

Howard Hughes Corp
Form 10-Q
August 10, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended June 30, 2015

or

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission file number 001-34856

THE HOWARD HUGHES CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	36-4673192
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification number)

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13355 Noel Road, 22nd Floor, Dallas, Texas 75240

(Address of principal executive offices, including zip code)

(214) 741-7744

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

The number of shares of common stock, \$0.01 par value, outstanding as of August 4, 2015 was 39,715,005.

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THE HOWARD HUGHES CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS

UNAUDITED

	June 30, 2015	December 31, 2014
	(In thousands, except share amounts)	
Assets:		
Investment in real estate:		
Master Planned Community assets	\$ 1,648,729	\$ 1,641,063
Land	319,194	317,211
Buildings and equipment	1,429,386	1,243,979
Less: accumulated depreciation	(192,886)	(157,182)
Developments	1,119,774	914,303
Net property and equipment	4,324,197	3,959,374
Investment in Real Estate and Other Affiliates	55,959	53,686
Net investment in real estate	4,380,156	4,013,060
Cash and cash equivalents	488,629	560,451
Accounts receivable, net	36,122	28,190
Municipal Utility District receivables, net	124,828	104,394
Notes receivable, net	25,138	28,630
Deferred expenses, net	72,705	75,070
Prepaid expenses and other assets, net	278,251	310,136
Total assets	\$ 5,405,829	\$ 5,119,931
Liabilities:		
Mortgages, notes and loans payable	\$ 2,286,174	\$ 1,993,470
Deferred tax liabilities	67,610	62,205
Warrant liabilities	432,270	366,080
Uncertain tax position liability	4,765	4,653
Accounts payable and accrued expenses	437,998	466,017
Total liabilities	3,228,817	2,892,425
Commitments and Contingencies (see Note 14)		
Equity:		
Preferred stock: \$.01 par value; 50,000,000 shares authorized, none issued	—	—
Common stock: \$.01 par value; 150,000,000 shares authorized, 39,715,005 shares issued and outstanding as of June 30, 2015 and 39,638,094 shares issued and outstanding as of December 31, 2014	398	396

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Additional paid-in capital	2,842,266	2,838,013
Accumulated deficit	(662,320)	(606,934)
Accumulated other comprehensive loss	(7,116)	(7,712)
Total stockholders' equity	2,173,228	2,223,763
Noncontrolling interests	3,784	3,743
Total equity	2,177,012	2,227,506
Total liabilities and equity	\$ 5,405,829	\$ 5,119,931

See Notes to Condensed Consolidated Financial Statements.

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THE HOWARD HUGHES CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

UNAUDITED

	Three Months Ended June 30		Six Months Ended June 30,	
	2015	2014	2015	2014
	(In thousands, except per share amounts)			
Revenues:				
Master Planned Community land sales	\$ 45,433	\$ 153,164	\$ 93,514	\$ 200,835
Builder price participation	7,907	3,843	13,605	7,940
Minimum rents	36,989	22,189	72,183	42,549
Tenant recoveries	10,701	6,893	20,368	12,908
Condominium rights and unit sales	86,513	4,358	121,370	7,484
Resort and conference center revenues	11,481	9,622	23,484	19,048
Other land revenues	3,145	2,698	6,438	5,210
Other rental and property revenues	6,994	6,864	13,291	12,310
Total revenues	209,163	209,631	364,253	308,284
Expenses:				
Master Planned Community cost of sales	24,236	42,719	48,132	65,797
Master Planned Community operations	11,963	11,389	21,946	20,650
Other property operating costs	19,634	16,600	37,779	30,405
Rental property real estate taxes	6,568	4,241	12,768	7,981
Rental property maintenance costs	2,900	2,174	5,644	4,089
Condominium rights and unit cost of sales	56,765	2,191	79,174	3,762
Resort and conference center operations	8,893	6,412	17,971	13,923
Provision for doubtful accounts	1,266	31	2,075	174
Demolition costs	1,496	3,435	1,613	5,951
Development-related marketing costs	5,594	5,299	11,837	9,522
General and administrative	19,606	17,497	38,569	34,379
Other income, net	(399)	(5,611)	(1,863)	(16,059)
Depreciation and amortization	25,069	11,473	46,579	21,982
Total expenses	183,591	117,850	322,224	202,556
Operating income	25,572	91,781	42,029	105,728
Interest income	271	18,625	407	20,813
Interest expense	(14,685)	(8,897)	(27,931)	(16,218)
Warrant liability gain (loss)	42,620	(67,370)	(66,190)	(163,810)
Reduction in tax indemnity receivable	—	(10,927)	—	(10,927)

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Equity in earnings from Real Estate and Other Affiliates	1,081	6,587	2,869	12,655
Income (loss) before taxes	54,859	29,799	(48,816)	(51,759)
Provision for income taxes	4,274	44,532	6,558	49,305
Net income (loss)	50,585	(14,733)	(55,374)	(101,064)
Net income attributable to noncontrolling interests	(12)	(27)	(12)	(12)
Net income (loss) attributable to common stockholders	\$ 50,573	\$ (14,760)	\$ (55,386)	\$ (101,076)
Basic income (loss) per share:	\$ 1.28	\$ (0.37)	\$ (1.40)	\$ (2.56)
Diluted income (loss) per share:	\$ 0.18	\$ (0.37)	\$ (1.40)	\$ (2.56)

See Notes to Condensed Consolidated Financial Statements.

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THE HOWARD HUGHES CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

UNAUDITED

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
	(In thousands)			
Comprehensive income (loss), net of tax:				
Net income (loss)	\$ 50,585	\$ (14,733)	\$ (55,374)	\$ (101,064)
Other comprehensive income (loss):				
Interest rate swaps (a)	196	(81)	708	118
Capitalized swap interest (b)	(53)	(44)	(112)	(177)
Other comprehensive income	143	(125)	596	(59)
Comprehensive income (loss)	50,728	(14,858)	(54,778)	(101,123)
Comprehensive income attributable to noncontrolling interests	(12)	(27)	(12)	(12)
Comprehensive income (loss) attributable to common stockholders	\$ 50,716	\$ (14,885)	\$ (54,790)	\$ (101,135)

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- (a) Amount is shown net of deferred tax expense of \$0.1 million and \$0.6 million for the three and six months ended June 30, 2015, respectively. For the six months ended June 30, 2015 the higher deferred tax expense is due to the tax effect of the swap associated with the Ward Village loan resulting from the revocation of our REIT status. For the three and six months ended June 30, 2014, amounts are shown net of deferred tax benefit of zero and \$0.1 million, respectively.
- (b) Net of deferred tax benefit of \$0.1 million for the three and six months ended June 30, 2015, respectively. For the three and six months ended June 30, 2014, amounts shown net of deferred tax benefit of zero and \$0.1 million, respectively.

See Notes to Condensed Consolidated Financial Statements.

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THE HOWARD HUGHES CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF EQUITY

UNAUDITED

(In thousands, except share amounts)	Shares	Common Stock	Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Noncontrolling Interests	Total Equity
Balance, January 1, 2014	39,576,344	\$ 396	\$ 2,829,813	\$ (583,403)	\$ (8,222)	\$ 6,562	\$ 2,245,146
Net loss		—	—	(101,076)	—	12	(101,064)
Preferred dividend payment on behalf of REIT subsidiary		—	—	—	—	(12)	(12)
Interest rate swaps, net of tax of \$49		—	—	—	118	—	118
Capitalized swap interest, net of tax of \$100		—	—	—	(177)	—	(177)
Stock plan activity	61,750	—	3,818	—	—	—	3,818
Balance, June 30, 2014	39,638,094	\$ 396	\$ 2,833,631	\$ (684,479)	\$ (8,281)	\$ 6,562	\$ 2,147,829
Balance, January 1, 2015	39,638,094	\$ 396	\$ 2,838,013	\$ (606,934)	\$ (7,712)	\$ 3,743	\$ 2,227,506
Net income (loss)		—	—	(55,386)	—	12	(55,374)
Distribution to noncontrolling interest		—	—	—	—	29	29
Interest rate swaps, net of tax of \$555		—	—	—	708	—	708
		—	—	—	(112)	—	(112)

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Capitalized
swap interest,
net of tax of
\$41

Stock plan activity	76,911	2	4,253	—	—	—	4,255
Balance, June 30, 2015	39,715,005	\$ 398	\$ 2,842,266	\$ (662,320)	\$ (7,116)	\$ 3,784	\$ 2,177,012

See Notes to Condensed Consolidated Financial Statements.

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THE HOWARD HUGHES CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

UNAUDITED

	Six Months Ended June 30,	
	2015	2014
	(In thousands)	
Cash Flows from Operating Activities:		
Net loss	\$ (55,374)	\$ (101,064)
Adjustments to reconcile net loss to cash provided by (used in) operating activities:		
Depreciation	37,155	19,580
Amortization	9,424	2,402
Amortization of deferred financing costs	3,192	1,649
Amortization of intangibles other than in-place leases	472	289
Straight-line rent amortization	(2,727)	(711)
Deferred income taxes	6,135	47,514
Restricted stock and stock option amortization	3,232	3,818
Gain on disposition of asset	—	(2,373)
Warrant liability loss	66,190	163,810
Reduction in tax indemnity receivable	—	10,927
Interest income related to tax indemnity	—	(20,246)
Equity in earnings from Real Estate and Other Affiliates, net of distributions	1,437	(10,423)
Provision for doubtful accounts	2,075	174
Master Planned Community land acquisitions	(1,928)	(67,284)
Master Planned Community development expenditures	(83,868)	(55,162)
Master Planned Community cost of sales	44,792	59,281
Condominium development expenditures	(79,500)	(17,821)
Condominium and other cost of sales	75,991	3,762
Percentage of completion revenue recognition from sale of condominium rights and units	(121,370)	(7,484)
Non-monetary consideration relating to land sale	—	(13,789)
Net changes:		
Accounts and notes receivable	(1,115)	23,845
Prepaid expenses and other assets	15,520	1,177
Condominium deposits received	18,423	103,240
Deferred expenses	240	(22,052)
Accounts payable and accrued expenses	(11,030)	(5,740)
Condominium deposits held in escrow	(18,423)	(103,240)

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Condominium deposits released from escrow	90,425	—
Other, net	(325)	(4,811)
Cash provided by (used in) operating activities	(957)	9,268
Cash Flows from Investing Activities:		
Property and equipment expenditures	(3,863)	(4,517)
Operating property improvements	(4,401)	(1,707)
Property developments and redevelopments	(364,044)	(292,128)
Proceeds from insurance claims	—	6,227
Proceeds from dispositions	—	5,500
Investment in KR Holdings, LLC	9,121	—
Investments in Real Estate and Other Affiliates, net	(501)	(2,117)
Change in restricted cash	(1,485)	(2,225)
Cash used in investing activities	(365,173)	(290,967)
Cash Flows from Financing Activities:		
Proceeds from mortgages, notes and loans payable	310,822	164,051
Principal payments on mortgages, notes and loans payable	(14,900)	(33,581)
Deferred financing costs	(1,614)	(4,139)
Preferred dividend payment on behalf of REIT subsidiary	—	(12)
Cash provided by financing activities	294,308	126,319
Net change in cash and cash equivalents	(71,822)	(155,380)
Cash and cash equivalents at beginning of period	560,451	894,948
Cash and cash equivalents at end of period	\$ 488,629	\$ 739,568

