

LGI Homes, Inc.
Form 10-K
February 26, 2019

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

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the fiscal year ended December 31, 2018
Commission file number 001-36126

LGI
HOMES,
INC.
(Exact
name of
registrant
as
specified
in its
charter)

Delaware 46-3088013
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

1450 Lake Robbins Drive, Suite 430, The Woodlands, Texas 77380
(Address of principal executive offices) (Zip code)
(281) 362-8998
(Registrant's Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(b) of the Act:
Title of each class Name of each exchange on which registered
Common Stock (\$0.01 par value) NASDAQ

Securities registered pursuant to Section 12(g) of the Act: None
Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes No

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

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

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Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer Accelerated filer

Non-accelerated filer Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of June 29, 2018, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was approximately \$1.1 billion based on the closing price of such stock on such date as reported on the NASDAQ Stock Market. As of February 22, 2019, there were 22,707,385 shares of the registrant's common stock, par value \$.01 per share, issued and outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions from the registrant's definitive Proxy Statement for the 2019 Annual Meeting of Stockholders are incorporated herein by reference (to the extent indicated) into Part III.

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PART I

ITEM 1. BUSINESS

General

We are engaged in the design, construction, and sale of new homes in markets in Texas, Arizona, Florida, Georgia, New Mexico, South Carolina, North Carolina, Colorado, Washington, Tennessee, Minnesota, Oklahoma, Alabama, California, Oregon, and Nevada. Our management team has been in the residential land development business since the mid-1990s. Since commencing home building operations in 2003, we have constructed and closed over 28,000 homes. During the year ended December 31, 2018, we had 6,512 home closings, compared to 5,845 home closings in 2017.

LGI Homes, Inc. is a Delaware corporation incorporated on July 9, 2013. Our principal executive offices are located at 1450 Lake Robbins Drive, Suite 430, The Woodlands, Texas 77380, and our telephone number is (281) 362-8998. Information on or linked to our website is not incorporated by reference into this Annual Report on Form 10-K unless expressly noted.

Unless otherwise indicated or the context requires, “LGI,” the “Company,” “we,” “our” and “us” refer collectively to LGI Homes, Inc. and its subsidiaries.

Business Opportunities

Since our initial public offering in November 2013, we have grown substantially by expanding our operations from nine markets in four states to 27 markets in 17 states. We believe there is an opportunity to continue to grow in our existing markets. Given our knowledge of and proven success in these markets, as well as the favorable demographic and economic trends forecasted for these markets, we expect to continue to grow in our current markets.

We intend to continue to expand into new markets where we identify opportunities to build homes and develop communities that meet our profit and return objectives. One of the keys to our successful geographic expansion is our operating model which enables us to enter new markets efficiently and effectively. During 2019, we expect to open new communities and have homes for sale in additional markets, including Columbia, South Carolina, Charleston, South Carolina, Richmond, Virginia, Riverside, California, and Sarasota, Florida.

We see opportunities to develop properties with multiple product lines and within the same communities which we believe will enable us to grow our business by increasing the number of price points in some of our existing markets. Our current product offerings include entry-level homes, including both detached homes and townhomes, and move-up homes, which are sold under our LGI Homes brand, and our luxury series homes, which are sold under our Terrata Homes brand. Wholesale home closings during 2018 and 2017 represented 466 and 201 homes, respectively. At December 31, 2018, we had 83 active communities with our LGI Homes brand and five with our Terrata Homes brand.

Our Terrata Homes brand allows us to leverage our systems and process approach, including our customer centric sales system, to deliver move-in ready homes with standardized features. During 2018, we closed 118 Terrata Homes, which had an average sales price of \$395,000, compared to 108 Terrata Homes, which had an average sales price of \$409,000, in 2017.

Our townhome product enables us to keep our entry-level price point within reach of more new homebuyers. We believe that our townhome product helps to counter rising land and home costs, and support our expansion into densely populated markets.

Similarly, we believe our wholesale home closings provide opportunities for us to leverage our systems and processes to meet the needs of companies looking to acquire multiple homes for rental purposes, primarily through bulk sales agreements.

We expect to continue to pursue a flexible land acquisition strategy of purchasing or optioning finished lots, if they can be acquired at attractive prices, or purchasing raw land for residential development. We generally target land acquisitions that are further away from urban centers than many other suburban communities but have access to major thoroughfares, retail districts and centers of business. These target areas that are further away from urban centers generally result in a better value for the homeowner through either lower price points or larger lot sizes. We consider development opportunities that meet our profit and return objectives, including opportunities which may involve the sale of home sites as a part of the product mix. We will continue to focus primarily on entry-level home buyers. We

expect our home closings in communities with our luxury series will be less than 5% of our annual home closings during 2019 and that our wholesale closings will be approximately 5% of our annual home closings during 2019.

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Sales and Marketing

We utilize a well-defined sales and marketing approach to identify leads for our communities and to educate potential buyers on the process and benefits of homeownership. For many of our communities, our marketing efforts are focused on converting renters of apartments and single-family homes into homeowners.

We use extensive print and digital advertising to attract potential homebuyers. We employ various marketing methods such as direct mail, social media and interactive online media as well as directional signage and billboards to attract and drive potential homebuyers to our information centers.

Our advertising methods are extensive and have proven to be effective in placing potential homebuyers in front of our trained sales professionals. These methods have proven to be effective in reaching our target market and communicating our core message of value and dream fulfillment.

With respect to our communities with higher price points or that include the sale of home sites, our sales and marketing approaches are tailored to the potential purchasers of such homes and home sites and include more involvement by real estate agents and brokers.

Across all price points, our marketing strategy calls for a balanced approach of corporate support and local expertise to attract potential homebuyers in a focused, efficient and cost-effective manner. Our proprietary customer relationship management system provides our management team with tools to continually monitor and measure the performance level of every sales professional through each phase of the sales process. Utilization of these tools allows us to assess the cost effectiveness of a particular advertising campaign and marketing medium as well as the strengths and weaknesses of every member of our sales team.

Our marketing efforts are generally designed to encourage the prospective homebuyer to call our information centers to schedule an appointment and our primary objective is to establish direct communication between the prospective homebuyer and the salesperson. Our professional salespeople are well-trained to determine specific needs and wants of the potential homebuyer and to provide the potential homebuyer with all information required to make a buying decision.

Our information centers are open approximately 12 hours per day, 359 days per year, and generally staffed by two to five sales professionals and supported by an independent on-site loan officer. Our commission-based sales professionals provide potential homebuyers with a comprehensive and thorough understanding of the steps required to achieve homeownership. Throughout the sales process, our sales professionals learn about the current housing situation of the potential homebuyers and seek to understand their individual needs while also educating them on the value we provide through superior quality and affordable prices.

We provide information regarding floor plans and pricing, credit and income qualifications and conduct tours of our homes based on the potential homebuyer's budget. In addition, we provide each potential homebuyer with a comprehensive introduction to the community and the surrounding area, providing them with detailed information regarding utilities, schools, homeowners association dues and restrictions, local entertainment and nearby dining and shopping options. We provide our potential homebuyers with a clear understanding of who we are by sharing our history, vision and values. As a result of our transparent approach, potential homebuyers receive all this information before making a buying decision, which we believe eliminates confusion during the home buying process and sets clear expectations. In addition, the potential home buyers benefit from the availability of move-in ready homes by seeing the completed or near-completed home that they will own.

Recruitment, Training and Development

We focus on identifying and attracting the best talent and providing them with world-class training and continuous development. We directly invest in our sales professionals by conducting an intensive 100-day introductory training program consisting of 30 days of initial in-depth, in-house education about our time-proven selling strategies, which includes a two-week training program at our headquarters, and an additional 70 days of secondary training at the local division. Our continued commitment to our sales personnel is reflected in the ongoing weekly training sessions held in each of our information centers coupled with quarterly regional training events. We also work closely with our subcontractors and construction managers, training them using a comprehensive construction manual that outlines the most efficient way to build an LGI home. Many of our subcontractors have worked on our homes since we commenced homebuilding operations in 2003, and therefore, are familiar with our business model.

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Homebuilding Operations

Our homebuilding operations are organized and managed by seven divisions: West, Northwest, Central, Midwest, Florida, Southeast and Mid-Atlantic.

West	Northwest	Central	Midwest	Florida	Southeast	Mid-Atlantic
Phoenix, AZ	Seattle, WA	Houston, TX	Minneapolis, MN	Tampa, FL	Atlanta, GA	Martinsburg, WV
Tucson, AZ	Portland, OR	Dallas/Ft. Worth, TX		Orlando, FL	Charlotte, NC/SC	
Albuquerque, NM	Denver, CO	San Antonio, TX		Fort Myers, FL	Nashville, TN	
Sacramento, CA	Colorado Springs, CO	Austin, TX		Jacksonville, FL	Raleigh, NC	
Las Vegas, NV		Oklahoma City, OK			Wilmington, NC	
					Winston-Salem, NC	
					Birmingham, AL	

Beginning in the fourth quarter of 2018, we changed from six reportable segments to five reportable segments: Central, Northwest, Southeast, Florida, and West. These segments reflect the way the Company evaluates its business performance and manages its operations. Additional information on our operating segments and product information is contained in Note 16 “Segment Information” to our consolidated financial statements included in Part II, Item 8 of this Annual Report on Form 10-K.

Our even-flow, or continuous, construction methodology enables us to build and maintain an inventory of move-in ready homes that are available for immediate sale. We offer a set number of floor plans in each community with standardized features that commonly include upgrades such as granite countertops, appliances and ceramic tile flooring. Our homes are designed to meet the preferences of our target market of potential homebuyers and enable cost efficient and effective construction processes. We have developed a collection of home designs, which can be modified for local conditions and market preferences, and implemented across multiple communities to maximize efficiency. We maintained an average home completion time of approximately 60 to 85 days during 2018; the homes closed during 2018 ranged from 1,000 to 4,100 square feet with prices ranging from the \$140,000’s to the \$600,000’s. We expect to continue to utilize our even flow construction methodology in communities with homes at all of our price points and will maintain our focus on marketing complete or move-in ready homes with standardized features. We employ experienced construction management professionals to perform the tasks of general contractors for home construction in each of our communities. Our employees provide the purchasing, construction management and quality assurance for the homes we build, while third-party subcontractors provide the material and labor components of our homes. In each of our markets, we employ construction managers with local market knowledge and expertise. Additionally, our construction managers monitor our compliance with zoning and other regulations, production schedules, and quality standards for our projects.

We endeavor to obtain favorable pricing from subcontractors through long-term relationships and consistent workflow. As we have expanded into new markets outside of Texas, the employees that we have hired in those markets have brought long-term relationships with several subcontracting firms. We have expanded upon existing relationships with subcontracting firms also located in Texas. A number of our trade partners have subcontracted on our projects since we commenced homebuilding operations in 2003. We purchase some components and materials centrally to leverage our purchasing power to achieve volume discounts, a practice that often reduces costs and ensures timely deliveries. We typically do not store significant inventories of construction materials, except for work in progress materials for homes under construction. Consistency of our trade partners is an integral part of our homebuilding operations that also leads us to reduced warranty costs. We believe in building long lasting relationships with our trade partners in order to provide consistent, quality and timely deliveries across our markets. We also work closely with our construction managers and subcontractors and train them using a comprehensive construction manual

that outlines the most efficient way to build an LGI home.

Throughout our homebuilding operations, we utilize a paperless purchase order system to conduct business with our subcontractors and suppliers. Our master build schedule allows our trade partners to receive their specific task from our electronic system and plan several weeks in advance before starting their work. This means of communication allows our subcontractors to schedule their crews efficiently, thereby allowing for better pricing and better quality of work. Typically, our contractors are paid every week, which contributes to the strength of our business relationships with them.

