Summit Hotel Properties, Inc.
Form S-11/A
September 23, 2010

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As filed with the United States Securities and Exchange Commission on September 22, 2010

Registration No. 333-168686

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

Amendment No. 1
to
Form S-11
FOR REGISTRATION UNDER THE SECURITIES ACT OF 1933
OF SECURITIES OF CERTAIN REAL ESTATE COMPANIES

SUMMIT HOTEL PROPERTIES, INC.
(Exact name of registrant as specified in governing instruments)

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Approximate date of commencement of proposed sale to the public: As soon as practicable after the effective date of this Registration Statement.

If any of the securities being registered on this form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act, check the following box: o

If this form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. o

If this form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. o

If this form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. o

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box. o

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

Large accelerated filer o	Accelerated filer o	Non-accelerated filer þ (Do not check if a smaller reporting company)	Smaller reporting company o

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the Registration Statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

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The information in this prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities, and it is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

Subject to Completion

PROSPECTUS

Shares of Common Stock

Summit Hotel Properties, Inc. is selling all of the common stock offered by this prospectus. Prior to this offering, there has been no public market for our common stock. The initial public offering price of our common stock is expected to be between $ and $ per share. We intend to apply to list our common stock on the New York Stock Exchange, or NYSE, under the symbol INN.

We intend to elect and qualify to be taxed as a real estate investment trust, or REIT, for federal income tax purposes. The common stock offered by this prospectus is subject to restrictions on ownership and transfer that are intended to, among other purposes, assist us in qualifying and maintaining our qualification as a REIT. Our charter generally limits beneficial and constructive ownership to no more than 9.8% in value or number of shares, whichever is more restrictive, of the outstanding shares of any class or series of our capital stock. See Description of Capital Stock Restrictions on Ownership and Transfer.

Investing in our common stock involves risks. See Risk Factors beginning on page 18 of this prospectus for a description of various risks you should consider in evaluating an investment in the shares.

	Per Share	**Total**
Public offering price	$	$
Underwriting discount	$	$
Proceeds, before expenses, to us	$	$

The underwriters have a 30-day option to purchase up to additional shares of common stock from us on the same terms set forth above to cover over-allotments, if any.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

Baird

The date of this prospectus is , 2010.

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You should rely only on the information contained in this prospectus and any free writing prospectus prepared by us. We have not, and the underwriters have not, authorized any other person to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. We are not, and the underwriters are not, making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. The information in this prospectus is current as of the date such information is presented. Our business, financial condition and results of operations and prospectus may have changed since those dates.

Through and including , 2010 (the 25th day after the date of this prospectus) federal securities law may require all dealers that effect transactions in these securities, whether or not participating in this offering, to deliver a prospectus. This requirement is in addition to the dealers obligation to deliver a prospectus when acting as underwriters and with respect to their unsold allotments or subscriptions.

This prospectus contains registered trademarks that are the exclusive property of their respective owners, which are companies other than us, including Marriott International, Inc., Hilton Worldwide, InterContinental Hotels Group, Hyatt Hotels Corp. and Resorts, Choice Hotels International, Inc. and Starwood Hotels and Resorts Worldwide, Inc. None of the owners of the trademarks appearing in this prospectus, their parents, subsidiaries or affiliates or any of their respective officers, directors, members, managers, stockholders, owners, agents or employees, which we refer to collectively as the trademark

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owners, is an issuer or underwriter of the shares being offered hereby, plays (or will play) any role in the offer or sale of our shares or has any responsibility for the creation or contents of this prospectus. In addition, none of the trademark owners has or will have any liability or responsibility whatsoever arising out of or related to the sale or offer of the shares being offered hereby, including any liability or responsibility for any financial statements, projections or other financial information or other information contained in this prospectus or otherwise disseminated in connection with the offer or sale of the shares offered by this prospectus. You must understand that, if you purchase our common stock in this offering, your sole recourse for any alleged or actual impropriety relating to the offer and sale of the common stock and the operation of our business will be against us (and/or, as may be applicable, the seller of such shares) and in no event may you seek to impose liability arising from or related to such activity, directly or indirectly, upon any of the trademark owners.

We use market data and industry forecasts and projections throughout this prospectus, including data from publicly available information and industry publications. These sources generally state that the information they provide has been obtained from sources believed to be reliable, but that the accuracy and completeness of the information are not guaranteed. The forecasts and projections are based on industry surveys and the preparers experience in the industry and there can be no assurance that any of the projections will be achieved. We believe that the surveys and market research others have performed are reliable, but we have not independently verified this information.

Summary

The following summary highlights information contained elsewhere in this prospectus. This summary is not complete and does not contain all of the information that you should consider before investing in our common stock. You should read the following summary together with the more detailed information regarding our company and an investment in our common stock, including the information under the caption Risk Factors and the historical and pro forma financial statements, including the related notes, appearing elsewhere in this prospectus. Unless the context otherwise requires or indicates, references in this prospectus to our predecessor refer to Summit Hotel Properties, LLC and its consolidated subsidiaries, including Summit Group of Scottsdale, Arizona, LLC, or Summit of Scottsdale. Unless the context otherwise requires or indicates, references in this prospectus to we, our, us, our company and the compar refer to Summit Hotel Properties, Inc., a Maryland corporation, together with its consolidated subsidiaries, including Summit Hotel OP, LP, a Delaware limited partnership, which we refer to in this prospectus as the operating partnership and Summit Hotel TRS, Inc., a Delaware corporation, which we refer to in this prospectus as Summit TRS. We refer to Summit TRS and the wholly owned subsidiaries of Summit TRS that will lease our hotels from our operating partnership as our TRS lessees.

In addition, unless the context otherwise requires or indicates, the information set forth in this prospectus assumes that: (i) the formation transactions described elsewhere in this prospectus have been completed; (ii) the underwriters over-allotment option is not exercised; (iii) the common stock to be sold in the offering is sold at $ per share, which is the mid-point of the initial public offering price range shown on the cover of this prospectus; and (iv) the value of each unit of limited partnership interest in our operating partnership, which we refer to as an OP unit, issued in the formation transactions is equivalent to the initial public offering price of one share of our common stock.

Overview

We are a self-managed hotel investment company that was recently organized to continue and expand the existing hotel investment business of our predecessor, Summit Hotel Properties, LLC, a leading U.S. hotel owner. We will focus exclusively on acquiring and owning premium-branded limited-service and select-service hotels in the upscale and midscale without food and beverage segments of the U.S. lodging industry. Following completion of this offering and the formation transactions, our initial portfolio will consist of 65 hotels with a total of 6,533 guestrooms located in 19 states. Our initial portfolio consists of what we consider both seasoned and unseasoned hotels that are located in markets in which we have extensive experience and that exhibit multiple demand generators, such as business and corporate headquarters, retail centers, airports and tourist attractions. Based on total number of rooms, 48% of our portfolio is positioned in the top 50 metropolitan statistical areas, or MSAs, and 68% is located within the top 100 MSAs.

Entities controlled by our Executive Chairman, Kerry W. Boekelheide, have been in the business of acquiring, developing, financing, operating and selling hotels since 1991, have acquired a total of 93 hotels in transactions having an aggregate value of approximately $606.8 million, and have sold, transferred or otherwise disposed of a total of 27 hotels in transactions having an aggregate value of approximately $104.6 million.

The majority of our hotels operate under premium franchise brands owned by Marriott International, Inc. (Courtyard by Marriott, Residence Inn, SpringHill Suites, Fairfield Inn and TownePlace Suites), Hilton Worldwide (Hampton Inn, Hampton Inn & Suites and Hilton Garden Inn), InterContinental Hotels Group (Holiday Inn Express and Staybridge Suites) and Hyatt Hotels and Resorts (Hyatt Place).

Since January 1, 2007, we have made approximately $305.4 million of capital investment through strategic acquisitions and upgrades and improvements to our hotels to be well-positioned for improving general lodging fundamentals. Further, we expect to use up to approximately $10.0 million of the net proceeds of this offering to make additional capital improvements to hotels in our portfolio. We believe the U.S. economy has begun to recover from the recent economic recession and, as a result, lodging industry fundamentals will strengthen over the near-term. As a result, we believe our portfolio is well-positioned for significant internal growth in hotel operating revenues in this environment based on our mix of seasoned hotels and unseasoned hotels.

We intend to identify and acquire undermanaged and underperforming hotels and use our expertise to renovate, rebrand and reposition the hotels to improve cash flows and long-term value. We believe we will be able to source a significant volume of acquisition opportunities, particularly due to the relative size of our target lodging industry segments, lack of available debt financing in the capital markets and the weakness experienced since mid-2008 in the lodging industry. We also believe that,

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while other public REITs and well-capitalized institutional owners seek to acquire assets that fit our investment criteria, we will be the only publicly traded REIT focused solely on these segments on a national basis.

We were organized as a Maryland corporation on June 30, 2010 and intend to elect to be taxed as a REIT for federal income tax purposes beginning with our short taxable year ending December 31, 2010. We will conduct substantially all of our business through our operating partnership, Summit Hotel OP, LP, a Delaware limited partnership. See Structure of Our Company.

Our Competitive Strengths

High-Quality Portfolio of Hotels. Our initial portfolio is composed of 65 hotels located in 19 states and that have an average age of 10.3 years. No single hotel accounted for more than 3.6% of our predecessor s hotel operating revenues for the 12-month period ended June 30, 2010. We believe all of our hotels are located in markets where there will be limited growth in lodging supply over the next several years. Additionally, in many of our markets, we own two or more hotels in close proximity to each other, which we believe allows our hotel managers to maintain rate integrity and maximize occupancy by referring travelers to our other hotels. Franchise areas of protection, which prohibit the opening of hotels with the same brand as one of our hotels within certain proximities of our hotels, provide barriers to entry in suburban markets where many of our hotels are located.

Seasoned Portfolio and Significant Upside Potential. Our initial portfolio is composed of 46 seasoned hotels with established track records and strong positions within their markets. We classify our other 19 hotels, which were either built after January 1, 2007 or experienced a brand conversion since January 1, 2008, as unseasoned. We believe that the market penetration of our unseasoned hotels is significantly less than that of our seasoned hotels due to the dramatic economic slowdown over the past two years that delayed these hotels from achieving anticipated growth rates and revenues. However, most of our unseasoned hotels are newer, larger and are located in larger markets than our seasoned hotels and operate under premium brands. As a result, we believe our unseasoned hotels can experience significant growth in RevPAR and profitability as the economy and industry fundamentals improve.

Experienced Executive Management Team With a Proven Track Record. Our management team, led by our Executive Chairman, Mr. Boekelheide, has extensive experience acquiring, developing, owning, operating, renovating, rebranding and financing hotel properties. Through this experience, our management team has developed strong execution capabilities as well as an extensive network of industry, corporate and institutional relationships, including relationships with the leading lodging franchisors in our targeted markets. We believe these relationships will provide insight and access to attractive investment opportunities and allow us to react to local market conditions by seeking the optimal franchise brand for the market in which each of our hotels is located.

Aggressive Asset Management and Experienced Asset Management Team. We will maintain a dedicated asset management team led by our Executive Vice President and Chief Operating Officer, Mr. Aniszewski, to analyze our portfolio as a whole and oversee our independent hotel managers. Our asset management team has managed hotel assets in every industry segment through multiple hotel business cycles. Our entire asset management team has worked together at The Summit Group, Inc., or The Summit Group, the manager of our predecessor and its hotels, for the last 10 years, which provides us expertise, operational stability and in-depth knowledge of our portfolio. We will work proactively with our hotel managers to continue to drive operational performance by identifying and implementing strategies to optimize hotel profitability through revenue management strategies, budgeting, analyzing cost structure, market positioning, evaluating and making capital improvements and continually reviewing and refining our overall business strategy. Among other techniques, we initially will employ three full-time asset managers who will assist our hotel management companies to structure room rate plans and develop occupancy strategies to achieve optimum revenues.

Strategic Focus on Largest Segments of Lodging Industry. We believe we will be the only publicly traded REIT that focuses exclusively on upscale hotels and midscale without food and beverage hotels on a national basis. By number of rooms, 81% of our hotels operate under brands owned by Marriott, Hilton, Intercontinental or Hyatt, which are generally regarded as the premium global franchises in our segments. We believe that business and leisure travelers prefer the consistent service and quality associated with these nationally recognized premium brands, and that brand serves as a significant driver of demand for hotel rooms. As reported by Smith Travel Research in 2010, of the approximately 29,735 branded hotels in the United States, 13,066 hotels, or 43.9%, are within our target segments (upscale: 3,536 hotels; midscale without food and beverage: 9,530 hotels). The size of this market represents a potential acquisition pool

significantly larger than the upper upscale (1,669 hotels, or 5.6%, of total branded hotels) or luxury (341 hotels, or 1.2%, of total branded hotels) segments. We believe the fragmented ownership of premium-branded limited-service and select-service hotels in the upscale and midscale without food and beverage segments, the size of the segments, our longstanding relationships with franchisors, the lack of well-capitalized competitors and our extensive experience and expertise provide us a distinct competitive advantage and a significant opportunity to profitably grow our company.

Growth-Oriented Capital Structure. Upon completion of this offering and the formation transactions, we expect to employ a prudent leverage structure that will provide us the ability to make strategic acquisitions as industry fundamentals and the lending environment improves. Upon completion of this offering and application of the net proceeds as described in Use of Proceeds, we will have approximately $ million in outstanding indebtedness and hotels unencumbered by indebtedness, including hotels with rooms operating under premium brands owned by Marriott, Hilton, Intercontinental or Hyatt available to secure future loans. We believe our capital structure positions us well to capitalize on what we expect to be significant acquisition opportunities.

Summary Risk Factors

An investment in our common stock involves various risks. You should carefully consider the matters discussed in Risk Factors beginning on page 18 of this prospectus before you decide whether to invest in our common stock. Some of the risks include the following:

§ Our business strategy depends significantly on achieving revenue and net income growth from anticipated increases in demand for hotel rooms any delay or a weaker than anticipated economic recovery will adversely affect our future results of operations and our growth prospects.

§ Our unseasoned hotels have limited operating history and may not achieve the operating performance we anticipate, and as a result, our overall returns may not improve as we expect or may decline.

§ We have no operating history as a publicly traded REIT and may not be successful in operating as a publicly traded REIT, which may adversely affect our ability to make distributions to our stockholders.

§ Our success depends on key personnel whose continued service is not guaranteed.

§ We may be unable to complete acquisitions that would grow our business, and even if they are completed, we may fail to successfully integrate and operate such acquired hotels.

§ Upon completion of this offering and the formation transactions, the management of all of the hotels in our portfolio will be concentrated in one hotel management company, , and termination of our hotel management agreement with that company may cause us to pay substantial termination fees or experience significant disruptions at our hotels.

§ Funds spent to maintain franchisor operating standards, the loss of a franchise license or a decline in the value of a franchise brand may have a material adverse effect on our business and financial results.

§ We will rely on external sources of capital to fund future capital needs, and if we encounter difficulty in obtaining such capital we may not be able to make future acquisitions necessary to grow our business or meet maturing obligations.

§

We have a significant amount of debt, and our organizational documents have no limitation on the amount of additional indebtedness that we may incur in the future. As a result, we may become highly leveraged in the future, which could adversely affect our financial condition.

§ The agreements governing our indebtedness place restrictions on us and our subsidiaries, reducing operational flexibility and creating default risks.

§ We may not be able to obtain a credit facility.

§ Our Executive Chairman, Mr. Boekelheide, and other members of our management team exercised significant influence with respect to the terms of the formation transactions, including transactions in which they determined the compensation they would receive.

- § Competition from other upscale and midscale without food and beverage hotels in the markets in which we operate could have a material adverse effect on our results of operations.
- § Our operating results and ability to make distributions to our stockholders may be adversely affected by the markets in which we operate and risks inherent to the ownership of hotels.
- § Illiquidity of real estate investments could significantly impede our ability to respond to adverse changes in the performance of hotels in which we may invest or to adjust our portfolio in response to changes in economic and other conditions, and, therefore, may harm our financial condition.
- § We may change the distribution policy with respect to our common stock in the future.
- § The cash available for distribution may not be sufficient to make distributions at expected levels, and we cannot assure you of our ability to make distributions in the future. We may use borrowed funds or funds from other sources to make distributions, which may adversely impact our operations.
- § We may use a portion of the net proceeds from this offering to make distributions to our stockholders, if necessary to permit us to satisfy the requirements for qualification as a REIT and eliminate federal income and excise taxes that otherwise would be imposed on us, which would, among other things, reduce our cash available for investing.
- § If you purchase shares of common stock in this offering, you will experience immediate dilution.
- § Failure to qualify as a REIT, or failure to remain qualified as a REIT, would cause us to be taxed as a regular corporation, which would substantially reduce funds available for distributions to our stockholders.

Our Growth Strategies and Investment Criteria

Our strategy focuses on maximizing the cash flow of our portfolio through focused asset management and targeted capital investment. Our primary objective is to enhance stockholder value over time by generating strong risk-adjusted returns for our stockholders. We believe we can create long-term value by pursuing the following strategies.

Internal Growth from Strengthening Lodging Industry Fundamentals. We believe our hotels will experience significant revenue growth as lodging industry fundamentals recover from the economic recession which caused industry-wide RevPAR to suffer a combined 18.4% decline in 2008 and 2009, according to Smith Travel Research. Industry conditions have shown improvement during the first eight months of 2010, with RevPAR growth across all segments of 4.0% as compared to the same period of 2009, according to Smith Travel Research. Colliers PKF Hospitality Research forecasts significant compound annual growth in RevPAR from 2010 to 2014 of 7.0% for the upscale segment and 8.5% for the midscale without food and beverage segment, the best forecast for any segment in the industry.

Disciplined Acquisition of Hotels. We intend to grow through acquisitions of existing hotels using a disciplined and targeted approach while maintaining a prudent leverage structure. We employ a proactive and continuous assessment of our hotels, markets and brands in order to quickly and efficiently upgrade our hotels as market conditions warrant. We intend to target upscale and midscale without food and beverage hotels that meet one or more of the following acquisition criteria:

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have potential for strong risk-adjusted returns located in the Top 50 MSAs, with a secondary focus on the next 100 markets;

§ operate under leading franchise brands, which include but are not limited to Marriott, Hilton, InterContinental and Hyatt;

§ are located in close proximity to multiple demand generators, including businesses and corporate headquarters, retail centers, airports, medical facilities, tourist attractions and convention centers, with a diverse source of potential guests, including corporate, government and leisure travelers;

§ are located in markets exhibiting barriers to entry due to franchise areas of protection or other factors;

§ can be acquired at a discount to replacement cost; and

§ provide an opportunity to add value through improved operating efficiencies, repositioning, renovation or rebranding.

Selective Hotel Development. We believe there will be attractive opportunities to partner on a selective basis with experienced hotel developers to acquire, upon completion, newly constructed hotels that meet our investment criteria.

Strategic Hotel Sales. Our strategy is to acquire and own hotels. However, consistent with our strategy of maximizing the cash flow of our portfolio and our return on invested capital, we periodically review hotels to determine if any significant

changes to area markets or our hotels have occurred or are anticipated to occur that would warrant the sale of a particular hotel.

Our Industry and Market Opportunity

We focus on hotels in the upscale and midscale without food and beverage segments of the lodging industry.

We believe that our focus on these segments provides us the opportunity to achieve stronger risk-adjusted returns across multiple lodging cycles than if we owned hotels in other segments of the lodging industry for several reasons, including:

RevPAR Growth. Colliers PKF Hospitality Research forecasts that our market segments will experience the largest amount of RevPAR growth of any segment in the industry.

Consistently Strong and Growing Demand. Over the last twenty years, our market segments have demonstrated the strongest compounded growth in demand of all segments of the lodging industry, and strong demand growth is expected to continue.

More Stable Cash Flow Potential. Our hotels can be operated with fewer employees than full-service hotels that offer more expansive food and beverage options, which we believe enables us to generate more consistent cash flows with less volatility resulting from reductions in RevPAR and less dependence on group travel.

Broad Customer Base. Our target brands deliver consistently high-quality hotel accommodations with value-oriented pricing that we believe appeals to a wider range of customers, including both business and leisure travelers, than more expensive full-service hotels. We believe that our hotels are particularly popular with frequent business travelers who seek to stay in hotels operating under Marriott, Hilton, Hyatt or InterContinental brands, which offer strong loyalty rewards program points that can be redeemed for family travel.

Enhanced Diversification. Premium select-service assets generally cost significantly less, on a per-key basis, than hotels in the midscale with food and beverage, upper upscale and luxury segments of the industry. As a result, we can diversify our ownership into a larger number of hotels than we could acquire in other segments.

Lodging Industry Fundamentals. Beginning in August 2008, the U.S. lodging industry experienced 19 consecutive months of RevPAR declines, as measured against the same month in the prior year, driven by a combination of deterioration in room-night demand and increasing supply. Although the lodging industry has historically lagged broader economic recoveries, economic fundamentals are beginning to improve from the recent declines resulting from the recessionary environment. In June 2010, the U.S. unemployment rate continued to show improvement from its high in late 2009. After continuing declines for almost two years prior, June 2010 marked the U.S. lodging industry s fourth consecutive month of positive year-over-year RevPAR growth with an 8.0% increase.