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THE HOWARD HUGHES CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

UNAUDITED

	Six Months Ended June 30,	
	2015	2014
	(In thousands)	
Supplemental Disclosure of Cash Flow Information:		
Interest paid	\$ 48,460	\$ 41,628
Interest capitalized	23,074	23,965
Income taxes paid	2,067	1,370
Non-Cash Transactions:		
Special Improvement District bond transfers associated with land sales	3,340	6,516
Property developments and redevelopments	(4,534)	51,377
Accrued interest on construction loan borrowing	1,359	—
MPC Land contributed to Real Estate Affiliates	15,234	—
Special Improvement District bond transfers to Real Estate Affiliates	(1,518)	—
Capitalized stock compensation	1,262	—

See Notes to Condensed Consolidated Financial Statements

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THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

NOTE 1 BASIS OF PRESENTATION AND ORGANIZATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial statements and in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X as issued by the Securities and Exchange Commission (the “SEC”). Such Condensed Consolidated Financial Statements do not include all of the information and disclosures required by GAAP for complete financial statements. In addition, readers of this Quarterly Report on Form 10-Q (“Quarterly Report”) should refer to The Howard Hughes Corporation’s (“HHC” or the “Company”) audited Consolidated Financial Statements which are included in the Company’s Annual Report on Form 10-K (the “Annual Report”) for the fiscal year ended December 31, 2014. In the opinion of management, all adjustments (consisting of normal recurring adjustments) necessary for a fair presentation of the financial position, results of operations and cash flows for the interim periods have been included. The results for the three and six months ended June 30, 2015 are not necessarily indicative of the results for the full fiscal year.

Management has evaluated for disclosure or recognition all material events occurring subsequent to the date of the Condensed Consolidated Financial Statements up to the date and time this Quarterly Report was filed.

NOTE 2 RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In April 2015, the Financial Accounting Standards Board (“FASB”) issued ASU 2015-03, “Simplifying the Presentation of Debt Issuance Costs.” This ASU requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The amendments in this ASU are effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. The standard requires a retrospective application to reflect the period-specific effects of applying the new guidance. The Company will begin presenting the carrying value of debt facilities, net of the debt issuance costs, in the first quarter of 2016. The Company does not expect the adoption of this ASU to have a material impact on the Company’s Consolidated Financial Statements

In February 2015, the FASB issued ASU 2015-02, “Consolidation (Topic 810) - Amendments to the Consolidation Analysis.” This ASU affects reporting entities that are required to evaluate whether they should consolidate certain legal entities. All legal entities are subject to reevaluation under the revised consolidation model. The standard is

effective for interim and annual periods beginning after December 15, 2015, and permits the use of a modified retrospective or retrospective approach. The Company does not expect the adoption of this ASU to have a material impact on the Company's Consolidated Financial Statements.

In August 2014, the FASB issued Accounting Standards Update ("ASU") 2014-15, "Presentation of Financial Statements – Going Concern: Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern." This ASU requires management to assess an entity's ability to continue as a going concern by incorporating and expanding upon certain principles that are currently in U.S. auditing standards as specified in the guidance. This ASU becomes effective for the annual period ending after December 15, 2016 and for annual and interim periods thereafter. Early adoption is permitted. The Company does not expect the adoption of this ASU to have a material impact on the Company's Consolidated Financial Statements.

In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers." This ASU states that entities should recognize revenue to properly depict the transfer of negotiated goods or services to customers in an amount that properly reflects the agreed upon consideration which the entity expects to be exchanged. The standard is effective for interim and annual periods beginning after December 15, 2017 and permits the use of either the retrospective or cumulative effect transition method. The Company is evaluating the impact of the adoption of this ASU on the Company's Consolidated Financial Statements.

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THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

NOTE 3 SPONSORS AND MANAGEMENT WARRANTS

On November 9, 2010, we issued warrants to purchase 8.0 million shares of our common stock to certain of our sponsors (the “Sponsors Warrants”) with an estimated initial value of approximately \$69.5 million. The initial exercise price for the warrants of \$50.00 per share and the number of shares of common stock underlying each warrant are subject to adjustment for future stock dividends, splits or reverse splits of our common stock or certain other events. In 2012, a sponsor exercised 1,525,272 shares, and we purchased 4,558,061 Sponsor Warrants from certain sponsors for a net cash amount of \$80.5 million. As a result of these transactions, \$108.6 million of additional paid in-capital was recorded in our financial statements in the year ended December 31, 2012. The Sponsors Warrants expire on November 9, 2017.

In November 2010 and February 2011, we entered into certain agreements (the “Management Warrants”) with David R. Weinreb, our Chief Executive Officer, Grant Herlitz, our President, and Andrew C. Richardson, our Chief Financial Officer, in each case prior to his appointment to such position to purchase shares of our common stock. The Management Warrants represent 2,862,687 underlying shares, which may be adjusted pursuant to a net settlement option, were issued pursuant to such agreements at fair value in exchange for a combined total of approximately \$19.0 million in cash from such executives at the commencement of their respective employment. Mr. Weinreb and Mr. Herlitz’s warrants have exercise prices of \$42.23 per share and Mr. Richardson’s warrants have an exercise price of \$54.50 per share. Generally, the Management Warrants become exercisable in November 2016 and expire in February 2018.

As of June 30, 2015, the estimated \$181.1 million fair value for the Sponsors Warrants representing warrants to purchase 1,916,667 shares and the estimated \$251.2 million fair value for the Management Warrants representing warrants to purchase 2,862,687 shares have been recorded as liabilities because the holders of these warrants could require us to settle such warrants in cash upon a change of control. The estimated fair values for the outstanding Sponsors Warrants and Management Warrants were \$157.1 million and \$209.0 million, respectively, as of December 31, 2014. The fair values were estimated using an option pricing model and Level 3 inputs due to the unavailability of comparable market data, as further discussed in Note 6 – Fair Value of Financial Instruments. Decreases and increases in the fair value of the Sponsors Warrants and the Management Warrants are recognized as either warrant liability gains or losses, respectively, in the Consolidated Statements of Operations.

NOTE 4 EARNINGS PER SHARE

Basic earnings (loss) per share (“EPS”) is computed by dividing net income (loss) available to common stockholders by the weighted average number of common shares outstanding. Diluted EPS is computed after adjusting the numerator and denominator of the basic EPS computation for the effects of all potentially dilutive common shares. The dilutive effect of options and nonvested stock issued under stock based compensation plans is computed using the “treasury stock” method. The dilutive effect of the Sponsors Warrants and Management Warrants is computed using the if converted method. Gains associated with the changes in the fair value of the Sponsors Warrants and Management Warrants are excluded from the numerator in computing diluted earnings per share because inclusion of such gains in the computation would be anti dilutive.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

Information related to our EPS calculations is summarized as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
	(In thousands, except per share amounts)		(In thousands, except per share amounts)	
Basic EPS:				
Numerator:				
Net income (loss)	\$ 50,585	\$ (14,733)	\$ (55,374)	\$ (101,064)
Net income attributable to noncontrolling interests	(12)	(27)	(12)	(12)
Net income (loss) attributable to common stockholders	\$ 50,573	\$ (14,760)	\$ (55,386)	\$ (101,076)
Denominator:				
Weighted average basic common shares outstanding	39,468	39,458	39,467	39,456
Diluted EPS:				
Numerator:				
Net income (loss) attributable to common stockholders	\$ 50,573	\$ (14,760)	\$ (55,386)	\$ (101,076)
Less: Warrant liability gain	(42,620)	—	—	—
Adjusted net income (loss) attributable to common stockholders	\$ 7,953	\$ (14,760)	\$ (55,386)	\$ (101,076)
Denominator:				
Weighted average basic common shares outstanding	39,468	39,458	39,467	39,456
Restricted stock and stock options	438	—	—	—
Warrants	3,291	—	—	—
Weighted average diluted common shares outstanding	43,197	39,458	39,467	39,456
Basic income (loss) per share:	\$ 1.28	\$ (0.37)	\$ (1.40)	\$ (2.56)

Diluted income (loss) per share:	\$ 0.18	\$ (0.37)	\$ (1.40)	\$ (2.56)
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The diluted EPS computation for the three months ended June 30, 2015 excludes 125,769 stock options. The diluted EPS computation for the six months ended June 30, 2015 excludes 1,048,750 stock options, 242,055 shares of restricted stock, 1,916,667 shares of common stock underlying the Sponsors Warrants and 2,862,687 shares of common stock underlying the Management Warrants because their inclusion would have been anti-dilutive.

The diluted EPS computations for the three and six months ended June 30, 2014 excludes 1,040,240 stock options, 172,690 shares of restricted stock, 1,916,667 shares of common stock underlying the Sponsor Warrants and 2,862,687 shares of common stock underlying the Management Warrants. All such amounts are excluded from the respective diluted EPS computations because their inclusion would have been anti-dilutive.

NOTE 5 IMPAIRMENT

We review our real estate assets, including operating assets, land held for development and sale and developments in progress, for potential impairment indicators whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. GAAP requires that if impairment indicators exist and the undiscounted cash flows expected to be generated by an asset are less than its carrying amount, an impairment charge should be recorded to write down the carrying amount of such asset to fair value (or for land and properties held for sale, fair value less cost to sell). The impairment analysis does not consider the timing of future cash flows and whether the asset is expected to earn an above or below market rate of return.

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THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

Our investment in each of the Real Estate and Other Affiliates is evaluated periodically and as deemed necessary for recoverability and valuation declines that are other-than-temporary. If the decrease in value of our investment in a Real Estate and Other Affiliate is deemed to be other-than-temporary, our investment in such Real Estate and Other Affiliate is reduced to its estimated fair value.

No impairment charges were recorded during the six months ended June 30, 2015 or 2014. We continually evaluate our strategic alternatives with respect to each of our properties and may revise our strategy from time to time, including our intent to hold the asset on a long-term basis or the timing of potential asset dispositions. For example, we may decide to sell property that is held for use and the sale price may be less than the carrying amount. As a result, these changes in strategy could result in impairment charges in future periods.

NOTE 6 FAIR VALUE OF FINANCIAL INSTRUMENTS

The following table presents, for each of the fair value hierarchy levels required under FASB Accounting Standards (“ASC”) 820 Fair Value Measurement, our assets and liabilities that are measured at fair value on a recurring basis.