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Land Acquisition Policies and Development

We continue to be an active and opportunistic acquirer of land for residential development in our markets. We source land from a wide range of landowners, brokers, lenders, builders and other land development companies. We generally acquire finished lots and raw land in affordable locations that are further away from urban centers than many other suburban communities but have access to major thoroughfares, retail districts and centers of business. We conduct thorough due diligence on each of our potential land acquisitions, and we look at numerous opportunities before finding one that meets our requirements. We test the market and speak with potential homebuyers before committing to purchase land. We also maintain a pipeline of desirable land positions for replacement communities and new communities. We increased our active communities to 88 as of December 31, 2018 from 78 as of December 31, 2017. We also increased our lot inventory to 51,442 owned or controlled lots as of December 31, 2018 from 39,709 owned or controlled lots as of December 31, 2017.

Our allocation of capital for land investment is performed at the corporate level with a disciplined approach to portfolio management. Our Acquisitions Committee meets periodically and consists of our Chief Executive Officer, Chief Financial Officer, and Executive Vice President of Acquisitions. Annually, our divisions prepare a strategic plan for their respective geographic areas. Supply and demand are analyzed to ensure land investment is targeted appropriately. The long-term plan is compared on an ongoing basis to our experience in the marketplace and is then adjusted to the extent necessary.

We have also purchased larger tracts of land across our markets which will provide us with more opportunities to build homes with multiple price points in our communities. We believe that our land development expertise will allow us to meet our growth and profit objectives with respect to opportunities in which we are the developer. Similar to our home building operations, our personnel oversee the contractors who perform the development work. Our land development projects may include the sale of home sites or commercial property as a part of the project.

We have strong relationships with the land brokerage community in many of our markets. We believe that in the brokerage community, we have a reputation for knowing our business, having the capital to close deals, and making accurate and timely decisions that benefit both the buyer and seller. For these reasons, we believe that brokers routinely notify us when desirable tracts of land are available for purchase.

In our land acquisition process, projects of interest are evaluated at the division level using an extensive due diligence checklist which includes assessing the permitting and regulatory requirements, environmental considerations, local market conditions, and anticipated floor plans, pricing, and financial returns. We also determine the number of residents in the market and rental households that are within driving distance to the proposed project and, in many cases, conduct test marketing which includes mailings to prospective homebuyers to get their feedback on our potential land acquisition. By testing the market before entering it and acquiring land in it, we are able to assess the level of interest in the location and amenities, determine the cost of rent in the area, and assess the size of the market opportunity. The amount of information that we are able to ascertain about potential home buyers, including renters, allows us to better identify the opportunity to sell move-in ready homes.

The table below shows (i) home closings by reportable segment for the year ended December 31, 2018 and (ii) our owned or controlled lots by reportable segment as of December 31, 2018.

Reportable Segment	Year	As of December 31, 2018		
	Ended December 31, 2018	Home Closings	Owned (1)	Controlled Total
Central	2,937	15,204	7,026	22,230
Northwest	760	1,856	1,786	3,642
Southeast	1,324	7,244	10,556	17,800
Florida	864	2,266	1,205	3,471
West	627	2,052	2,247	4,299
Total	6,512	28,622	22,820	51,442

(1) Of the 28,622 owned lots as of December 31, 2018, 17,381 were raw/under development lots and 11,241 were finished lots.

Homes in Inventory

When entering a new community, we build a sufficient number of move-in ready homes to meet our budgets. We base future home starts on closings. As homes are closed, we start more homes to maintain our inventory. As of December 31, 2018, we had a total of 1,942 completed homes, including information centers, and 987 homes in progress.

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The following is a summary of our homes in inventory by reportable segment as of December 31, 2018 (dollar values in thousands):

Reportable Segment	Homes in Inventory (1)	Inventory Value (1)
Central	1,160	\$ 179,820
Northwest	354	84,234
Southeast	551	88,442
Florida	333	49,535
West	431	68,644
Total	2,829	\$ 470,675

(1) Includes homes in progress and completed homes; excludes information centers.

Backlog

See discussion included in “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Backlog.”

Raw Materials and Labor

When constructing homes, we use various materials and components. We generally contract for our materials and labor at a fixed price for the anticipated construction period of our homes. This allows us to mitigate the risks associated with increases in building materials and labor costs between the time construction begins on a home and the time it is closed. Typically, the raw materials and most of the components used in our business are readily available in the United States. In addition, the majority of our raw materials is supplied to us by our subcontractors, and is included in the price of our contract with such contractors. Most of the raw materials necessary for our subcontractors are standard items carried by major suppliers. Substantially all of our construction work is done by third-party subcontractors, most of whom are non-unionized. We continue to monitor the supply markets to achieve the best prices available. Typically, the price changes that most significantly influence our operations are price increases in labor, commodities, and lumber.

Seasonality

The homebuilding industry generally exhibits seasonality. We have historically experienced, and in the future expect to continue to experience, variability in our results on a monthly and quarterly basis. See discussion included in “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Seasonality.”

Government Regulation and Environmental Matters

We are subject to numerous local, state, federal and other statutes, ordinances, rules and regulations concerning zoning, development, building design, construction and similar matters which impose zoning and density requirements, the result of which is to limit the number of homes or mandate the type of structure that can be built, within the boundaries of a particular area. Projects that are not entitled may be subjected to periodic delays, changes in use, less intensive development or elimination of development in certain specific areas due to government regulations. We may also be subject to periodic delays or may be precluded entirely from developing in certain communities due to building moratoriums or “slow-growth” or “no-growth” initiatives that could be implemented in the future. Local governments also have broad discretion regarding the imposition of development fees for projects in their jurisdiction. Projects for which we have received land use and development entitlements or approvals may still require a variety of other governmental approvals and permits during the development process and can also be impacted adversely by unforeseen health, safety and welfare issues, which can further delay these projects or prevent their development. We are also subject to a variety of local, state, federal and other statutes, ordinances, rules and regulations concerning the environment. The particular environmental laws which apply to any given homebuilding site vary according to multiple factors, including the site’s location, its environmental conditions and the present and former uses of the site, as well as adjoining properties. Environmental laws and conditions may result in delays, may cause us to incur substantial compliance and other costs, and can prohibit or severely restrict homebuilding activity in environmentally sensitive regions or areas. In addition, in those cases where an endangered or threatened species is involved, environmental rules and regulations can result in the restriction or elimination of development in identified

environmentally sensitive areas. From time to time, the United States Environmental Protection Agency (the “EPA”) and similar federal or state agencies review homebuilders’ compliance with environmental laws and may levy fines and penalties for failure to strictly comply with applicable environmental laws or impose additional requirements for future compliance as a result of past failures. Any such actions taken with respect to us may increase our costs. Further, we expect

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that increasingly stringent requirements may be imposed on homebuilders in the future. Environmental regulations can also have an adverse impact on the availability and price of certain raw materials such as lumber.

Under various environmental laws, current or former owners of real estate, as well as certain other categories of parties, may be required to investigate and clean up hazardous or toxic substances or petroleum product releases, and may be held liable to a governmental entity or to third parties for related damages, including for bodily injury, and for investigation and clean-up costs incurred by such parties in connection with the contamination. A mitigation system may be installed during the construction of a home if a cleanup does not remove all contaminants of concern or to address a naturally occurring condition such as methane. Some homebuyers may not want to purchase a home with a mitigation system.

Competition

The U.S. homebuilding industry is highly competitive. We compete in each of our markets with numerous other national, regional and local homebuilders for homebuyers, desirable properties, raw materials and skilled labor. We also compete with sales of existing homes and with the rental housing market. Our homes compete on the basis of quality, price, design, mortgage financing terms and location. There has been some consolidation among national homebuilders in the United States, and we expect that this trend may continue.

Employees

As of December 31, 2018, we employed 857 people, of whom 98 were located at our corporate headquarters, 509 were on-site sales and support personnel, and 250 were involved with construction. None of our employees are covered by collective bargaining agreements. We believe we have good relations with our employees.

Available Information

We make available, as soon as reasonably practicable, on our website, www.lgihomes.com, all of our reports required to be filed with the Securities and Exchange Commission (“SEC”). These reports can be found on the “Investor Relations” page of our website under “SEC Filings” and include our annual and quarterly reports on Form 10-K and 10-Q (including related filings in XBRL format), current reports on Form 8-K, beneficial ownership reports on Forms 3, 4, and 5, proxy statements and amendments to such reports. Our SEC filings are also available to the public on the SEC’s website at www.sec.gov. In addition to our SEC filings, our corporate governance documents, including our Corporate Governance Guidelines and Code of Business Conduct and Ethics, are available on the “Investor Relations” page of our website under “Corporate Governance” at <https://investor.lgihomes.com/corporate-governance>. Our stockholders may also obtain these documents in paper format free of charge upon request made to our Investor Relations department.

Executive Officers

The following table sets forth information regarding our executive officers as of February 26, 2019:

Name	Age	Position
Eric Lipar	48	Chief Executive Officer and Chairman of the Board
Michael Snider	47	President and Chief Operating Officer
Charles Merdian	49	Chief Financial Officer and Treasurer
Jack Lipar	50	Executive Vice President of Acquisitions
Rachel Eaton	37	Chief Marketing Officer
Scott Garber	47	General Counsel and Corporate Secretary

Eric Lipar. Mr. Lipar is our Chief Executive Officer and serves as Chairman of our Board of Directors. He has served as our Chief Executive Officer since 2009, as a director since June 2013 and as Chairman of the Board since July 2013. Previously, Mr. Lipar served as our President from 2003 until 2009. Mr. Lipar has been in the residential land development business since the mid-1990s and is one of our founders. He has overseen land acquisition, development and the sales of over 28,000 homes since our inception. Mr. Lipar currently serves on the Residential Neighborhood Development Council for the Urban Land Institute and is a Policy Advisor Board Member for the Harvard Joint Center of Housing Studies.

Michael Snider. Mr. Snider has served as our President since 2009 and our Chief Operating Officer since July 2013. He oversees all aspects of our sales, construction, and product development. Prior to serving as our President, Mr. Snider was Executive Vice President of Homebuilding (2005-2009) and in the role of Homebuilding Manager (2004). Before joining the Company in 2004, Mr. Snider was a Project Manager for Tadian Homes, a homebuilder based in Troy, Michigan.

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Charles Merdian. Mr. Merdian has served as our Chief Financial Officer and Treasurer since 2013, and served as our Secretary from 2013 to 2016. Prior to becoming our Chief Financial Officer in 2010, Mr. Merdian was our Controller from 2004 through 2010. Prior to joining us in 2004, Mr. Merdian served as Accounting and Finance Manager for The Woodlands Operating Company where he specialized in accounting and financial analysis of real estate ventures, focusing primarily on residential and commercial developments. Prior to The Woodlands Operating Company, Mr. Merdian served as an accounting manager working at the Williamson-Dickie Manufacturing Co. and as a senior auditor for Coopers & Lybrand, LLP. Mr. Merdian has worked in residential real estate and homebuilding finance since 1998. Mr. Merdian is a Certified Public Accountant and is a member of the Texas Society of Certified Public Accountants.

Jack Lipar. Mr. Lipar has served as our Executive Vice President of Acquisitions since March 2013. He previously served as Vice President of Acquisitions from December 2010 through February 2013, and Acquisitions Manager from 2006 to December 2010. Mr. Lipar oversees land acquisitions and development for the Company. Prior to joining us, Mr. Lipar worked at HP Pelzer, an auto parts manufacturing company based in Germany, as the Vice President of Purchasing and Director of Operations. Mr. Lipar was also the General Manager and a member of the Board of Directors at Alliance Interiors, an affiliate of HP Pelzer. Prior to HP Pelzer, Mr. Lipar was a worldwide Purchasing Manager for Cooper Standard, one of the world's leading manufacturers of automotive parts.