According to Smith Travel Research, RevPAR increased 4.3% and 2.2% in our target upscale and midscale without food and beverage segments, respectively, for the first eight months of 2010 as compared to the same period of 2009, and we expect RevPAR growth to continue as the U.S. economy continues to strengthen. Colliers PKF Hospitality Research currently projects RevPAR growth of upscale hotels to be 4.2% in 2011, 11.1% in 2012 and 9.5% in 2013 and RevPAR growth of midscale without food and beverage hotels to be 5.9% in 2011, 12.2% in 2012 and 10.9% in 2013, among the highest in any industry segment. We expect that our hotels, and particularly our unseasoned hotels, will realize significant RevPAR gains as the economy and lodging industry improve.

Demand Overview. Room-night demand in the U.S. lodging industry is directly correlated to macroeconomic trends. Key drivers of demand include growth in gross domestic product, or GDP, corporate profits, capital investments and employment. Following periods of recession, recovery in room-night demand for lodging historically has lagged improvements in the overall economy.

Supply Overview. Growth in lodging supply typically lags growth in room-night demand. Key drivers of lodging supply include the availability and cost of capital, construction costs, local real estate market conditions and availability and pricing of existing properties. As a result of scarcity of financing, the severe recession and declining operating fundamentals during 2008 and 2009, many planned hotel developments have been cancelled or postponed, and the number of rooms under construction and in planning has declined significantly. According to Lodging Econometrics, during the second quarter of 2010, approximately 68,000 new hotel rooms were under construction in the U.S., as compared to approximately 242,000 rooms under construction in the second quarter of 2008, a decline of 72%. New hotel construction is expected to remain below historical averages through 2014 according to Colliers PKF Hospitality Research.

Attractive Transaction Landscape. We believe that the significant decline in lodging fundamentals and cash flows has created a difficult environment for hotel owners lacking ready access to financing or suffering from reduced cash flows due to declining industry fundamentals since 2008. As a result, we believe that the significant number of hotel properties experiencing substantial declines in operating cash flow, coupled with tight credit markets, near-term debt maturities and, in some instances, covenant defaults relating to outstanding indebtedness, will present attractive investment opportunities to acquire hotel properties at prices significantly below replacement cost, with substantial appreciation potential as the U.S. economy recovers from the current recession.

Our Formation Transactions

Historically, the 65 hotels in our initial portfolio were owned or controlled by our predecessor and were managed by The Summit Group, which is wholly owned and controlled by our Executive Chairman, Mr. Boekelheide. We will engage in the transactions described below, which we refer to as our formation transactions, in order to consolidate the business of our predecessor into a publicly traded REIT.

§ We will sell shares of our common stock in this offering.

§ We will contribute the net proceeds of this offering to our operating partnership in exchange for OP units. We will continue to be the sole general partner of our operating partnership and will own an approximate % (% if the underwriters exercise their over-allotment option in full) partnership interest in our operating partnership upon completion of the formation transactions and this offering.

§ Our predecessor will merge with and into our operating partnership, which will be the survivor of the merger. Pursuant to the merger, our predecessor s members, including two of our executive officers and their affiliates as described below, will receive an aggregate of 9,993,992 OP units having an aggregate assumed value of $ based on the mid-point of the anticipated initial public offering price range shown on the cover of this prospectus. The total number of OP units to be issued to our predecessor s members in the merger reflects our predecessor s 100% ownership of 63 of our initial hotels prior to the merger and its ownership of a 49% Class A membership interest in Summit of Scottsdale, the owner of two Scottsdale, Arizona hotels prior to the merger. Of the 9,993,992 OP units to be issued in the merger, (1) our Executive Chairman, Mr. Boekelheide, and his affiliates, including The Summit Group, will receive an aggregate of 1,517,879 OP units having an aggregate assumed value of $ based on the mid-point of the anticipated initial public offering price range shown on the cover of this prospectus and (2) our Executive Vice President and Chief Operating Officer, Craig J. Aniszewski, will receive an aggregate of 4,105 OP units having an aggregate value of $ based on the mid-point of the anticipated initial public offering price range shown on the cover of this prospectus. The merger is subject to customary closing conditions, including obtaining all required third-party consents and approvals and completion of this offering. In addition to the OP units issued in the merger, our operating partnership will issue 106,800 OP units pursuant to the Summit of Scottsdale transaction described below.

§ The Summit Group will contribute its 36% Class B membership interest in Summit of Scottsdale to our operating partnership in exchange for 74,829 OP units having an aggregate assumed value of $ based on the mid-point of the anticipated initial public offering price range shown on the cover of this prospectus. An unaffiliated third-party investor will contribute its 15% Class C membership interest in Summit of Scottsdale to our operating partnership in exchange for 31,179 OP units having an aggregate assumed value of $ based on the mid-point of the anticipated initial public offering price range shown on the cover of this prospectus. The contributions of the Class B and Class C membership interests in Summit of Scottsdale are subject to customary closing conditions, including obtaining all required third-party consents and approvals and

completion of this offering.

Our predecessor s 49% Class A membership interest in Summit of Scottsdale will be acquired through the merger described above. Our predecessor owns a 49% Class A membership interest in Summit of Scottsdale, which our operating partnership will acquire in the merger. As a result of these contributions and the merger, our operating partnership will assume approximately $13.8 million of existing mortgage debt secured by the Courtyard by Marriott and the SpringHill Suites by Marriott, both located in Scottsdale, Arizona, or the Scottsdale hotels, and will become the sole owner of the two Scottsdale hotels.

§ Upon completion of the merger and the contributions described above, our operating partnership will become the sole owner of our 65 initial hotels and will enter into new lease agreements with our TRS lessees with respect to the 65 hotels in our initial portfolio.

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§ The Summit Group will assign all of the hotel management agreements pursuant to which it managed the hotels owned by our predecessor to for consideration payable to the Summit Group of , and our TRS lessees will enter into hotel management agreements with pursuant to which our initial hotels will be operated.

§ Our operating partnership intends to use the net proceeds of this offering as follows: (1) approximately $ million to repay or extinguish existing indebtedness that we will assume following completion of the formation transactions, including estimated costs related to debt repayment totaling approximately $ million; (2) approximately $10.0 million to fund capital improvements at our initial hotels; and (3) the balance for general corporate and working capital purposes, including possible future acquisitions of hotels.

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Our Structure

The following diagram depicts our ownership structure immediately following completion of this offering and the formation transactions:

Material Benefits to Related Parties

Upon completion of this offering and the formation transactions, certain of our executive officers and directors will receive, either directly or indirectly, the financial and other benefits summarized below. For a more detailed discussion of these benefits see Management and Certain Relationships and Related Transactions.

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Formation Transactions. In connection with the formation transactions, Mr. Boekelheide, our Executive Chairman, and his affiliates, including The Summit Group, which is wholly owned and controlled by Mr. Boekelheide, and Mr. Aniszewski, our Executive Vice President and Chief Operating Officer, will receive the following benefits:

Name	Benefits Received
Kerry W. Boekelheide, *Executive Chairman and Director*	In the formation transactions, Mr. Boekelheide and The Summit Group will receive an aggregate of 1,200,993 OP units, including: (1) 17,000 OP units to be issued to a revocable trust, the trustee and sole beneficiary of which is Mr. Boekelheide, in exchange for the trust s Class A membership interests in our predecessor; (2) 1,109,164 OP units to be issued to The Summit Group in the merger; and (3) 74,829 OP units to be issued to The Summit Group in exchange for its 36% Class B membership interest in Summit of Scottsdale. These OP units will represent approximately % of our combined common stock and OP units outstanding upon completion of this offering and the formation transactions and have an aggregate value of $ million based on the mid-point of the anticipated initial public offering price range shown on the cover of this prospectus. In addition, entities affiliated with Mr. Boekelheide other than The Summit Group will receive an aggregate of 316,886 OP units. Mr. Boekelheide will share voting and investment power over these OP units with individuals who are not affiliated with us. These OP units will represent approximately % of our combined common stock and OP units outstanding upon completion of this offering and the formation transactions and have a combined aggregate value of $ million based on the mid-point of the anticipated initial public offering price range shown on the cover of this prospectus. In consideration for assigning to them the existing hotel management agreements with our predecessor, The Summit Group will receive a cash payment from in the amount of $.
Craig J. Aniszewski, *Executive Vice President and Chief Operating Officer*	In the merger, Mr. Aniszewski will receive an aggregate of 4,105 OP units in exchange for his Class B membership interests in our predecessor. These OP units represent approximately % of our combined common stock and OP units outstanding upon completion of this offering and the formation transactions and have an aggregate value of $ based on the mid-point of the anticipated initial public offering price range shown on the cover of this prospectus.

In addition to the OP units and other material benefits described above to be received in connection with the formation transactions, our executive officers will also benefit from the following:

- § employment agreements that will provide for salary, bonus and other benefits, including severance benefits in the event of a termination of employment in certain circumstances (see Management Employment Agreements);
- § options to purchase an aggregate of shares of our common stock at the initial public offering price of the shares in this offering that will be granted to our executive officers upon completion of this offering pursuant

to the 2010 Equity Incentive Plan (see Management Executive Compensation);

- agreements providing for indemnification by us for certain liabilities and expenses incurred as a result of actions brought, or threatened to be brought, against them as an officer and/or director of our company (see Management Indemnification Agreements and Material Provisions of Maryland Law and of Our Charter and Bylaws); and

- redemption and registration rights under our operating partnership s partnership agreement with respect to OP units to be issued in the formation transactions (see Description of the Partnership Agreement).

Furthermore, in connection with the formation transactions, our operating partnership will offer to enter into tax protection agreements with a limited number of the members of our predecessor, including The Summit Group and Mr. Aniszewski. See Formation Transactions Tax Protection Agreements.

Our Financing Strategy

We expect to maintain a prudent capital structure and intend to limit the sum of the outstanding principal amount of our consolidated net indebtedness to not more than 5.5x of our earnings before interest, tax, depreciation and amortization, or EBITDA, for the 12-month period preceding the incurrence of such debt. Over time, we intend to finance our long-term growth with common and preferred equity issuances and debt financing having staggered maturities. Our debt may include mortgage debt secured by hotels and unsecured debt.

Following completion of this offering, we anticipate entering into a credit facility to fund future acquisitions, as well as for property redevelopments, capital expenditures and working capital requirements. We may not succeed in obtaining a credit facility on favorable terms or at all. We cannot predict the size of the credit facility if we are able to obtain one.

When purchasing hotel properties, we may issue OP units as full or partial consideration to sellers who may desire to take advantage of tax deferral on the sale of a hotel or participate in the potential appreciation in value of our common stock.

Conflicts of Interest

Following completion of this offering and the formation transactions, there will be conflicts of interest between the holders of OP units, including certain of our executive officers and directors, and our stockholders with respect to certain transactions. In addition to their ownership of OP units, these executive officers and directors may have conflicting duties because, in their capacities as our executive officers and directors, they have a duty to us and our stockholders, while at the same time, in our capacity as general partner of our operating partnership, they have a fiduciary duty to the limited partners. Conflicts may arise when the interests of our stockholders and the limited partners of the operating partnership diverge, particularly in circumstances in which there may be an adverse tax consequence to the limited partners. For example, the sale of any of the hotels in our portfolio or the repayment of indebtedness may have different tax consequences to holders of OP units as compared to our stockholders. The amended and restated limited partnership agreement of the operating partnership contains a provision that in the event of a conflict of interest between our stockholders and the limited partners of our operating partnership, we will endeavor in good faith to resolve the conflict in a manner not adverse to either our stockholders or the limited partners of our operating partnership, and, if we, in our sole discretion as general partner of the operating partnership, determine that a conflict cannot be resolved in a manner not adverse to our stockholders and the limited partners of our operating partnership, the conflict will be resolved in favor of our stockholders. Our board of directors has adopted a policy that any transaction involving our company in which a director has an interest must be approved by a majority of the disinterested directors.

Both we and our predecessor have sought to structure the formation transactions so as to minimize potential conflicts of interest, including by appointing a special committee of our predecessor s independent managers to review the terms of the proposed merger of our predecessor into our operating partnership. However, we did not conduct arm s-length negotiations with our predecessor s members or the members of Summit of Scottsdale with respect to the terms of the formation transactions, including the merger. Our Executive Chairman, Mr. Boekelheide, and his affiliates, including The Summit Group, have substantial, pre-existing ownership interests in our predecessor and Summit of Scottsdale. In addition, Mr. Aniszewski, our Executive Vice President and Chief Operating Officer, has a pre-existing ownership interest in our predecessor. Both Mr. Boekelheide and Mr. Aniszewski sat on the board of managers of our predecessor that approved the terms of the formation transactions. In the course of structuring the formation transactions, Mr. Boekelheide and Mr. Aniszewski had the ability to influence the type and level of benefits they will receive from us. Although our predecessor s special committee received a fairness opinion from an independent

third-party financial advisor that is not one of the underwriters of this offering with respect to the fairness, from a financial point of view, of the merger consideration to the former members of our predecessor, assuming that the value of the OP units issued as the merger consideration was between $140 million and $160 million, we did not obtain a fairness opinion with respect to the fairness of the merger consideration to us and we did not obtain recent third-party appraisals for all of the hotels to be acquired by us in the formation transactions. As a result, the consideration to be paid by us to the members of our predecessor in the merger and the acquisition of the 49% ownership interest in the two Scottsdale hotels may exceed the fair market value of the hotels and other assets being acquired by us in the formation transactions.

Our Tax Status

We intend to elect to be taxed as a REIT for federal income tax purposes commencing with our short taxable year ending December 31, 2010. Our qualification as a REIT will depend upon our ability to meet, on a continuing basis, through actual investment and operating results, various complex requirements under the Internal Revenue Code, as

amended, or the Code, relating to, among other things, the sources of our gross income, the composition and values of our assets, our distribution levels and the diversity of ownership of our shares of capital stock. We believe that we will be organized in conformity with the requirements for qualification as a REIT under the Code and that our intended manner of operation will enable us to meet the requirements for qualification and taxation as a REIT for federal income tax purposes commencing with our short taxable year ending December 31, 2010 and continuing thereafter.

In order for the income from our hotel operations to constitute rents from real property for purposes of the gross income tests required for REIT qualification, we cannot directly operate any of our hotel properties. Instead, we must lease our hotel properties. Accordingly, we will lease each of our hotel properties to one of our TRS lessees, which will be wholly owned by our operating partnership. Our TRS lessees will pay rent to us that can qualify as rents from real property, provided that the TRS lessees engage eligible independent contractors to manage our hotels. A TRS is a corporate subsidiary of a REIT that jointly elects with the REIT to be treated as a TRS of the REIT and that pays federal income tax at regular corporate rates on its taxable income. We expect that all of the hotels in our portfolio will be leased to one of our TRS lessees, which will be able to pay us rent out of the revenue of the hotels. Our TRS lessees will engage to manage the hotels in our initial portfolio. We believe will qualify as an eligible independent contractor.

As a REIT, we generally will not be subject to federal income tax on our REIT taxable income that we distribute currently to our stockholders. Under the Code, REITs are subject to numerous organizational and operational requirements, including a requirement that they distribute each year at least 90% of their taxable income, determined without regard to the deduction for dividends paid and excluding any net capital gains. If we fail to qualify for taxation as a REIT in any taxable year and do not qualify for certain statutory relief provisions, our income for that year will be taxed at regular corporate rates, and we will be disqualified from taxation as a REIT for the four taxable years following the year during which we ceased to qualify as a REIT. Even if we qualify as a REIT for federal income tax purposes, we may still be subject to state and local taxes on our income and assets and to federal income and excise taxes on our undistributed income. Additionally, any income earned by our TRS lessees will be fully subject to federal, state and local corporate income tax.

Distribution Policy

To qualify as a REIT, we must distribute annually to our stockholders an amount at least equal to 90% of our REIT taxable income, determined without regard to the deduction for dividends paid and excluding any net capital gain. We will be subject to income tax on our taxable income that is not distributed and to an excise tax to the extent that certain percentages of our taxable income are not distributed by specified dates. See Material Federal Income Tax Considerations. Income as computed for purposes of the foregoing tax rules will not necessarily correspond to our income as determined for financial reporting purposes. Our cash available for distribution may be less than the amount required to meet the distribution requirements for REITs under the Code, and we may be required to borrow money, sell assets or issue capital stock to satisfy the distribution requirements. Additionally, we may pay future distributions from the proceeds from this offering or other securities offerings.

We intend to make regular quarterly cash distributions to our stockholders, as more fully described below. We plan to pay a pro rata dividend with respect to the period commencing on completion of this offering and ending , based on a rate of $ per share for a full quarter. On an annualized basis, this would be $ per share, or an estimated initial annual dividend rate of approximately % based on the mid-point of the anticipated initial public offering price range shown on the cover of this prospectus. We do not intend to reduce the expected dividend per share if the underwriters option to purchase additional shares is exercised.

The timing and frequency of distributions will be authorized by our board of directors and declared by us based upon a variety of factors deemed relevant by our directors, including restrictions under applicable law and our loan

agreements, capital requirements of our company and the REIT requirements of the Code. Distributions to stockholders generally will be taxable to our stockholders as ordinary income, although a portion of such distributions may be designated by us as long-term capital gain or may constitute a return of capital. We will furnish annually to each of our stockholders a statement setting forth distributions paid during the preceding year and their federal income tax status. For a discussion of the federal income tax treatment of our distributions, see Material Federal Income Tax Considerations.

Restrictions on Ownership of Our Capital Stock

In order to assist us in qualifying as a REIT, our charter, subject to certain exceptions, restricts the amount of shares of our capital stock that a person may beneficially or constructively own. Our charter provides that, subject to certain exceptions,

no person may beneficially or constructively own more than 9.8% in value or in number of shares, whichever is more restrictive, of the outstanding shares of any class or series of our capital stock. Our charter also prohibits any person from:

§ beneficially owning shares of our capital stock to the extent that such beneficial ownership would result in our being closely held within the meaning of Section 856(h) of the Code (without regard to whether the ownership interest is held during the last half of the taxable year);

§ transferring shares of our capital stock to the extent that such transfer would result in shares of our capital stock being beneficially owned by fewer than 100 persons (determined under the principles of Section 856(a)(5) of the Code);

§ beneficially or constructively owning shares of our capital stock to the extent such beneficial or constructive ownership would cause us to constructively own ten percent or more of the ownership interests in a tenant (other than a TRS) of our real property within the meaning of Section 856(d)(2)(B) of the Code; or

§ beneficially or constructively owning or transferring shares of our capital stock if such beneficial or constructive ownership or transfer would otherwise cause us to fail to qualify as a REIT under the Code, including, but not limited to, as a result of any hotel management companies failing to qualify as an eligible independent contractor under the REIT rules.

Our board of directors, in its sole discretion, may prospectively or retroactively exempt a person from certain of these limits and may establish or increase an excepted holder percentage limit for such person. The person seeking an exemption must provide to our board of directors such representations, covenants and undertakings as our board of directors may deem appropriate in order to conclude that granting the exemption will not cause us to lose our status as a REIT.

Our Corporate Information

We were formed as a Maryland corporation on June 30, 2010 and intend to elect and qualify to be taxed as a REIT for federal income tax purposes commencing with our short taxable year ending December 31, 2010. Our corporate offices are located at 2701 South Minnesota Avenue, Suite 6, Sioux Falls, South Dakota 57105. Our telephone number is (605) 361-9566. Our website is *www.shpreit.com*. The information contained on, or accessible through, our website is not incorporated by reference into this prospectus and should not be considered a part of this prospectus.

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The Offering

Common stock offered by us	shares
Common stock to be outstanding after this offering and the formation transactions	shares[1]
Common stock and OP units to be outstanding after this offering and the formation transactions	shares and OP units[2]
Use of proceeds	We estimate that we will receive net proceeds from this offering of approximately $ million, or approximately $ million if the underwriters over-allotment option is exercised in full, after deducting the underwriting discounts and commissions and estimated expenses of this offering. We intend to use the net proceeds of this offering as follows: (1) approximately $ million to repay or extinguish existing indebtedness that we will assume upon completion of the formation transactions, including estimated related costs totaling approximately $ million; (2) approximately $10.0 million to fund capital improvements at our hotels; and (3) the balance for general corporate and working capital purposes, including possible future hotel acquisitions. See Use of Proceeds for additional information.
Ownership and transfer restrictions	In order to assist us in qualifying as a REIT, our charter provides that, subject to certain exceptions, no person may beneficially or constructively own more than 9.8% in value or in number of shares, whichever is more restrictive, of our common stock and places certain other restrictions on ownership of our stock.
Proposed NYSE symbol	INN

(1) Immediately prior to the closing of this offering, we have a total of 1,000 shares of common stock outstanding. We sold these shares to our Executive Chairman, Mr. Boekelheide, in connection with our formation and initial capitalization for total consideration of $1,000. At the closing of this offering, we will repurchase these shares from Mr. Boekelheide for $1,000. The number of shares of common stock to be outstanding immediately after the repurchase of these shares and the closing of this offering includes: (i) shares of common stock to be sold in this offering and (ii) an aggregate of shares of common stock to be issued to our independent director nominees pursuant to the 2010 Equity Incentive Plan upon completion of this offering. The number of shares of common stock to be outstanding immediately after the closing of this offering excludes: (i) up to shares of common stock issuable upon exercise of the underwriters over-allotment option; (ii) an aggregate of shares of common stock issuable upon exercise of options that we will grant to our Executive Chairman, Mr. Boekelheide, our President and Chief Executive Officer, Mr. Hansen, our Executive Vice President and Chief Operating Officer, Mr. Aniszewski, our Executive Vice President and Chief Financial Officer, Stuart J. Becker, and our Vice President of Acquisitions, Ryan A. Bertucci, pursuant to the 2010 Equity Incentive Plan upon completion of this offering; (iii) additional shares of common stock available for future issuance under the 2010 Equity Incentive Plan; and (iv) up to 10,100,000 shares of common stock issuable upon redemption of the 10,100,000 OP units to be issued by our operating partnership in the formation transactions.