	June 30, 2015				December 31, 2014			
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(In thousands)				(In thousands)			
Assets:								
Cash equivalents	\$ 18	\$ 18	\$ —	\$ —	\$ 75,027	\$ 75,027	\$ —	\$ —
Liabilities:								
Warrants	432,270 2,993	—	— 2,993	432,270 —	366,080 3,144	—	— 3,144	366,080 —

Interest rate
swaps

Cash equivalents consist of registered money market mutual funds which invest in United States treasury securities that are valued at the net asset value of the underlying shares in the funds as of the close of business at the end of each period. The fair value approximates carrying value.

The valuation of warrants is based on an option pricing valuation model. The inputs to the model include the fair value of stock related to the warrants, exercise price of the warrants, term, expected volatility, risk-free interest rate and dividend yield and, with respect to the Management Warrants, a discount for lack of marketability.

The fair values of interest rate swaps are determined using the market standard methodology of netting the discounted future fixed cash payments and the discounted expected variable cash receipts. The variable cash receipts are based on an expectation of future interest rates derived from observable market interest rate curves.

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The following table presents a reconciliation of the beginning and ending balances of the fair value measurements of our Sponsors and Management Warrants using significant unobservable inputs (Level 3):

	2015	2014
	(In thousands)	
Balance as of January 1	\$ 366,080	\$ 305,560
Warrant liability loss (a)	66,190	163,810
Balance as of June 30	\$ 432,270	\$ 469,370

(a) All losses during 2015 and 2014 were unrealized.

The fair values were estimated using an option pricing model and Level 3 inputs due to the unavailability of comparable market data. Changes in the fair values of the Sponsors Warrants and the Management Warrants are recognized in earnings as a warrant liability gain or loss.

The significant unobservable inputs used in the fair value measurement of our warrants designated as Level 3 as of June 30, 2015 are as follows:

	Fair Value (In thousands)	Valuation Technique	Unobservable Inputs	
			Expected Volatility (a)	Marketability Discount (b)
Warrants	\$ 432,270	Option Pricing Valuation Model	24.1%	14.0% - 16.0%

(a) Based on our implied equity volatility.

(b) Represents the discount rate for lack of marketability of the Management Warrants. The discount rates ranged from 18.0%-20.0% at December 31, 2014.

Generally, an increase in expected volatility would increase the fair value of the liability, while a decrease in expected volatility would decrease the fair value of the liability, and the impact of the volatility on fair value diminishes as the market value of the stock increases above the strike price. As the period of restriction lapses, the marketability discount reduces to zero and increases the fair value of the warrants.

The estimated fair values of our financial instruments that are not measured at fair value on a recurring basis are as follows:

	Fair Value Hierarchy	June 30, 2015		December 31, 2014	
		Carrying Amount (In thousands)	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Assets:					
Cash and cash equivalents	Level 1	\$ 488,611	\$ 488,611	\$ 485,424	\$ 485,424
Notes receivable, net (a)	Level 3	25,138	25,138	28,630	28,630
Liabilities:					
Fixed-rate debt	Level 2	\$ 1,047,606	\$ 1,102,460	\$ 1,030,554	\$ 1,050,333
Variable-rate debt	Level 2	1,238,568	1,238,568	962,916	962,916
Total mortgages, notes and loans payable		\$ 2,286,174	\$ 2,341,028	\$ 1,993,470	\$ 2,013,249

(a) Notes receivable is shown net of an allowance of \$0.3 million as of June 30, 2015 and \$0.5 million as of December 31, 2014.

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Notes receivable are carried at net realizable value which approximates fair value. The estimated fair values are based on certain factors, such as current interest rates, terms of the note and credit worthiness of the borrower.

The fair value of fixed-rate debt in the table above, not including our Senior Notes (please refer to Note 8 – Mortgages, Notes and Loans Payable), was estimated based on a discounted future cash payment model, which includes risk premiums and a risk free rate derived from the current London Interbank Offered Rate (“LIBOR”) or U.S. Treasury obligation interest rates. The discount rates reflect our judgment as to what the approximate current lending rates for loans or groups of loans with similar maturities and credit quality would be if credit markets were operating efficiently and assuming that the debt is outstanding through maturity. The fair values of our Senior Notes, included in fixed rate debt in the table above, are based upon the last trade price closest to the end of the period presented.

The carrying amounts for our variable-rate debt approximate fair value given that the interest rates are variable and adjust with current market rates for instruments with similar risks and maturities.

The carrying amounts of cash and cash equivalents and accounts receivable approximate fair value because of the short term maturity of these instruments.

NOTE 7 REAL ESTATE AND OTHER AFFILIATES

In the ordinary course of business, we enter into partnerships or joint ventures primarily for the development and operations of real estate assets that are referred to as “Real Estate Affiliates”. These partnerships or joint ventures are accounted for in accordance with FASB ASC 810 Consolidation.

In accordance with ASC 810, we assess our joint ventures at inception to determine if any meet the qualifications of a variable interest entity (“VIE”). We consider a partnership or joint venture a VIE if: (a) the total equity investment is not sufficient to permit the entity to finance its activities without additional subordinated financial support; (b) characteristics of a controlling financial interest are missing (either the ability to make decisions through voting or

other rights, the obligation to absorb the expected losses of the entity or the right to receive the expected residual returns of the entity); or (c) the voting rights of the equity holders are not proportional to their obligations to absorb the expected losses of the entity and/or their rights to receive the expected residual returns of the entity, and substantially all of the entity's activities either involve or are conducted on behalf of an investor that has disproportionately few voting rights. Upon the occurrence of certain events outlined in ASC 810, we reassess our initial determination of whether the partnership or joint venture is a VIE.

We perform a qualitative assessment of each VIE to determine if we are the primary beneficiary, as required by ASC 810. Under ASC 810, a company concludes that it is the primary beneficiary and consolidates the VIE if the company has both (a) the power to direct the economically significant activities of the entity and (b) the obligation to absorb losses of, or the right to receive benefits from, the entity that could potentially be significant to the VIE. The company considers the contractual agreements that define the ownership structure, distribution of profits and losses, risks, responsibilities, indebtedness, voting rights and board representation of the respective parties in determining if the company is the primary beneficiary. As required by ASC 810, management's assessment of whether the company is the primary beneficiary of a VIE is continuously performed.

We account for investments in joint ventures deemed to be VIEs for which we are not considered to be the primary beneficiary but have significant influence, using the equity method, and investments in joint ventures where we do not have significant influence over the joint venture's operations and financial policies, using the cost method. Generally, the operating agreements with respect to our Real Estate Affiliates provide that assets, liabilities and funding obligations are shared in accordance with our ownership percentages.

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Our investment in real estate and other affiliates that are reported on the equity and cost methods are as follows:

	Economic/Legal Ownership		Carrying Value		Share of Earnings/Dividends			
	June 30, 2015 (In percentages)	December 31, 2014	June 30, 2015 (In thousands)	December 31, 2014 (In thousands)	Three Months Ended June 30, 2015 (In thousands)	Three Months Ended June 30, 2014 (In thousands)	Six Months Ended June 30, 2015 (In thousands)	Six Months Ended June 30, 2014 (In thousands)
Equity Method Investments								
Master Planned Communities:								
Discovery Land	N/A	N/A	\$ 12,052	\$ —	\$ —	\$ —	\$ —	\$ —
Operating Assets:								
Millennium Woodlands Phase II, LLC (a) (b)	81.43 %	81.43 %	—	1,023	(489)	(99)	(1,150)	(135)
Stewart Title Summerlin Las Vegas Baseball Club, LLC (b)	50.00 %	50.00 %	3,714	3,869	302	425	496	518
The Metropolitan Downtown Columbia (c)	50.00 %	50.00 %	4,472	4,800	(89)		(408)	
Woodlands Sarofim Strategic Developments:								
Circle T Ranch and Power Center	50.00 %	50.00 %	9,004	9,004	—	—	—	—
	50.00 %	50.00 %	10	10	10	193	549	483

HHMK Development (b)										
KR Holdings (b)	50.00	%	50.00	%	688	9,183	911	5,726	1,276	9,735
Parcel C (b)	50.00	%	50.00	%	6,998	8,737	—	—	—	—
Summerlin Apartments, LLC (b)	50.00	%	50.00	%	1,661	—	—	—	—	—
					52,019	49,769	1,081	6,587	1,122	10,874
Cost basis investments					3,940	3,917	—	—	1,747	1,781
Investment in Real Estate and Other Affiliates					\$ 55,959	\$ 53,686	\$ 1,081	\$ 6,587	\$ 2,869	\$ 12,655

N/A – Not Applicable

- (a) Millennium Woodlands Phase II, LLC was placed into service in the beginning of the third quarter of 2014.
- (b) Equity method variable interest entities.
- (c) The Metropolitan Downtown Columbia was placed into service in the first quarter 2015.

We are not the primary beneficiary of any of the equity method variable interest entities listed above because we do not have the power to direct activities that most significantly impact the economic performance of such joint ventures; therefore, we report our interests on the equity method. Our maximum exposure to loss as a result of these investments is limited to the aggregate carrying value of the investment as we have not provided any guarantees or otherwise made firm commitments to fund amounts on behalf of these VIEs. The aggregate carrying value of the unconsolidated VIEs was \$20.2 million and \$29.5 million as of June 30, 2015 and December 31, 2014, respectively, and was classified as Investments in Real Estate and Other Affiliates in the Consolidated Balance Sheets.

As of June 30, 2015, approximately \$100.1 million of indebtedness was secured by the properties owned by our Real Estate and Other Affiliates of which our share was approximately \$60.1 million based upon our economic ownership. All of this indebtedness is non-recourse to us.

The Company is the primary beneficiary of one VIE which is consolidated in the financial statements. The creditors of the consolidated VIE do not have recourse to the Company. As of June 30, 2015, the carrying values of the assets and liabilities associated with the operations of the consolidated VIE were \$21.3 million and \$0.9 million, respectively. As of December 31, 2014, the carrying values of the assets and liabilities associated with operations of the consolidated VIE were \$21.1 million and \$0.6 million, respectively. The assets of the VIE are restricted for use only by the particular VIE and are not available for our general operations.

Our recent and more significant investments in Real Estate Affiliates and the related accounting considerations are described below.

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Discovery Land

During the first quarter 2015, our joint venture with Discovery Land Company (“Discovery Land”) was formed, and we contributed land with a book basis of \$13.4 million and transferred SID bonds related to such land with a carrying value of \$1.3 million to the joint venture at the agreed upon value of \$226,000 per acre, or \$125.4 million. At the time of our contribution, we determined that the entity did not meet the criterion of a VIE. Because our partner has substantive participation rights we do not control the joint venture, and we account for it using the equity method. Discovery Land is required to fund up to a maximum of \$30.0 million cash as their capital contribution and we have no further capital obligations.

After receipt of our capital contribution and a 5.0% preferred return, Discovery Land is entitled to all remaining cash distributed by the joint venture until two times its equity contribution has been repaid. Any further cash distributions are shared 50/50. Discovery Land is the manager on the project, and development began in the second quarter 2015 with the first lot closings expected to begin by the end of 2015.