Rachel Eaton. Ms. Eaton serves as our Chief Marketing Officer and is responsible for the overall growth and direction of our marketing initiatives, brand image, and social media. Prior to becoming our Chief Marketing Officer in June 2013, Ms. Eaton served as our Vice President of Marketing and Administration from May 2012 through May 2013 and Director of Marketing & Special Events from 2007 to May 2012. Ms. Eaton joined the Company in 2003.

Scott Garber. Mr. Garber has served as our General Counsel and Corporate Secretary since April 2018. His responsibilities include all company legal matters, as well as corporate governance and risk management. Prior to joining the Company, Mr. Garber served as Assistant General Counsel at Chevron Phillips Chemical Company (CPChem), where he was responsible for major company transactions (both domestic and international) and corporate governance of its Qatar-based joint ventures, and managed commercial legal matters for various company product lines and divisions. Prior to joining CPChem, Mr. Garber served as Associate General Counsel for United Airlines (formerly Continental Airlines), then the world's largest airline, where he was responsible for its litigation, antitrust and intellectual property matters. Mr. Garber previously worked at Howrey Simon Arnold & White, a major international law firm, where he specialized in all aspects of intellectual property law. Mr. Garber is a member of the State Bar of Texas and is also admitted to practice before the U.S. Patent & Trademark Office. Mr. Garber is also a member of the Board of Directors of Archway Insurance, Ltd, a captive insurance company.

Board of Directors of LGI Homes, Inc.

Mr. Eric Lipar - Chief Executive Officer of LGI Homes, Inc. and serves as Chairman of our Board of Directors.

Ms. Laura Miller - Senior Vice President and Global Chief Information Officer of InterContinental Hotels Group PLC, a multinational hospitality company.

Mr. Bryan Sansbury - Chief Operating Officer and a founding partner of AEGIS Energy Risk, LLC. and serves as our Lead Independent Director.

Mr. Ryan Edone - Chief Financial Officer of Petroleum Wholesale L.P., a distributor of branded and wholesale motor fuel products and operator of retail convenience stores/travel centers.

Mr. Duncan Gage - Retired. Former President and Chief Executive Officer of Giant Cement Holdings, Inc. and currently manages his personal investments.

Mr. Steven Smith - Shareholder of Baker Donelson, a law firm.

Mr. Robert Vahradian - Senior Managing Director of GTIS Partners, LP, a global real estate investment firm.

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ITEM 1A. RISK FACTORS

Discussion of our business and operations included in this Annual Report on Form 10-K should be read together with the risk factors set forth below. They describe various risks and uncertainties we are or may become subject to, many of which are difficult to predict or beyond our control. These risks and uncertainties, together with other factors described elsewhere in this report, have the potential to affect our business, financial condition, results of operations, cash flows, strategies or prospects in a material and adverse manner.

Risks Related to Our Business

Tightening of mortgage lending standards and mortgage financing requirements and rising interest rates could adversely affect the availability of mortgage loans for potential purchasers of our homes and thereby reduce our sales. Almost all purchasers of our homes finance their acquisition through lenders that provide mortgage financing. According to the Federal Home Loan Mortgage Corporation (“Freddie Mac”), the 30-year average mortgage rate was approximately 4.46% in January 2019 and is expected to increase during 2019. If mortgage interest rates increase, the ability of prospective homebuyers to finance home purchases may be adversely affected, and, as a result, our operating results may be significantly negatively impacted. Our homebuilding activities are dependent upon the availability of mortgage financing to homebuyers. The availability of mortgage financing is expected to be impacted by continued regulatory changes and risk appetite of lenders. The financial documentation, down payments amounts and income to debt ratios requirements are subject to change and could become more restrictive. First-time homebuyers are generally more affected by the availability of mortgage financing than other potential homebuyers. These homebuyers are a key source of demand for our new homes. A limited availability of home mortgage financing may adversely affect the volume and sales price of our home sales.

The federal government has a significant role in supporting mortgage lending through its conservatorship of Federal National Mortgage Association (“Fannie Mae”) and Freddie Mac, both of which purchase or insure mortgage loans and mortgage loan-backed securities, and its insurance of mortgage loans through or in connection with the Federal Housing Administration (“FHA”), the Veterans Administration (“VA”) and the U.S. Department of Agriculture (“USDA”). FHA and USDA backing of mortgage loans has been particularly important to the mortgage finance industry and to our business. If either the FHA or USDA raised their down payment requirements or lowered maximum loan amounts, our business could be materially affected. Increased lending volume and losses insured by the FHA have resulted in a reduction of the FHA insurance fund. The USDA rural development program provides for zero down payment and 100% financing for homebuyers in qualifying areas. If the USDA program was discontinued or if funding was decreased, then our business could be adversely affected. In addition, if the USDA changed its determination of areas that are eligible to qualify for the program, it could have an adverse effect on our business. In addition, changes in governmental regulation with respect to mortgage lenders could adversely affect demand for housing.

The availability and affordability of mortgage loans, including interest rates for such loans, could also be adversely affected by a scaling back or termination of the federal government’s mortgage loan-related programs or policies. Because Fannie Mae-, Freddie Mac-, FHA-, USDA- and VA-backed mortgage loans have been an important factor in marketing and selling many of our homes, any limitations or restrictions in the availability of, or higher consumer costs for, such government-backed financing could reduce our business, prospects, liquidity, and financial condition and results of operations could be materially and adversely affected. The elimination or curtailment of state bonds to assist homebuyers could materially and adversely affect our business, prospects, liquidity, financial condition and results of operations.

In addition, the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) established several new standards and requirements relating to the origination, securitizing and servicing of residential consumer mortgage loans. These and other laws and regulations could further restrict the availability and affordability of mortgage loans, which could adversely affect our home sales, financial condition and results of operations.

The long-term sustainability and growth in our home closings depends in part upon our ability to acquire finished lots and land parcels suitable for residential homebuilding at reasonable prices.

The long-term sustainability of our operations as well as future growth depends in large part on the price at which we are able to obtain suitable finished lots and land parcels for development to support our homebuilding operation. Our ability to acquire finished lots and land parcels for new single-family homes and other projects may be adversely

affected by changes in the general availability of land parcels, the willingness of land sellers to sell land parcels at reasonable prices, competition for available land parcels, availability of financing to acquire land parcels, zoning, regulations that limit housing density, the ability to obtain building permits, environmental requirements and other market conditions and regulatory requirements. If suitable lots or land at reasonable prices become less available, the number of homes we may be able to build and sell could be reduced, and the cost of land could be increased substantially, which could adversely impact us. As competition for suitable land increases, the cost of undeveloped lots and the cost of developing owned land could also rise and the availability of suitable land at acceptable prices may decline, which could adversely impact us. The availability of suitable land assets could also affect the success of our land acquisition

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strategy, which may impact our ability to maintain or increase the number of our active communities, as well as to sustain and grow our revenue and margins, and achieve or maintain profitability. Additionally, developing undeveloped land is capital intensive and time consuming and we may develop land based upon forecasts and assumptions that prove to be inaccurate, resulting in projects that are not economically viable.

Risks associated with our land and lot inventories could adversely affect our business or financial results.

Risks inherent in controlling, purchasing, holding and developing land for new home construction are substantial. The risks inherent in purchasing and developing land parcels increase as consumer demand for housing decreases and the holding period increases. As a result, we may buy and develop land parcels on which homes cannot be profitably built and sold. In certain circumstances, a grant of entitlements or development agreement with respect to a particular parcel of land may include restrictions on the transfer of such entitlements to a buyer of such land, which would negatively impact the price of such entitled land by restricting our ability to sell it for its full entitled value. In addition, inventory carrying costs can be significant and can result in reduced margins or losses in a poorly performing community or market. Developing land and constructing homes takes a significant amount of time and requires a substantial cash investment. Land development is a key part of our operations and we develop land in all of our markets. The time and investment required for development may adversely impact our business. We have substantial real estate inventories which regularly remain on our balance sheet for significant periods of time, during which time we are exposed to the risk of adverse market developments, prior to their sale. Our business model is based on building homes before a sales contract is executed and a customer deposit is received. Because interest and other expenses are capitalized only during construction, we recognize interest and maintenance expense on unsold completed homes in inventory. As of December 31, 2018, we had 1,942 completed homes in inventory and 987 homes in progress in inventory. In the event there is a downturn in home sales in our markets, our inventory of completed homes could increase, leading to additional financing costs and lower margins, which could have a material adverse effect on our financial results and operations. In the event of significant changes in economic or market conditions, we may have to sell homes at significantly lower margins or at a loss, if we are able to sell them at all. Additionally, deteriorating market conditions could cause us to record significant inventory impairment charges. The recording of a significant inventory impairment could negatively affect our reported earnings per share and negatively impact the market perception of our business.

Because real estate investments are relatively illiquid, our ability to promptly sell one or more properties for reasonable prices in response to changing economic, financial and investment conditions may be limited and we may be forced to hold non-income producing properties for extended periods of time.

Real estate investments are relatively difficult to sell quickly. As a result, our ability to promptly sell one or more properties in response to changing economic, financial and investment conditions is limited and we may be forced to hold non-income producing assets for an extended period of time or sell homes or land at a loss either of which may require us to record impairment charges. We cannot predict whether we will be able to sell any property for the price or on the terms that we set or whether any price or other terms offered by a prospective purchaser would be acceptable to us. We also cannot predict the length of time needed to find a willing purchaser and to close the sale of a property. Labor and raw material shortages and price fluctuations could delay or increase the cost of home construction, which could materially and adversely affect us.

The residential construction industry experiences labor and raw material shortages from time to time, including shortages in qualified tradespeople, and supplies of insulation, drywall, cement, steel and lumber. These labor and raw material shortages can be more severe during periods of strong demand for housing or during periods following natural disasters that have a significant impact on existing residential and commercial structures. Our markets may exhibit a reduced level of skilled labor relative to increased homebuilding demand in these markets. It is uncertain whether these shortages will continue as is, improve or worsen. Labor and raw material shortages and any resulting price increases could cause delays in and increase our costs of home construction, which in turn could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

Our business and results of operations are dependent on the availability, skill and performance of subcontractors.

We engage subcontractors to perform the construction of our homes, and, in many cases, to select and obtain the raw materials. Accordingly, the timing and quality of our construction depend on the availability and skill of our

subcontractors. While we anticipate being able to obtain sufficient materials and reliable subcontractors and believe that our relationships with subcontractors are good, we do not have long-term contractual commitments with any subcontractors, and we can provide no assurance that skilled subcontractors will continue to be available at reasonable rates and in our markets. The inability to contract with skilled subcontractors at reasonable rates on a timely basis could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations. Despite our quality control efforts, we may discover that our subcontractors have engaged in improper construction practices or have installed defective materials in our homes. When we discover these issues, we utilize our subcontractors to repair the

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homes in accordance with our new home warranty and as required by law. The adverse costs of satisfying our warranty and other legal obligations in these instances may be significant and we may be unable to recover the costs of warranty-related repairs from subcontractors, suppliers and insurers, which could have a material impact on our business, prospects, liquidity, financial condition and results of operations. We may also suffer reputational damage from the actions of subcontractors, which are beyond our control.

We could be adversely affected by efforts to impose joint employer liability on us for labor law violations committed by our subcontractors.

Our homes are constructed by employees of subcontractors and other parties. We do not have the ability to control what these parties pay their employees or the rules they impose on their employees. However, various governmental agencies have taken actions to hold parties like us responsible for violations of wage and hour laws and other labor laws by subcontractors. Governmental rulings that hold us responsible for labor practices by our subcontractors could create substantial exposures for us under our subcontractor relationships, which could have a material impact on our business, prospects, liquidity, financial condition and results of operations.