(2)

Includes all of the shares of common stock identified in the third sentence of footnote (1) above, and 10,100,000 OP units to be issued in the formation transactions to our predecessor s former members and the former Class B and Class C members of Summit of Scottsdale in exchange for their membership interests in those entities. Pursuant to the limited partnership agreement of our operating partnership, limited partners, other than us, will have redemption rights which will enable them to cause our operating partnership to redeem their OP units in exchange for cash or, at our operating partnership s option, shares of our common stock on a one-for-one basis. The number of shares of common stock issuable upon redemption of OP units may be adjusted upon the occurrence of certain events described under Description of the Partnership Agreement Redemption Rights.

Summary Pro Forma Financial Information

You should read the following summary pro forma financial and operating data in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and our unaudited pro forma condensed consolidated financial statements and our predecessor s consolidated financial statements, including the related notes, appearing elsewhere in this prospectus.

The following unaudited summary pro forma financial information is presented to reflect:

§ the initial public offering of shares of our common stock in this offering at $ per share, the mid-point of the anticipated initial public offering price range shown on the cover of this prospectus, for approximately $260.2 million of estimated net proceeds, after the deduction of the underwriting discount and the payment by us of approximately $3.6 million of expenses related to this offering and the formation transactions;

§ the merger of our predecessor with and into our operating partnership, with our predecessor as the acquirer for accounting purposes, and the issuance by our operating partnership of an aggregate of 9,993,992 OP units to the Class A, Class A-1, Class B and Class C members of our predecessor in exchange for their membership interests in our predecessor;

§ the contribution to our operating partnership of the Class B and Class C membership interests in Summit of Scottsdale held by The Summit Group and an unaffiliated third-party investor in exchange for an aggregate of 106,008 OP units;

§ the contribution of the net proceeds of this offering to our operating partnership in exchange for OP units that represent an approximate % partnership interest in our operating partnership, including the sole general partnership interest;

§ the repayment or extinguishment of approximately $225.2 million of outstanding indebtedness and the payment of estimated costs and expenses of approximately $3.8 million in connection with the retirement of this indebtedness; and

§ the grant upon completion of this offering of an aggregate of 5,000 shares of our common stock to our independent director nominees and options to purchase an aggregate of 940,000 shares of our common stock to Messrs. Boekelheide, Hansen, Aniszewski, Becker and Bertucci pursuant to the 2010 Equity Incentive Plan.

Following completion of the merger, the historical consolidated financial statements of our predecessor will become our historical consolidated financial statements, and our assets and liabilities will be recorded at their respective historical carrying values as of the date of completion of the merger.

The unaudited pro forma balance sheet data appearing below assumes that each of these transactions occurred on June 30, 2010. The unaudited pro forma statements of operations and other operating data assume that each of these transactions occurred on January 1, 2009.

In the opinion of our management, all material adjustments to reflect the effects of the preceding transactions have been made. The unaudited pro forma balance sheet data is presented for illustrative purposes only and is not necessarily indicative of what our actual financial position would have been had the transactions referred to above occurred on June 30, 2010, nor does it purport to represent our future financial position. The unaudited pro forma condensed statements of operations and other operating data are presented for illustrative purposes only and are not

necessarily indicative of what our actual results of operations would have been had the transactions referred to above occurred on January 1, 2009, nor do they purport to represent our future results of operations.

The following table presents summary unaudited pro forma balance sheet data as of June 30, 2010 (dollars in thousands):

	Pro Forma as of June 30, 2010 (unaudited)
Cash and cash equivalents	$ 34,287
Property and equipment, net	$ 460,632
Total assets	$ 534,274
Mortgages and notes payable	$ 199,440
Total liabilities	$ 211,417
Stockholders equity	$ 256,005
Noncontrolling interest	$ 66,852
Total liabilities and equity	$ 534,274

The following table presents summary unaudited pro forma statement of operations and other data for the six months ended June 30, 2010 and for the year ended December 31, 2009 (dollars in thousands, except per share data):

	Pro Forma Six Months Ended June 30, 2010 (unaudited)	Pro Forma Year Ended December 31, 2009 (unaudited)
Statement of Operations Data:		
Revenue		
Room revenues	$ 65,939	$ 118,960
Other hotel operations revenues	1,273	2,240
Total Revenue	**67,212**	**121,200**
Expenses[1]		
Hotel operating expenses:		
Rooms	20,048	36,720
Other direct	8,287	18,048
Other indirect	18,303	33,238
Other	302	681
Total hotel operating expenses	46,940	88,687
Depreciation and amortization	13,346	23,088
Corporate general and administrative:		
Salaries and other compensation	1,683	3,564
Equity-based compensation		
Other	916	1,633

Hotel property acquisition costs	56	1,389
Loss on impairment of assets		7,506
Total expenses	**62,941**	**125,867**
Income (loss) from operations	**4,271**	**(4,667)**
Other Income (expense):		
Interest income	24	50
Interest expense	(5,199)	(9,052)
Loss on disposal of assets	(40)	(4)
Total other expense	**(5,215)**	**(9,006)**
Loss from continuing operations	**(944)**	**(13,673)**
Net loss before income taxes	**(944)**	**(13,673)**
Income tax expense	(450)	(840)
Net loss	**$ (1,394)**	**$ (14,513)**

	Pro Forma Six Months Ended June 30, 2010 (unaudited)	Pro Forma Year Ended December 31, 2009 (unaudited)
Net loss attributable to noncontrolling interest		
Net loss attributable to common shareholders		
Pro forma net income (loss) per common share:		
Basic		
Diluted		
Pro forma weighted-average number of shares outstanding:		
Basic		
Diluted		
Other Data:		
FFO(2)	$ 11,952	$ 8,575
EBITDA(3)	$ 17,577	$ 18,417

(1) Historically, our predecessor segregated its operating expenses (direct hotel operations expense, other hotel operating expense, general, selling and administrative expense and repairs and maintenance) from its other operating expenses, such as depreciation and amortization and impairment losses. Following completion of this offering, we intend to reclassify our operating expenses into categories of hotel operating expenses (room expenses, other direct expenses, other indirect expenses and other expenses) and reclassify our predecessor s historical items of hotel operating expense to increase the comparability of our hotel operating expenses and our hotel operating results with other publicly traded hospitality REITs. Accordingly, historical balances included in our predecessor s:

- § direct hotel operations expense related to (1) wages, payroll taxes and benefits, linens, cleaning and guestroom supplies and complimentary breakfast will be reclassified to rooms expense in our consolidated statements of operations and (2) franchise fees will be reclassified to other indirect expense in our consolidated statements of operations;
- § other hotel operating expenses related to (1) utilities and telephone will be reclassified to other direct expenses in our consolidated statements of operations and (2) real and personal property taxes, insurance and cable will be reclassified to other indirect expenses in our consolidated statements of operations;
- § general, selling and administrative expenses related to (1) office supplies, advertising, miscellaneous operating expenses and bad debt expense will be reclassified to other direct expenses in our consolidated statements of operations, (2) credit card/travel agent commissions, management company expenses, management company legal and accounting fees and franchise fees will be reclassified to other indirect expenses in our consolidated statements of operations, (3) hotel development and startup costs will be reclassified to hotel property acquisition costs in our consolidated statements of operations and (4) ground rent and other miscellaneous expenses will be reclassified to other expenses in our consolidated statements of operations; and
- § repairs and maintenance will be reclassified to other direct expenses in our consolidated statements of operations.

On a pro forma basis, the reclassification reduces total hotel operating expenses (direct hotel operations expense, other hotel operating expense, general, selling and administrative expense and repairs and maintenance) by $56,000 for the six months ended June 30, 2010 and $1.4 million for the year ended December 31, 2009, which were reclassified to hotel operating costs. The reclassification does not impact amounts reported by our predecessor as total expenses (total hotel operating expenses, depreciation and amortization and loss on impairment of assets),

income from operations, total other income, income (loss) from continuing operations, income (loss) from discontinued operations, net income (loss) before income taxes or net income (loss). See Unaudited Pro Forma Condensed Consolidated Financial Statements for additional information.

(2) As defined by the National Association of Real Estate Investment Trusts, or NAREIT, funds from operations, or FFO, represents net income or loss (computed in accordance with GAAP), excluding gains (or losses) from sales of property, plus real estate depreciation and amortization (excluding amortization of deferred financing costs). We present FFO because we consider it an important supplemental measure of our operational performance and believe it is frequently used by securities analysts, investors and other interested parties in the evaluation of REITs, many of which present FFO when reporting their results. FFO is intended to exclude GAAP historical cost depreciation and amortization of real estate and related assets, which assumes that the value of real estate assets diminishes ratably over time. Historically, however, real estate values have risen or fallen with market conditions. Because FFO excludes depreciation and amortization unique to real estate, gains and losses from property dispositions and extraordinary items, it provides a performance measure that, when compared year over year, reflects the impact to operations from trends in occupancy rates, room rates, operating costs, development activities and interest costs, providing perspective not immediately apparent from net income. We will compute FFO in accordance with standards established by the Board of Governors of NAREIT in its March 1995 White Paper (as amended in November 1999 and April 2002), which may differ from the methodology for calculating FFO utilized by other equity REITs and, accordingly, may not be comparable to such other REITs. Further, FFO does not represent amounts available for management s discretionary use because of needed capital replacement or expansion, debt service obligations, or other commitments and uncertainties. FFO should not be considered as an alternative to net income (loss) (computed in accordance with GAAP) as an indicator of our liquidity, nor is it indicative of funds available to fund our cash needs, including our ability to pay dividends or make distributions. We caution investors that amounts presented in accordance with our definitions of FFO may not be comparable to similar measures disclosed by other companies, since not all companies calculate this non-GAAP measure in the same manner. FFO should not be considered as an alternative measure of our net income (loss) or operating performance. FFO may include funds that may not be available for our discretionary use due to functional requirements to conserve funds for capital expenditures and property acquisitions and other commitments and uncertainties. Although we believe that FFO can enhance your understanding of our financial condition and results of operations, this non-GAAP financial measure is not necessarily a better indicator of any trend as compared to a comparable GAAP measure such as net income (loss). Below, we include a quantitative

reconciliation of pro forma FFO to the most directly comparable GAAP financial performance measure, which is pro forma net income (loss) (dollars in thousands):

	Pro Forma Six Months Ended June 30, 2010	Pro Forma Year Ended December 31, 2009
Net loss	$ (1,394)	$ (14,513)
Depreciation and amortization	13,346	23,088
FFO	$ 11,952	$ 8,575

(3) EBITDA represents net income or loss, excluding: (i) interest, (ii) income tax expense and (iii) depreciation and amortization. We believe EBITDA is useful to an investor in evaluating our operating performance because it provides investors with an indication of our ability to incur and service debt, to satisfy general operating expenses, to make capital expenditures and to fund other cash needs or reinvest cash into our business. We also believe it helps investors meaningfully evaluate and compare the results of our operations from period to period by removing the impact of our asset base (primarily depreciation and amortization) from our operating results. Our management also uses EBITDA as one measure in determining the value of acquisitions and dispositions. We caution investors that amounts presented in accordance with our definitions of EBITDA may not be comparable to similar measures disclosed by other companies, since not all companies calculate this non-GAAP measure in the same manner. EBITDA should not be considered as an alternative measure of our net income (loss) or operating performance. EBITDA may include funds that may not be available for our discretionary use due to functional requirements to conserve funds for capital expenditures and property acquisitions and other commitments and uncertainties. Although we believe that EBITDA can enhance your understanding of our financial condition and results of operations, this non-GAAP financial measure is not necessarily a better indicator of any trend as compared to a comparable GAAP measure such as net income (loss). Below, we include a quantitative reconciliation of pro forma EBITDA to the most directly comparable GAAP financial performance measure, which is pro forma net income (loss) (dollars in thousands):

	Pro Forma Six Months Ended June 30, 2010	Pro Forma Year Ended December 31, 2009
Net loss	$ (1,394)	$ (14,513)
Interest income	(24)	(50)
Interest expense	5,199	9,052
Income tax expense	450	840
Depreciation and amortization	13,346	23,088
EBITDA	$ 17,577	$ 18,417

Risk Factors

An investment in our common stock involves risks. Before making an investment decision, you should carefully consider the following risk factors, which address the material risks concerning our business and an investment in our common stock, together with the other information contained in this prospectus. If any of the risks discussed in this prospectus were to occur, our business, prospects, financial condition, results of operation and our ability to service our debt and make distributions to our stockholders could be materially and adversely affected, the market price per share of our common stock could decline significantly and you could lose all or a part of your investment. Some statements in this prospectus, including statements in the following risk factors constitute forward-looking statements. Please refer to the section entitled Cautionary Note Regarding Forward-Looking Statements.

Risks Related to Our Business

Our business strategy depends significantly on achieving revenue and net income growth from anticipated increases in demand for hotel rooms any delay or a weaker than anticipated economic recovery will adversely affect our future results of operations and our growth prospects.

Our hotel properties experienced declining operating performance across various U.S. markets during the recent economic recession. Our business strategy depends significantly on achieving revenue and net income growth from anticipated improvement in demand for hotel rooms as part of a future economic recovery. We, however, cannot provide any assurances that demand for hotel rooms will increase from current levels. If demand does not increase in the near future, or if demand weakens further, our operating results and growth prospects could be adversely affected. In particular, we already have reduced our operating expenses significantly in response to the recent economic recession and our ability to reduce operating expenses further to improve our operating performance is limited. As a result, any delay or a weaker than anticipated economic recovery will adversely affect our future results of operations and our growth prospects.

Our unseasoned hotels have limited, if any, operating history and may not achieve the operating performance we anticipate, and as a result, our overall returns may not improve as we expect or may decline.

Our unseasoned hotels have experienced extended stabilization periods as a result of the significant decline in general economic conditions. Consequently, many of these hotels continue to generate negative cash flow beyond our original expectations for them. Significant increases in anticipated hotel room supply or decreases in hotel room demand in the markets where any one or more of our unseasoned hotels are located could cause the operating performance of those hotels to be below our original plans for them. If macroeconomic conditions or conditions specific to their markets do not improve significantly or our anticipated improved results for these hotels do not otherwise materialize, our overall returns may not improve as we expect or may decline.

We have no operating history as a publicly traded REIT and may not be successful in operating as a publicly traded REIT, which may adversely affect our ability to make distributions to our stockholders.

We have no operating history as a publicly traded REIT. The REIT rules and regulations are highly technical and complex. We cannot assure you that our management team s past experience will be sufficient to successfully operate our company as a publicly traded REIT, implement appropriate operating and investment policies and comply with Code or Treasury Regulations that are applicable to us. Failure to comply with the income, asset, and other requirements imposed by the REIT rules and regulations could prevent us from qualifying as a REIT, and could force us to pay unexpected taxes and penalties which may adversely affect our ability to make distributions to our

stockholders.

Our success depends on key personnel whose continued service is not guaranteed.

We depend on the efforts and expertise of our management team to manage our day-to-day operations and strategic business direction. The loss of services from any of the members of our management team, particularly our Executive Chairman, Kerry W. Boekelheide, and our President and Chief Executive Officer, Daniel P. Hansen, and our inability to find suitable replacements on a timely basis could have an adverse effect on our operations.

We may be unable to complete acquisitions that would grow our business.

Our growth strategy includes the disciplined acquisition of hotels as opportunities arise. Our ability to acquire hotels on satisfactory terms or at all is subject to the following significant risks:

§ we may be unable to acquire or may be forced to acquire at significantly higher prices desired hotels because of competition from other real estate investors with more capital, including other real estate operating companies, REITs and investment funds;

§ we may be unable to obtain the necessary debt or equity financing to consummate an acquisition or, if obtainable, financing may not be on satisfactory terms;

§ agreements for the acquisition of hotels are typically subject to customary conditions to closing, including satisfactory completion of due diligence investigations, and we may spend significant time and money on potential acquisitions that we do not consummate;

If we cannot complete hotel acquisitions on favorable terms or at all, our business, financial condition, results of operations and cash flow, the market price per share of our common stock and our ability to satisfy our debt service obligations and make distributions to our stockholders could be materially and adversely affected.

We may fail to successfully integrate and operate newly acquired hotels.

Our ability to successfully integrate and operate newly acquired hotels is subject to the following risks:

§ we may not possess the same level of familiarity with the market dynamics and market conditions of any new markets that we may enter, which could result in us paying too much for hotels in new markets;

§ market conditions may result in lower than expected occupancy rates and lower than expected room rates;

§ we may acquire hotels without any recourse, or with only limited recourse, for liabilities, whether known or unknown, such as clean-up of environmental contamination, claims by tenants, vendors or other persons against the former owners of the hotels and claims for indemnification by general partners, directors, officers and others indemnified by the former owners of the hotels.

§ we may need to spend more than budgeted amounts to make necessary improvements or renovations to our newly acquired hotels; and

§ we may be unable to quickly and efficiently integrate new acquisitions, particularly acquisitions of portfolios of hotels, into our existing operations.

If we cannot operate acquired hotels to meet our goals or expectations, our business, financial condition, results of operations and cash flow, the market price per share of our common stock and our ability to satisfy our debt service obligations and make distributions to our stockholders could be materially and adversely affected.

We may not succeed in managing our growth, in which case our financial results could be adversely affected.

Our ability to grow our business depends upon our management team s business contacts and their ability to successfully hire, train, supervise and manage additional personnel. We may not be able to hire and train sufficient

personnel or develop management, information and operating systems suitable for our expected growth. If we are unable to manage any future growth effectively, our operations and financial results could be adversely affected.

Upon completion of this offering and the formation transactions, the management of all of the hotels in our initial portfolio will be concentrated in one hotel management company.

Upon completion of this offering and the formation transactions, all of the hotels in our initial portfolio will be operated by . This significant concentration of credit and operational risk in one hotel management company makes us more vulnerable economically than if we entered into hotel management agreements with several hotel management companies. Any adverse developments in s business and affairs, financial strength or ability to operate our hotels efficiently and effectively could have a material adverse effect on our results of operations. We cannot assure you that will have sufficient assets, income and access to financing and insurance coverage to enable it to satisfy its obligations to us or effectively and efficiently operate our initial hotel properties. The failure or inability of to satisfy its obligations to us or effectively and efficiently operate our initial hotel properties would materially reduce our revenues and net income, which could in turn reduce the amount of our distributable cash and cause the market price per share of our common stock to decline.

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Termination of our hotel management agreement with may cause us to pay substantial termination fees or to experience significant disruptions at the affected hotels.

If we replace as the hotel manager of any of our hotels, we may be required to pay a substantial termination fee and we may experience significant disruptions at the affected hotel. If we experience disruptions at the affected hotel, our financial condition, results of operations and our ability to service debt and make distributions to our stockholders could be materially and adversely affected.

Restrictive covenants in hotel management and franchise agreements could preclude us from taking actions with respect to the sale or refinancing of a hotel that would otherwise be in our best interest.

Hotel management and franchise agreements typically contain restrictive covenants that do not provide us with flexibility to sell or refinance a hotel without the consent of a manager or franchisor. For example, the terms of some of these agreements may restrict our ability to sell a hotel unless the purchaser is not a competitor of the hotel management company, assumes the related agreement and meets specified other conditions. We could be forced to pay consent or possibly termination fees to hotel managers or franchisors under these agreements. As a result of these types of restrictive covenants, we may be precluded from taking actions that would otherwise be in our best interest or could cause us to incur substantial expense.

We may not be able to cause our hotel management companies to operate any of our hotels in a manner satisfactory to us, which could adversely affect our financial condition, results of operations and our ability to service debt and make distributions to our stockholders.