ONE Ala Moana Condominium Project

KR Holdings is a 50/50 joint venture that was formed to develop a 206-unit luxury condominium tower at the One Ala Moana Center in Honolulu, Hawaii. The venture substantially completed construction in the fourth quarter 2014 and closed on the sale of 201 out of 206 total units. The venture used the percentage of completion method to recognize earnings. All remaining units available for sale were sold and closed during the six months ended June 30, 2015.

Millennium Woodlands Phase II, LLC

On May 14, 2012, we entered into a joint venture, Millennium Woodlands Phase II, LLC (“Millennium Phase II”), with The Dinerstein Companies, for the construction of a new 314-unit Class A multi family complex in The Woodlands Town Center. Our partner is the managing member of Millennium Phase II. As the managing member, our partner controls, directs, manages and administers the affairs of Millennium Phase II. On July 5, 2012, Millennium Phase II was capitalized by our contribution of 4.8 acres of land valued at \$15.5 million, our partner’s contribution of

\$3.0 million in cash and a construction loan in the amount of \$37.7 million which is guaranteed by our partner. The development of Millennium Phase II further expands our multi-family portfolio in The Woodlands Town Center. During 2014, the joint venture completed construction, was placed in service and transferred into the Operating Assets segment.

Parcel C

On October 4, 2013, we entered into a joint venture agreement with a local developer, Kettler, Inc. (“Kettler”), to construct a 437-unit, Class A apartment building with 31,000 square feet of ground floor retail on Parcel C in downtown Columbia, Maryland. We contributed approximately five acres of land having an approximate book value of \$4.0 million to the joint venture. Our land was valued at \$23.4 million or \$53,500 per constructed unit. When the venture closes on the construction loan and upon completion of certain other conditions, including obtaining completed site development and construction plans and an approved project budget, our partner will be required to contribute cash to the venture.

Summerlin Apartments, LLC

On January 24, 2014, we entered into a joint venture with a national multi-family real estate developer, The Calida Group (“Calida”), to construct, own and operate a 124-unit gated luxury apartment development in Summerlin, Nevada. We, and our partner, each own 50% of the venture, and unanimous consent of the partners is required for all major decisions. This project represents the first residential development in Summerlin’s 400-acre downtown. In the first quarter 2015, we

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contributed a 4.5-acre parcel of land with an agreed value of \$3.2 million in exchange for a 50% interest in the venture. Our partner contributed \$3.2 million of cash for their 50% interest, acts as the development manager, funded all pre-development activities, obtained construction financing in the first quarter 2015 and provided guarantees required by the lender. Upon a sale of the property, we are entitled to 50% of the proceeds up to, and 100% of the proceeds in excess of, an amount determined by applying a 7.0% capitalization rate to net operating income (“NOI”). The venture commenced construction in February 2015 with the first units expected to become available for rent by second quarter 2016.

Summerlin Las Vegas Baseball Club, LLC

On August 6, 2012, we entered into a joint venture for the purpose of acquiring 100% of the operating assets of the Las Vegas 51s, a Triple A baseball team, which is a member of the Pacific Coast League. We own 50% of the venture and our partners jointly own the remaining 50%. Unanimous consent of the partners is required for all major decisions. As of the date the joint venture acquired the baseball team, we had funded our capital contribution of \$10.5 million. Our strategy in owning an interest is to pursue a potential relocation of the team to a to be built stadium in our Summerlin master planned community. Efforts to relocate the team are ongoing and there can be no assurance that such a stadium will ultimately be built.

The Metropolitan Downtown Columbia Project

On October 27, 2011, we entered into a joint venture, Parcel D Development, LLC (“Parcel D”), with Kettler to construct a 380-unit Class A apartment building with ground floor retail space in downtown Columbia, Maryland. We, and our partner, each own 50% of the venture, and unanimous consent of the partners is required for all major decisions. On July 11, 2013, the joint venture closed a \$64.1 million construction loan, which is non recourse to us, and \$56.2 million is outstanding as of June 30, 2015. The loan bears interest at one-month LIBOR plus 2.40% and matures in July 2020. At loan closing, our land contribution was valued at \$53,500 per unit, or \$20.3 million, and Kettler contributed \$13.3 million in cash, of which \$7.0 million was distributed to us. Both we and Kettler made additional contributions of \$3.1 million to the joint venture in accordance with the loan agreement, thus increasing our total capital account to \$16.4 million. The venture substantially completed construction of The Metropolitan Downtown Columbia Project during the first quarter of 2015 and the property was reclassified into our Operating Assets segment.

NOTE 8 MORTGAGES, NOTES AND LOANS PAYABLE

Mortgages, notes and loans payable are summarized as follows:

	June 30, 2015	December 31, 2014
	(In thousands)	
Fixed-rate debt:		
Collateralized mortgages, notes and loans payable	\$ 1,030,090	\$ 1,008,165
Special Improvement District bonds	17,516	22,389
Variable-rate debt:		
Collateralized mortgages, notes and loans payable (a)	1,238,568	962,916
Total mortgages, notes and loans payable	\$ 2,286,174	\$ 1,993,470

(a) As more fully described below, \$212.0 million of variable rate debt has been swapped to a fixed rate for the term of the related debt.

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The following table presents our mortgages, notes, and loans payable by property:

\$ In thousands	Maturity (a)	Interest		Maximum Facility Amount	Carrying Value	
		Rate			June 30, 2015	December 31, 2014
Master Planned Communities						
Bridgeland Land Loan	June 2022	5.50	%		\$ 15,874	\$ 15,874
Bridgeland Development Loan	July 2016	5.00	%	\$ 30,000	25,106	10
Summerlin South SID Bonds - S108	December 2016	5.95	%		411	563
Summerlin South SID Bonds - S124	December 2019	5.95	%		177	236
Summerlin South SID Bonds - S128	December 2020	6.05	%		535	623
Summerlin South SID Bonds - S128C	December 2030	6.05	%		5,025	5,274
Summerlin South SID Bonds - S132	December 2020	6.00	%		1,844	2,936
Summerlin South SID Bonds - S151	June 2025	6.00	%		4,714	6,211
Summerlin West SID Bonds - S808/S810	April 2031	6.00	%		1,069	2,805
The Woodlands Master Credit Facility (c)	August 2018	2.94	% (b)	200,000	192,663	176,663
Master Planned Communities Total					247,418	211,195
Operating Assets						
10-60 Columbia Corporate Centers (d)	May 2022	2.67	% (b)		80,000	—
70 Columbia Corporate Center	July 2019	2.44	% (b)		20,000	20,000
Columbia Regional Building	March 2018	2.19	% (b)	23,008	22,122	20,513
Downtown Summerlin	July 2019	2.44	% (b)	311,800	276,417	229,153
Downtown Summerlin SID Bonds - S108	December 2016	5.95	%		310	310
Downtown Summerlin SID Bonds - S128	December 2030	6.05	%		3,431	3,431
One Hughes Landing	December 2029	4.30	%		52,000	52,000

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	September					
Two Hughes Landing	2018	2.84	% (b)	41,230	31,250	19,992
Hughes Landing Retail	December 2018	2.14	% (b)	36,575	23,393	17,424
1701 Lake Robbins	April 2017	5.81	%		4,600	4,600
Millennium Waterway Apartments	June 2022	3.75	%		55,584	55,584
110 N. Wacker	October 2019	5.21	% (e)		28,370	29,000
9303 New Trails	December 2023	4.88	%		12,906	13,074
	November					
One Lake's Edge	2018	2.69	% (b)	73,525	59,169	40,787
Outlet Collection at Riverwalk	October 2018	2.94	% (b)	64,400	55,454	47,118
3831 Technology Forest Drive	March 2026	4.50	%		22,940	—
The Woodlands Resort & Conference Center	February 2019	3.69	% (b)	95,000	83,109	76,027
	September					
Ward Village (f)	2016	3.36	% (b)	250,000	238,716	238,716
20/25 Waterway Avenue	May 2022	4.79	%		14,221	14,330
3 Waterway Square	August 2028	3.94	%		52,000	52,000
4 Waterway Square	December 2023	4.88	%		37,797	38,289
Capital lease obligations	various	3.60	%		91	135
Operating Assets Total					1,173,880	972,483
Strategic Developments						
1725-35 Hughes Landing Boulevard	June 2019	2.09	% (b)	143,000	72,617	47,513
Lakeland Village Center	May 2020	2.54	% (b)	14,000	—	—
Three Hughes Landing	December 2019	2.54	% (b)	65,455	9,695	—
Hughes Landing Hotel	October 2020	2.69	% (b)	37,100	1,133	—
	November					
Waiea and Anaha Condominiums	2019	6.94	% (b)	600,000	7,985	—
Waterway Square Hotel	August 2019	2.84	% (b)	69,300	11,369	—
Strategic Developments Total					102,799	47,513
Other Corporate Financing						
Arrangements	June 2018	3.00	%	22,700	19,313	19,968
Senior Notes	October 2021	6.88	%		750,000	750,000
Unamortized underwriting fees					(7,236)	(7,689)
					\$ 2,286,174	\$ 1,993,470

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- (a) Maturity date includes any extension periods that can be exercised at our option and are subject to customary extension terms.
- (b) The interest rate presented is based on the one month LIBOR rate, as applicable, which was 0.19% at June 30, 2015.
- (c) The Woodlands Credit Facility was amended and restated on July 31, 2015.
- (d) \$40.0 million of the outstanding principal balance is swapped to a 3.41% fixed rate maturity.
- (e) The \$29.0 million outstanding principal balance is swapped to a 5.21% fixed rate through maturity.
- (f) \$143.0 million of the outstanding principal balance is swapped to a 3.81% fixed rate maturity.

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The weighted average interest rate on our mortgages, notes and loans payable, inclusive of interest rate hedges, was 4.43% and 4.61% as of June 30, 2015 and December 31, 2014, respectively.

All of the mortgage debt is secured by the individual properties as listed in the table above and is non-recourse to HHC, except for:

- (i) \$750.0 million of Senior Notes;
- (ii) \$311.8 million financing for the Downtown Summerlin development which has an initial maximum recourse of 35.0% of the outstanding balance, which will reduce to 15.0% upon completion of the project and achievement of a 1.15:1.0 debt service coverage ratio. The recourse further reduces to 10% upon achievement of a 1.25:1.0 debt service coverage ratio, a 90% occupancy level, and average tenant sales of at least \$500.00 per net rentable square foot;
- (iii) \$64.4 million of construction financing for the Outlet Collection at Riverwalk with an initial maximum recourse of 50% of the outstanding balance, which will be reduced to 25.0% upon completion of the project and the achievement of an 11.0% debt yield and a minimum level of tenant sales per square foot for twelve months;
- (iv) \$20.4 million of Other Corporate Financing Arrangements; and
- (v) \$7.0 million parent guarantee associated with the 110 N. Wacker mortgage.