Any limitation on, or reduction or elimination of, tax benefits associated with homeownership would have an adverse effect upon the demand for homes, which could be material to our business.

Changes in federal and state income tax laws, including the federal tax legislation, P.L. 115-97, informally known as the Tax Cuts and Jobs Act (the "Tax Act"), may affect demand for new homes. Prior to January 1, 2018, tax laws generally permitted significant expenses associated with homeownership, primarily mortgage interest expense and real estate taxes, to be deducted for the purpose of calculating an individual's federal and, in many cases, state taxable income. The Tax Act significantly limited the ability to deduct mortgage interest expense and real estate taxes for federal income tax purposes. While the recent tax changes are not currently expected to have a significant effect on our home sales, the federal government or a state government may change or further change its income tax laws by further eliminating, limiting or substantially reducing these income tax benefits without offsetting provisions, which may increase the after-tax cost of owning a new home for many of our potential homebuyers. Any such future changes may have an adverse effect on the homebuilding industry in general. For example, the loss or reduction of homeowner tax deductions could decrease the demand for new homes. Any such future changes could have a material impact on our business, prospects, liquidity, financial condition and results of operations.

The recent growth in the housing market may not continue at the same rate, and any decline in the growth rate in our served housing markets or for the homebuilding industry may materially and adversely affect our business and financial condition.

Although the housing markets in the geographic areas in which we operate are generally stronger than they have been in recent years, we cannot predict whether and to what extent this will continue, particularly if interest rates for mortgage loans, land costs, and construction costs continue to rise. Other factors which might impact growth in the homebuilding industry include uncertainty in domestic and international financial, credit and consumer lending markets amid slow growth or recessionary conditions in various regions or industries around the world; tight lending standards and practices for mortgage loans that limit consumers' ability to qualify for mortgage financing to purchase a home, including increased minimum credit score requirements, credit risk/mortgage loan insurance premiums and/or other fees and required down payment amounts, higher home prices, more conservative appraisals, changing consumer preferences, higher loan-to-value ratios and extensive buyer income and asset documentation requirements, changes to mortgage regulations, slower rates of population growth or population decline in our markets, or Federal Reserve policy changes. Given these factors, we can provide no assurance that present housing market trends will continue, whether overall or in our markets.

If there is limited economic growth or declines in employment and consumer income and/or tightening of mortgage lending standards, practices and regulation in the geographic areas in which we operate or if interest rates for mortgage loans or home prices rise, there could likely be a corresponding adverse effect on our business, prospects, liquidity, financial condition and results of operations, including, but not limited to, the number of homes we sell, our average selling prices, the amount of revenues or profits we generate, and the effect may be material.

If we are unable to develop our communities successfully or within expected time-frames, our results of operations could be adversely affected.

Before a community generates any revenue, time and material expenditures are required to acquire land, obtain development approvals and construct significant portions of project infrastructure, amenities and sales facilities. It can take several years from the time we acquire control of an undeveloped property to the time we make our first home sale on the site. Delays in the development of communities, including delays associated with subcontractors performing the development activities or entitlements, expose us to the risk of changes in market conditions for homes. A decline in our ability to develop and market one of our new undeveloped communities successfully and to generate positive cash flow from these operations in a timely manner could have a material adverse effect on our business and results of operations and on our ability to service our debt and to meet our working capital

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requirements. In addition, higher than expected absorption rates in existing communities may result in lower than expected inventory levels until the development for replacement communities is completed.

Third-party lenders may not complete mortgage loan originations for our homebuyers in a timely manner or at all, which can lead to cancellations and a lower backlog of orders, or to significant delays in our closing homes sales and recognizing revenues from those homes.

Our homebuyers may obtain mortgage financing for their home purchases from any lender or other provider of their choice. If, due to credit or consumer lending market conditions, reduced liquidity, increased risk retention or minimum capital level obligations and/or regulatory restrictions related to the Dodd-Frank Act or other laws, or other factors or business decisions, these lenders refuse or are unable to provide mortgage loans to our homebuyers, or increase the costs to borrowers to obtain such loans, the number of homes we close and our business, prospects, liquidity, financial condition and results of operations may be materially adversely affected.

We may be unable to obtain suitable bonding for the development of our housing projects.

We are often required to provide bonds, letters of credit or guarantees to governmental authorities and others to ensure the completion of our projects. As a result of market conditions, some surety providers have been reluctant to issue new bonds and providers may require credit enhancements (such as cash deposits or letters of credit) in order to maintain existing bonds or to issue new bonds. If we are unable to obtain required bonds in the future for our projects, or if we are required to provide credit enhancements with respect to our current or future bonds or in place of bonds, our business, prospects, liquidity, financial condition and results of operations could be materially and adversely affected.

We may incur a variety of costs to engage in future growth or expansion of our operations, including through add-on acquisitions, and the anticipated benefits may never be realized.

We intend to grow our operations in existing markets, and we may expand into new markets or pursue opportunistic purchases of other home builders on attractive terms as they present themselves. We may be unable to achieve the anticipated benefits of any such growth or expansion, including through add-on acquisitions, the anticipated benefits may take longer to realize than expected or we may incur greater costs than expected in attempting to achieve the anticipated benefits. In such cases, we will likely need to employ additional personnel or consultants that are knowledgeable of such markets. There can be no assurance that we will be able to employ or retain the necessary personnel, to successfully implement a disciplined management process and culture with local management, or that our expansion operations will be successful. This could disrupt our ongoing operations and divert management resources that would otherwise focus on developing our existing business, or that we will be able to successfully integrate any acquired homebuilder or new market. Accordingly, any such expansion could expose us to significant risks, beyond those associated with operating our existing business, and may adversely affect our business, prospects, liquidity, financial condition and results of operations.

The homebuilding industry is highly competitive and, if our competitors are more successful or offer better value to our customers, our business could decline.

We operate in a very competitive environment which is characterized by competition from a number of other homebuilders and land developers in each market in which we operate. Additionally, there are relatively low barriers to entry into our business. We compete with large national and regional homebuilding companies, many of which have greater financial and operational resources than us, and with smaller local homebuilders and land developers, some of which may have lower administrative costs than us. We may be at a competitive disadvantage with regard to certain of our large national and regional homebuilding competitors whose operations are more geographically diversified than ours, as these competitors may be better able to withstand any future regional downturn in the housing market. Furthermore, we generally have a lower market share in each of our markets as compared to many of our competitors. Many of our competitors may also have longer operating histories and longstanding relationships with subcontractors and suppliers in the markets in which we operate. This may give our competitors an advantage in marketing their products, securing materials and labor at lower prices and allowing their homes to be delivered to customers more quickly and at more favorable prices. We compete for, among other things, homebuyers, desirable land parcels, financing, raw materials and skilled management and labor resources. Our competitors may independently develop land and construct homes that are substantially similar to our products.

Increased competition could hurt our business, as it could prevent us from acquiring attractive land parcels on which to build homes or make such acquisitions more expensive, hinder our market share expansion and cause us to increase our selling incentives and reduce our prices. An oversupply of homes available for sale or discounting of home prices could adversely affect pricing for homes in the markets in which we operate. Oversupply and price discounting have periodically adversely affected certain markets, and it is possible that our markets will be adversely affected by these factors in the future.

If we are unable to compete effectively in our markets, our business could decline disproportionately to our competitors, and our results of operations and financial condition could be adversely affected. We can provide no assurance that we will be

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able to continue to compete successfully in any of our markets. Our inability to continue to compete successfully in any of our markets could have a material adverse effect on our business, prospects, liquidity, financial condition or results of operations.

We cannot make any assurances that our growth or expansion strategies will be successful or not expose us to additional risks.

We have expanded our business through selected investments in new geographic markets and by diversifying our products in certain markets. Investments in land, lots and home inventories can expose us to risks of economic loss and inventory impairments if housing conditions weaken or we are unsuccessful in implementing our growth strategies.

We may develop communities in which we build townhomes or other multi-family homes in addition to single-family homes, sell acreage home sites as a part of the development, sell homes to investors or portfolio management companies, or develop commercial properties that may be complementary to our communities. We might acquire another homebuilder or developer in order to accomplish our growth or expansion strategies. We can give no assurance that we will be able to successfully identify, acquire or implement these new strategies in the future. Accordingly, any such expansion, including through acquisition, could expose us to significant risks, beyond those associated with operating our existing business, including understanding and complying with the laws and regulations of new jurisdictions, diversion of our management's attention from ongoing business concerns, difficulties in integrating an acquired business, and incurrence of unanticipated liabilities and expenses and may materially adversely affect our business, prospects, liquidity, financial condition and results of operations.

New and existing laws and regulations or other governmental actions may increase our expenses, limit the number of homes that we can build or delay completion of our projects.

We are subject to numerous local, state, federal and other statutes, ordinances, rules and regulations concerning zoning, development, building design, construction and other matters which among other things, impose restrictive zoning and density requirements, the result of which is to limit the number of homes that can be built within the boundaries of a particular area. We may encounter issues with entitlement, not identify all entitlement requirements during the pre-development review of a project site, or encounter zoning changes that impact our operations. Projects that are not entitled may be subjected to periodic delays, changes in use, less intensive development or elimination of development in certain specific areas due to government regulations. We may also be subject to periodic delays or may be precluded entirely from developing in certain communities due to building moratoriums or zoning changes. Such moratoriums generally relate to insufficient water supplies, sewage facilities, delays in utility hook-ups, or inadequate road capacity within specific market areas or subdivisions. Local governments also have broad discretion regarding the imposition of development fees for projects in their jurisdiction. Projects for which we have received land use and development entitlements or approvals may still require a variety of other governmental approvals and permits during the development process and can also be impacted adversely by unforeseen health, safety and welfare issues, which can further delay these projects or prevent their development. As a result of any of these statutes, ordinances, rules or regulations, our home sales could be delayed, could decline and/or our costs could increase, which could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations. We are subject to environmental laws and regulations, which may increase our costs, result in liabilities, limit the areas in which we can build homes and delay completion of our projects.

We are subject to a variety of local, state, federal and other laws, statutes, ordinances, rules and regulations concerning the environment, hazardous materials, the discharge of pollutants and human health and safety. The particular environmental requirements which apply to any given site vary according to multiple factors, including the site's location, its environmental conditions, the current and former uses of the site, the presence or absence of endangered plants or animals or sensitive habitats, and conditions at nearby properties. We may not identify all of these concerns during any pre-acquisition or pre-development review of project sites. Environmental requirements and conditions may result in delays, may cause us to incur substantial compliance and other costs, and can prohibit or severely restrict development and homebuilding activity in environmentally sensitive regions or in areas contaminated by others before we commence development. We are also subject to third-party challenges, such as by environmental groups or neighborhood associations, under environmental laws and regulations to the permits and other approvals for our

projects and operations. Sometimes regulators from different governmental agencies do not concur on development, remedial standards or property use restrictions for a project, and the resulting delays or additional costs can be material for a given project.

From time to time, the EPA and similar federal, state or local agencies review land developers' and homebuilders' compliance with environmental laws and may levy fines and penalties or other enforcement actions for failure to strictly comply with applicable environmental laws, including those applicable to control storm water discharges during construction, or impose additional requirements for future compliance as a result of past failures. Any such actions taken with respect to us may increase our costs and result in project delays. We expect that increasingly stringent requirements will be imposed on land developers and homebuilders in the future. We cannot assure you that environmental, health and safety laws will not change or become more stringent in the future in a manner that could have a material adverse effect on our business.

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Environmental regulations can also have an adverse impact on the availability and price of certain raw materials, such as lumber.