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1,618,544

September 30, 2016

West Segment
$
586,420

$
172,015

$
6,577

$
765,012

East Segment	276,785	30,036	20,930	327,751
Southeast Segment	276,385	10,955	1,090	288,430
Corporate and unallocated [b]	186,987	—	1,099	188,086
Total	$ 1,326,577	$ 213,006	$ 29,696	$ 1,569,279

[a] Projects in progress include homes under construction, development projects in progress, capitalized interest and model home categories from the preceding table.
[b] Projects in progress amount includes capitalized interest and indirect costs that are maintained within Corporate and unallocated.
Land held for sale amount includes parcels held by our discontinued operations.
Inventory Impairments. When conducting our community level review for the recoverability of our inventory related to projects in progress, we establish a quarterly “watch list” of communities that carry gross margins in backlog and in our forecast that are below a minimum threshold of profitability, as well as recent closings that have gross margins less than a specific threshold. Each community is first evaluated qualitatively to determine if there are temporary factors driving the low profitability levels. Following our qualitative evaluation, communities with more than 10 homes remaining to close are subjected to substantial additional financial and operational analyses and review that consider the competitive environment and other factors contributing to gross margins below our watch list threshold. Our assumptions about future home sales prices and absorption rates require significant judgment because the residential homebuilding industry is cyclical and is highly sensitive to changes in economic conditions. For certain communities, we determined that it is prudent to reduce sales prices or further increase sales incentives in response to a variety of factors, including competitive market conditions in those specific submarkets for the product and locations of these communities. For communities where the current competitive and market dynamics indicate that these factors may be other than temporary, which may call into question the recoverability of our investment, a formal impairment analysis is performed. The formal impairment analysis consists of both qualitative competitive market analyses and a quantitative analysis reflecting market and asset specific information. Market deterioration that exceeds our initial estimates may lead us to incur impairment charges on previously impaired homebuilding assets, in addition to homebuilding assets not currently impaired but for which indicators of impairment may arise if markets deteriorate. For the quarter ended December 31, 2016, there were eight communities on our watch list, seven in our West segment and the other in our East segment. However, none of these communities required further analysis to be performed after considering certain qualitative factors. For the quarter ended December 31, 2015, there were no communities on our quarterly watch list that required further impairment analysis to be performed.

Impairments on land held for sale generally represent write downs of these properties to net realizable value, less estimated costs to sell, and are based on current market conditions and our review of recent comparable transactions. Our assumptions about land sales prices require significant judgment because the real estate market is highly sensitive to changes in economic conditions. We calculate the estimated fair value of land held for sale based on current market conditions and assumptions made by management, which may differ materially from actual results and may result in additional impairments if market conditions deteriorate.

From time-to-time, we also determine that the proper course of action with respect to a community is to not exercise an option and to write off the deposit securing the option takedown and the related pre-acquisition costs, as applicable. In determining

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whether to abandon lots or lot option contracts, our evaluation is primarily based upon the expected cash flows from the property. Additionally, in certain limited instances, we are forced to abandon lots due to permitting or other regulatory issues that do not allow us to build on those lots. If we intend to abandon or walk away from a property, we record a charge to earnings for the deposit amount and any related capitalized costs in the period such decision is made. Abandonment charges generally relate to our decision to abandon lots or not exercise certain option contracts that are not projected to produce adequate results, no longer fit with our long-term strategic plan or, in limited circumstances, are not suitable for building due to regulatory or environmental restrictions that are enacted.

We did not have any land held for sale inventory impairments, nor did we have any abandonment charges, during the three months ended December 31, 2016. The following table presents, by reportable segment, our total impairment and abandonment charges for the three months ended December 31, 2015:

(In thousands)	Three Months Ended December 31, 2015
Land Held for Sale:	
East	$ 197
Southeast	371
Total impairment charges on land held for sale	$ 568
Abandonments:	
Southeast	$ 788
Total abandonments charges	$ 788
Total impairment and abandonment charges	$ 1,356

Lot Option Agreements and Variable Interest Entities (VIEs). As previously discussed, we also have access to land inventory through lot option contracts, which generally enable us to defer acquiring portions of properties owned by third parties and unconsolidated entities until we have determined whether to exercise our lot option. The majority of our lot option contracts require a non-refundable cash deposit or irrevocable letter of credit based on a percentage of the purchase price of the land for the right to acquire lots during a specified period of time at a specified price. Under lot option contracts, purchase of the properties is contingent upon satisfaction of certain requirements by us and the sellers. Our liability under option contracts is generally limited to forfeiture of the non-refundable deposits, letters of credit and other non-refundable amounts incurred. We expect to exercise, subject to market conditions and seller satisfaction of contract terms, most of our remaining option contracts. Various factors, some of which are beyond our control, such as market conditions, weather conditions and the timing of the completion of development activities, will have a significant impact on the timing of option exercises or whether lot options will be exercised at all.

The following table provides a summary of our interests in lot option agreements as of December 31, 2016 and September 30, 2016:

(In thousands)	Deposits & Non-refundable Pre-acquisition Costs Incurred	Remaining Obligation
As of December 31, 2016		
Unconsolidated lot option agreements	$ 78,001	$ 412,881
As of September 30, 2016		
Unconsolidated lot option agreements	$ 80,433	$ 446,414

(6) Interest

Our ability to capitalize interest incurred during the three months ended December 31, 2016 and 2015 was limited by our inventory eligible for capitalization. The following table presents certain information regarding interest for the periods presented:

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(In thousands)	Three Months Ended December 31, 2016	2015
Capitalized interest in inventory, beginning of period	$138,108	$123,457
Interest incurred	27,087	30,088
Interest expense not qualified for capitalization and included as other expense [a]	(5,252)	(7,432)
Capitalized interest amortized to home construction and land sales expenses [b]	(15,644)	(13,651)
Capitalized interest in inventory, end of period	$144,299	$132,462

[a] The amount of interest we are able to capitalize is dependent upon our qualified inventory balance, which considers the status of our inventory holdings. Our qualified inventory balance includes the majority of our homes under construction and development projects in progress, but excludes land held for future development and land held for sale.

[b] Capitalized interest amortized to home construction and land sale expenses varies based on the number of homes closed during the period and land sales, if any, as well as other factors.

(7) Borrowings

As of December 31, 2016 and September 30, 2016, we had the following debt, net of premiums/discounts and unamortized debt issuance costs:

(In thousands)	Maturity Date	December 31, 2016	September 30, 2016
5 3/4% Senior Notes	June 2019	$ 321,393	$ 321,393
7 1/2% Senior Notes	September 2021	198,000	198,000
8 3/4% Senior Notes	March 2022	500,000	500,000
7 1/4% Senior Notes	February 2023	199,834	199,834
Unamortized debt premium, net		2,260	2,362
Unamortized debt issuance costs		(13,314)	(14,063)
Total Senior Notes, net		1,208,173	1,207,526
Term Loan (net of unamortized discount of $725 and $880, respectively, and unamortized debt issuance costs of $1,195 and $1,451, respectively)	March 2018	53,080	52,669
Junior Subordinated Notes (net of unamortized accretion of $40,387 and $40,903, respectively)	July 2036	60,387	59,870
Other Secured Notes payable	Various Dates	14,843	11,813
Total debt, net		$ 1,336,483	$ 1,331,878

Secured Revolving Credit Facility. Our Secured Revolving Credit Facility (the Facility) provides us with working capital and letter of credit capacity. On October 13, 2016, we executed a third amendment (the Third Amendment) to the Facility. The Third Amendment (1) extended the termination date of the Facility from January 15, 2018 to February 15, 2019; (2) increased the maximum aggregate amount of commitments under the Facility (including borrowings and letters of credit) from $145.0 million to $180.0 million; (3) reduced the aggregate collateral ratio (as defined by the underlying Credit Agreement) from 5.00 to 1.00 to 4.00 to 1.00; and (4) reduced the after-acquired exclusionary condition (also as defined by the underlying Credit Agreement) from $1.0 billion to $800.0 million. The facility continues to be with three lenders. For additional discussion of the Facility, refer to Note 8 to the audited consolidated financial statements within our 2016 Annual Report.

As of December 31, 2016 and September 30, 2016, we had no borrowings outstanding under the Facility. As of December 31, 2016, we had $37.5 million in letters of credit outstanding under the Facility, leaving us with $142.5 million in remaining capacity. The Facility contains certain covenants, including negative covenants and financial maintenance covenants, with which we are required to comply. As of December 31, 2016, we were in compliance with all such covenants.

Letter of Credit Facilities. We have entered into stand-alone, cash-secured letter of credit agreements with banks to maintain our pre-existing letters of credit and to provide for the issuance of new letters of credit (in addition to the

letters of credit issued under the Facility). As of December 31, 2016 and September 30, 2016, we had letters of credit outstanding under these additional facilities of $11.5 million and $12.1 million, respectively, all of which were secured by cash collateral in restricted accounts. The Company may enter into additional arrangements to provide further letter of credit capacity.

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Senior Notes. Our Senior Notes are unsecured obligations ranking pari passu with all other existing and future senior indebtedness. Substantially all of our significant subsidiaries are full and unconditional guarantors of the Senior Notes and are jointly and severally liable for obligations under the Senior Notes and the Facility. Each guarantor subsidiary is a 100% owned subsidiary of Beazer Homes. See Note 15 for further information.

All unsecured Senior Notes rank equally in right of payment with all of our existing and future senior unsecured obligations, senior to all of the Company's existing and future subordinated indebtedness and effectively subordinated to the Company's existing and future secured indebtedness, including indebtedness under the Facility and the term loan (defined below), to the extent of the value of the assets securing such indebtedness. The unsecured Senior Notes and related guarantees are structurally subordinated to all indebtedness and other liabilities of all of the Company's subsidiaries that do not guarantee these notes. The unsecured Senior Notes are fully and unconditionally guaranteed jointly and severally on a senior basis by the Company's wholly-owned subsidiaries party to each applicable Indenture.

The Company's Senior Notes are issued under indentures that contain certain restrictive covenants which, among other things, restrict our ability to pay dividends, repurchase our common stock, incur certain types of additional indebtedness and to make certain investments. Compliance with our Senior Note covenants does not significantly impact our operations. We were in compliance with the covenants contained in the indentures of all of our Senior Notes as of December 31, 2016.

The table below summarizes the redemption terms for our Senior Notes:

Senior Note Description	Issuance Date	Maturity Date	Redemption Terms
5 3/4% Senior Notes	April 2014	June 2019	Callable at any time before March 15, 2019, in whole or in part, at a redemption price equal to 100% of the principal amount, plus a customary make-whole premium; on or after March 15, 2019, callable at 100% of the principal amount plus, in each case, accrued and unpaid interest
7 1/2% Senior Notes	September 2013	September 2021	Callable at a redemption price equal to 105.625% of the principal amount; on or after September 15, 2017, callable at a redemption price equal to 103.75% of the principal amount; on or after September 15, 2018, callable at a redemption price equal to 101.875% of the principal amount; on or after September 15, 2019, callable at 100% of the principal amount plus, in each case, accrued and unpaid interest
8 3/4% Senior Notes	September 2016	March 2022	Callable at any time prior to March 15, 2019, in whole or in part, at a redemption price equal to 100% of the principal amount, plus a customary make-whole premium; on or after March 15, 2019, callable at a redemption price equal to 104.375% of the principal amount; on or after March 15, 2020, callable at a redemption price equal to 102.188% of the principal amount; on or after March 15, 2021, callable at a redemption price equal to 100% of the principal amount plus, in each case, accrued and unpaid interest
7 1/4% Senior Notes	February 2013	February 2023	Callable at any time prior to February 1, 2018, in whole or in part, at a redemption price equal to 100% of the principal amount, plus a customary make-whole premium; on or after February 1, 2018, callable at a redemption price equal to 103.625% of the principal amount; on or after February 1, 2019, callable at a redemption price equal to 102.41% of the principal amount; on or after February 1, 2020, callable at a redemption price equal to 101.208% of the principal amount; on or after February 1, 2021, callable at 100% of the principal amount plus, in each case, accrued and unpaid interest

During the first quarter of our fiscal 2016, we paid down $22.9 million of the then outstanding Senior Notes due June 2016, which resulted in a loss on extinguishment of debt of $0.8 million.

Term Loan. In March 2016, we entered into a credit agreement (the Credit Agreement) that provided us with a $140 million, two-year secured term loan (the Term Loan). The Term Loan requires quarterly principal payments of $17.5

million that started on June 30, 2016, and bears interest at the London Interbank Offered Rate (LIBOR) plus 550 basis points (6.750% as of December 31, 2016). The Term Loan will mature and all remaining amounts outstanding thereunder will be due and payable on March 11, 2018, but can be pre-paid at any time without penalty. In addition to regularly scheduled payments on the Term Loan made during our fiscal 2016, we made a prepayment of $50.0 million during the fourth quarter of fiscal 2016.

Substantially all of our subsidiaries are guarantors of the obligations under the Credit Agreement. Collectively, we granted security interests and mortgage liens on substantially all of our tangible and intangible assets on a second lien basis, since they are subordinate to those that exist on the Facility.

The Credit Agreement contains covenants which, subject to certain exceptions, limit the ability of the Company and its restricted subsidiaries (as defined in the Credit Agreement) to, among other things, incur additional indebtedness, engage in certain asset sales, make certain types of restricted payments and create liens on assets of the Company or its restricted subsidiaries; these covenants are similar to existing covenants under our Senior Notes. In addition, the Credit Agreement requires the Company's inventory (as defined in the Credit Agreement) to be no less than $1.25 billion as of the last day of any fiscal quarter. The Credit Agreement also includes customary events of default, including, but not limited to, the failure to pay any interest, principal or fees when due; the failure to perform or the violation of any covenant or agreement; inaccurate or false representations or warranties; a default on other material indebtedness, insolvency or bankruptcy; a change of control; and the occurrence of certain material judgments against the Company. As of December 31, 2016, we were in compliance with all such covenants.

Junior Subordinated Notes. Our unsecured junior subordinated notes (Junior Subordinated Notes) mature on July 30, 2036. The Junior Subordinated Notes are redeemable at par and paid interest at a fixed rate of 7.987% for the first ten years ending July 30, 2016. The securities now have a floating interest rate as defined in the Junior Subordinated Notes Indenture, which was a weighted-average of 4.02% as of December 31, 2016 (because the rate on the portion of the Junior Subordinated Notes that was modified, as discussed below, is subject to a floor). The obligations relating to these notes are subordinated to the Facility, the Senior Notes and the Term Loan. In January 2010, we modified the terms of $75.0 million of these notes and recorded them at their then estimated fair value. Over the remaining life of the Junior Subordinated Notes, we will increase their carrying value until this carrying value equals the face value of the notes. As of December 31, 2016, the unamortized accretion was $40.4 million and will be amortized over the remaining life of the notes. As of December 31, 2016, we were in compliance with all covenants under our Junior Subordinated Notes.

Other Secured Notes Payable. We periodically acquire land through the issuance of notes payable. As of December 31, 2016 and September 30, 2016, we had outstanding secured notes payable of $14.8 million and $11.8 million, respectively, primarily related to land acquisitions. These secured notes payable related to land acquisitions have varying expiration dates between 2017 and 2019, and have a weighted-average fixed interest rate of 3.12% as of December 31, 2016. These notes are secured by the real estate to which they relate.

The agreements governing these secured notes payable contain various affirmative and negative covenants. There can be no assurance that we will be able to obtain any future waivers or amendments that may become necessary without significant additional cost or at all. In each instance, however, a covenant default can be cured by repayment of the indebtedness.

(8) Contingencies

Beazer Homes and certain of its subsidiaries have been and continue to be named as defendants in various construction defect claims, complaints and other legal actions. The Company is subject to the possibility of loss contingencies arising from its business. In determining loss contingencies, we consider the likelihood of loss, as well as the ability to reasonably estimate the amount of such loss or liability. An estimated loss is recorded when it is considered probable that a liability has been incurred and the amount of loss can be reasonably estimated.

Warranty Reserves. We currently provide a limited warranty (ranging from one to two years) covering workmanship and materials per our defined performance quality standards. In addition, we provide a limited warranty for up to ten years covering only certain defined structural element failures.

Our homebuilding work is performed by subcontractors that typically must agree to indemnify us with regard to their work and provide us with certificates of insurance demonstrating that they have met our insurance requirements and that we are named as an additional insured under their policies. Therefore, many claims relating to workmanship and materials that result in warranty spending are the primary responsibility of these subcontractors. In addition, we maintain insurance coverage related to our construction efforts that can result in recoveries of warranty and construction defect costs above certain specified limits.

Our warranty reserves are included in other liabilities on our consolidated balance sheets, and the provision for warranty accruals is included in home construction expenses in our consolidated statements of income. We record reserves covering anticipated warranty expense for each home we close. Management reviews the adequacy of warranty reserves each reporting period based on historical experience and management's estimate of the costs to

remediate the claims, and adjusts these provisions accordingly. Our review includes a quarterly analysis of the historical data and trends in warranty expense by division. An analysis by division allows us to consider market specific factors such as our warranty experience, the number of home closings, the prices of homes, product mix and other data in estimating our warranty reserves. In addition, our analysis also contemplates the existence of any non-recurring or community-specific warranty-related matters that might not be included in our historical data and trends. While we adjust our estimated warranty liabilities each reporting period to the extent required as a result of our quarterly analyses, historical data and trends may not accurately predict actual warranty costs, which could lead to a significant change in the reserve.

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Changes in our warranty reserves are as follows for the periods presented:

(In thousands)	Three Months Ended December 31, 2016		2015	
Balance at beginning of period	$	39,131	$	27,681
Accruals for warranties issued [a]	2,658		2,615	
Changes in liability related to warranties existing in prior periods [b]	5,392		10,600	
Payments made [b]	(14,872	)	(11,983	)
Balance at end of period	$	32,309	$	28,913

[a] Accruals for warranties issued are a function of the number of home closings in the period, the selling prices of the homes closed and the rates of accrual per home estimated as a percentage of the selling price of the home.
[b] Changes in liability related to warranties existing and payments made in all periods presented are elevated due to charges and subsequent payments related to water intrusion issues in certain of our communities located in Florida (refer to separate discussion below).

Florida Water Intrusion Issues

In the latter portion of fiscal 2014, we began to experience an increase in calls from homeowners reporting stucco and water intrusion issues in certain of our communities in Florida (the Florida stucco issues). These issues continued to be reported to us throughout our fiscal 2015 and fiscal 2016. Other builders were also dealing with stucco issues, some of which also received local media coverage. Through December 31, 2016, we cumulatively recorded charges related to these issues of $83.2 million (of which $9.0 million was recorded in the three months ended December 31, 2015). As of September 30, 2016, the accrual to cover outstanding payments and potential repair costs for the impacted homes was $22.6 million, after considering the repair costs already paid. For an additional discussion of this matter and the related expenses recorded in prior periods, refer to Note 9 to the audited consolidated financial statements within our 2016 Annual Report.

During the first quarter of our fiscal 2017, the number of homeowner calls beyond those anticipated based on our procedures and previous call history continued to trend down. However, largely due to increased cost estimates for repairs of homes discovered in more recent periods, we recorded additional warranty expense related to the Florida stucco issues of $4.6 million during the three months ended December 31, 2016. As of December 31, 2016, 705 homes have been identified as likely to require repairs (an increase of 16 homes over those that were anticipated to require repairs as of the end of our fiscal 2016), of which 510 homes have been repaired. We made payments related to the Florida stucco issues of $10.0 million during the three months ended December 31, 2016, including payments on fully repaired homes, as well as payments on homes for which remediation is not yet complete, bringing the remaining accrual related to this issue to $17.2 million as of December 31, 2016, which is included in our overall warranty liability detailed above. As of December 31, 2016, other homes in the impacted communities remain within the period of the applicable statute of repose, but as of the end of the current quarter are not deemed likely to require repairs and, accordingly, no reserve has been established for these homes. The cost to repair these homes would be approximately $4.2 million if the current cost estimates were applied to these additional homes.

Our assessment of the Florida stucco issues is ongoing. As a result, we anticipate that the ultimate magnitude of our liability may change as additional information is obtained. Certain visual and other inspections of the homes that could be subject to defect often do not reveal the severity or extent of the defects, which can only be discovered once we receive a homeowner call and begin repairs. The current quarter charges were offset by additional insurance

recoveries; for a discussion of the amounts we have already recovered or anticipate recovering from our insurer, refer to "Insurance Recoveries" section below.

In addition, we believe that we will also recover a portion of such repair costs from sources other than our own insurer, including the subcontractors involved with the construction of these homes and their insurers; however, no amounts related to subcontractor recoveries have been recorded in our unaudited condensed consolidated financial statements as of December 31, 2016. Any amounts recovered from our subcontractors related to homes closed during policy years for which we have exceeded the deductible in our insurance policies would be remitted to our insurers, while recoveries in other policy years would be retained by us.

Insurance Recoveries

The Company has insurance policies that provide for the reimbursement of certain warranty costs incurred by us above a specified threshold for each period covered. We have surpassed these thresholds for certain policy years, particularly those that cover most of the homes impacted by the Florida stucco issues discussed above. As such, beginning with the first quarter of our fiscal 2015, we expect a substantial majority of additional costs incurred for warranty work on homes within these policy years to be reimbursed

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by our insurers. For one policy year, our accruals have exceeded the insurance claim limit for one division under our first layer of coverage; however, we expect to claim and recover such amounts under our excess insurance coverage. Warranty expense beyond the deductibles set in our insurance policies was recorded related to homes impacted by the Florida stucco issues, as well as other various warranty issues that are in excess of our insurance thresholds, resulting in our recognition of $3.9 million in insurance recoveries during the three months ended December 31, 2016 that we deem probable of receiving; this amount largely offset the current quarter expense related to the Florida stucco issues. For the three months ended December 31, 2015, $13.7 million was recorded in insurance recoveries. The recoveries recorded during the prior year quarter were $3.6 million greater than the underlying expense related to the Florida stucco issues of $9.0 million, as we began to recover more costs than initially anticipated. The remaining recovery amount during the first quarter of fiscal 2016 related to expenditures for warranty issues that were individually immaterial but were also in excess of our insurance thresholds.