The Woodlands Master Credit Facility and The Woodlands Resort & Conference Center loans are recourse to the entities that directly own The Woodlands operations. Certain of our loans contain provisions which grant the lender a security interest in the operating cash flow of the property that represents the collateral for the loan. Certain mortgage notes may be prepaid, but may be subject to a prepayment penalty equal to a yield-maintenance premium, defeasance, or a percentage of the loan balance. As of June 30, 2015, land, buildings and equipment and developments with a cost basis of \$2.5 billion have been pledged as collateral for our mortgages, notes and loans payable.

As of June 30, 2015, we were in compliance with all of the financial covenants related to our debt agreements.

Master Planned Communities

The Woodlands Master Credit Facility was amended and restated on July 31, 2015 to a \$200.0 million maximum facility amount consisting of a \$100.0 million term loan and a \$100.0 million revolver (together, the “TWL Facility”). The TWL Facility bears interest at one-month LIBOR plus 2.75% and has an August 2016 initial maturity date with two, one-year extension options. The extension options require a reduction of the total commitment to \$175.0 million for the first extension and semi-annual principal payments of \$25.0 million during the second extension period. The TWL Facility also contains certain covenants that, among other things, require the maintenance of specified financial ratios, limit the incurrence of additional recourse indebtedness at The Woodlands, and limit distributions from The Woodlands to us based on a loan to value test. The amendment also modified certain covenants to allow for more construction loan guarantees by the entities that directly own The Woodlands than would otherwise have been permitted by the prior facility. As of June 30, 2015, there is no undrawn availability based on the collateral value underlying the facility.

The Bridgeland Land Loan bears a fixed interest rate of 5.50% for the first five years and three-month LIBOR plus 2.75% for the remaining term and matures in June 2022. Annual principal payments are required in the amount of 5.00% of the then outstanding principal balance. In addition, Bridgeland has a revolving credit facility with aggregate maximum borrowing capacity of \$140.0 million, of which \$130.3 million has been utilized as of June 30, 2015, and which has a \$30.0 million maximum outstanding loan amount at any time. The revolving loan bears interest at the greater of 5.00% or one-month LIBOR plus 3.25%. In June 2015, we obtained a one-year extension for the revolver, which now matures on July 15, 2016. We expect to refinance this loan prior to its maturity. This loan is intended to provide working capital at Bridgeland to accelerate development efforts to meet the demand of homebuilders for finished lots in the community. The

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Bridgeland loans are cross collateralized and cross defaulted and the Bridgeland Master Planned Community serves as collateral for the loans. The loans also require that Bridgeland maintain a minimum \$3.0 million cash balance and a minimum net worth of \$250.0 million. Additionally, we are restricted from making cash distributions from Bridgeland unless the revolving credit facility has no outstanding balance and one year of real estate taxes and debt service on the term loan have been escrowed with the lender.

Operating Assets

On May 6, 2015, we closed on an \$80.0 million non-recourse mortgage financing for the 10-60 Columbia Corporate Center office buildings. The loan bears interest at LIBOR plus 1.75% and has an initial maturity date of May 6, 2020, with two, one-year extension options.

On March 25, 2015, we closed on a \$23.0 million non-recourse mortgage financing for 3831 Technology Forest Drive. The loan bears fixed interest at 4.50% and matures on March 24, 2026.

Corporate

The \$750.0 million in aggregate principal amount of 6.875% Senior Notes matures in 2021 (the "Senior Notes"). Interest is payable semiannually, on April 1 and October 1 of each year starting in April 2014. At any time prior to October 1, 2016, we may redeem up to 35% of the Senior Notes at a price equal to 106.875% using the proceeds from equity offerings. We may redeem all or part of the Senior Notes at any time on or after October 1, 2016 with a declining call premium thereafter to maturity. The Senior Notes contain customary terms and covenants for non investment grade senior notes and have no maintenance covenants.

NOTE 9 DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

We are exposed to interest rate risk related to our variable interest rate debt, and we manage this risk by utilizing interest rate derivatives. Our objectives in using interest rate derivatives are to add stability to interest costs by reducing our exposure to interest rate movements. To accomplish this objective, we use interest rate swaps and caps as part of our interest rate risk management strategy. Interest rate swaps designated as cash flow hedges involve the receipt of variable amounts from a counterparty in exchange for the Company's fixed rate payments over the life of the agreements without exchange of the underlying notional amount. Interest rate caps designated as cash flow hedges involve the receipt of variable amounts from a counterparty if interest rates rise above the strike rate on the contract in exchange for an up front premium.

The effective portion of changes in the fair value of derivatives designated and that qualify as cash flow hedges is recorded in Accumulated Other Comprehensive Income ("AOCI") and is subsequently reclassified into earnings in the period that the hedged forecasted transaction affects earnings. The ineffective portion of the change in fair value of the derivatives is recognized directly in earnings. During the six months ended June 30, 2015, the ineffective portion recorded in earnings was insignificant.

As of June 30, 2015, we had gross notional amounts of \$211.4 million for interest rate swaps and a \$100.0 million interest rate cap that were designated as cash flow hedges of interest rate risk. The fair value of the interest rate cap derivative was insignificant.

If the interest rate swap agreements are terminated prior to their maturity, the amounts previously recorded in AOCI are recognized into earnings over the period that the hedged transaction impacts earnings. If the hedging relationship is discontinued because it is probable that the forecasted transaction will not occur according to the original strategy, any related amounts previously recorded in AOCI are recognized in earnings immediately.

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Amounts reported in AOCI related to derivatives will be reclassified to interest expense as interest payments are made on our variable rate debt. Over the next 12 months, we estimate that an additional \$2.5 million will be reclassified to interest expense.

The table below presents the fair value of our derivative financial instruments, which are included in accounts payable and accrued liabilities in the Consolidated Balance Sheets:

	June 30, 2015 (In thousands)	December 31, 2014
Interest Rate Swaps	\$ 2,993	\$ 3,144

The table below presents the effect of our derivative financial instruments on the Consolidated Statements of Operations for the three and six months ended June 30, 2015 and 2014:

	Three Months Ended June 30,		Location of Loss Reclassified from AOCI into Earnings	Three Months Ended June 30,	
	2015	2014		2015	2014
Cash Flow Hedges	Amount of Loss Recognized in OCI (In thousands)	Amount of Loss Recognized in OCI (In thousands)		Amount of Loss Reclassified from AOCI into Earnings (In thousands)	Amount of Loss Reclassified from AOCI into Earnings (In thousands)
Interest Rate Swaps	\$ (240)	\$ (629)	Interest Expense	\$ (436)	\$ (548)

	Six Months Ended June 30,		Location of Loss Reclassified from AOCI into Earnings	Six Months Ended June 30,	
	2015	2014		2015	2014
Cash Flow Hedges	Amount of Loss Recognized in OCI (In thousands)	Amount of Loss Recognized in OCI		Amount of Loss Reclassified from AOCI into Earnings (In thousands)	Amount of Loss Reclassified from AOCI into Earnings
Interest Rate Swaps	\$ (103)	\$ (971)	Interest Expense	\$ (811)	\$ (1,089)

NOTE 10 INCOME TAXES

Two of our subsidiaries are involved in a dispute with the IRS relating to years in which those subsidiaries were owned by General Growth Properties (“GGP”), and in connection therewith, GGP provided us with an indemnity against certain potential tax liabilities. Pursuant to the Tax Matters Agreement with GGP, GGP had indemnified us from and against 93.75% of any and all losses, claims, damages, liabilities and reasonable expenses to which we become subject (the “Tax Indemnity”), in each case solely to the extent directly attributable to certain taxes related to sales of certain assets in our Master Planned Communities segment prior to March 31, 2010 (“MPC Taxes”), in an amount up to \$303.8 million, plus interest and penalties related to these amounts (the “Indemnity Cap”) so long as GGP controlled the action in the United States Tax Court (the “Tax Court”) related to the dispute with the IRS.

On May 6, 2011, GGP filed Tax Court petitions on behalf of the two former REIT subsidiaries of GGP seeking a redetermination of federal income tax for the years 2007 and 2008. The petitions sought to overturn determinations by the IRS that the taxpayers were liable for combined deficiencies totaling \$144.1 million. The case was heard by the Tax Court in November 2012 and filed its ruling in favor of the IRS on June 2, 2014.

In December 2014, we entered into a tax indemnity and mutual release agreement with GGP (the “Settlement Agreement”)

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pursuant to which, in consideration of the full satisfaction of GGP's obligation for reimbursement of taxes and interest related to certain assets in our Master Planned Communities segment prior to March 31, 2010, GGP (i) made a cash payment to us in the amount of \$138.0 million and (ii) conveyed to us fee simple interest in six office properties and related parking garages located in Columbia, Maryland, known as 10-60 Columbia Corporate Center, for an agreed upon total value of \$130.0 million. Under the Settlement Agreement, the Company now controls the right to decide whether to appeal the decision rendered by the Tax Court. On December 15, 2014, the Company paid the MPC Taxes and filed an appeal of the decision to the Fifth Circuit Court of Appeals. The appeal seeks to overturn the lower court decision and allow the Company to continue to use its current method of tax accounting for the sale of assets in the Company's Master Planned Communities Segment. If the decision stands, we may be required to change our method of tax accounting for certain transactions, which could affect the timing of our future tax payments. The appellate court has tentatively scheduled this case for oral arguments during the week beginning August 31, 2015.

Unrecognized tax benefits pursuant to uncertain tax positions were \$184.2 million as of June 30, 2015 and December 31, 2014, none of which would impact our effective tax rate. This amount is not reduced for either amounts reclassified under ASU 2013-11, or payments made to the IRS pursuant to the appeal filed with the Fifth Circuit Court of Appeals. A significant amount of the unrecognized tax benefits is related to the appeal of the Tax Court decision, which is expected to be resolved within the next 12 months.

We have significant permanent differences, primarily from warrant liability gains and losses, interest income on the tax indemnity receivable and changes in valuation allowances that cause our effective tax rate to deviate from statutory rates. The effective tax rates based upon actual operating results were 7.8% and (13.4)% for the three and six months ended June 30, 2015 compared to 149.6% and (95.2)% for the three and six months ended June 30, 2014. The changes in the tax rates were primarily attributable to changes in the warrant liability, valuation allowance and unrecognized tax benefits.

We file a consolidated corporate tax return which, through December 31, 2014, includes all of our subsidiaries with the exception of Victoria Ward, Limited ("Ward"). Ward elected to be taxed as a REIT commencing with the taxable year beginning January 1, 2002 and ending with the taxable year ending December 31, 2014. Beginning on January 1, 2015, Ward will be included in our consolidated tax return.

NOTE 11 STOCK BASED PLANS

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Our stock based plans are described, and informational disclosures are provided, in the Notes to the Consolidated Financial Statements included in our Form 10-K for the year ended December 31, 2014.

