurance that the lender will agree to a consensual resolution.

Beaumont. We acquired 102 lots in the City of Beaumont during the third quarter of 2005. Followin