Amounts recorded for anticipated insurance recoveries are reflected within our consolidated statements of income as a reduction of our home construction expenses, and associated amounts not yet received from our insurer are recorded on a gross basis (i.e. not net of any associated warranty expense) as a receivable within accounts receivable on our consolidated balance sheets.

Amounts still to be recovered under our insurance policies will vary based on whether expected additional warranty costs are actually incurred for periods for which our threshold has already been met. As a result, we anticipate the balance of our established receivable for insurance recoveries to fluctuate for potential future reimbursements, as well as the amounts ultimately owed to us from our insurer.

Litigation

From time-to-time, we receive claims from institutions that have acquired mortgages originated by our subsidiary, Beazer Mortgage Corporation (BMC), demanding damages or indemnity or that we repurchase such mortgages. BMC stopped originating mortgages in 2008. We have been able to resolve these claims for no cost or for amounts that are not material to our consolidated financial statements. We cannot rule out the potential for additional mortgage loan repurchase or indemnity claims in the future from other investors. At this time, we do not believe that the exposure related to any such claims would be material to our consolidated financial condition, results of operations or cash flows. As of December 31, 2016, no liability has been recorded for any additional claims related to this matter, as such exposure is not both probable and reasonably estimable.

A purported class action lawsuit was filed on July 7, 2016 against the Company in Maricopa County Arizona Superior Court on behalf of all homeowners in Arizona that purchased homes from the Company that included a certain type of roof underlayment. The complaint alleges various construction defects, but principally claims that the roof underlayment is susceptible to leaks and was not installed in accordance with best practices. We removed this case to federal court and filed motions to dismiss the class action allegations on various grounds. The plaintiffs have now withdrawn the class action allegations without prejudice and filed an amended complaint. In light of the dismissal of the class action allegations, the Company is handling this matter in the ordinary course of defending against alleged construction defect claims covered by the Company’s warranty. As such, the Company does not plan to report further on this case in future periodic reports.

In the normal course of business, we are subject to various lawsuits. We cannot predict or determine the timing or final outcome of these lawsuits or the effect that any adverse findings or determinations in pending lawsuits may have on us. In addition, an estimate of possible loss or range of loss, if any, cannot presently be made with respect to certain of these pending matters. An unfavorable determination in any of the pending lawsuits could result in the payment by us of substantial monetary damages, which may not be fully covered by insurance. Further, the legal costs associated with the lawsuits and the amount of time required to be spent by management and the Board of Directors on these matters, even if we are ultimately successful, could have a material adverse effect on our financial condition, results of operations or cash flows.

Other Matters

During January 2017, we made our final payment under the Deferred Prosecution Agreement and associated Bill of Information (the DPA) entered into on July 1, 2009 with the United States Attorney for the Western District of North Carolina and a separate but related agreement with the United States Department of Housing and Urban Development

(HUD) and the Civil Division of the United States Department of Justice (the HUD Agreement). For a further discussion of the HUD Agreement, refer to Note 9 to the audited consolidated financial statements within our 2016 Annual Report. During the three months ended December 31, 2015, we accrued $1.2 million related to the HUD Agreement, which was recorded within general and administrative expenses (G&A) in our consolidated statement of income.

We and certain of our subsidiaries have been named as defendants in various claims, complaints and other legal actions, most relating to construction defects, moisture intrusion and product liability. Certain of the liabilities resulting from these actions are covered in whole or in part by insurance. In our opinion, based on our current assessment, the ultimate resolution of these matters will not have a material adverse effect on our financial condition, results of operations or cash flows.

We have an accrual of $9.2 million and $10.2 million in other liabilities on our consolidated balance sheets related to litigation and other matters, excluding warranty, as of December 31, 2016 and September 30, 2016, respectively.
We had outstanding letters of credit and performance bonds of approximately $49.0 million and $220.5 million, respectively, as of December 31, 2016, related principally to our obligations to local governments to construct roads and other improvements in various developments. We have an immaterial amount of outstanding letters of credit relating to our land option contracts as of December 31, 2016.

(9) Fair Value Measurements

As of the dates presented, we had assets on our consolidated balance sheets that were required to be measured at fair value on a recurring or non-recurring basis. We use a fair value hierarchy that requires us to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value as follows:

- Level 1 – Quoted prices in active markets for identical assets or liabilities;
- Level 2 – Inputs other than quoted prices included in Level 1 that are observable either directly or indirectly through corroboration with market data; and
- Level 3 – Unobservable inputs that reflect our own estimates about the assumptions market participants would use in pricing the asset or liability.

Certain of our assets are required to be recorded at fair value on a recurring basis. The fair value of our deferred compensation plan assets is based on market-corroborated inputs (Level 2).

Certain of our assets are required to be recorded at fair value on a non-recurring basis when events and circumstances indicate that the carrying value of these assets may not be recovered. We review our long-lived assets, including inventory, for recoverability when factors indicate an impairment may exist, but no less than quarterly. Fair value on assets deemed to be impaired are determined based upon the type of asset being evaluated. The fair value of our owned inventory assets, when required to be calculated, is discussed within Notes 2 and 5. The fair value of our investments in unconsolidated entities is determined primarily using a discounted cash flow model to value the underlying net assets of the respective entities.

Determining which hierarchical level an asset or liability falls within requires significant judgment. We evaluate our hierarchy disclosures each quarter.

The following table presents the period-end balances of our assets measured at fair value on a recurring basis, and the impairment-date fair value of certain assets measured at fair value on a non-recurring basis, for each hierarchy level. These balances represent only those assets whose carrying values were adjusted to fair value during the periods presented:

(In thousands)	Level 1	Level 2	Level 3	Total
Three Months Ended December 31, 2016				
Deferred compensation plan assets [a]	$ —	$ 1,006	$ —	$ 1,006
Three Months Ended December 31, 2015				
Deferred compensation plan assets [a]	—	747	—	747
Land held for sale [b]	—	—	16,213 [c]	16,213
As of September 30, 2016				
Deferred compensation plan assets [a]	—	765	—	765

[a] Measured at fair value on a recurring basis.
[b] Measured at fair value on a non-recurring basis.
[c] Amount represents the impairment-date fair value of certain land held for sale assets that were impaired during the three months ended December 31, 2015.

The fair value of our cash and cash equivalents, restricted cash, accounts receivable, trade accounts payable, other liabilities, amounts due under the Facility (if outstanding) and other secured notes payable approximate their carrying amounts due to the short maturity of these assets and liabilities. When outstanding, obligations related to land not owned under option agreements approximate fair value.

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The following table presents the carrying value and estimated fair value of certain of our other financial liabilities as of December 31, 2016 and September 30, 2016:

(In thousands)	As of December 31, 2016 Carrying Amount [a]	As of December 31, 2016 Fair Value	As of September 30, 2016 Carrying Amount [a]	As of September 30, 2016 Fair Value
Senior Notes [b]	$1,208,173	$1,282,912	$1,207,526	$1,253,614
Term Loan	53,080	53,080	52,669	52,669
Junior Subordinated Notes	60,387	60,387	59,870	59,870
	$1,321,640	$1,396,379	$1,320,065	$1,366,153

[a] Carrying amounts are net of unamortized debt premium/discounts, debt issuance costs or accretion.

[b] The estimated fair value for our publicly-held Senior Notes has been determined using quoted market rates (Level 2).

(10) Income Taxes

Income Tax Provision. Our income tax provision for quarterly interim periods is based on an estimated annual effective income tax rate calculated separately from the effect of significant, infrequent or unusual items. Our total income tax benefit, including discontinued operations, was $2.6 million for the three months ended December 31, 2016, compared to income tax expense of $0.6 million for the three months ended December 31, 2015. Our current quarter income tax benefit was primarily driven by (1) the loss in earnings from continuing operations in the current period and (2) the Company's completion of work necessary to claim an additional $1.2 million in tax credits, which were recorded in the current quarter but related to our fiscal 2016. The tax expense for the three months ended December 31, 2015 was primarily driven by our earnings from continuing operations.

Deferred Tax Assets and Liabilities. The Company continues to evaluate its deferred tax assets each period to determine if a valuation allowance is required based on whether it “is more likely than not” that some portion of these deferred tax assets will not be realized. As of September 30, 2016 and again as of December 31, 2016, we concluded that it is more likely than not that a substantial portion of our deferred tax assets will be realized. As of December 31, 2016, our conclusions on the valuation allowance of $66.3 million and Internal Revenue Code Section 382 limitations related to our deferred tax assets remain consistent with the determinations we made during the period ended September 30, 2016 and are based on similar company specific and industry factors to those discussed in Note 13 to the audited consolidated financial statements within our 2016 Annual Report.

Miscellaneous Tax Matters. In the normal course of business, we are subject to audits by federal and state tax authorities regarding various tax liabilities. Certain state income tax returns for various fiscal years are under routine examination. The statute of limitations for our major tax jurisdictions remains open for examination for our fiscal 2007 and subsequent years.

(11) Stock-based Compensation

Our total stock-based compensation expense is included in G&A in our consolidated statements of income. A summary of the expense related to stock-based compensation by award type is as follows for the periods presented:

(In thousands)	Three Months Ended December 31, 2016	Three Months Ended December 31, 2015
Stock options expense	$107	$148
Restricted stock awards expense	2,069	1,608
Before tax stock-based compensation expense	2,176	1,756
Tax benefit	(774)	(597)
After tax stock-based compensation expense	$1,402	$1,159

During the three months ended December 31, 2016 and 2015, employees surrendered 30,018 shares and 14,536 shares, respectively, to us in payment of minimum tax obligations upon the vesting of stock awards under our stock incentive plans. We valued this stock at the market price on the date of surrender, for an aggregate value of

approximately $387,000 and $201,000 for the three months ended December 31, 2016 and 2015, respectively.
Stock Options. The fair value of each stock option granted is estimated on the date of grant using the Black-Scholes option-pricing model (Black-Scholes Model). The intrinsic value of a stock option is the amount by which the market value of the underlying stock exceeds the exercise price. As of December 31, 2016, the intrinsic value of our stock options outstanding, vested and expected to vest and exercisable were $0.7 million, $0.7 million and $0.3 million, respectively. As of December 31, 2016 and September 30, 2016, there was $0.5 million and $0.4 million, respectively, of total unrecognized compensation cost related to

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nonvested stock options. The cost remaining as of December 31, 2016 is expected to be recognized over a weighted-average period of 2.0 years.

During the three months ended December 31, 2016, we issued 27,110 stock options, each for one share of the Company's stock. These stock options typically vest ratably over three years from the date of grant, or two years from the date of grant if issued under the Employee Stock Option Program (EOP; refer to Note 16 of the notes to the consolidated financial statements in our 2016 Annual Report). We used the following assumptions for stock options granted, which derived the weighted average fair value shown, for the period presented:

	Three Months Ended December 31, 2016	
Expected life of options	5.4 years	
Expected volatility	50.26	%
Expected dividends	—	
Weighted average risk-free interest rate	1.83	%
Weighted average fair value	$ 5.87	

We relied upon a combination of the observed exercise behavior of our prior grants with similar characteristics, the vesting schedule of the current grants and an index of peer companies with similar grant characteristics to determine the expected life of the options granted. We considered historic returns of our stock and the implied volatility of our publicly-traded options in determining expected volatility. We assumed no dividends would be paid, since our Board of Directors has suspended payment of dividends indefinitely and payment of dividends is restricted under our Senior Note covenants. The risk-free interest rate is based on the term structure of interest rates at the time of the option grant.

Activity related to stock options for the period presented is as follows:

	Three Months Ended December 31, 2016	
	Shares	Weighted Average Exercise Price
Outstanding at beginning of period	672,669	$ 16.49
Granted	27,110	12.52
Forfeited	(1,334)	8.37
Outstanding at end of period	698,445	$ 16.35
Exercisable at end of period	567,599	$ 17.79
Vested or expected to vest in the future	694,487	$ 16.40

Restricted Stock Awards. The fair value of each restricted stock award with any market conditions is estimated on the date of grant using the Monte Carlo valuation method. The fair value of any restricted stock awards without market conditions is based on the market price of the Company's common stock on the date of grant. If applicable, the cash-settled component of any awards granted to employees is accounted for as a liability, which is adjusted to fair value each reporting period until vested.

Compensation cost arising from restricted stock awards granted to employees is recognized as an expense using the straight-line method over the vesting period. As of December 31, 2016 and September 30, 2016, there was $15.8 million and $11.0 million, respectively, of total unrecognized compensation cost related to nonvested restricted stock awards. The cost remaining as of December 31, 2016 is expected to be recognized over a weighted average period of 2.0 years.

We issued two types of restricted stock awards during the current quarter as follows: (1) performance-based restricted stock awards with a payout based on the Company's performance and certain market conditions and (2) time-based restricted stock awards. Each award type is discussed further below.

Performance-Based Restricted Stock Awards. During the three months ended December 31, 2016, we issued 263,696 shares of performance-based restricted stock (2017 Performance Shares) to our executive officers and certain other employees that also have market conditions. The 2017 Performance Shares are structured to be awarded based on the Company's performance under three pre-determined financial metrics at the end of the three-year performance period. After determining the number of shares earned based on these financial metrics, which can range from 0% to 175% of the targeted number of shares, the award will be subject to further upward or downward adjustment by as much as 20% based on the Company's relative total shareholder return

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(TSR) compared against the S&P Homebuilders Select Industry Index during the three-year performance period. The 2017 Performance Shares were valued using the Monte Carlo valuation model due to the existence of the TSR market condition and had an estimated fair value of $13.60 per share on the date of grant.

A Monte Carlo valuation model requires the following inputs: (1) the expected dividend yield on the underlying stock; (2) the expected price volatility of the underlying stock; (3) the risk-free interest rate for the period corresponding with the expected term of the award; and (4) the fair value of the underlying stock. For the Company and each member of the peer group, the following inputs were used, as applicable, in the Monte Carlo valuation model to determine the fair value as of the grant date for the 2017 Performance Shares: 0% dividend yield for the Company, expected price volatility ranging from 32.6% to 66.0% and a risk-free interest rate of 1.30%. The methodology used to determine these assumptions is similar to the Black-Scholes Model; however, the expected term is determined by the model in the Monte Carlo simulation.

Each Performance Share represents a contingent right to receive one share of the Company's common stock if vesting is satisfied at the end of the three-year performance period. Any 2017 Performance Shares earned in excess of the target number of 263,696 shares may be settled in cash or additional shares at the discretion of the Compensation Committee of our Board of Directors. Any portion of these that do not vest at the end of the period will be forfeited.

Time-Based Restricted Stock Awards. During three months ended December 31, 2016, we also issued 269,402 shares of time-based restricted stock (Restricted Shares) to our directors, executive officers and certain other employees. The Restricted Shares granted to our non-employee directors vest on the one-year anniversary of the date of grant, while the Restricted Shares granted to our executive officers and other employees vest ratably over three years from the date of grant.

Activity relating to restricted stock awards for the period presented is as follows:

	Three Months Ended December 31, 2016					
	Performance-Based Restricted Stock		Time-Based Restricted Stock		Total Restricted Stock	
	Shares	Weighted Average Grant Date Fair Value	Shares	Weighted Average Grant Date Fair Value	Shares	Weighted Average Grant Date Fair Value
Beginning of period	448,693	$ 16.71	807,124	$ 17.52	1,255,817	$ 17.23
Granted	263,696	13.60	269,402	12.51	533,098	13.05
Vested	—	—	(183,730)	15.49	(183,730)	15.49
Forfeited	(28,690)	11.65	—	—	(28,690)	11.65
End of period	683,699	$ 15.72	892,796	$ 16.43	1,576,495	$ 16.12

(12) Earnings Per Share

Basic income (loss) per share is calculated by dividing net income (loss) by the weighted-average number of shares outstanding during the period. Diluted income per share adjusts the basic income per share for the effects of any potentially dilutive instruments, only in periods in which the Company has net income and such effects are dilutive under the treasury stock method. Basic and diluted income (loss) per share is calculated using unrounded numbers.

The Company reported a net loss for the three months ended December 31, 2016. Accordingly, all common stock equivalents were excluded from the computation of diluted loss per share because inclusion would have resulted in anti-dilution. For the three months ended December 31, 2016 and 2015, 1.5 million and 1.2 million shares, respectively, related to nonvested stock-based compensation awards were excluded from our calculation of diluted income per share as a result of their anti-dilutive effect.

The weighted average number of common shares outstanding used to calculate basic income (loss) per share is reconciled to shares used to calculate diluted income (loss) per share as follows for the periods presented:

Three Months Ended

	December 31,	
(In thousands)	2016	2015
Basic shares	31,893	31,757
Shares issuable upon vesting/exercise of stock awards/options	—	87
Diluted shares	31,893	31,844

(13) Other Liabilities

Other liabilities include the following as of December 31, 2016 and September 30, 2016:

(In thousands)	December 31, 2016	September 30, 2016
Accrued warranty expense	$ 32,309	$ 39,131
Accrued interest	25,089	11,530
Accrued bonuses and deferred comp	14,464	30,466
Customer deposits	13,273	12,140
Litigation accrual	9,187	10,178
Income tax liabilities	1,772	1,718
Other	25,617	29,090
Total other liabilities	$ 121,711	$ 134,253

(14) Segment Information

We currently operate in 13 states that are grouped into three homebuilding segments based on geography. Revenues from our homebuilding segments are derived from the sale of homes that we construct and from land and lot sales. Our reportable segments have been determined on a basis that is used internally by management for evaluating segment performance and resource allocations. We have considered the applicable aggregation criteria, and have combined our homebuilding operations into three reportable segments as follows:

West: Arizona, California, Nevada and Texas

East: Delaware, Indiana, Maryland, New Jersey[a], Tennessee and Virginia

Southeast: Florida, Georgia, North Carolina and South Carolina

[a] During our fiscal 2015, we made the decision that we would not continue to reinvest in new homebuilding assets in our New Jersey division; therefore, it is no longer considered an active operation. However, it is included in this listing because the segment information below continues to include New Jersey.

Management's evaluation of segment performance is based on segment operating income. Operating income for our homebuilding segments is defined as homebuilding, land sale and other revenues less home construction, land development and land sales expense, commission expense, depreciation and amortization and certain G&A expenses that are incurred by or allocated to our homebuilding segments. The accounting policies of our segments are described in Note 2 to the consolidated financial statements within our 2016 Annual Report.

The following tables contain our revenue, operating income and depreciation and amortization by segment for the periods presented:

	Three Months Ended December 31,	
(In thousands)	2016	2015
Revenue		
West	$171,749	$157,196
East	84,159	100,557
Southeast	83,333	86,696
Total revenue	$339,241	$344,449

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(In thousands)	Three Months Ended December 31, 2016	2015
Operating income		
West	$21,015	$16,786
East [a]	1,557	4,147
Southeast [b]	5,015	10,657
Segment total	27,587	31,590
Corporate and unallocated [c]	(26,312)	(22,442)
Total operating income	$1,275	$9,148

(In thousands)	Three Months Ended December 31, 2016	2015
Depreciation and amortization		
West	$1,248	$1,218
East	529	797
Southeast	466	449
Segment total	2,243	2,464
Corporate and unallocated [b]	434	527
Total depreciation and amortization	$2,677	$2,991

[a] Operating income for our East segment for the three months ended December 31, 2016 was impacted by a charge to G&A of $2.7 million related to the write-off of a deposit on a legacy investment in a development site that we deemed noncollectible.

[b] Operating income for our Southeast segment for the three months ended December 31, 2015 was impacted by unexpected warranty costs related to the Florida stucco issues, net of expected insurance recoveries. This impact was a credit of $3.6 million.

[c] Corporate and unallocated operating loss includes amortization of capitalized interest; movement in capitalized indirects; expenses related to numerous shared services functions that benefit all segments but are not allocated to the operating segments reported above, including information technology, treasury, corporate finance, legal, branding and national marketing; and certain other amounts that are not allocated to our operating segments.

Corporate and unallocated depreciation and amortization represents depreciation and amortization related to assets held by our corporate functions that benefit all segments.

The following table contains our capital expenditures by segment for the periods presented:

(In thousands)	Three Months Ended December 31, 2016	2015
Capital Expenditures		
West	$1,184	$1,133
East	771	467
Southeast	618	969
Corporate and unallocated	301	94
Total capital expenditures	$2,874	$2,663

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The following table contains our asset balance by segment as of December 31, 2016 and September 30, 2016:

(In thousands)	December 31, 2016	September 30, 2016
Assets		
West	$ 796,962	$ 778,521
East	346,524	344,898
Southeast	344,074	333,501
Corporate and unallocated [a]	700,583	756,238
Total assets	$ 2,188,143	$ 2,213,158

[a] Primarily consists of cash and cash equivalents, restricted cash, deferred taxes, capitalized interest and indirects and other items that are not allocated to the segments.