There is a variety of new legislation being enacted, or considered for enactment at the federal, state and local level relating to energy and climate change. This legislation relates to items such as carbon dioxide emissions control and building codes that impose energy efficiency standards. New building code requirements that impose stricter energy efficiency standards could significantly increase our cost to construct homes. As climate change concerns continue to grow, legislation and regulations of this nature are expected to continue and become costlier to comply with.

Similarly, energy-related initiatives affect a wide variety of companies throughout the United States and because our operations are heavily dependent on significant amounts of raw materials, such as lumber, steel, and concrete, they could have an indirect adverse impact on our operations and profitability to the extent the manufacturers and suppliers of our materials are burdened with expensive cap and trade or similar energy related regulations.

Ownership, leasing or occupation of land and the use of hazardous materials carries potential environmental risks and liabilities.

We are subject to a variety of local, state and federal statutes, rules and regulations concerning easements, land use and the protection of health and the environment, including those governing discharge of pollutants to soil, water and air, including asbestos, the handling of hazardous materials and the cleanup of contaminated sites. We may be liable for the costs of removal, investigation or remediation of man-made or natural hazardous or toxic substances located on, under or in a property currently or formerly owned, leased or occupied by us, whether or not we caused or knew of the pollution.

The particular impact and requirements of environmental laws that apply to any given community vary greatly according to the site, its environmental conditions and the present and former uses of the site. We expect that increasingly stringent requirements may be imposed on land developers and homebuilders in the future.

Environmental laws may result in delays, cause us to implement time consuming and expensive compliance programs and prohibit or severely restrict development in certain environmentally sensitive regions or areas, such as wetlands.

Concerns could arise due to post-acquisition changes in laws or agency policies, or the interpretation thereof.

Furthermore, we could incur substantial costs, including cleanup costs, fines, penalties and other sanctions and damages from third-party claims for property damage or personal injury, as a result of our failure to comply with, or liabilities under, applicable environmental laws and regulations. In addition, we are subject to third-party challenges, such as by environmental groups or neighborhood associations, under environmental laws and regulations to the permits and other approvals required for our projects and operations. These matters could adversely affect our business, prospects, liquidity, financial condition and results of operations.

As a homebuilding and land development business with a wide variety of historic ownership, development, homebuilding and construction activities, we could be liable for future claims for damages as a result of the past or present use of hazardous materials, including building materials or fixtures known or suspected to be hazardous or to contain hazardous materials or due to use of building materials or fixtures which are associated with mold. Any such claims may adversely affect our business, prospects, financial condition and results of operations. Insurance coverage for such claims may be limited or nonexistent.

Difficulties with appraisal valuations in relation to the proposed sales price of our homes could force us to reduce the price of our homes for sale.

Each of our home sales may require an appraisal of the home value before closing. These appraisals are professional judgments of the market value of the property and are based on a variety of market factors. If our internal valuations of the market and pricing do not line up with the appraisal valuations and appraisals are not at or near the agreed upon sales price, we may be forced to reduce the sales price of the home to complete the sale. These appraisal issues could have a material adverse effect on our business and results of operations.

Because of the seasonal nature of our business, our quarterly operating results fluctuate.

As discussed under “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Seasonality,” we have historically experienced, and in the future expect to continue to experience, variability in our results on a quarterly and monthly basis. We close more homes in our second, third and fourth quarters. Thus, our revenue may fluctuate on a quarterly basis and we may have higher capital requirements in our second, third and

fourth quarters. Accordingly, there is a risk that we will invest significant amounts of capital in the acquisition and development of land and construction of homes that we do not sell at anticipated pricing levels or within anticipated time frames. If, due to market conditions, construction delays or other causes, we do not complete home sales at anticipated pricing levels or within anticipated time frames, our business, prospects, liquidity, financial condition and results of operations would be adversely affected. We expect this seasonal pattern to continue over the long term but we can make no assurances as to the degree to which our historical seasonal patterns will occur in the future.

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Adverse weather and geological conditions may increase costs, cause project delays and reduce consumer demand for housing, all of which could materially and adversely affect us.

As a homebuilder and land developer, we are subject to the risks associated with numerous weather-related and geologic events. These weather-related and geologic events include but are not limited to hurricanes, tornadoes, droughts, floods, brushfires, wildfires, prolonged periods of precipitation, landslides, soil subsidence and earthquakes and other natural disasters. The occurrence of any of these events could damage our land parcels and projects, cause delays in completion of our projects, reduce consumer demand for housing, and cause shortages and price increases in labor or raw materials, any of which could affect our sales and profitability. In addition to directly damaging our land or projects, many of these natural events could damage roads and highways providing access to those assets or affect the desirability of our land or projects, thereby adversely affecting our ability to market homes or sell land in those areas and possibly increasing the costs of homebuilding completion.

There are some risks of loss for which we may be unable to purchase insurance coverage. For example, losses associated with hurricanes, landslides, prolonged periods of precipitation, earthquakes and other weather-related and geologic events may not be insurable and other losses, such as those arising from terrorism, may not be economically insurable. A sizeable uninsured loss could materially and adversely affect our business, prospects, liquidity, financial condition and results of operations.

Our geographic concentration could materially and adversely affect us if the homebuilding industry in our current markets should experience a decline.

Our business strategy is focused on the acquisition of suitable land and the design, construction and sale of primarily single-family homes in residential subdivisions, including planned communities, in Texas, Arizona, Florida, Georgia, New Mexico, Colorado, North Carolina, South Carolina, Washington, Tennessee, Minnesota, Oklahoma and Oregon as well as our expansion states of Alabama, California, Nevada, Virginia, and West Virginia. Because our operations are currently concentrated in these areas, a prolonged economic downturn in the future in one or more of these areas or a particular industry that is fundamental to one of these areas, particularly within Texas or a specific geographical region, could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations, and a disproportionately greater impact on us than other homebuilders with more diversified operations. To the extent the oil and gas industries, which can be very volatile, are negatively impacted by declining commodity prices, climate change, legislation or other factors, a result could be a reduction in employment, or other negative economic consequences, which in turn could adversely impact our home sales and activities in Texas and certain of our other markets.

Moreover, certain insurance companies doing business in Florida and Texas have restricted, curtailed or suspended the issuance of homeowners' insurance policies on single-family homes. This has both reduced the availability of hurricane and other types of natural disaster insurance in Florida and Texas, in general, and increased the cost of such insurance to prospective purchasers of homes in Florida and Texas. Mortgage financing for a new home is conditioned, among other things, on the availability of adequate homeowners' insurance. There can be no assurance that homeowners' insurance will be available or affordable to prospective purchasers of our homes offered for sale in the Florida and Texas markets. Long-term restrictions on, or unavailability of, homeowners' insurance in the Florida and Texas markets could have an adverse effect on the homebuilding industry in that market in general, and on our business within that market in particular. Additionally, the availability of permits for new homes in new and existing developments has been adversely affected by the significantly limited capacity of the schools, roads, and other infrastructure in that market.

If adverse conditions in these markets develop in the future, it could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations. Furthermore, if buyer demand for new homes in these markets decreases, home prices could decline, which would have a material adverse effect on our business. Difficulty in obtaining sufficient capital could result in an inability to acquire land for our developments or increased costs and delays in the completion of development projects, increase home construction costs or delay home construction entirely.

The homebuilding and land development industry is capital-intensive and requires significant up-front expenditures to acquire land parcels and begin development. In addition, if housing markets are not favorable or permitting or

development takes longer than anticipated, we may be required to hold our investments in land for extended periods of time. If internally generated funds are not sufficient, we may seek additional capital in the form of equity or debt financing from a variety of potential sources, including additional bank financings and/or securities offerings. The availability of borrowed funds, especially for land acquisition and construction financing, may be constrained regionally or nationally, and the lending community may require increased amounts of equity to be invested in a project by borrowers in connection with both new loans and the extension of existing loans. Since the global recession in 2008, credit and capital markets have, from time to time, experienced unusual volatility. If we are required to seek additional financing to fund our operations, continued volatility in these markets may restrict our flexibility to access such financing. If we are not successful in obtaining sufficient funding for our planned capital and other expenditures or if we do not properly allocate our funding, we may be unable to acquire additional land for development and/or to construct new housing. Additionally, if we cannot obtain additional financing to fund the purchase of land under our purchase contracts, we may incur

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contractual penalties, fees and increased expenses from the write-off of due diligence and pre-acquisition costs. Any difficulty in obtaining sufficient capital for planned development expenditures could also cause project delays and any such delay could result in cost increases. Any one or more of the foregoing events could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

Our industry is cyclical and adverse changes in general and local economic conditions could reduce the demand for homes and, as a result, could have a material adverse effect on us.

Our business can be substantially affected by adverse changes in general economic or business conditions that are outside of our control, including changes in short-term and long-term interest rates; employment levels and job and personal income growth; housing demand from population growth, household formation and other demographic changes, among other factors; availability and pricing of mortgage financing for homebuyers; consumer confidence generally and the confidence of potential homebuyers in particular; financial system and credit market stability; private party and government mortgage loan programs (including changes in FHA, USDA, VA, Fannie Mae and Freddie Mac conforming mortgage loan limits, credit risk/mortgage loan insurance premiums and/or other fees, down payment requirements and underwriting standards), and federal and state regulation, oversight and legal action regarding lending, appraisal, foreclosure and short sale practices; federal and state personal income tax rates and provisions, including provisions for the deduction of mortgage loan interest payments, real estate taxes and other expenses; supply of and prices for available new or resale homes (including lender-owned homes) and other housing alternatives, such as apartments, single-family rentals and other rental housing; homebuyer interest in our current or new product designs and new home community locations; general consumer interest in purchasing a home compared to choosing other housing alternatives; interest of financial institutions or other businesses in purchasing wholesale homes; and real estate taxes. Adverse changes in these conditions may affect our business nationally or may be more prevalent or concentrated in particular submarkets in which we operate. Inclement weather, natural disasters (such as earthquakes, hurricanes, tornadoes, floods, prolonged periods of precipitation, droughts and fires), other calamities and other environmental conditions can delay the delivery of our homes and/or increase our costs. Civil unrest or acts of terrorism can also have a negative effect on our business. If the homebuilding industry experiences another significant or sustained downturn, it would materially adversely affect our business and results of operations in future years.

The potential difficulties described above can cause demand and prices for our homes to fall or cause us to take longer and incur more costs to develop the land and build our homes. We may not be able to recover these increased costs by raising prices because of market conditions. The potential difficulties could also lead some homebuyers to cancel or refuse to honor their home purchase contracts altogether.

Inflation could adversely affect our business and financial results.

Inflation could adversely affect our business and financial results by increasing the costs of land, raw materials and labor needed to operate our business. If our markets have an oversupply of homes relative to demand, we may be unable to offset any such increases in costs with corresponding higher sales prices for our homes. Inflation may also accompany higher interest rates, which could adversely impact potential customers' ability to obtain financing on favorable terms, thereby further decreasing demand. If we are unable to raise the prices of our homes to offset the increasing costs of our operations, our margins could decrease. Furthermore, if we need to lower the price of our homes to meet demand, the value of our land inventory may decrease. Inflation may also raise our costs of capital and decrease our purchasing power, making it more difficult to maintain sufficient funds to operate our business.

Interest rate changes may adversely affect us.

We currently do not hedge against interest rate fluctuations. We may obtain in the future one or more forms of interest rate protection in the form of swap agreements, interest rate cap contracts or similar agreements to hedge against the possible negative effects of interest rate fluctuations. However, we cannot assure you that any hedging will adequately relieve the adverse effects of interest rate increases or that counterparties under these agreements will honor their obligations thereunder. In addition, we may be subject to risks of default by hedging counterparties. Adverse economic conditions could also cause the terms on which we borrow to be unfavorable. We could be required to liquidate one or more of our assets at times which may not permit us to receive an attractive return on our assets in order to meet our debt service obligations.