Stock Options

The following table summarizes our stock option plan:

	Stock Options	Weighted Average Exercise Price
Stock Options outstanding at January 1, 2015	1,046,490	\$ 72.61
Granted	67,000	147.33
Forfeited	(64,740)	106.52
Stock Options outstanding at June 30, 2015	1,048,750	\$ 75.38

For the three and six months ended June 30, 2015, stock option expense was \$0.7 million and \$0.9 million, respectively. For the three and six months ended June 30, 2014, stock option expense was \$1.0 million and \$2.0 million, respectively.

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Restricted Stock

The following table summarizes restricted stock activity:

	Restricted Stock	Weighted Average Grant Date Fair Value
Restricted stock outstanding at January 1, 2015	172,690	\$ 92.02
Granted	80,913	121.59
Vested	(7,546)	147.56
Forfeited	(4,002)	99.33
Restricted Stock outstanding at June 30, 2015	242,055	\$ 100.05

For the three and six months ended June 30, 2015, compensation expense related to restricted stock awards was \$1.2 million and \$2.1 million, respectively. For the three and six months ended June 30, 2014, compensation expense related to restricted stock awards was \$1.0 million and \$1.8 million, respectively

NOTE 12 OTHER ASSETS AND LIABILITIES

Prepaid Expenses and Other Assets

The following table summarizes the significant components of prepaid expenses and other assets.

	June 30, 2015	December 31, 2014
	(In thousands)	
Special Improvement District receivable	\$ 31,866	\$ 33,318
Equipment, net of accumulated depreciation of \$3.2 million and \$2.4 million, respectively	19,528	20,284
Tenant incentives and other receivables	19,843	14,264
Federal income tax receivable	8,623	8,629
Prepaid expenses	7,869	9,196
Below-market ground leases	19,494	19,663
Condominium deposits	79,590	151,592
Condominium receivables	42,491	—
Security and escrow deposits	12,353	9,829
Above-market tenant leases	4,089	4,656
Uncertain tax position asset	422	383
In-place leases	26,558	32,715
Intangibles	3,932	3,593
Other	1,593	2,014
	\$ 278,251	\$ 310,136

The \$31.9 million decrease as of June 30, 2015 compared to December 31, 2014 primarily relates to a \$72.0 million decrease in condominium deposits at Ward Village due to utilization of deposits for construction costs. The \$6.2 million decrease related to in-place leases is attributable to normal amortization of these intangibles, and is primarily due to the recently acquired 10-60 Columbia Corporate Center office buildings. These decreases are partially offset by a \$42.5 million increase in condominium receivables, which represents revenue recognized in excess of buyer deposits received for our Waiea and Anaha projects.

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Accounts Payable and Accrued Expenses

The following table summarizes the significant components of accounts payable and accrued expenses.

	June 30, 2015	December 31, 2014
	(In thousands)	
Construction payables	\$ 192,210	\$ 170,935
Accounts payable and accrued expenses	27,009	34,154
Condominium deposits	22,102	82,150
Membership deposits	21,346	21,023
Above-market ground leases	2,192	2,272
Deferred income	69,502	65,675
Accrued interest	15,239	14,791
Accrued real estate taxes	9,639	9,903
Tenant and other deposits	31,181	12,756
Accrued payroll and other employee liabilities	16,822	25,838
Interest rate swaps	2,993	3,144
Other	27,763	23,376
	\$ 437,998	\$ 466,017

The \$28.0 million decrease as of June 30, 2015 compared to December 31, 2014 is primarily due to the decrease of \$60.0 million in condominium deposits for the two market rate towers at Ward Village as revenue was recognized during the period, \$9.0 million decrease in accrued payroll and other employee liabilities due to annual incentive compensation payments, which are accrued for throughout the year and typically paid in the first quarter, and a \$7.1 million decrease in accounts payable and accrued expenses. These decreases are partially offset by a \$21.3 million increase in construction payables primarily due to continued development activities at Ward Village, 1725-35 Hughes Landing Boulevard, South Street Seaport, Waterway Hotel, Hughes Landing Hotel and Three Hughes Landing, and an \$18.4 million increase in tenant and other deposits primarily related to tenant incentives at 1725-35 Hughes Landing Boulevard.

NOTE 13 ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS) (“AOCI”)

The following table summarizes AOCI for the period indicated:

Changes in Accumulated Other Comprehensive Income (Loss) by Component (a)

Gains and (Losses) on Cash Flow Hedges

(In Thousands)

	For the Three Months Ended June 30, 2015
Balance as of March 31, 2015	\$ (7,259)
Other comprehensive loss before reclassifications	(293)
Amounts reclassified from accumulated other comprehensive loss	436
Net current-period other comprehensive income	143
Balance as of June 30, 2015	\$ (7,116)

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	For the Six Months Ended June 30, 2015
Balance as of January 1, 2015	\$ (7,712)
Other comprehensive income before reclassifications	(215)
Amounts reclassified from accumulated other comprehensive loss	811
Net current-period other comprehensive income	596
Balance as of June 30, 2015	\$ (7,116)

(a) All amounts are net of tax.

The following table summarizes the amounts reclassified out of AOCI for the period indicated:

Reclassifications out of Accumulated Other Comprehensive Income (Loss)

(In Thousands)

Accumulated Other Comprehensive Income (Loss) Components	Amounts reclassified from Accumulated Other Comprehensive Income (Loss)		
	For the Three Months Ended June 30, 2016	For the Six Months Ended June 30, 2016	For the Six Months Ended June 30, 2015
Gains and losses on cash flow hedges			For the Three Months Ended June 30, 2016
Interest rate swap contracts	\$ (705)	\$ (1,301)	For the Six Months Ended June 30, 2016
	269	490	For the Six Months Ended June 30, 2015
Total reclassifications for the period	\$ (436)	\$ (811)	Statement of Operations
			Interest expense
			Provision for income taxes
			Net of tax

NOTE 14 COMMITMENTS AND CONTINGENCIES

In the normal course of business, from time to time, we are involved in legal proceedings relating to the ownership and operations of our properties. In management's opinion, the liabilities, if any, that may ultimately result from such legal actions are not expected to have a material effect on our consolidated financial position, results of operations or liquidity.

We had outstanding letters of credit and surety bonds totaling \$76.0 million and \$53.7 million as of June 30, 2015 and December 31, 2014, respectively. These letters of credit and bonds were issued primarily in connection with insurance requirements, special real estate assessments and construction obligations.

On June 27, 2013, the City of New York executed the amended and restated ground lease for South Street Seaport. The restated lease terms provide for annual fixed rent of \$1.2 million starting July 1, 2013 with an expiration of December 30, 2072, including options to extend. The rent escalates at 3.0% compounded annually. On July 1, 2048 the base rent will be adjusted to the higher of the fair market value or the then base rent. In addition to the annual base rent of \$1.2 million, we are required to make annual payments of \$210,000 as additional rent through the term of the lease. The additional rent escalates annually at the Consumer Price Index. We are entitled to a total rent credit of \$1.5 million, to be taken monthly over a 30-month period. Simultaneously with the execution of the lease, we executed a completion guaranty for the redevelopment of Pier 17. The completion guaranty requires us to perform certain obligations under the lease, including the commencement of construction by October 1, 2013 with a scheduled completion date in 2017.

In the fourth quarter of 2012, the historic area of South Street Seaport suffered damage due to flooding as a result of Superstorm Sandy. Reconstruction efforts are ongoing and the property is only partially operating. We have received \$47.9 million in insurance proceeds through June 30, 2015 related to our claim and recognized Other income of \$0.3

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million for the six months ended June 30, 2015 for the amounts received during that period. We are in litigation with several of the insurance carriers to recover additional amounts that we believe are owed to us under the policies. We believe that our insurance will reimburse substantially all of the costs of repairing the property and will also compensate us for substantially all lost income resulting from the storm.

Please refer to Note 10 – Income Taxes for additional contingencies related to our uncertain tax positions.

NOTE 15 SEGMENTS

We have three business segments which offer different products and services. Our three segments are managed separately because each requires different operating strategies or management expertise and are reflective of management's operating philosophies and methods. In addition, our segments or assets within such segments could change in the future as development of certain properties commences or other operational or management changes occur. We do not distinguish or group our combined operations on a geographic basis. Furthermore, all operations are within the United States. Our reportable segments are as follows:

- Master Planned Communities ("MPCs") – includes the development and sale of land, in large scale, long term community development projects in and around Las Vegas, Nevada; Houston, Texas; and Columbia, Maryland.
- Operating Assets – includes retail, office, and multi-family properties, The Woodlands Resort & Conference Center, The Club at Carlton Woods and other real estate investments. These assets are currently generating revenues, and we believe there is an opportunity to redevelop, reposition, or sell certain of these assets to improve segment performance.
- Strategic Developments – includes our condominium and commercial property projects currently under development and all other properties held for development which have no substantial operations.

Revenue recognition for contracted individual units in a condominium project are accounted for under the percentage of completion method when the following criteria are met: a) construction is beyond a preliminary stage; b) buyer is unable to require a refund of its deposit, except for non delivery of the unit; c) sufficient units are sold to assure that it

will not revert to a rental property; d) sales prices are collectible; and e) aggregate sales proceeds and costs can be reasonably estimated. Those units that do not meet the criteria are accounted for using the full accrual or deposit method which defers revenue recognition until the unit is closed.

Revenue recognized on the percentage-of-completion method is calculated based upon the ratio of project costs incurred to date compared to total estimated project cost. Total estimated project costs include direct costs such as the carrying value of our land, site planning, architectural, construction costs, financing costs and indirect cost allocations for certain infrastructure and amenity costs which benefit the project based upon the relative fair value of the land prior to development. Changes in estimated project costs impact the amount of revenue and profit recognized on a percentage of completion basis during the period in which they are determined and future periods.