(15) Supplemental Guarantor Information

As discussed in Note 7, our obligations to pay principal, premium, if any, and interest under certain debt are guaranteed on a joint and several basis by substantially all of our subsidiaries. Certain of our immaterial subsidiaries do not guarantee our Senior Notes, Term Loan or the Facility. The guarantees are full and unconditional and the guarantor subsidiaries are 100% owned by Beazer Homes USA, Inc. The following unaudited financial information presents the line items of our unaudited condensed consolidated financial statements separated by amounts related to the parent issuer, guarantor subsidiaries, non-guarantor subsidiaries and consolidating adjustments as of or for the periods presented.

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Beazer Homes USA, Inc.
Unaudited Condensed Consolidating Balance Sheet Information
December 31, 2016
(In thousands)

	Beazer Homes USA, Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Beazer Homes USA, Inc.
ASSETS					
Cash and cash equivalents	$ 159,886	$ 4,292	$ 853	$ (6,408)	$ 158,623
Restricted cash	14,683	1,280	—	—	15,963
Accounts receivable (net of allowance of $350)	—	51,797	—	—	51,797
Income tax receivable	288	—	—	—	288
Owned inventory	—	1,618,544	—	—	1,618,544
Investments in unconsolidated entities	773	4,292	—	—	5,065
Deferred tax assets, net	312,666	—	—	—	312,666
Property and equipment, net	—	19,335	—	—	19,335
Investments in subsidiaries	713,629	—	—	(713,629)	—
Intercompany	789,502	—	2,376	(791,878)	—
Other assets	822	5,040	—	—	5,862
Total assets	$ 1,992,249	$ 1,704,580	$ 3,229	$ (1,511,915)	$ 2,188,143
LIABILITIES AND STOCKHOLDERS' EQUITY					
Trade accounts payable	$ —	$ 86,730	$ —	$ —	$ 86,730
Other liabilities	25,014	96,345	352	—	121,711
Intercompany	2,376	795,910	—	(798,286)	—
Total debt (net of premium and debt issuance costs)	1,321,640	14,843	—	—	1,336,483
Total liabilities	1,349,030	993,828	352	(798,286)	1,544,924
Stockholders' equity	643,219	710,752	2,877	(713,629)	643,219
Total liabilities and stockholders' equity	$ 1,992,249	$ 1,704,580	$ 3,229	$ (1,511,915)	$ 2,188,143

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Beazer Homes USA, Inc.
Unaudited Condensed Consolidating Balance Sheet Information
September 30, 2016
(In thousands)

	Beazer Homes USA, Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Beazer Homes USA, Inc.
ASSETS					
Cash and cash equivalents	$ 215,646	$ 16,866	$ 859	$ (4,500)	$ 228,871
Restricted cash	12,867	1,538	—	—	14,405
Accounts receivable (net of allowance of $354)	—	53,225	1	—	53,226
Income tax receivable	292	—	—	—	292
Owned inventory	—	1,569,279	—	—	1,569,279
Investments in unconsolidated entities	773	9,697	—	—	10,470
Deferred tax assets, net	309,955	—	—	—	309,955
Property and equipment, net	—	19,138	—	—	19,138
Investments in subsidiaries	701,931	—	—	(701,931)	—
Intercompany	734,766	—	2,574	(737,340)	—
Other assets	577	6,930	15	—	7,522
Total assets	$ 1,976,807	$ 1,676,673	$ 3,449	$ (1,443,771)	$ 2,213,158
LIABILITIES AND STOCKHOLDERS' EQUITY					
Trade accounts payable	$ —	$ 104,174	$ —	$ —	$ 104,174
Other liabilities	11,315	122,561	377	—	134,253
Intercompany	2,574	739,266	—	(741,840)	—
Total debt (net of premium and debt issuance costs)	1,320,065	11,813	—	—	1,331,878
Total liabilities	1,333,954	977,814	377	(741,840)	1,570,305
Stockholders' equity	642,853	698,859	3,072	(701,931)	642,853
Total liabilities and stockholders' equity	$ 1,976,807	$ 1,676,673	$ 3,449	$ (1,443,771)	$ 2,213,158

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Beazer Homes USA, Inc.
Unaudited Consolidating Statements of Income (Loss) and Unaudited Comprehensive Income (Loss)
(In thousands)

	Beazer Homes USA, Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Beazer Homes USA, Inc.
Three Months Ended December 31, 2016					
Total revenue	$ —	$ 339,241	$ 36	$ (36)	$ 339,241
Home construction and land sales expenses	15,644	269,970	—	(36)	285,578
Gross profit (loss)	(15,644)	69,271	36	—	53,663
Commissions	—	13,323	—	—	13,323
General and administrative expenses	—	36,365	23	—	36,388
Depreciation and amortization	—	2,677	—	—	2,677
Operating income (loss)	(15,644)	16,906	13	—	1,275
Equity in income of unconsolidated entities	—	22	—	—	22
Other (expense) income, net	(5,252)	57	(1)	—	(5,196)
Income (loss) before income taxes	(20,896)	16,985	12	—	(3,899)
Expense (benefit) from income taxes	(7,569)	5,025	4	—	(2,540)
Equity in income of subsidiaries	11,968	—	—	(11,968)	—
Income (loss) from continuing operations	(1,359)	11,960	8	(11,968)	(1,359)
Loss from discontinued operations	(70)	—	—	—	(70)
Equity in loss of subsidiaries from discontinued operations	—	(67)	(3)	70	—
Net income (loss) and comprehensive income (loss)	$ (1,429)	$ 11,893	$ 5	$ (11,898)	$ (1,429)

	Beazer Homes USA, Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Beazer Homes USA, Inc.
Three Months Ended December 31, 2015					
Total revenue	$ —	$ 344,449	$ 73	$ (73)	$ 344,449
Home construction and land sales expenses	13,367	272,217	—	(73)	285,511
Inventory impairments and abandonments	—	1,356	—	—	1,356
Gross profit (loss)	(13,367)	70,876	73	—	57,582
Commissions	—	13,774	—	—	13,774
General and administrative expenses	—	31,642	27		31,669
Depreciation and amortization	—	2,991	—	—	2,991
Operating income (loss)	(13,367)	22,469	46	—	9,148
Equity in income of unconsolidated entities	—	60	—	—	60
Loss on extinguishment of debt	(828)	—	—	—	(828)
Other (expense) income, net	(7,432)	868	(1)	—	(6,565)
Income (loss) before income taxes	(21,627)	23,397	45	—	1,815
Expense (benefit) from income taxes	(10,143)	10,742	17	—	616
Equity in income of subsidiaries	12,683	—	—	(12,683)	—
Income from continuing operations	1,199	12,655	28	(12,683)	1,199
Loss from discontinued operations	—	(197)	(3)	—	(200)
Equity in loss of subsidiaries from discontinued operations	(200)	—	—	200	—
Net income and comprehensive income	$ 999	$ 12,458	$ 25	$ (12,483)	$ 999

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Beazer Homes USA, Inc.
Unaudited Condensed Consolidating Statements of Cash Flow Information
(In thousands)

	Beazer Homes USA, Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Beazer Homes USA, Inc.
Three Months Ended December 31, 2016					
Net cash used in operating activities	$ (2,902)	$ (59,928)	$ (4)	$ —	$ (62,834)
Cash flows from investing activities:					
Capital expenditures	—	(2,874)	—	—	(2,874)
Proceeds from sale of fixed assets	—	46	—	—	46
Investments in unconsolidated entities	—	(1,397)	—	—	(1,397)
Return of capital from unconsolidated entities	—	1,621	—	—	1,621
Increases in restricted cash	(1,817)	(1,829)	—	—	(3,646)
Decreases in restricted cash	—	2,088	—	—	2,088
Advances to/from subsidiaries	(50,314)	—	—	50,314	—
Net cash used in investing activities	(52,131)	(2,345)	—	50,314	(4,162)
Cash flows from financing activities:					
Repayment of debt	—	(2,525)	—	—	(2,525)
Debt issuance costs	(340)	—	—	—	(340)
Advances to/from subsidiaries	—	52,224	(2)	(52,222)	—
Other financing activities	(387)	—	—	—	(387)
Net cash (used in) provided by financing activities	(727)	49,699	(2)	(52,222)	(3,252)
Decrease in cash and cash equivalents	(55,760)	(12,574)	(6)	(1,908)	(70,248)
Cash and cash equivalents at beginning of period	215,646	16,866	859	(4,500)	228,871
Cash and cash equivalents at end of period	$ 159,886	$ 4,292	$ 853	$ (6,408)	$ 158,623

	Beazer Homes USA, Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Beazer Homes USA, Inc.
Three Months Ended December 31, 2015					
Net cash used in operating activities	$ (22,794)	$ (55,038)	$ (17)	$ —	$ (77,849)
Cash flows from investing activities:					
Capital expenditures	—	(2,663)	—	—	(2,663)
Proceeds from sale of fixed assets	—	2,437	—	—	2,437
Investments in unconsolidated entities	—	(1,779)	—	—	(1,779)
Return of capital from unconsolidated entities	—	1,142	—	—	1,142
Increases in restricted cash	—	(1,119)	—	—	(1,119)
Decreases in restricted cash	—	669	—	—	669
Advances to/from subsidiaries	(33,119)	—	—	33,119	—
Net cash used in investing activities	(33,119)	(1,313)	—	33,119	(1,313)
Cash flows from financing activities:					
Repayment of debt	(22,875)	(4,051)	—	—	(26,926)
Debt issuance costs	(413)	—	—	—	(413)
Advances to/from subsidiaries	—	38,312	(1)	(38,311)	—
Other financing activities	(201)	—	—	—	(201)
	(23,489)	34,261	(1)	(38,311)	(27,540)

Net cash (used in) provided by financing activities					
Decrease in cash and cash equivalents	(79,402)	(22,090)	(18)	(5,192)	(106,702)
Cash and cash equivalents at beginning of period	232,226	21,543	1,006	(3,192)	251,583
Cash and cash equivalents at end of period	$ 152,824	$ (547)	$ 988	$ (8,384)	$ 144,881

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(16) Discontinued Operations

We continually review each of our markets in order to refine our overall investment strategy and to optimize capital and resource allocations in an effort to enhance our financial position and to increase stockholder value. This review entails an evaluation of both external market factors and our position in each market, and over time has resulted in the decision to discontinue certain of our homebuilding operations. During our fiscal 2015, we made the decision that we would not continue to reinvest in new homebuilding assets in our New Jersey division; therefore, it is no longer considered an active operation. However, the results of our New Jersey division are not included in the discontinued operations information shown below.

We have classified the results of operations of our discontinued operations separately in the accompanying unaudited condensed consolidated statements of income for all periods presented. There were no material assets or liabilities related to these discontinued operations as of December 31, 2016 or September 30, 2016. Discontinued operations were not segregated in the unaudited condensed consolidated statements of cash flows. Therefore, amounts for certain captions in the unaudited condensed consolidated statements of cash flows will not agree with the respective data in the unaudited condensed consolidated statements of income. The results of our discontinued operations in the unaudited condensed consolidated statements of income for the periods presented were as follows:

	Three Months Ended December 31,	
(In thousands)	2016	2015
Total revenue	$—	$—
Home construction and land sales expenses	78	308
Gross loss	(78)	(308)
General and administrative expenses	31	2
Loss from discontinued operations before income taxes	(109)	(310)
Benefit from income taxes	(39)	(110)
Loss from discontinued operations, net of tax	$(70)	$(200)

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Executive Overview and Outlook

Market Conditions

In any period, the demand for new homes is dependent on a variety of factors, including job growth, changes in population and demographics, the availability and cost of mortgage financing, the supply of new and existing homes and, importantly, consumer confidence. These factors all fluctuate over time at both a national and a more localized market level. While we believe that there are multiple factors that point to further improvement in the homebuilding market in the next several years, such as rising levels of household formation, tight housing supply in many markets, job and wage growth and mortgage rates that continue to be historically low, there are several risks that could significantly impact our business during our fiscal 2017. These risks include fragile consumer confidence, continued volatility in our domestic and international stock markets, political uncertainty and possible legislative reform, rising interest rates, and potential mortgage reform, as well as a variety of local market risks where we do business. However, we continue to believe that we are well positioned in key markets, and that the underlying fundamentals that drive home purchases are supportive.

Overview of Results for Our Fiscal First Quarter

For the quarter ended December 31, 2016, we recorded a net loss from continuing operations of $1.4 million, a decline of $2.6 million from the prior year quarter's net income from continuing operations of $1.2 million. However, the following items impacted the comparability of our net income/loss from continuing operations between periods: (1) during the current quarter, we recorded a $2.7 million charge within our general and administrative expenses (G&A) to write off a deposit on a legacy investment in a development site that we deemed noncollectible and (2) during the prior year quarter, we recorded a credit to cost of sales of $3.6 million for insurance recoveries received or anticipated to be received that were greater than charges recorded in the prior year quarter related to the Florida stucco issues (see Note 8 of the notes to our unaudited condensed consolidated financial statements in this Form 10-Q).

Looking at our underlying operating results, year-over-year closings declined by 5.1%, from 1,049 in the prior year quarter to 995 in the current quarter, due primarily to our anticipated decline in average community count, but our average selling price (ASP) increased over the prior year quarter by 5.3%. Combined, these factors caused our homebuilding revenue to be relatively flat, falling only slightly from $336.6 million in the prior year quarter to $336.1 million in the current quarter. Our homebuilding gross margin, excluding impairments, abandonments, interest and, in the prior year quarter, the credit to cost of sales related to the Florida stucco issues mentioned above, showed slight year-over-year improvement to 20.5% in the current quarter from 20.4% in the prior year quarter. Commissions expense declined year-over-year due to the modest revenue decline, but remained consistent as a percentage of homebuilding revenue. Finally, our G&A increased year-over-year by $4.7 million, and has increased as a percentage of total revenue from 9.2% in the prior year quarter to 10.7% in the current quarter. This increase includes the write off of the deposit discussed above, which is partially offset by the recording of $1.2 million in expense related to the Deferred Prosecution Agreement (DPA) in the prior year quarter (see Note 8 of the notes to our unaudited condensed consolidated financial statements in this Form 10-Q). The remaining increase in G&A is due to higher compensation-related expenditures, as we look to right-size our team and prepare for future growth opportunities.

We ended the quarter with a backlog of 1,926 units, which represents a 0.7% increase over the 1,912 backlog units we had as of the end of the prior year quarter. Although we entered the current quarter with 122 fewer backlog units when compared to the prior year quarter, an 8.9% increase in new order activity versus the prior year quarter allowed us to build up our backlog stronger than where it was a year ago. The current quarter ending backlog has an ASP of $345.8 thousand, a year-over-year increase of 4.2%.

Reaching "2B-10"

In November 2013, we introduced a multi-year "2B-10" plan, which provided a roadmap of revenue and margin metrics to achieve $2 billion in revenue with a 10% Adjusted EBITDA margin. Taken together, reaching "2B-10" would result in Adjusted EBITDA of at least $200 million. In November 2015, we refined the specific metrics we expect will lead us to our "2B-10" objectives by providing ranges to each metric instead of point estimates. Since we rolled out our "2B-10" plan, we have consistently noted that there are a number of paths to achieving our underlying goal of $200 million of EBITDA, and that we continue our commitment to reaching these objectives as soon as possible. We expect

to reach these objectives by making improvements on five key metrics: (1) sales per community per month (our absorption rate); (2) ASP; (3) active community count; (4) homebuilding gross margin; and (5) cost leverage as measured by selling, general and administrative costs (SG&A) as a percentage of total revenue.

Since introducing our "2B-10" plan, we have made significant progress on achieving our Adjusted EBITDA goal (refer to "EBITDA: Reconciliation of Net Income (Loss) to Adjusted EBITDA" section below), driven by improvements with regard to the majority

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of our key metrics over time due to the intense focus we have placed on the operational drivers of this plan, and, in part, to stronger home pricing conditions. Our progress on each metric is discussed in more detail below:

- Sales per community per month was 2.2 and 1.8 for the quarters ended December 31, 2016 and December 31, 2015, respectively. Our strong emphasis on sales absorptions within our lower active community count allowed us to achieve a significant year-over-year increase in this metric and to rebuild our backlog unit levels. Sales per community per month increased to 2.8 for the trailing 12 months ended December 31, 2016 versus 2.7 a year ago, and is within the range established in our "2B-10" plan of 2.8 to 3.2. We continue to believe that we are among the industry leaders in sales absorption rates, and are focused on maintaining our strong sales momentum through the remainder of our fiscal 2017.
- Our ASP for closings during the trailing 12 months ended December 31, 2016 was $332.6 thousand, up 4.6% year-over-year, and our ASP in backlog as of December 31, 2016 has risen 4.2% versus the prior year quarter to $345.8 thousand. Our targeted metric for ASP established in November 2015 was a range of $330.0 thousand to $340.0 thousand, which we have achieved and believe we can maintain based on the gradual increase in our ASP on closed homes, our ASP on homes in backlog as of December 31, 2016 and our current mix of communities available for sale. As such, we are increasing our targeted metric for ASP to a range of $340.0 thousand to $350.0 thousand.
- During the current quarter, we had an average active community count of 156, down 7.9% from the prior year quarter, and ended the quarter with 154 active communities. This decline in community count was anticipated, as we focused during our fiscal 2016 on balancing our community count with our goal of reducing our outstanding debt balance. However, we expect higher spend on land and land development activities during the current fiscal year, and a corresponding growth in community count in fiscal 2018 and beyond. We invested another $103.2 million in land and land development during the current quarter, bringing our total spending for the trailing 12-month period to $328.2 million. Additionally, we have (1) increasingly focused on the use of option contracts and developed lot deals to maximize the efficiency of our capital, and (2) continued to activate certain parcels of land held for future development so that these assets can begin to generate revenue. We continue to strategically evaluate opportunities to purchase land within our geographic footprint, balancing our desire to reduce our leverage with land acquisition strategies that minimize our capital employed. Our "2B-10" target metric is an active community count range between 170 and 175.
- Homebuilding gross margin excluding impairments, abandonments and interest for the trailing 12 months ended December 31, 2016 was 21.5%, which is within our "2B-10" target metric range of between 21.0% and 22.0%. However, excluding the $15.5 million reduction in cost of sales recorded during the third quarter of our fiscal 2016 resulting from an agreement entered into with our third-party insurer to resolve certain issues related to the extent of our insurance coverage for multiple policy years, our homebuilding gross margin for the trailing 12 months ended December 31, 2016 would have been 20.6%, just below our target metric range. Our homebuilding gross margin has been impacted by a number of headwinds, including the increasing cost of land, driven by both market conditions and the structure of our land deals, and labor, as well as geographic, product and community mix (including an increasing number of closings from recently activated assets formerly classified as land held for future development, which generally have lower margins). While we anticipate these headwinds to continue, we expect our homebuilding margin, as it has in the current quarter, to stabilize and modestly improve in the coming quarters.
- SG&A for the trailing 12 months ended December 31, 2016 was 12.6% of total revenue, an increase of 30 basis points from the prior year. However, excluding the $2.7 million charge to write off a deposit on a legacy investment in a development site that we deemed noncollectible, SG&A for the trailing 12 months ended December 31, 2016 was 12.4% of total revenue. Although it is slightly above our "2B-10" target range of between 11.0% and 12.0%, we believe that as we grow revenue from our larger base of communities expected during our fiscal 2018 and beyond, as well as higher ASPs, we will demonstrate improved SG&A cost leverage.

For the trailing 12 months ended December 31, 2016, our revenue was $1.8 billion, up 6.5% year-over-year. Excluding the non-recurring items detailed in the full reconciliation of our EBITDA (refer to section below entitled "EBITDA: Reconciliation of Net Income (Loss) to Adjusted EBITDA"), Adjusted EBITDA for the trailing 12 months ended December 31, 2016 increased $1.1 million, or 0.7%, to $154.8 million.

We expect to continue our focus on our “2B-10” metrics throughout fiscal 2017, with particular emphasis on driving sales absorptions and improving our homebuilding gross margin.

Debt Reduction and Capital Efficiency

During our fiscal 2016, we reduced our debt balance by nearly $157 million, which surpassed our initial debt reduction target for the prior fiscal year. We will continue to focus on deleveraging, and plan to further reduce our debt by at least another $100 million through our fiscal 2018. We believe that doing so in a strong housing market will create long-term shareholder value. By actively managing our debt structure, we were successful in paying off certain secured senior notes in part by issuing unsecured senior

debt with a later maturity date. See Note 7 of the notes to our unaudited condensed consolidated financial statements in this Form 10-Q for further discussion of our outstanding borrowings.

Additionally, we have increasingly sought to maximize our return on capital by carefully managing our investment in land, so that our debt reduction targets can be achieved while still concentrating on community count. To reduce the risks associated with these investments and to maximize our capital base, we have increasingly used options to control land. Furthermore, we have activated certain parcels of land held for future development so that these assets can begin to generate revenue for the Company.