We are subject to warranty and liability claims arising in the ordinary course of business that can be significant. As a homebuilder and developer, we are subject to construction defect, product liability and home and other warranty claims, including moisture intrusion and related claims, arising in the ordinary course of business. These claims are common to the homebuilding industry and can be costly. There can be no assurance that any developments we undertake will be free from defects once completed and any defects attributable to us may lead to significant contractual or other liabilities. We maintain, and require our subcontractors to maintain, general liability insurance (including construction defect and bodily injury coverage) and workers' compensation insurance and generally seek to require our subcontractors to indemnify us for liabilities arising from their work.

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While these insurance policies, subject to deductibles and other coverage limits, and indemnities protect us against a portion of our risk of loss from claims related to our land development and homebuilding activities, we cannot provide assurance that these insurance policies and indemnities will be adequate to address all our home and other warranty, product liability and construction defect claims in the future, or that any potential inadequacies will not have an adverse effect on our business, financial condition or results of operations. Additionally, the coverage offered by and the availability of general liability insurance for completed operations and construction defects are currently limited and costly. We cannot provide assurance that coverage will not be further restricted, increasing our risks and financial exposure to claims, and/or become costlier.

We may suffer uninsured losses or suffer material losses in excess of insurance limits.

We could suffer physical damage to property and liabilities resulting in losses that may not be fully recoverable by insurance. Insurance against certain types of risks, such as terrorism, earthquakes or floods or personal injury claims, may be unavailable, available in amounts that are less than the full market value or replacement cost of investment or underlying assets or subject to a large deductible or self-insurance retention amount. In addition, there can be no assurance certain types of risks which are currently insurable will continue to be insurable on an economically feasible basis. Should an uninsured loss or a loss in excess of insured limits occur or be subject to deductibles or self-insurance retention, we could sustain financial loss or lose capital invested in the affected property as well as anticipated future income from that property. Furthermore, we could be liable to repair damage or meet liabilities caused by risks that are uninsured or subject to deductibles. We may be liable for any debt or other financial obligations related to affected property. Material losses or liabilities in excess of insurance proceeds may occur in the future.

If the market value of our land inventory decreases, our results of operations could be adversely affected by impairments and write-downs.

The market value of our land and housing inventories depends on market conditions. We acquire land for expansion into new markets and for replacement of land inventory and expansion within our current markets. There is an inherent risk that the value of the land owned by us may decline after purchase. The valuation of property is inherently subjective and based on the individual characteristics of each property. We may have acquired options on or bought and developed land at a cost we will not be able to recover fully or on which we cannot build and sell homes profitably. In addition, our deposits for lots controlled under purchase, option or similar contracts may be put at risk. Factors such as changes in regulatory requirements and applicable laws (including in relation to building regulations, taxation and planning), political conditions, the condition of financial markets, both local and national economic conditions, the financial condition of customers, potentially adverse tax consequences, and interest and inflation rate fluctuations are subject to uncertainty. Moreover, our valuations are made on the basis of assumptions that may not prove to reflect economic or demographic reality.

If housing demand fails to meet our expectations when we acquired our inventory, our profitability may be adversely affected and we may not be able to recover our costs when we build and sell houses. We regularly review the value of our land holdings and continue to review our holdings on a periodic basis. Material write-downs and impairments in the value of our inventory may be required, and we may in the future sell land or homes at a loss, which could adversely affect our results of operations and financial condition.

Fluctuations in real estate values may require us to write-down the book value of our real estate assets.

The homebuilding and land development industries are subject to significant variability and fluctuations in real estate values. As a result, we may be required to write-down the book value of our real estate assets in accordance with U.S. GAAP, and some of those write-downs could be material. Any material write-downs of assets could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

Acts of war or terrorism may seriously harm our business.

Acts of war, any outbreak or escalation of hostilities between the United States and any foreign power or acts of terrorism may cause disruption to the U.S. economy, or the local economies of the markets in which we operate, cause shortages of building materials, increase costs associated with obtaining building materials, result in building code changes that could increase costs of construction, result in uninsured losses, affect job growth and consumer confidence, or cause economic changes that we cannot anticipate, all of which could reduce demand for our homes and adversely impact our business, prospects, liquidity, financial condition and results of operations.

A major health and safety incident relating to our business could be costly in terms of potential liabilities and reputational damage.

Building sites are inherently dangerous, and operating in the homebuilding and land development industry poses certain inherent health and safety risks. Due to health and safety regulatory requirements and the number of projects we work on, health and safety performance is critical to the success of all areas of our business.

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Any failure in health and safety performance may result in penalties for non-compliance with relevant regulatory requirements or litigation, and a failure that results in a major or significant health and safety incident is likely to be costly in terms of potential liabilities incurred as a result. Such a failure could generate significant negative publicity and have a corresponding impact on our reputation and our relationships with relevant regulatory agencies, governmental authorities and local communities, which in turn could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

We may become subject to litigation, which could materially and adversely affect us.

In the future, we may become subject to litigation or enforcement actions, including claims relating to our operations, securities offerings and otherwise in the ordinary course of business. Some of these claims may result in significant defense costs and potentially significant judgments against us, some of which are not, or cannot be, insured against. We cannot be certain of the ultimate outcomes of any claims that may arise in the future. Resolution of these types of matters against us may result in our having to pay significant fines, judgments, or settlements, which, if uninsured, or if the fines, judgments and settlements exceed insured levels, could adversely impact our earnings and cash flows, thereby materially and adversely affecting us. Certain litigation or the resolution of certain litigation may affect the availability or cost of some of our insurance coverage, which could materially and adversely impact us, expose us to increased risks that would be uninsured, and materially and adversely impact our ability to attract directors and officers.

Poor relations with the residents of our communities could negatively impact sales, which could cause our revenue or results of operations to decline.

Residents of communities we develop rely on us to resolve issues or disputes that may arise in connection with the operation or development of their communities. Efforts made by us to resolve these issues or disputes could be deemed unsatisfactory by the affected residents and subsequent actions by these residents could adversely affect our sales or our reputation. In addition, we could be required to make material expenditures related to the settlement of such issues or disputes or to modify our community development plans, which could adversely affect our results of operations.

An information systems interruption or breach in security could adversely affect us.

We rely on accounting, financial and operational management information systems to conduct our operations. Any cyber incident or attack or other disruption or failure in these information systems could adversely affect our ability to conduct our business and could have a material adverse effect on our business, liquidity, financial condition and results of operations. Furthermore, any failure or security breach of information systems or data could result in a violation of applicable privacy and other laws, significant legal and financial exposure, damage to our reputation, and a loss of confidence in our security measures, which could harm our business and could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

Our business is subject to complex and evolving U.S. laws and regulations regarding privacy and data protection. The regulatory environment surrounding data privacy and protection is constantly evolving and can be subject to significant change. New laws and regulations governing data privacy and the unauthorized disclosure of confidential information, including recent California legislation, pose increasingly complex compliance challenges and potentially elevate our costs. Any failure, or perceived failure, by us to comply with applicable data protection laws could result in proceedings or actions against us by governmental entities or others, subject us to significant fines, penalties, judgments and negative publicity, require us to change our business practices, increase the costs and complexity of compliance, and adversely affect our business. As noted above, we are also subject to the possibility of cyber incidents or attacks, which themselves may result in a violation of these laws. Additionally, if we acquire a company that has violated or is not in compliance with applicable data protection laws, we may incur significant liabilities and penalties as a result.

Termination of the employment agreement with our Chief Executive Officer could be costly and prevent a change in control of our company.

The employment agreement with our Chief Executive Officer, Eric Lipar, provides that if his employment with us terminates under certain circumstances, we may be required to pay him a significant amount of severance compensation, thereby making it costly to terminate his employment. Furthermore, these provisions could delay or

prevent a transaction or a change in control of our company that might involve a premium paid for shares of our common stock or otherwise be in the best interests of our stockholders, which could adversely affect the market price of our common stock.

Any future government shutdowns or slowdowns may materially adversely affect our business or financial results.

Any future government shutdowns or slowdowns may materially adversely affect our business or financial results. We can make no assurances that potential closings affected by any such shutdown or slowdown will occur after the shutdown or slowdown has ended.

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Negative publicity could adversely affect our reputation as well as our business, financial results and stock price. Unfavorable media related to our industry, company, brands, marketing, personnel, operations, business performance, or prospects may affect our stock price and the performance of our business, regardless of its accuracy or inaccuracy. The speed at which negative publicity can be disseminated has increased dramatically with the capabilities of electronic communication, including social media outlets, websites, blogs, or newsletters. Our success in maintaining, extending and expanding our brand image depends on our ability to adapt to this rapidly changing media environment. Adverse publicity or negative commentary from any media outlet could damage our reputation and reduce the demand for our homes, which would adversely affect our business.

Risks Related to Our Organization and Structure

We depend on key management personnel and other experienced employees.

Our success depends to a significant degree upon the contributions of certain key management personnel including, but not limited to, Eric Lipar, our Chief Executive Officer and Chairman of our board of directors. Although we have entered into an employment agreement with Mr. Lipar, there is no guarantee that Mr. Lipar will remain employed by us. If any of our key management personnel were to cease employment with us, our operating results could suffer. Our ability to retain our key management personnel or to attract suitable replacements should any members of our management team leave is dependent on the competitive nature of the employment market. The loss of services from key management personnel or a limitation in their availability could materially and adversely impact our business, prospects, liquidity, financial condition and results of operations. Further, such a loss could be negatively perceived in the capital markets. We have not obtained key man life insurance that would provide us with proceeds in the event of death or disability of any of our key management personnel.

Experienced employees in the homebuilding, land acquisition, development, and construction industries are fundamental to our ability to generate, obtain and manage opportunities. In particular, local knowledge and relationships are critical to our ability to source attractive land acquisition opportunities. Experienced employees working in the homebuilding, development and construction industries are highly sought after. Failure to attract and retain such personnel or to ensure that their experience and knowledge is not lost when they leave the business through retirement, redundancy or otherwise may adversely affect the standards of our service and may have an adverse impact on our business, prospects, liquidity, financial condition and results of operations. The loss of any of our key personnel could adversely impact our business, prospects, financial condition and results of operations. We may change our operational policies, investment guidelines and our business and growth strategies without stockholder consent, which may subject us to different and more significant risks in the future.

Our board of directors will determine our operational policies, investment guidelines and our business and growth strategies. Our board of directors may make changes to, or approve transactions that deviate from, those policies, guidelines and strategies without a vote of, or notice to, our stockholders. This could result in us conducting operational matters, making investments or pursuing different business or growth strategies than those contemplated in this Annual Report on the Form 10-K. Under any of these circumstances, we may expose ourselves to different and more significant risks in the future, which could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

Changes in accounting rules, assumptions and/or judgments could materially and adversely affect us.

Accounting rules and interpretations for certain aspects of our financial reporting are highly complex and involve significant assumptions and judgment. These complexities could lead to a delay in the preparation and dissemination of our financial statements. Furthermore, changes in accounting rules and interpretations or in our accounting assumptions and/or judgments, such as asset impairments, could significantly impact our financial statements. In some cases, we could be required to apply a new or revised standard retroactively, resulting in restating prior period financial statements. Any of these circumstances could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

We expect to use leverage in executing our business strategy, which may adversely affect the return on our assets.