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The assets included in each segment as of June 30, 2015, are contained in the following chart

Master Planned Communities	Operating Assets		Strategic Developments	
	Retail	Office	Under Construction	Other
• Bridgeland	Columbia Regional Building	10-70 Columbia Corporate Center	Anaha Condominiums	Alameda Plaza
• Conroe	Cottonwood Square	Columbia Office Properties	Three Hughes Landing	ONE Ala Moana (d)
• Maryland	Creekside Village Green (b)	One Hughes Landing	1725-35 Hughes Landing	Alden Bridge Self-Storage
• Summerlin (a)	Downtown Summerlin	Two Hughes Landing	Boulevard	AllenTowne
• The Woodlands	Hughes Landing Retail (b)	2201 Lake Woodlands Drive	Hughes Landing Hotel (Embassy Suites)	Bridges at Mint Hill
	1701 Lake Robbins	9303 New Trails		Century Plaza Mall
	Landmark Mall	110 N. Wacker	Lakeland Village Center	Circle T Ranch and Power Center (c)
	Outlet Collection at Riverwalk	3831 Technology Forest Drive	Summerlin Apartments, LLC (c)	
	Park West	3 Waterway Square	Waiea Condominiums	Cottonwood Mall
	South Street Seaport (under construction)	4 Waterway Square	Waterway Square Hotel	Elk Grove Promenade
	Ward Village	1400 Woodloch Forest	(Westin)	80% Interest in Fashion Show Air Rights
	20/25 Waterway Avenue			Kendall Town Center
	Waterway Garage Retail			Lakemoor (Volo) Land
				Maui Ranch Land

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Other		Parcel C (c)
Golf Courses at TPC	Stewart Title of	Seaport District
Summerlin	Montgomery	Assemblage
and TPC Las Vegas	County, TX (c)	Ward Block M
(participation	Summerlin Hospital	Ward Gateway
interest)	Medical	Towers
Kewalo Basin	Center (c)	Ward Workforce
Harbor		Tower
Merriweather Post	Summerlin Las	West Windsor
Pavilion	Vegas	
Millennium	Baseball Club (c)	
Waterway		
Apartments		
Millennium	The Metropolitan	
Woodlands	Downtown	
Phase II (c)	Columbia Project	
	(b) (c)	
One Lake's Edge (b)	The Club at Carlton	
	Woods	
85 South Street	The Woodlands	
	Resort &	
	Conference Center	
	The Woodlands	
	Parking Garages	
	Woodlands Sarofim	
	#1 (c)	

-
- (a) The Summerlin MPC includes our Discovery Land joint venture.
- (b) Asset was placed in service and moved from the Strategic Developments segments to the Operating Assets segment during 2015.
- (c) A non-consolidated investment.
- (d) Asset consists of two equity method investments. Construction was substantially completed in the fourth quarter of 2014 and the last available unit was sold in the second quarter of 2015.

As our segments are managed separately, different operating measures are utilized to assess operating results and allocate resources among the segments. The one common operating measure used to assess operating results for the business segments is Real Estate Property Earnings Before Taxes ("REP EBT"), which represents the operating revenues of the properties less property operating expenses and adjustments for interest, as further described below. We believe REP EBT provides useful information about the operating performance for all of our properties.

REP EBT, as it relates to our business, is defined as net income (loss) excluding general and administrative expenses, other income, corporate interest income, corporate interest and depreciation expense, provision for income taxes, warrant liability gain or loss and the change in tax indemnity receivable. We present REP EBT because we use this measure, among others, internally to assess the operating performance of our assets. We also present this measure because we believe certain investors use it as a measure of a company's historical operating performance and its ability to service and incur debt. We believe that the inclusion of certain adjustments to net income (loss) to calculate REP EBT is appropriate to provide additional information to investors.

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Segment operating results are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
	(In thousands)		(In thousands)	
Master Planned Communities				
Land sales	\$ 45,433	\$ 153,164	\$ 93,514	\$ 200,835
Builder price participation	7,907	3,843	13,605	7,940
Minimum rents	215	207	430	404
Other land revenues	3,140	2,689	6,426	5,193
Other rental and property revenues	9	108	7	175
Total revenues	56,704	160,011	113,982	214,547
Cost of sales – land	24,236	42,719	48,132	65,797
Land sales operations	9,721	9,275	17,300	16,579
Land sales real estate and business taxes	2,242	2,135	4,646	4,089
Depreciation and amortization	95	103	190	203
Interest income	(15)	(22)	(31)	(79)
Interest expense (*)	(4,684)	(4,813)	(9,446)	(9,879)
Total expenses	31,595	49,397	60,791	76,710
MPC EBT	25,109	110,614	53,191	137,837
Operating Assets				
Minimum rents	36,697	21,918	71,009	41,818
Tenant recoveries	10,693	6,941	20,266	12,825
Resort and conference center revenues	11,481	9,622	23,484	19,048
Other rental and property revenues	6,971	6,570	13,245	11,680
Total revenues	65,842	45,051	128,004	85,371
Other property operating costs	18,350	15,485	35,836	28,666
Rental property real estate taxes	5,990	3,762	11,510	6,869
Rental property maintenance costs	2,785	2,008	5,412	3,808
Resort and conference center operations	8,893	6,412	17,971	13,923
Provision for doubtful accounts	1,266	31	2,075	174
Demolition costs	1,496	3,434	1,613	5,928

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Development-related marketing costs	2,748	2,711	5,014	4,790
Depreciation and amortization	22,887	9,531	41,649	18,541
Interest income	(9)	(11)	(19)	(130)
Interest expense	7,629	3,928	14,123	5,972
Equity in Earnings from Real Estate and Other				
Affiliates	(160)	(767)	(1,044)	(2,572)
Total expenses	71,875	46,524	134,140	85,969
Operating Assets EBT	(6,033)	(1,473)	(6,136)	(598)
Strategic Developments				
Minimum rents	77	73	744	336
Tenant recoveries	8	(57)	102	74
Condominium rights and unit sales	86,513	4,358	121,370	7,484
Other land revenues	5	9	12	17
Other rental and property revenues	14	186	39	455
Total revenues	86,617	4,569	122,267	8,366
Condominium rights and unit cost of sales	56,765	2,191	79,174	3,762
Other property operating costs	1,284	1,094	1,943	1,721
Real estate taxes	578	479	1,258	1,112
Rental property maintenance costs	115	166	232	281
Demolition costs	—	1	—	23
Development-related marketing costs	2,846	2,588	6,823	4,732
Depreciation and amortization	601	614	1,617	1,038
Other income	—	—	(334)	(2,373)
Interest income	(166)	—	(166)	—
Interest expense (*)	(1,580)	(3,981)	(3,385)	(6,630)
Equity in Earnings from Real Estate and Other				
Affiliates	(921)	(5,820)	(1,825)	(10,083)
Total expenses	59,522	(2,668)	85,337	(6,417)
Strategic Developments EBT	27,095	7,237	36,930	14,783
REP EBT	\$ 46,171	\$ 116,378	\$ 83,985	\$ 152,022

(*)Negative interest expense amounts are due to interest capitalized in our Master Planned Communities and Strategic Developments segments related to Operating Assets segment debt and the Senior Notes.

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The following reconciles REP EBT to GAAP basis income (loss) before taxes:

Reconciliation of REP EBT to GAAP income (loss) before taxes	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
	(In thousands)		(In thousands)	
REP EBT	\$ 46,171	\$ 116,378	\$ 83,985	\$ 152,022
General and administrative	(19,606)	(17,497)	(38,569)	(34,379)
Corporate interest income/(expense), net	(13,235)	4,829	(26,447)	(6,151)
Warrant liability gain (loss)	42,620	(67,370)	(66,190)	(163,810)
Reduction in tax indemnity receivable	—	(10,927)	—	(10,927)
Corporate other income, net	396	5,611	1,529	13,686
Corporate depreciation and amortization	(1,487)	(1,225)	(3,124)	(2,200)
Income (loss) before taxes	\$ 54,859	\$ 29,799	\$ (48,816)	\$ (51,759)

The following reconciles segment revenues to GAAP basis consolidated revenues:

Reconciliation of Segment Basis Revenues to GAAP Revenues	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
	(In thousands)		(In thousands)	
Master Planned Communities	\$ 56,704	\$ 160,011	\$ 113,982	\$ 214,547
Operating Assets	65,842	45,051	128,004	85,371
Strategic Developments	86,617	4,569	122,267	8,366
Total revenues	\$ 209,163	\$ 209,631	\$ 364,253	\$ 308,284

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The assets by segment and the reconciliation of total segment assets to the total assets in the Condensed Consolidated Balance Sheets are summarized as follows:

	June 30, 2015	December 31, 2014
	(In thousands)	
Master Planned Communities	\$ 1,919,445	\$ 1,877,043
Operating Assets	2,132,283	1,934,350
Strategic Developments	1,031,491	879,896
Total segment assets	5,083,219	4,691,289
Corporate and other	322,610	428,642
Total assets	\$ 5,405,829	\$ 5,119,931

The \$151.6 million increase in the Strategic Developments segment asset balance as of June 30, 2015 compared to December 31, 2014 is primarily due to the following:

Increases in asset balance

- Development expenditures of \$91.4 million for the 80 South Street Assemblage, \$52.9 million for the 1725-35 Hughes Landing Boulevard office buildings, \$29.7 million for Waterway Square Hotel (Westin), \$28.7 million for the Three Hughes Landing office building, \$23.7 million for Ward Village, \$17.6 million for Hughes Landing Hotel (Embassy Suites) and \$14.2 million for our Waiea Condominiums;
- \$42.1 million in condominium receivables due to percent complete revenue recognition in excess of buyers deposits;

Reductions in asset balance

- \$125.3 million resulting from the transfer of Hughes Landing Retail, One Lake's Edge, The Metropolitan Downtown Columbia Project and Creekside Village to the Operating Assets segment;
- \$8.5 million in cash distributions from our equity investment in ONE Ala Moana. The cash was moved to the Corporate segment.

Corporate and other assets as of June 30, 2015 consist primarily of Cash and cash equivalents. The \$106.0 million decrease compared to December 31, 2014 is primarily due to our development activities.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis should be read in conjunction with the Condensed Consolidated Financial Statements and notes and the company's Annual Report on Form 10-K for the year ended December 31, 2014. All references to numbered Notes are to specific notes to our Condensed Consolidated Financial Statements included in this Quarterly Report.

Forward-looking information

We may make forward-looking statements in this Quarterly Report and in other reports that we file with the SEC. In addition, our management may make forward-looking statements orally to analysts, investors, creditors, the media and others.

Forward-looking statements include:

- projections of our revenues, operating income, net income, earnings per share, REP EBT Net Operating Income ("NOI"), capital expenditures, income tax, other contingent liabilities, dividends, leverage, capital structure or other financial items;
- forecasts of our future economic performance; and
- descriptions of assumptions underlying or relating to any of the foregoing.

In this Quarterly Report, for example, we make forward-looking statements discussing our expectations about:

- capital required for our operations and development opportunities for the properties in our Operating Assets and Strategic Developments segments;
- expected performances of our Master Planned Communities segment and other current income producing properties; and
- future liquidity, development opportunities, development spending and management plans.

Forward-looking statements discuss matters that are not historical facts. Because they discuss future events or conditions, forward-looking statements often include words such as "anticipate," "believe," "can," "could," "estimate," "expect," "forecast," "intend," "may," "likely," "plan," "project," "realize," "should," "target," "would," and other words of similar expressions. Forward-looking statements should not be unduly relied upon. They give our expectations about the future and are not guarantees.

There are several factors, many beyond our control, which could cause results to differ materially from our expectations. These risk factors are described in our Annual Report on Form 10-K for the year ended December 31, 2014 (the “Annual Report”) and are incorporated herein by reference. Any factor could, by itself, or together with one or more other factors, adversely affect our business, results of operations or financial condition. There may also be other factors that we have not described in this Quarterly Report or in our Annual Report that could cause results to differ from our expectations. These forward-looking statements present our estimates and assumptions only as of the date of this Quarterly Report. Except as may be required by law, we undertake no obligation to modify or revise any forward-looking statements to reflect events or circumstances occurring after the date of this Quarterly Report.