Seasonal and Quarterly Variability: Our homebuilding operating cycle generally reflects escalating new order activity in the second and third fiscal quarters and increased closings in the third and fourth fiscal quarters. Accordingly, our financial results for the three months ended December 31, 2016 may not accurately predict our ultimate full year results.

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RESULTS OF CONTINUING OPERATIONS:

The following table summarizes certain key income statement metrics for the periods presented:

	Three Months Ended December 31,			
($ in thousands)	2016		2015	
Revenues:				
Homebuilding	$336,126		$336,593	
Land sales and other	3,115		7,856	
Total	$339,241		$344,449	
Gross profit:				
Homebuilding	$53,204		$58,063	
Land sales and other	459		(481	)
Total	$53,663		$57,582	
Gross margin:				
Homebuilding[a]	15.8	%	17.3	%
Land sales and other	14.7	%	(6.1	)%
Total	15.8	%	16.7	%
Commissions	$13,323		$13,774	
General and administrative expenses (G&A)	36,388		31,669	
SG&A (commissions plus G&A) as a percentage of total revenue	14.7	%	13.2	%
G&A as a percentage of total revenue	10.7	%	9.2	%
Depreciation and amortization	$2,677		$2,991	
Operating income	$1,275		$9,148	
Operating income as a percentage of total revenue	0.4	%	2.7	%
Effective Tax Rate[c]	65.1	%	33.9	%
Equity in income of unconsolidated entities	$22		$60	
Loss on extinguishment of debt	—		828	

[a] In addition to other items impacting homebuilding gross margin, for the three months ended December 31, 2015, this metric was impacted by warranty costs related to the Florida stucco issues, net of the associated insurance recoveries. Refer to further discussion of these items below in section titled “Homebuilding Gross Profit and Gross Margin.”

[b] In addition to other items impacting G&A, for the three months ended December 31, 2016, this metric was impacted by a $2.7 million charge to write off a deposit on a legacy investment in a development site that we deemed noncollectible.

[c] Calculated as tax expense (benefit) for the period divided by income (loss) from continuing operations. Due to the effects of a variety of factors, including the impact of discrete tax items on our effective tax rate, our income tax expense (benefit) is not always directly correlated to the amount of pretax income (loss) for the associated periods, particularly when focusing on individual quarters.

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EBITDA: Reconciliation of Net Income (Loss) to Adjusted EBITDA

Reconciliation of Adjusted EBITDA (earnings before interest, taxes, depreciation, amortization, debt extinguishment, impairments and abandonments) to total company net income (loss), the most directly comparable GAAP measure, is provided for each period presented below. Management believes that Adjusted EBITDA, which is a non-GAAP measure, assists investors in understanding and comparing the operating characteristics of homebuilding activities by eliminating many of the differences in companies' respective capitalization, tax position and level of impairments. These EBITDA measures should not be considered alternatives to net income determined in accordance with GAAP as an indicator of operating performance.

In addition, given the unusual size and nature of certain amounts recorded during the periods presented, Adjusted EBITDA is also shown excluding these amounts in the following table. Management believes that this representation best reflects the operating characteristics of the Company.

The following table reconciles our net income (loss) to Adjusted EBITDA for the periods presented:

	Three Months Ended December 31,			LTM Ended December 31, [a]		
(In thousands)	2016	2015	16 vs 15	2016	2015	16 vs 15
Net income (loss)	$(1,429)	$999	$(2,428)	$2,265	$367,433	$(365,168)
Expense (benefit) from income taxes	(2,579)	506	(3,085)	13,139	(324,724)	337,863
Interest amortized to home construction and land sales expenses, capitalized interest impaired and interest expense not qualified for capitalization	20,896	21,083	(187)	104,523	89,035	15,488
Depreciation and amortization and stock-based compensation amortization	4,859	4,747	112	21,864	20,505	1,359
Inventory impairments and abandonments [b]	—	1,356	(1,356)	13,216	4,465	8,751
Loss on debt extinguishment	—	828	(828)	12,595	908	11,687
Adjusted EBITDA	$21,747	$29,519	$(7,772)	$167,602	$157,622	$9,980
Unexpected warranty costs related to Florida stucco issues (net of expected insurance recoveries)	—	(3,612)	3,612	—	(3,612)	3,612
Additional insurance recoveries from third-party insurer	—	—	—	(15,500)	—	(15,500)
Litigation settlement in discontinued operations	—	—	—	—	(340)	340
Write-off of deposit on legacy land investment	2,700	—	2,700	2,700	—	2,700
Adjusted EBITDA excluding unexpected warranty costs (net of recoveries), additional insurance recoveries, litigation settlement and write-off of deposit	$24,447	$25,907	$(1,460)	$154,802	$153,670	$1,132

[a] "LTM" indicates amounts for the trailing 12 months.

[b] Amounts for the trailing 12 months ended December 31, 2016 and 2015 excludes capitalized interest impaired during the period. Capitalized interest that is impaired is included in the line above titled "Interest amortized to home construction and land sales expenses, capitalized interest impaired and interest expense not qualified for capitalization."

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Homebuilding Operations Data

The following table summarizes new orders, net and cancellation rates by reportable segment for the periods presented:

	Three Months Ended December 31,				
	New Orders, net			Cancellation Rates	
	2016	2015	16 vs 15	2016	2015
West	467	422	10.7 %	20.2 %	24.1 %
East	228	248	(8.1)%	22.7 %	25.7 %
Southeast	310	253	22.5 %	21.5 %	28.5 %
Total	1,005	923	8.9 %	21.2 %	25.8 %

Sales per community per month was 2.2 and 1.8 for the quarters ended December 31, 2016 and December 31, 2015, respectively, an increase of 18.2%. Our strong emphasis on sales absorptions within our lower active community count allowed us to achieve a significant year-over-year increase in this metric and to rebuild our backlog unit levels. Our average active communities declined 7.9% year-over-year from 169 to 156 during the quarter ended December 31, 2016, partially offsetting our stronger absorptions and ultimately resulting in an 8.9% increase in new orders, net.

For the three months ended December 31, 2016, the increase in new orders, net in our West segment was driven by all of our markets except for Texas, where we had a decline in order activity, particularly in Houston due to a lower community count in response to local economic conditions. The decrease in new orders, net in our East segment for the three months ended December 31, 2016 was caused by a decline in our Maryland market, due to a particularly strong prior year sales performance as we sold additional speculative (spec) homes to generate capital, and our New Jersey market, which did not have any order activity in the current quarter but was winding down in the prior year quarter. Finally, the year-over-year increase in new orders, net for the three months ended December 31, 2016 in our Southeast segment was primarily driven by strong order activity in our Raleigh market, where we have increased our community count, and our Charleston market, as several newer communities have started to gain momentum.

The table below summarizes backlog units by reportable segment, as well as aggregate dollar value of homes in backlog and ASP for homes in backlog as of December 31, 2016 and December 31, 2015:

	As of December 31,		
	2016	2015	16 vs 15
Backlog Units:			
West	785	885	(11.3)%
East	455	478	(4.8)%
Southeast	686	549	25.0 %
Total	1,926	1,912	0.7 %
Aggregate dollar value of homes in backlog (in millions)	$666.1	$634.6	5.0 %
ASP in backlog (in thousands)	$345.8	$331.9	4.2 %

Backlog above reflects the number of homes for which the Company has entered into a sales contract with a customer but has not yet delivered the home. Backlog units as of December 31, 2016 increased by 0.7% from the prior year due to the increase in new orders, net described above, coupled with lower closings as compared to the prior year period. Although we entered the current year quarter with fewer backlog units and a lower community count, we were able to build our backlog through a substantial improvement in sales absorptions year-over-year.

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Homebuilding Revenue, Average Selling Price and Closings

The table below summarizes homebuilding revenue, the ASP of our homes closed and closings by reportable segment for the periods presented:

	Three Months Ended December 31,								
	Homebuilding Revenue			Average Selling Price			Closings		
($ in thousands)	2016	2015	16 vs 15	2016	2015	16 vs 15	2016	2015	16 vs 15
West	$171,749	$157,196	9.3 %	$336.8	$319.5	5.4%	510	492	3.7 %
East	81,250	94,345	(13.9)%	374.4	367.1	2.0%	217	257	(15.6)%
Southeast	83,127	85,052	(2.3)%	310.2	283.5	9.4%	268	300	(10.7)%
Total	$336,126	$336,593	(0.1)%	$337.8	$320.9	5.3%	995	1,049	(5.1)%

The change in ASP for the three months ended December 31, 2016 was impacted primarily by a change in mix of closings between geographies, products and among communities within each individual market as compared to the prior year period. It was also positively impacted by our operational strategies, as well as improved market conditions in certain geographies.

Generally, closings for the three months ended December 31, 2016 declined due to our lower year-over-year community count in comparative periods, and, more specifically, was also driven by (1) a sharp decline in our Maryland market, where we sold and closed a significant number of spec homes in the prior year quarter to generate capital for debt reduction; (2) fewer closings in our Texas market, as the prior year quarter benefited from additional closings that were pushed out of the end of our fiscal 2015 due to the weather conditions in that region; (3) no closings from our de-activated New Jersey market in the current quarter, whereas we were still closing homes in the prior year quarter; and (4) fewer backlog units entering the current quarter when compared to the prior year quarter. These declines were partially offset by improved performance in communities that have recently opened, as we continue to gain sales and closings momentum.

The increase in our ASP nearly canceled out the decline in closings, resulting in homebuilding revenue that was relatively flat year-over-year, as shown in the table above. On average, we anticipate that our ASP will likely continue to increase in future quarters, as indicated by our ASP for homes in backlog.

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Homebuilding Gross Profit and Gross Margin

The following tables present our homebuilding (HB) gross profit and gross margin by reportable segment and total homebuilding gross profit and gross margin, as well as such amounts excluding inventory impairments and abandonments and interest amortized to cost of sales (COS) for the periods presented. Homebuilding gross profit is defined as homebuilding revenue less home cost of sales (which includes land and land development costs, home construction costs, capitalized interest, indirect costs of construction, estimated warranty costs, closing costs and inventory impairment and abandonment charges). Additionally, we have shown the impact of unexpected warranty costs related to the Florida stucco issues, net of insurance recoveries, which we consider to be a non-recurring item, on our gross profit and gross margin for the prior year quarter.

	Three Months Ended December 31, 2016							
($ in thousands)	HB Gross Profit (Loss)	HB Gross Margin	Impairments & Abandonments (I&A)	HB Gross Profit (Loss) w/o I&A	HB Gross Margin w/o I&A	Interest Amortized to COS	HB Gross Profit w/o I&A and Interest	HB Gross Margin w/o I&A and Interest
West	$36,817	21.4 %	$ —	$ 36,817	21.4 %	$ —	$36,817	21.4 %
East	13,428	16.5 %	—	13,428	16.5 %	—	13,428	16.5 %
Southeast	14,577	17.5 %	—	14,577	17.5 %	—	14,577	17.5 %
Corporate & unallocated	(11,618)		—	(11,618)		15,644	4,026	
Total homebuilding	$53,204	15.8 %	$ —	$ 53,204	15.8 %	$ 15,644	$68,848	20.5 %

	Three Months Ended December 31, 2015							
($ in thousands)	HB Gross Profit (Loss)	HB Gross Margin	Impairments & Abandonments (I&A)	HB Gross Profit (Loss) w/o I&A	HB Gross Margin w/o I&A	Interest Amortized to COS	HB Gross Profit w/o I&A and Interest	HB Gross Margin w/o I&A and Interest
West	$32,213	20.5 %	$ —	$ 32,213	20.5 %	$ —	$32,213	20.5 %
East	14,598	15.5 %	—	14,598	15.5 %	—	14,598	15.5 %
Southeast	19,649	23.1 %	788	20,437	24.0 %	—	20,437	24.0 %
Corporate & unallocated	(8,397)		—	(8,397)		13,367	4,970	
Total homebuilding	$58,063	17.3 %	$ 788	$ 58,851	17.5 %	$ 13,367	$72,218	21.5 %
Unexpected warranty costs related to Florida stucco issues (net of expected insurance recoveries)	(3,612)						(3,612)	
Adjusted homebuilding	54,451	16.2 %					68,606	20.4 %

Our overall homebuilding gross profit declined by $4.9 million to $53.2 million for the three months ended December 31, 2016, from $58.1 million in the prior year period, despite homebuilding revenue being essentially flat. However, the comparability of our gross profit, as shown in the tables above, was impacted by several items as follows: (1) prior year quarter gross profit included a credit to cost of sales of $3.6 million for insurance recoveries received or anticipated to be received that were greater than that quarter's charges related to the Florida stucco issues; (2) prior year gross profit also included $0.8 million in impairment and abandonment charges taken in our Southeast segment; and (3) interest amortized to homebuilding cost of sales increased by $2.3 million, from $13.4 million in the prior year quarter to $15.6 million in the current quarter (refer to Note 6 of the notes to our unaudited condensed

consolidated financial statements in this Form 10-Q). When these items are taken into consideration, year-over-year gross profit, like homebuilding revenue, is essentially flat, and our homebuilding gross margin improved by 10 basis points.

Our gross margin continues to be impacted by the following factors: (1) mix of closings between geographies/markets, individual communities within each market, and product type; (2) activation of assets formerly classified as land held for future development, which generally have lower margins; (3) the structure of our land purchase transactions, since finished lot purchases tend to result in lower gross margins; (4) the mix between speculative homes and "to be built" homes closed in each period; and (5) higher labor costs.

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Total homebuilding gross profit and gross margin excluding inventory impairments and abandonments, interest amortized to cost of sales and other non-recurring items that we disclose are not GAAP financial measures. These measures should not be considered alternatives to homebuilding gross profit and gross margin determined in accordance with GAAP as an indicator of operating performance.

In particular, the magnitude and volatility of non-cash inventory impairment and abandonment charges for the Company, and for other homebuilders, have been significant and, as such, have made financial analysis of our industry more difficult. Homebuilding metrics excluding these charges, as well as interest amortized to cost of sales, and other similar presentations by analysts and other companies are frequently used to assist investors in understanding and comparing the operating characteristics of homebuilding activities by eliminating many of the differences in companies' respective level of impairments and levels of debt. Management believes these non-GAAP measures enable holders of our securities to better understand the cash implications of our operating performance and our ability to service our debt obligations as they currently exist and as additional indebtedness is incurred in the future. These measures are also useful internally, helping management compare operating results and as a measure of the level of cash which may be available for discretionary spending.

In a given period, our reported gross profit is generated from both communities previously impaired and communities not previously impaired. In addition, as indicated above, certain gross profit amounts arise from recoveries of prior period costs, including warranty items, that are not directly tied to communities generating revenue in the period. Home closings from communities previously impaired would, in most instances, generate very low or negative gross margins prior to the impact of the previously recognized impairment. Gross margin for each home closing is higher for a particular community after an impairment because the carrying value of the underlying land was previously reduced to the present value of future cash flows as a result of the impairment, leading to lower cost of sales at the home closing. This improvement in gross margin resulting from one or more prior impairments is frequently referred to in the aggregate as the “impairment turn” or “flow-back” of impairments within the reporting period. The amount of this impairment turn may exceed the gross margin for an individual impaired asset if the gross margin for that asset prior to the impairment would have been negative. The extent to which this impairment turn is greater than the reported gross margin for the individual asset is related to the specific historical cost basis of that individual asset.

The asset valuations that result from our impairment calculations are based on discounted cash flow analyses and are not derived by simply applying prospective gross margins to individual communities. As such, impaired communities may have gross margins that are somewhat higher or lower than the gross margin for unimpaired communities. The mix of home closings in any particular quarter varies to such an extent that comparisons between previously impaired and never impaired communities would not be a reliable way to ascertain profitability trends or to assess the accuracy of previous valuation estimates. In addition, since any amount of impairment turn is tied to individual lots in specific communities, it will vary considerably from period to period. As a result of these factors, we review the impairment turn impact on gross margin on a trailing 12-month basis rather than a quarterly basis as a way of considering whether our impairment calculations are resulting in gross margins for impaired communities that are comparable to our unimpaired communities. For the trailing 12-month period, our homebuilding gross margin was 16.2% and excluding interest and inventory impairments, it was 21.5%. For the same trailing 12-month period, homebuilding gross margin was as follows in those communities that have previously been impaired, which represented 8.0% of total closings during this period:

Homebuilding Gross Margin from previously impaired communities:	
Pre-impairment turn gross margin	(7.6)%
Impact of interest amortized to COS related to these communities	5.1 %
Pre-impairment turn gross margin, excluding interest amortization	(2.5)%
Impact of impairment turns	13.9 %
Gross margin (post impairment turns), excluding interest amortization	11.4 %

For a further discussion of our impairment policies, refer to Notes 2 and 5 of the notes to unaudited condensed consolidated financial statements in this Form 10-Q.

Land Sales and Other Revenues and Gross Profit (Loss)

Land sales relate to land and lots sold that did not fit within our homebuilding programs and strategic plans in certain markets. Other revenues included net fees we received for general contractor services we performed on behalf of a third party and broker fees. The following tables summarize our land sales and other revenues and related gross profit (loss) by reportable segment for the periods presented:

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	Land Sales and Other Revenues			Land Sales and Other Gross Profit (Loss)		
	Three Months Ended December 31,			Three Months Ended December 31,		
(In thousands)	2016	2015	16 vs 15	2016	2015	16 vs 15
West	$ —	$ —	$ —	$ 278	$ 351	$ (73)
East	2,909	6,212	(3,303)	131	(246)	377
Southeast	206	1,644	(1,438)	50	(214)	264
Corporate and unallocated [a]	—	—	—	—	(372)	372
Total	$ 3,115	$ 7,856	$ (4,741)	$ 459	$ (481)	$ 940

[a] Corporate and unallocated includes interest and indirects related to land sold that was costed off.

Although not as significant as in the prior year period, to further support our efforts to reduce our leverage, we continued to focus on closing on a number of land sales in the three months ended December 31, 2016 that did not fit within our strategic plans. We expect additional land sales to occur during the remainder of our fiscal 2017. However, future land and lot sales will depend on a variety of factors, including local market conditions, individual community performance and changing strategic plans.

Operating Income

The table below summarizes operating income (loss) by reportable segment for the periods presented:

	Three Months Ended December 31,		
(In thousands)	2016	2015	16 vs 15
West	$21,015	$16,786	$4,229
East [a]	1,557	4,147	(2,590)
Southeast [b]	5,015	10,657	(5,642)
Corporate and Unallocated [c]	(26,312)	(22,442)	(3,870)
Operating income	$1,275	$9,148	$(7,873)

[a] Operating income for our East segment for the three months ended December 31, 2016 was impacted by a charge to G&A of $2.7 million related to the write-off of a deposit on a legacy investment in a development site that we deemed noncollectible.

[b] Operating income for our Southeast segment for the three months ended December 31, 2015 was impacted by a credit to cost of sales of $3.6 million for unexpected warranty costs related to the Florida stucco issues, net of expected insurance recoveries.

[c] Corporate and unallocated operating loss includes amortization of capitalized interest; movement in capitalized indirects; expenses related to numerous shared services functions that benefit all segments but are not allocated to the operating segments; and certain other amounts that are not allocated to our operating segments.

Our operating income declined by $7.9 million to $1.3 million for the three months ended December 31, 2016, compared to $9.1 million for the three months ended December 31, 2015. As discussed above, our homebuilding gross profit during the current quarter declined by $4.9 million (but was relatively flat when adjusted for non-recurring items, impairments and abandonments, and interest amortized to cost of sales). In addition to lower year-over-year gross profit, our decline in operating income was also driven by an increase in G&A of $4.7 million. Higher G&A was the result of: (1) a charge of $2.7 million related to the write-off of a deposit on a legacy investment in a development site that we deemed noncollectible and (2) higher compensation-related expenditures, as we look to right-size our team and prepare for future growth opportunities, such as the Gatherings active adult communities, offset by (3) the recording of $1.2 million in expense related to the DPA in the prior year quarter (see Note 8 of the notes to our unaudited condensed consolidated financial statements in this Form 10-Q). Lower gross profit and higher G&A during the current quarter were partially offset by a $0.9 million increase in land sales and other gross profit, as well as a year-over-year decline in commissions expense of $0.5 million.

Below operating income, we had two noteworthy year-over-year fluctuations for the three months ended December 31, 2016 as follows: (1) we had a current quarter decline in our other expense, net, mainly driven by a

reduction in our interest costs on a lower outstanding debt balance (refer to Note 6 of the notes to our unaudited condensed consolidated financial statements in this Form 10-Q) and (2) we recorded a loss on the extinguishment of debt in the prior year quarter of $0.8 million from paying down $22.9 million of the then outstanding Senior Notes due June 2016; no debt repurchase activity occurred during the current quarter.