We expect to employ prudent levels of leverage to finance the acquisition and development of our lots and construction of our homes. Our existing indebtedness is recourse to us and we anticipate that future indebtedness will likewise be recourse. As of December 31, 2018, we had a \$500.0 million revolving credit facility (the "Credit Facility")

or “Credit Agreement”) to finance our construction and development activities. As of December 31, 2018, we had outstanding borrowings of \$293.8 million under the Credit Facility and we could borrow an additional \$26.3 million under the Credit Facility. As of December 31, 2018, borrowings under the Credit Facility bore interest at a rate of LIBOR plus 2.90% per annum. In addition, as of December 31, 2018, we had outstanding \$70.0 million aggregate principal amount of our 4.25% Convertible Notes due 2019 (the “Convertible Notes”) and \$300.0 million aggregate principal amount of our 6.875% Senior Notes due 2026 (“the Senior Notes”).

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Our board of directors will consider a number of factors when evaluating our level of indebtedness and when making decisions regarding the incurrence of new indebtedness, including the purchase price of assets to be acquired with debt financing, if any, the estimated market value of our assets and the ability of particular assets, and our company as a whole, to generate cash flow to cover the expected debt service. As a means of sustaining our long-term financial health and limiting our exposure to unforeseen dislocations in the debt and financing markets, we currently expect to remain conservatively capitalized. However, our certificate of incorporation does not contain a limitation on the amount of indebtedness we may incur and our board of directors may change our target debt levels at any time without the approval of our stockholders.

Incurring substantial indebtedness could subject us to many risks that, if realized, would adversely affect us, including the risk that:

- our cash flow from operations may be insufficient to make required payments of principal of and interest on the debt, which is likely to result in acceleration of such indebtedness;

- our indebtedness may increase our vulnerability to adverse economic and industry conditions with no assurance that our profitability will increase with higher financing cost;

- we may be required to dedicate a portion of our cash flow from operations to payments on our indebtedness, thereby reducing funds available for operations and capital expenditures, future investment opportunities or other purposes; and

- the terms of any refinancing may not be as favorable as the terms of the indebtedness being refinanced.

If we do not have sufficient funds to repay our indebtedness at maturity, it may be necessary to refinance the indebtedness through additional debt or additional equity financings. If, at the time of any refinancing, prevailing interest rates or other factors result in higher interest rates on refinancings, increases in interest expense could adversely affect our cash flows and results of operations. If we are unable to refinance our indebtedness on acceptable terms, we may be forced to dispose of our assets on disadvantageous terms, potentially resulting in losses. To the extent we cannot meet any future debt service obligations, we will risk losing some or all of our assets that may be pledged to secure our obligations to foreclosure. Unsecured debt agreements may contain specific cross-default provisions with respect to specified other indebtedness, giving the unsecured lenders the right to declare a default if we are in default under other indebtedness in some circumstances. Defaults under the Credit Facility and our other debt agreements, if any, could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

Access to financing sources may not be available on favorable terms, or at all, especially in light of current market conditions, which could adversely affect our ability to maximize our returns.

Our access to additional third-party sources of financing will depend, in part, on:

- general market conditions;

- the market's perception of our growth potential;

- with respect to acquisition and/or development financing, the market's perception of the value of the land parcels to be acquired and/or developed;

- our current debt levels;

- our current and expected future earnings;

- our cash flow; and

- the market price per share of our common stock.

Since the global recession in 2008, domestic financial markets have, from time to time, experienced unusual volatility, uncertainty and a tightening of liquidity in both the high yield debt and equity capital markets. Credit spreads for major sources of capital widened significantly during the U.S. credit crisis as investors demanded a higher risk premium. Given such possible volatility and weakness in the capital and credit markets, potential lenders may be unwilling or unable to provide us with financing that is attractive to us or may increase collateral requirements or may charge us prohibitively high fees in order to obtain financing. Consequently, our ability to access the credit market in order to attract financing on reasonable terms may be adversely affected. Investment returns on our assets and our ability to make acquisitions could be adversely affected by our inability to secure additional financing on reasonable

terms, if at all.

Depending on market conditions at the relevant time, we may have to rely more heavily on additional equity financings or on less efficient forms of debt financing that require a larger portion of our cash flow from operations, thereby reducing funds available for our operations, future business opportunities and other purposes. We may not have access to such equity or debt capital on favorable terms at the desired times, or at all.

Our current financing arrangements contain, and our future financing arrangements likely will contain, restrictive provisions.

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Our current financing agreements contain, and the financing arrangements we enter into in the future likely will contain, provisions that limit our ability to do certain things. In particular, the Credit Agreement requires us to maintain (i) a tangible net worth of not less than \$400.0 million plus 75% of the net proceeds of all equity issuances plus 50% of the amount of our positive net income in any fiscal quarter after December 31, 2017, (ii) a leverage ratio of not greater than 64.0%, (iii) liquidity of at least \$50.0 million and (iv) a ratio of EBITDA to interest expense for the most recent four quarters of at least 2.50 to 1.00. The Credit Agreement contains various covenants that, among other restrictions, limit the amount of our additional debt and our ability to make certain investments.

If we fail to meet or satisfy any of these provisions, we would be in default under the Credit Agreement and our lenders could elect to declare outstanding amounts due and payable, terminate their commitments, require the posting of additional collateral and enforce their respective interests against existing collateral. A default also could limit significantly our financing alternatives, which could cause us to curtail our investment activities and/or dispose of assets when we otherwise would not choose to do so. In addition, future indebtedness may contain financial covenants limiting our ability to, for example, incur additional indebtedness, make certain investments, reduce liquidity below certain levels and pay dividends to our stockholders, and otherwise affect our operating policies. If we default on one or more of our debt agreements, it could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

In addition, upon the occurrence of a “Fundamental Change” (as defined in the indenture governing the Convertible Notes), subject to certain conditions, the Convertible Notes include terms that allow a holder of the Convertible Notes to require to purchase all or a portion of such holder’s Convertible Notes for cash at a price equal to 100% of the principal amount of the Convertible Notes to be purchased, plus any then accrued, but unpaid, interest.

Interest expense on debt we incur may limit our cash available to fund our growth strategies.

As of December 31, 2018, we had total outstanding borrowings of \$293.8 million under the Credit Facility, and we could borrow an additional \$26.3 million under the Credit Facility. As of December 31, 2018, borrowings under the Credit Facility bore interest at a rate of LIBOR plus 2.90% per annum. In addition, as of December 31, 2018, we had outstanding \$70.0 million aggregate principal amount of the Convertible Notes and \$300.0 million aggregate principal amount of the Senior Notes. As of December 31, 2018, the Convertible Notes and the Senior Notes had a fixed rate of 4.25% and 6.875%, respectively. If our operations do not generate sufficient cash from operations at levels currently anticipated, we may seek additional capital in the form of debt financing. Our current indebtedness includes, and any additional indebtedness we subsequently incur may have, a floating rate of interest. Higher interest rates could increase debt service requirements on our current floating rate indebtedness and on any floating rate indebtedness we subsequently incur, and could reduce funds available for operations, future business opportunities or other purposes. If we need to repay existing indebtedness during periods of rising interest rates, we could be required to refinance our then-existing indebtedness on unfavorable terms or liquidate one or more of our assets to repay such indebtedness at times which may not permit realization of the maximum return on such assets and could result in a loss. The occurrence of either such event or both could materially and adversely affect our cash flows and results of operations. We are a holding company, and we are accordingly dependent upon distributions from our subsidiaries to service our debt and pay dividends, if any, taxes and other expenses.

We are a holding company and will have no material assets other than our ownership of membership interests or limited partnership interests in our subsidiaries. We have no independent means of generating revenue. We intend to cause our subsidiaries to make distributions to their members or partners in an amount sufficient to cover all applicable taxes payable and dividends, if any, declared by us. Our ability to service our debt depends on the results of operations of our subsidiaries and upon the ability of such subsidiaries to provide us with cash, whether in the form of dividends, loans or other distributions, to pay amounts due on our obligations. Future financing arrangements may contain negative covenants, limiting the ability of our subsidiaries to declare or pay dividends or make distributions. Our subsidiaries are separate and distinct legal entities; to the extent that we need funds, and our subsidiaries are restricted from making such dividends or distributions under applicable law or regulations, or are otherwise unable to provide such funds (for example, due to restrictions in future financing arrangements that limit the ability of our operating subsidiaries to distribute funds), our liquidity and financial condition could be materially harmed.

The obligations associated with being a public company will require significant resources and management attention.

As a public company with listed equity securities, we must comply with laws, regulations and requirements, including the requirements of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), certain corporate governance provisions of the Sarbanes-Oxley Act of 2002 (the “Sarbanes-Oxley Act”), related regulations of the SEC and requirements of the NASDAQ Global Select Market. The Exchange Act requires that we file annual, quarterly and current reports with respect to our business and financial condition. The Sarbanes-Oxley Act requires, among other things, that we establish and maintain effective internal controls and procedures for financial reporting.

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Section 404 of the Sarbanes-Oxley Act (“Section 404”) requires our management and independent auditors to report annually on the effectiveness of our internal control over financial reporting. As of December 31, 2017, we are no longer an “emerging growth company,” and, therefore, we are no longer subject to emerging growth company exemptions from various reporting requirements applicable to other public companies, including, but not limited to, not being required to comply with the auditor attestation requirements of Section 404. As of December 31, 2017, when we became a “large accelerated filer” (as defined in the relevant SEC rules), we are required to include an opinion from our independent auditors on the effectiveness of our internal control over financial reporting.

These reporting and other obligations place significant demands on our management, administrative, operational and accounting resources and cause us to incur significant expenses. We may need to upgrade our systems or create new systems, implement additional financial and management controls, reporting systems and procedures, create or outsource an internal audit function, and hire additional accounting and finance staff. If we are unable to accomplish these objectives in a timely and effective fashion, our ability to comply with the financial reporting requirements and other rules that apply to reporting companies could be impaired. Any failure to maintain effective internal control over financial reporting could have a material adverse effect on our business, prospects, liquidity, financial condition and results of operations.

If we fail to implement and maintain an effective system of internal controls, we may not be able to accurately determine our financial results or prevent fraud. As a result, investors could lose confidence in our financial results, which could materially and adversely affect us.

Effective internal controls are necessary for us to provide reliable financial reports and effectively prevent fraud. We may in the future discover areas of our internal controls that need improvement. We cannot be certain that we will be successful in maintaining adequate internal control over our financial reporting and financial processes. Furthermore, as we grow our business, our internal controls will become more complex, and we will require significantly more resources to ensure our internal controls remain effective. Additionally, the existence of any material weakness or significant deficiency would require management to devote significant time and incur significant expense to remediate any such material weakness or significant deficiency and management may not be able to remediate any such material weakness or significant deficiency in a timely manner. The existence of any material weakness in our internal control over financial reporting could also result in errors in our financial statements that could require us to restate our financial statements, cause us to fail to meet our reporting obligations and cause investors to lose confidence in our reported financial information, all of which could materially and adversely affect us.

Any joint venture investments that we make could be adversely affected by our lack of sole decision making authority, our reliance on the financial condition of our joint venture partners and disputes between us and our joint venture partners.

We may co-invest in the future with third parties through partnerships, joint ventures or other entities, acquiring non-controlling interests in or sharing responsibility for managing the affairs of a land acquisition and/or a development. In this event, we would not be in a position to exercise sole decision-making authority regarding the acquisition and/or development, and our investment may be illiquid due to our lack of control. Investments in partnerships, joint ventures, or other entities may, under certain circumstances, involve risks not present were a third-party not involved, including the possibility that our joint venture partners might become bankrupt, fail to fund their share of required capital contributions, make poor business decisions or block or delay necessary decisions. Our joint venture partners may have economic or other business interests or goals which are inconsistent with our business interests or goals, and may be in a position to take actions contrary to our policies or objectives. Such investments may also have the potential risk of impasses on decisions, such as a sale, because neither we nor our joint venture partners would have full control over the land acquisition or development. Disputes between us and our joint venture partners may result in litigation or arbitration that would increase our expenses and prevent our officers and/or directors from focusing their time and effort on our business. In addition, we may in certain circumstances be liable for the actions of our joint venture partners.