Real Estate Property Earnings Before Taxes

We use a number of operating measures for assessing operating performance of our communities, assets, properties and projects within our segments, some of which may not be common among all three of our segments. We believe that investors may find some operating measures more useful than others when separately evaluating each segment. One common operating measure used to assess operating results for our business segments is Real Estate Property Earnings Before Taxes (“REP EBT”). We also give measures based on adjusted REP EBT which excludes depreciation and amortization, demolition and development-related marketing costs. We believe REP EBT provides useful information about our operating performance because it excludes certain non-recurring and non-cash items, which we believe are not

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indicative of our core business. REP EBT may be calculated differently by other companies in our industry, limiting its usefulness as a comparative measure.

REP EBT, as it relates to our business, is defined as net income (loss) excluding general and administrative expenses, corporate interest income and corporate interest and depreciation expense, provision for income taxes, warrant liability gain (loss), other income and, prior to 2015, the changes in tax indemnity receivable. We present REP EBT because we use this measure, among others, internally to assess the core operating performance of our assets. We also present this measure because we believe certain investors use it as a measure of a company's historical operating performance and its ability to service and incur debt. We believe that the inclusion of certain adjustments to net income (loss) to calculate REP EBT is appropriate to provide additional information to investors. A reconciliation of REP EBT to consolidated net income (loss) as computed in accordance with GAAP has been presented in Note 15 – Segments.

REP EBT and adjusted REP EBT should not be considered as alternatives to GAAP net income (loss) attributable to common stockholders or GAAP net income (loss), as each has limitations as an analytical tool, and should not be considered in isolation, or as a substitute for analysis of our results as reported under GAAP. Some of the limitations of these metrics are that they do not include the following:

- cash expenditures, or future requirements for capital expenditures or contractual commitments;
- corporate general and administrative expenses;
- interest expense on our corporate debt;
- income taxes that we may be required to pay;
- any cash requirements for replacement of depreciated or amortized assets; and
- limitations on, or costs related to, transferring earnings from our Real Estate and Other Affiliates to us.

Operating Assets Net Operating Income

We believe that NOI is a useful supplemental measure of the performance of our Operating Assets because it provides a performance measure that, when compared year over year, reflects the revenues and expenses directly associated with owning and operating real estate properties and the impact on operations from trends in rental and occupancy rates and operating costs. We define NOI as revenues (rental income, tenant recoveries and other income) less expenses (real estate taxes, repairs and maintenance, marketing and other property expenses). NOI excludes straight line rents and amortization of tenant incentives, net interest expense, ground rent amortization, demolition costs, amortization, depreciation, development-related marketing costs and equity in earnings from Real Estate and Other Affiliates. We use NOI to evaluate our operating performance on a property-by-property basis because NOI allows us to evaluate the impact that factors such as lease structure, lease rates and tenant base, which vary by property, have on our operating results, gross margins and investment returns.

Although we believe that NOI provides useful information to investors about the performance of our Operating Assets, due to the exclusions noted above, NOI should only be used as an alternative measure of the financial performance of such assets and not as an alternative to GAAP net income (loss). For reference, and as an aid in understanding our computation of NOI, a reconciliation of NOI to REP EBT has been presented in the Operating Assets segment discussion below.

Results of Operations

Our revenues are primarily derived from the sale of individual lots at our master planned communities to homebuilders, from tenants at our operating assets in the form of fixed minimum rents, overage rent and recoveries of operating expenses, and from the sale of condominium units.

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The following table reflects our results of operations for the three and six months ended June 30, 2015 and 2014, respectively:

	Three Months Ended			Six Months Ended June		
	June 30, 2015	2014	Change	2015	2014	Change
	(In thousands, except per share amounts)			(In thousands, except per share amounts)		
Revenues						
MPC segment revenues	\$ 56,704	\$ 160,011	\$ (103,307)	\$ 113,982	\$ 214,547	\$ (100,565)
Operating Assets segment revenues	65,842	45,051	20,791	128,004	85,371	42,633
Strategic Developments segment revenues	86,617	4,569	82,048	122,267	8,366	113,901
Total segment revenues	\$ 209,163	\$ 209,631	\$ (468)	\$ 364,253	\$ 308,284	\$ 55,969
MPC segment REP EBT						
Operating Assets segment REP EBT	(6,033)	(1,473)	(4,560)	(6,136)	(598)	(5,538)
Strategic Developments segment REP EBT	27,095	7,237	19,858	36,930	14,783	22,147
Total segment REP EBT	46,171	116,378	(70,207)	83,985	152,022	(68,037)
General and administrative	(19,606)	(17,497)	(2,109)	(38,569)	(34,379)	(4,190)
Corporate interest expense, net	(13,235)	4,829	(18,064)	(26,447)	(6,151)	(20,296)
Warrant liability gain (loss)	42,620	(67,370)	109,990	(66,190)	(163,810)	97,620
Increase (reduction) in tax indemnity receivable	-	(10,927)	10,927	-	(10,927)	10,927
Corporate other income, net	396	5,611	(5,215)	1,529	13,686	(12,157)
Corporate depreciation and amortization	(1,487)	(1,225)	(262)	(3,124)	(2,200)	(924)
Provision for income taxes	(4,274)	(44,532)	40,258	(6,558)	(49,305)	42,747
Net income (loss)	50,585	(14,733)	65,318	(55,374)	(101,064)	45,690
Net income attributable to noncontrolling interests	(12)	(27)	15	(12)	(12)	-
Net income (loss) attributable to common stockholders	\$ 50,573	\$ (14,760)	\$ 65,333	\$ (55,386)	\$ (101,076)	\$ 45,690
Diluted income (loss) per share						
	\$ 0.18	\$ (0.37)	\$ 0.55	\$ (1.40)	\$ (2.56)	\$ 1.16

For the three months ended June 30, 2015, consolidated revenues were flat compared to the same period in 2014. The lower land sales in our Houston MPCs and the commercial land sales totaling \$88.0 million at The Woodlands for the three months ended June 30, 2014 were substantially offset by condominium sales revenue from the Waiea and Anaha towers at Ward Village during the second quarter 2015, and increases to Operating Assets revenue as a result of

placing properties in service.

Consolidated revenues for the six months ended June 30, 2015 increased compared to the same period in 2014 primarily due to higher revenues in our Operating Assets and Strategic Developments segments which were offset by the decrease in Houston MPC land sales described above. Operating Assets segment revenue increased primarily due to higher minimum rents and tenant recoveries from both our retail and office properties. The growth related to our retail properties is primarily due to the openings in 2014 of Downtown Summerlin and The Outlet Collection at Riverwalk, higher rental rates and a bad debt recovery at Ward Village and openings in The Woodlands in the first quarter 2015. The increase in our office properties is due to our recent acquisition of six office buildings in Downtown Columbia during the fourth quarter 2014 and openings in the first quarter 2015 in The Woodlands. Strategic Developments segment revenue increased due to recognition of revenue related to our Waiea and Anaha Condominiums.

The Operating Assets segment REP EBT decreased primarily due to higher non-cash depreciation expense, a majority of which relates to assets placed into service and accelerated depreciation on certain assets at Ward Village. The properties placed into service in 2014 will stabilize over the next 12 to 24 months, but the full amount of their annual depreciation and amortization begins as soon as they are placed into service. Please refer to the Operating Assets Segment discussion for a more complete discussion of the impact of depreciation and amortization on our Operating Assets segment REP EBT.

General and administrative expenses for the three and six months ended June 30, 2015 increased compared to the same period in 2014 primarily due to increased headcount.

Corporate interest expense, net for the three and six months ended June 30, 2015 increased compared to the same period in 2014 due to the accrual of additional interest income on the GGP Tax Indemnity Receivable as a result of the Tax Court ruling in the second quarter of 2014. The GGP Tax Indemnity was settled in December 2014, therefore, we no longer record interest income related to the indemnity.

Corporate other income for the three and six months ended June 30, 2015 decreased compared to the same period in 2014

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primarily because the amounts for the prior periods included a pre-tax gain recognized for insurance proceeds received, related to South Street Seaport, of \$5.3 million and \$13.1 million, respectively.

The warrant liability gain for the three months ended June 30, 2015 resulted from a decrease in our stock price during this period, which decreased the value of the warrants. The warrant liability loss for the three months ended June 30, 2014 and the six months ended June 30, 2015 and 2014 was due to increases in our stock price during these periods, which increased the value of the warrants.

The decrease in the provision for income taxes for the three and six months ended June 30, 2015 compared to 2014 is attributable to decreases in income (loss) before taxes, excluding the impact of the changes in the warrant liability.

We have significant permanent differences, primarily from warrant liability gains and losses, interest income on the tax indemnity receivable (prior to 2015), and changes in valuation allowances that cause our effective tax rate to deviate greatly from statutory rates. The effective tax rates based upon actual operating results were 7.8% and (13.4%) for the three and six months ended June 30, 2015 compared to 149.6% and (95.2)% for the three and six months ended June 30, 2014. The changes in the tax rate were primarily attributable to the changes in the warrant liability, valuation allowance and unrecognized tax benefits as well as other permanent items. If changes in the warrant liability, valuation allowance, unrecognized tax benefits and other material discrete adjustments to deferred tax liabilities were excluded from the effective tax rate computation, the effective tax rates would have been 34.9% and 34.7% for the three and six months ended June 30, 2015, respectively, compared to 35.9% and 35.0% for the three and six months ended June 30, 2014.

The improvement in net income (loss) attributable to common stockholders and decrease in net (loss) attributable to common stockholders for the three and six months ended June 30, 2015 compared to the same periods in 2014, respectively, is primarily caused by the following:

Increases in earnings

- A warrant liability gain in the three months ended June 30, 2015 and a lower warrant liability loss in the six months ended June 30, 2015, due to changes in our stock price; and
- Lower income taxes due to lower income (loss) before taxes, excluding the warrant liability loss,

Reductions in earnings

- Higher depreciation expense from assets placed in service during 2014 and accelerated depreciation of certain Ward Village assets due to their expected impending demolition to make way for development;
- Lower other income in 2015 due to the receipt of Superstorm Sandy insurance proceeds in 2014; and
- Higher corporate interest expense, net due to higher mortgage indebtedness and an accrual of additional interest income on the GGP Tax Indemnity Receivable as a result of the Tax Court ruling in the second quarter 2014.

Please refer to the individual segment operations sections that follow for explanations of the segment performance.

Segment Operations

Please refer to Note 15 - Segments for additional information including reconciliations of our segment basis results to generally accepted accounting principles (“GAAP”) basis results.

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Master Planned Communities Segment

Master Planned Communities Revenues and Expenses(*)

For the three months ended June 30, 2015 and 2014

(In thousands)

Bridgeland		Conroe		Maryland		Summerlin		The	Total
2015	2014	2015	2014	2015	2014	2015	2014	Woodlands	MPC