Income taxes

Our income tax assets and liabilities and related effective tax rate are affected by various factors, the most significant of which is the valuation allowance recorded against substantially all of our deferred tax assets, but was partially released in the fourth quarter

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of our fiscal 2015. Due to the effect of our valuation allowance adjustments beginning in fiscal 2008, a comparison of our annual effective tax rates must consider the changes in our valuation allowance. As such, our effective tax rates have not been meaningful metrics, as our income tax expense/benefit was not directly correlated to the amount of pretax income or loss for the associated periods. Beginning in our fiscal 2016, the Company started using an annualized effective tax rate in interim periods to determine its tax expense/benefit, which should more closely correlate with our pretax income or loss in periods, but will continue to be impacted by discrete tax items.

Our current quarter income tax benefit was primarily driven by (1) the loss in earnings from continuing operations in the current period and (2) the Company's completion of work necessary to claim an additional $1.2 million in tax credits, which were recorded in the current quarter but related to our fiscal 2016. The tax expense for the three months ended December 31, 2015 was primarily driven by our earnings from continuing operations.

As discussed in our Annual Report on Form 10-K for the fiscal year ended September 30, 2016, we executed a restructuring effort in the current quarter that involved changes in the legal forms and tax elections for certain of our operating entities. These efforts were undertaken to reduce our effective tax rate to an amount that is in-line with our peers, while also providing cash tax savings in jurisdictions where we no longer have significant loss carryforwards available. Our fiscal 2017 annualized effective tax rate, excluding the impacts of discrete items recorded in the period, is currently in-line with our peers, and we expect to remain in that range in subsequent fiscal years.

Refer to Note 10 of the notes to our unaudited condensed consolidated financial statements included in this Form 10-Q for a further discussion of our income taxes.

Three months ended December 31, 2016 as compared to 2015

West Segment: Homebuilding revenue increased 9.3% for the three months ended December 31, 2016 compared to the prior year quarter due to a 3.7% increase in closings (particularly in our Sacramento market, which reopened during our fiscal 2015), as well as a year-over-year increase in ASP of 5.4%, which improved in the majority of our markets in the West segment. As compared to the prior year period, our homebuilding gross profit increased by $4.6 million, due mainly to the increase in revenue already discussed, as well as an increase in homebuilding gross margin from 20.5% to 21.4%. Gross margin increased in the majority of our markets in the West segment, particularly in Sacramento where our re-opened communities continue to gain momentum. The $4.2 million increase in operating income resulted from the aforementioned increase in homebuilding gross profit, partially offset by a modest increase in G&A costs, particularly with the growth of the Sacramento market.

East Segment: Homebuilding revenue decreased by 13.9% for the three months ended December 31, 2016 compared to the prior year quarter, primarily due to a 15.6% decline in closings (mainly driven by our Maryland market, where we sold and closed a significant number of spec homes in the prior year quarter to generate capital for debt reduction, and the absence of closings from our de-activated New Jersey market in the current quarter, where we were still closing homes in the prior year quarter as we wound down operations), partially offset by the impact of a 2.0% increase in ASP. As compared to the prior year period, our homebuilding gross profit decreased $1.2 million, related mainly to the aforementioned decline in homebuilding revenue, offset by higher homebuilding gross margin, which increased from 15.5% in the prior year quarter to 16.5%. Gross margin increased for all of our markets in the East segment, and were driven up for the segment overall due to the closing of additional low-margin spec homes in our Maryland market during the prior year quarter to return capital to the company and the closeout of our New Jersey division, which generated several lower margin closings in the prior year period. The $2.6 million decline in operating income resulted from the decrease in gross profit as previously discussed, and higher G&A costs, driven by a charge of $2.7 million related to the write-off of a deposit on a legacy investment in a development site that we deemed noncollectible. However, outside of the deposit write-off, commissions, sales and marketing and G&A costs all declined due to lower business volume and the wind down of our New Jersey operations.

Southeast Segment: Homebuilding revenue decreased by 2.3% for the three months ended December 31, 2016 compared to the prior year quarter due to a 10.7% decline in closings (particularly in our Charleston and Orlando markets), partially offset by the impact of a 9.4% increase in ASP. Our homebuilding gross profit in the Southeast segment decreased by $5.1 million due to the aforementioned decline in homebuilding revenue, as well as a decline in gross margin from 23.1% to 17.5%. However, our year-over-year comparison of gross profit and gross margin is impacted by the Florida stucco issues and impairments and abandonments recorded during the prior year quarter.

When adjusting for these items, gross profit declined by $2.2 million, and gross margin declined from 19.8% to 17.5%. The decrease in gross margin in the Southeast segment was primarily attributable to the the close out of certain higher-margin communities; the mix of closings between markets, communities and product type; and certain unexpected warranty costs incurred on homes closed in prior periods. The decrease in operating income of $5.6 million resulted from the decline in gross profit already described, as well as higher G&A, particularly in our Atlanta market as we try to increase our business in this market.

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Corporate and Unallocated: Our Corporate and unallocated results include amortization of capitalized interest; movement in capitalized indirects; expenses for various shared services functions that benefit all segments but are not allocated, including information technology, treasury, corporate finance, legal, branding and national marketing; and certain other amounts that are not allocated to our operating segments. For the three months ended December 31, 2016, corporate and unallocated net costs increased by $3.9 million from the prior year quarter, primarily due to (1) a year-over-year increase in interest amortized to cost of sales of $2.3 million (refer to Note 6 of the notes to our unaudited condensed consolidated financial statements included in this Form 10-Q) and (2) higher corporate costs incurred due to business growth, including costs associated with the opportunity to increase the scope of our Gatherings projects for active adults, partially offset by (3) the recording of $1.2 million in expense related to the DPA in the prior year quarter, an accrual for which was not needed in the current quarter due to the expiration of the DPA as of the end of our fiscal 2016.

Derivative Instruments and Hedging Activities. We are exposed to fluctuations in interest rates. From time-to-time, we may enter into derivative agreements to manage interest costs and hedge against risks associated with fluctuating interest rates. However, as of December 31, 2016, we were not a party to any such derivative agreements. We do not enter into or hold derivatives for trading or speculative purposes.

Liquidity and Capital Resources. Our sources of liquidity include, but are not limited to: (1) cash from operations; (2) proceeds from Senior Notes, our Secured Revolving Credit Facility (the Facility) and other bank borrowings; (3) the issuance of equity and equity-linked securities; and (4) other external sources of funds. Our short-term and long-term liquidity depends primarily upon our level of net income, working capital management (cash, accounts receivable, accounts payable and other liabilities) and available credit facilities.

Cash and cash equivalents decreased as follows for the periods presented:

	Three Months Ended December 31,	
(In thousands)	2016	2015
Cash used in operating activities	$(62,834)	$(77,849)
Cash used in investing activities	(4,162)	(1,313)
Cash used in financing activities	(3,252)	(27,540)
Net decrease in cash and cash equivalents	$(70,248)	$(106,702)

Operating Activities. We spent $103.2 million on land and land development activities during the three months ended December 31, 2016, a decrease of $8.5 million, or 7.6%, compared to $111.7 million in land-related spending for the three months ended December 31, 2015. We expect our spend on land and land development activities to increase during the remainder of our fiscal 2017. Our level of land and land development spend, which partly drives our change in inventory, had a significant impact on our cash flows from operating activities in both years, bringing net cash used in operating activities to $62.8 million and $77.8 million for the three months ended December 31, 2016 and 2015, respectively. Our cash used in operating activities was also impacted by changes in our working capital balances, particularly trade payables and other liabilities; these changes were more favorable in the current quarter when compared with the prior year quarter, but were a net use of cash during both periods. However, our year-over-year decline in earnings, once adjusted for non-cash items, negatively impacted cash flows from operating activities in the current quarter versus the prior year quarter, and was driven by lower revenues and additional G&A costs in the current quarter.

Investing Activities. Net cash used in investing activities was $4.2 million for the three months ended December 31, 2016, driven by capital expenditures, primarily for model homes, and a net increase in our restricted cash balances (which are primarily used to support our outstanding letters of credit under our stand-alone, cash-secured letter of credit agreements). Net cash used in investing activities was $1.3 million for the three months ended December 31, 2015, primarily driven by capital expenditures for model homes and additional investments made in unconsolidated entities, partially offset by proceeds received from the sale of a building owned by the Company.

Financing Activities. Net cash used in financing activities was $3.3 million for the three months ended December 31, 2016 due to payments made on secured notes payable used to acquire certain land parcels. Net cash used in financing activities was $27.5 million for the three months ended December 31, 2015, primarily related to principal payments on

the then outstanding Senior Notes due June 2016.

Financial Position. As of December 31, 2016, our liquidity position consisted of:

- $158.6 million in cash and cash equivalents;
- $142.5 million of remaining capacity under the Facility (due to the use of the Facility to secure $37.5 million in letters of credit); and

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•$16.0 million of restricted cash, the majority of which is used to secure certain stand-alone letters of credit.
While we believe we possess sufficient liquidity, we are mindful of potential short-term or seasonal requirements for enhanced liquidity that may arise to grow our business. We expect to be able to meet our liquidity needs in fiscal 2017 and to maintain a significant liquidity position, subject to changes in market conditions that would alter our expectations for land and land development expenditures or capital market transactions, which could increase or decrease our cash balance on a period-to-period basis.
During the first quarter of our fiscal 2016, we paid down $22.9 million of the then outstanding Senior Notes due June 2016, which resulted in a loss on extinguishment of debt of $0.8 million. We had no debt repayment activity on our Senior Notes or term loan (defined in Note 7 of the notes to our unaudited condensed consolidated financial statements in this Form 10-Q) during the current quarter.
Debt. We generally fulfill our short-term cash requirements with cash generated from our operations and available borrowings. Additionally, we maintain the Facility, which has a total capacity of $180 million and an available capacity of $142.5 million as of December 31, 2016 after considering our outstanding letters of credit backed by the Facility of $37.5 million.
We have also entered into a number of stand-alone, cash secured letter of credit agreements with banks. These combined facilities provide for letter of credit needs collateralized by either cash or assets of the Company. We currently have $11.5 million of outstanding letters of credit under these facilities (in addition to the $37.5 million outstanding letters of credit backed by the Facility), which are secured by cash collateral that is maintained in restricted accounts totaling $14.7 million.
In the future, we may from time-to-time seek to continue to retire or purchase our outstanding debt through cash repurchases or in exchange for other debt securities, in open market purchases, privately-negotiated transactions or otherwise. We also may seek to expand our business through acquisition, which may be funded through cash, additional debt or equity. In addition, any material variance from our projected operating results could require us to obtain additional equity or debt financing. There can be no assurance that we will be able to complete any of these transactions in the future on favorable terms or at all. See Note 7 of the notes to our unaudited condensed consolidated financial statements in this Form 10-Q for more information.
Credit Ratings. Our credit ratings are periodically reviewed by rating agencies. In September 2016, Moody's reaffirmed the Company's issuer default debt rating of B3 and upgraded the Company’s senior unsecured notes to B3 from Caa1. Moody’s outlook on the Company remains positive. In August 2016, S&P reaffirmed the Company's corporate credit rating of B- and upgraded its rating on the Company’s senior unsecured notes to B- from CCC+. In September 2016, Fitch reaffirmed the Company's long-term debt rating of B- and revised its outlook to stable. These ratings and our current credit condition affect, among other things, our ability to access new capital. Negative changes to these ratings may result in more stringent covenants and higher interest rates under the terms of any new debt. Our credit ratings could be lowered or rating agencies could issue adverse commentaries in the future, which could have a material adverse effect on our business, financial condition, results of operations and liquidity. In particular, a weakening of our financial condition, including any further increase in our leverage or decrease in our profitability or cash flows, could adversely affect our ability to obtain necessary funds, could result in a credit rating downgrade or change in outlook or could otherwise increase our cost of borrowing.
Stock Repurchases and Dividends Paid. The Company did not repurchase any shares in the open market during the three months ended December 31, 2016 or 2015. Any future stock repurchases, to the extent allowed by our debt covenants, must be approved by the Company’s Board of Directors or its Finance Committee.
The indentures under which our Senior Notes were issued contain certain restrictive covenants, including limitations on the payment of dividends. There were no dividends paid during the three months ended December 31, 2016 or 2015.
Off-Balance Sheet Arrangements and Aggregate Contractual Commitments. As of December 31, 2016, we controlled 23,300 lots. We owned 74.2%, or 17,296 of these lots, and 6,004 of these lots, or 25.8%, were under option contracts with land developers and land bankers, which generally require the payment of cash or the posting of a letter of credit for the right to acquire lots during a specified period of time at a certain price. We historically have attempted to control a portion of our land supply through options. As a result of the flexibility that these options provide us, upon a

change in market conditions, we may renegotiate the terms of the options prior to exercise or terminate the agreement. Under option contracts, purchase of the properties is contingent upon satisfaction of certain requirements by us and the sellers, and our liability is generally limited to forfeiture of the non-refundable deposits and other non-refundable amounts incurred, which totaled approximately $78.0 million as of December 31, 2016. The total remaining purchase price, net of cash deposits, committed under all options was $412.9 million as of December 31, 2016. Based on market conditions and our liquidity, we may further expand our use of option agreements to supplement our owned inventory supply.

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We expect to exercise, subject to market conditions and seller satisfaction of contract terms, most of our option contracts. Various factors, some of which are beyond our control, such as market conditions, weather conditions and the timing of the completion of development activities, will have a significant impact on the timing of option exercises or whether lot options will be exercised at all.

We have historically funded the exercise of lot options with operating cash flows. We expect these sources to continue to be adequate to fund anticipated future option exercises. Therefore, we do not anticipate that the exercise of our lot options will have a material adverse effect on our liquidity.

Occasionally, we use legal entities in which we have less than a controlling interest. We enter into the majority of these arrangements with land developers, other homebuilders and financial partners to acquire attractive land positions, to manage our risk profile and to leverage our capital base. The underlying land positions are developed into finished lots for sale to the unconsolidated entity's members or other third parties. We account for our interest in unconsolidated entities under the equity method.

Historically, we and our partners have provided varying levels of guarantees of debt or other obligations of our unconsolidated entities. As of December 31, 2016, we have no repayment guarantees outstanding related to the debt of our unconsolidated entities. See Note 4 of the notes to our unaudited condensed consolidated financial statements in this Form 10-Q for more information.

We had outstanding performance bonds of approximately $220.5 million as of December 31, 2016, related principally to our obligations to local governments to construct roads and other improvements in various developments.

Critical Accounting Policies: Our critical accounting policies require the use of judgment in their application and/or require estimates of inherently uncertain matters. Although our accounting policies are in compliance with accounting principles generally accepted in the United States of America (GAAP), a change in the facts and circumstances of the underlying transactions could significantly change the application of the accounting policies and the resulting financial statement impact. It is also possible that other professionals, applying reasonable judgment to the same set of facts and circumstances, could develop a different conclusion. As disclosed in our 2016 Annual Report, our most critical accounting policies relate to (1) inventory valuation (projects in progress, land held for future development and land held for sale); (2) homebuilding revenues and costs; (3) warranty reserves; and (4) income tax valuation allowances and ownership changes. Since September 30, 2016, there have been no significant changes to these critical accounting policies.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

We are exposed to a number of market risks in the ordinary course of business. Our primary market risk exposure relates to fluctuations in interest rates. We do not believe that our exposure in this area is material to cash flows or results of operations. As of December 31, 2016, we had variable rate debt outstanding totaling approximately $158 million, a portion of which will be reduced during our fiscal 2017 according to the underlying debt agreements. A one percent increase in the interest rate for these variable-rate issuances would result in an increase of our interest expense by $1.4 million over the next twelve-month period. The estimated fair value of our fixed-rate debt as of December 31, 2016 was $1.30 billion, compared to a carrying value of $1.22 billion. The effect of a hypothetical one-percentage point decrease in our estimated discount rates would increase the estimated fair value of the fixed rate debt instruments from $1.30 billion to $1.35 billion as of December 31, 2016.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

As of the end of the period covered by this report, an evaluation was performed based on criteria established in the Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 Framework) under the supervision and with the participation of the Company’s management, including the Chief Executive Officer (CEO) and Chief Financial Officer (CFO), of the effectiveness of the Company’s disclosure controls and procedures as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the Act). Based on that evaluation, the CEO and CFO concluded that the Company’s disclosure controls and procedures were effective as of December 31, 2016, at a reasonable assurance level.

Attached as exhibits to this Quarterly Report on Form 10-Q are certifications of our CEO and CFO, which are required by Rule 13a-14 of the Act. This Disclosure Controls and Procedures section includes information concerning management’s evaluation of disclosure controls and procedures referred to in those certifications and, as such, should be read in conjunction with the certifications of the CEO and CFO.

Changes in Internal Control Over Financial Reporting

There have been no changes in the Company’s internal controls over financial reporting during the quarter ended December 31, 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

Litigation

From time-to-time, we receive claims from institutions that have acquired mortgages originated by our subsidiary, Beazer Mortgage Corporation (BMC), demanding damages or indemnity or that we repurchase such mortgages. BMC stopped originating mortgages in 2008. We have been able to resolve these claims for no cost or for amounts that are not material to our consolidated financial statements. We cannot rule out the potential for additional mortgage loan repurchase or indemnity claims in the future from other investors. At this time, we do not believe that the exposure related to any such claims would be material to our consolidated financial condition, results of operations or cash flows.

A purported class action lawsuit was filed on July 7, 2016 against the Company in Maricopa County Arizona Superior Court on behalf of all homeowners in Arizona that purchased homes from the Company that included a certain type of roof underlayment. The complaint alleges various construction defects, but principally claims that the roof underlayment is susceptible to leaks and was not installed in accordance with best practices. We removed this case to federal court and filed motions to dismiss the class action allegations on various grounds. The plaintiffs have now withdrawn the class action allegations without prejudice and filed an amended complaint. In light of the dismissal of the class action allegations, the Company is handling this matter in the ordinary course of defending against alleged construction defect claims covered by the Company’s warranty. As such, the Company does not plan to report further on this case in future periodic reports.

In the normal course of business, we are subject to various lawsuits. We cannot predict or determine the timing or final outcome of these lawsuits or the effect that any adverse findings or determinations in pending lawsuits may have on us. In addition, an estimate of possible loss or range of loss, if any, cannot presently be made with respect to certain of these pending matters. An unfavorable determination in any of the pending lawsuits could result in the payment by us of substantial monetary damages, which may not be fully covered by insurance. Further, the legal costs associated with the lawsuits and the amount of time required to be spent by management and the Board of Directors on these matters, even if we are ultimately successful, could have a material adverse effect on our financial condition, results of operations or cash flows.

Other Matters

During January 2017, we made our final payment under the Deferred Prosecution Agreement and associated Bill of Information (the DPA) entered into on July 1, 2009 with the United States Attorney for the Western District of North

Carolina and a separate but related agreement with the United States Department of Housing and Urban Development (HUD) and the Civil Division of the United States Department of Justice (the HUD Agreement). For a further discussion of the HUD Agreement, refer to Note 9 to the audited consolidated financial statements within our 2016 Annual Report. During the three months ended December 31, 2015, we accrued $1.2 million related to the HUD Agreement, which was recorded within general and administrative expenses in our consolidated statement of income.

We and certain of our subsidiaries have been named as defendants in various claims, complaints and other legal actions, most relating to construction defects, moisture intrusion and product liability. Certain of the liabilities resulting from these actions are covered in whole or part by insurance. In our opinion, based on our current assessment, the ultimate resolution of these matters will not have a material adverse effect on our financial condition, results of operations or cash flows.

Item 1A. Risk Factors

Except for the addition of the risk factor below, there have been no material changes to the risk factors we previously disclosed in our Annual Report on Form 10-K for the year ended September 30, 2016.

The value of our deferred income tax asset could be significantly reduced if corporate tax rates in the United States (U.S.) are lowered or if other changes in the U.S. corporate tax system occur.

Due to the recent change of our President, discussions in the U.S. Congress regarding comprehensive tax reform have increased. Such legislation could significantly alter the existing tax code, including a reduction in corporate income tax rates. Although a reduction in the corporate income tax rate could result in lower future tax expense and tax payments, it would reduce, perhaps significantly, the value of our existing deferred tax asset and could result in a charge to our earnings from the write-down of this asset. It is uncertain whether or when any such tax reform proposals will be enacted into law, and whether or how they will affect our deferred tax asset.

Item 6. Exhibits

10.1*	Form of 2014 Long-Term Incentive Plan Award Agreement for Performance Shares (Named Executive Officers).
31.1	Certification of Chief Executive Officer pursuant to 17 CFR 240.13a-14 promulgated under Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to 17 CFR 240.13a-14 promulgated under Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101	The following financial statements from Beazer Homes USA, Inc.'s Quarterly Report on Form 10-Q for the period ended December 31, 2016, filed on February 9, 2017, formatted in XBRL (Extensible Business Reporting Language): (i) Unaudited Condensed Consolidated Balance Sheets, (ii) Unaudited Condensed Consolidated Statements of Income, (iii) Unaudited Condensed Consolidated Statements of Cash Flows and (iv) Notes to Unaudited Condensed Consolidated Financial Statements.

* Represents a management contract or compensatory plan or arrangement.

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SIGNATURES

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

Date: February 9, 2017	Beazer Homes USA, Inc.	
	By:	/s/ Robert L. Salomon
	Name:	Robert L. Salomon Executive Vice President and Chief Financial Officer

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