Cautionary Statement about Forward-Looking Statements

From time to time we make statements concerning our expectations, beliefs, plans, objectives, goals, strategies, future events or performance and underlying assumptions and other statements that are not historical facts. These statements

are “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Actual results may differ materially from those expressed or implied by these statements. You can generally identify our forward-looking statements by the words “anticipate,” “believe,” “continue,” “could,” “estimate,” “expect,” “forecast,” “goal,” “may,” “objective,” “plan,” “potential,” “predict,” “projection,” “should,” “will” or other similar words.

We have based our forward-looking statements on our management’s beliefs and assumptions based on information available to our management at the time the statements are made. We caution you that assumptions, beliefs, expectations, intentions and projections about future events may, and often do, vary materially from actual results. Therefore, we cannot assure you that actual results will not differ materially from those expressed or implied by our forward-looking statements.

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The following are some of the factors that could cause actual results to differ materially from those expressed or implied in forward-looking statements:

- adverse economic changes either nationally or in the markets in which we operate, including, among other things, increases in unemployment, volatility of mortgage interest rates and inflation and decreases in housing prices;
- a slowdown in the homebuilding industry;
- volatility and uncertainty in the credit markets and broader financial markets;
- the cyclical and seasonal nature of our business;
- our future operating results and financial condition;
- our business operations;
- changes in our business and investment strategy;
- the success of our operations in recently opened new markets and our ability to expand into additional new markets;
- our ability to successfully extend our business model to building homes with higher price points, developing larger communities and producing and selling multi-unit products, townhouses, wholesale products, and acreage home sites;
- our ability to develop our projects successfully or within expected timeframes;
- our ability to identify potential acquisition targets and close such acquisitions;
- our ability to successfully integrate any acquisitions, including the Wynn Homes acquisition, with our existing operations;
- availability of land to acquire and our ability to acquire such land on favorable terms or at all;
- availability, terms and deployment of capital;
- decisions of the lender group of the Credit Facility;
- the occurrence of the specific conversion events that enable early conversion of the Convertible Notes;
- decline in the market value of our land portfolio;
- disruption in the terms or availability of mortgage financing or increase in the number of foreclosures in our markets;
- shortages of or increased prices for labor, land, or raw materials used in land development and housing construction;
- delays in land development or home construction resulting from natural disasters, adverse weather conditions or other events outside our control;
- uninsured losses in excess of insurance limits;
- the cost and availability of insurance and surety bonds;
- changes in, liabilities under, or the failure or inability to comply with, governmental laws and regulations;
- the timing of receipt of regulatory approvals and the opening of projects;
- the degree and nature of our competition;
- increases in taxes or government fees;
- poor relations with the residents of our projects;
- existing and future litigation, arbitration or other claims;
- availability of qualified personnel and third-party contractors and subcontractors;
- information system interruptions or breaches in security;
- our ability to retain our key personnel;
- our leverage and future debt service obligations;
- the impact on our business of any future government shutdown;
- other risks and uncertainties inherent in our business; and
- other factors we discuss under the section entitled “Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

You should not place undue reliance on forward-looking statements. Each forward-looking statement speaks only as of the date of the particular statement. We expressly disclaim any intent, obligation or undertaking to update or revise any forward-looking statements to reflect any change in our expectations with regard thereto or any change in events, conditions or circumstances on which any such statements are based. All subsequent written and oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements contained in this Annual Report on Form 10-K.

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ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

We lease approximately 22,000 square feet in The Woodlands, Texas for our corporate headquarters; this lease expires in 2028. In addition, to adequately meet the needs of our operations, we lease offices in Arizona, Florida, Georgia, Washington, California, West Virginia, and North Carolina. See “Business—Land Acquisition Policies and Development” for a summary of the other property which we owned or controlled as of December 31, 2018.

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ITEM 3. LEGAL PROCEEDINGS

In the ordinary course of doing business, we are subject to claims or proceedings from time to time relating to the purchase, development, and sale of real estate and homes and other aspects of our homebuilding operations. Management believes that these claims include usual obligations incurred by real estate developers and residential homebuilders in the normal course of business. In the opinion of management, these matters will not have a material effect on our consolidated financial position, results of operations or cash flows.

We have provided unsecured environmental indemnities to certain lenders and other contractual counterparties. In each case, we have performed due diligence on the potential environmental risks including obtaining an independent environmental review from outside environmental consultants. These indemnities obligate us to reimburse the guaranteed parties for damages related to environmental matters. There is no term or damage limitation on these indemnities; however, if an environmental matter arises, we may have recourse against other previous owners. In the ordinary course of doing business, we are subject to regulatory proceedings from time to time related to environmental and other matters. In the opinion of management, these matters will not have a material effect on our consolidated financial position, results of operations, or cash flows.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

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PART II

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

Our common stock is listed on the NASDAQ Stock Market (NASDAQ) under the symbol “LGIH.” As of February 22, 2019, the closing price of our common stock on the NASDAQ was \$61.96, and we had 26 stockholders of record, including Cede & Co. as nominee of The Depository Trust Company.

Shelf Registration Statement and ATM Offering Programs

On August 24, 2018, we and certain of our subsidiaries filed an automatic shelf registration statement on Form S-3 (Registration No. 333-227012), registering the offering and sale of an indeterminate amount of debt securities, guarantees of debt securities, preferred stock, common stock, warrants, depositary shares, purchase contracts and units that include any of these securities. Under our prior shelf registration statement, we established an at the market common stock offering program in September 2015 (the “2015 ATM Program”) and September 2016 (the “2016 ATM Program”) with Deutsche Bank Securities Inc., J.P. Morgan Securities LLC, JMP Securities LLC and Builder Advisor Group, LLC, as sales agents to sell up to \$30.0 million and \$25.0 million, respectively, of our common stock. We issued and sold 743,554 shares of our common stock under the 2015 ATM Program, and received net proceeds of approximately \$19.8 million, during 2016. We issued and sold 354,620 and 250,000 shares of our common stock under the 2016 ATM Program, and received net proceeds of approximately \$15.5 million and \$9.0 million, during 2017 and 2016, respectively.

Dividends

We currently intend to retain our future earnings, if any, to finance the development and expansion of our business and, therefore, do not intend to pay cash dividends on our common stock for the foreseeable future. Any future determination to pay dividends will be at the discretion of our board of directors and will depend on our financial condition, results of operations, capital requirements, restrictions contained in any of our financing arrangements and such other factors as our board of directors may deem relevant. We have not previously declared or paid any cash dividends on our common stock.

Stock Performance Graph

This chart compares the cumulative total return on our common stock with that of the Standard & Poor’s 500 Companies Stock Index (the “S&P 500 Index”) and the Standard & Poor’s Homebuilders Select Industry Index (the “S&P Homebuilders Index”). The chart assumes \$100.00 was invested at the close of market on December 31, 2013 and assumes the reinvestment of any dividends. The stock price performance on the following graph is not necessarily indicative of future stock price performance.

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Comparison of Cumulative Total Return among LGI Homes, Inc. Common Stock, the S&P 500 Index, and the S&P Homebuilders Index for the years ended December 31, 2018, 2017, 2016, 2015 and 2014.

	12/31/2013	12/31/2014	12/31/2015	12/31/2016	12/31/2017	12/31/2018
LGIH	\$100.00	\$83.87	\$136.76	\$161.50	\$421.75	\$254.19
S&P 500 Index	\$100.00	\$111.39	\$110.58	\$121.13	\$144.65	\$135.63
S&P Homebuilders Index	\$100.00	\$102.52	\$102.71	\$101.78	\$132.97	\$97.65

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ITEM 6. SELECTED FINANCIAL DATA

The selected historical balance sheet and statement of operations information presented as of December 31, 2018, 2017, 2016, 2015 and 2014 and for the years then ended have been derived from our audited historical consolidated financial statements. The following table should be read together with, and is qualified in its entirety by reference to, our historical consolidated financial statements and the accompanying notes included elsewhere in this Annual Report. The table should also be read together with “Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

The following table presents our selected historical financial and operating data as of the dates and for the periods indicated.

	Year Ended December 31,				
	2018	2017	2016	2015	2014
	(dollars in thousands, except per share data and average home sales price)				
Statement of Operations Data:					
Revenues:					
Home sales revenues	\$ 1,504,400	\$ 1,257,960	\$ 838,320	\$ 630,236	\$ 383,268
Expenses:					
Cost of sales	1,124,484	937,540	616,707	463,304	280,481
Selling expenses	109,460	94,957	66,984	52,998	36,672
General and administrative	70,345	55,662	43,158	34,260	23,744
Operating income	200,111	169,801	111,471	79,674	42,371
Loss on extinguishment of debt	3,599	—	—	—	—
Other income, net	(2,586)	(1,601)	(2,201)	(606)	(708)
Net income before income taxes	199,098	171,402	113,672	80,280	43,079
Income tax provision	43,812	58,096	38,641	27,450	14,868
Net income	\$ 155,286	\$ 113,306	\$ 75,031	\$ 52,830	\$ 28,211
Basic earnings per share ⁽¹⁾	\$ 6.89	\$ 5.24	\$ 3.61	\$ 2.65	\$ 1.37
Diluted earnings per share ⁽¹⁾	\$ 6.24	\$ 4.73	\$ 3.41	\$ 2.44	\$ 1.33
Other Financial and Operating Data:					
Active communities at end of year	88	78	63	52	39
Home closings	6,512	5,845	4,163	3,404	2,356
Average sales price of homes closed	\$ 231,020	\$ 215,220	\$ 201,374	\$ 185,146	\$ 162,677
Gross margin ⁽²⁾	\$ 379,916	\$ 320,420	\$ 221,613	\$ 166,932	\$ 102,787
Gross margin % ⁽³⁾	25.3	% 25.5	% 26.4	% 26.5	% 26.8
Adjusted gross margin ⁽⁴⁾	\$ 405,635	\$ 338,066	\$ 232,778	\$ 175,120	\$ 108,111
Adjusted gross margin % ⁽³⁾⁽⁴⁾	27.0	% 26.9	% 27.8	% 27.8	% 28.2
EBITDA ⁽⁵⁾	\$ 224,120	\$ 189,593	\$ 125,441	\$ 87,221	\$ 45,445
EBITDA margin % ⁽³⁾⁽⁵⁾	14.9	% 15.1	% 15.0	% 13.8	% 11.9
Adjusted EBITDA ⁽⁵⁾	\$ 226,541	\$ 188,238	\$ 123,725	\$ 88,746	\$ 48,357
Adjusted EBITDA margin % ⁽³⁾⁽⁵⁾	15.1	% 15.0	% 14.8	% 14.1	% 12.6

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	December 31,				
	2018	2017	2016	2015	2014
Balance Sheet Data:	(in thousands)				
Cash and cash equivalents	\$46,624	\$67,571	\$49,518	\$37,568	\$31,370
Real estate inventory	\$1,228,256	\$918,933	\$717,681	\$531,228	\$367,908
Goodwill and intangibles	\$12,018	\$12,018	\$12,018	\$12,234	\$12,481
Total assets	\$1,395,473	\$1,079,892	\$814,514	\$618,702	\$434,289
Notes payable	\$653,734	\$475,195	\$400,483	\$304,561	\$212,261
Total liabilities	\$739,530	\$590,046	\$459,313	\$371,313	\$251,790
Total equity	\$655,943	\$489,846	\$355,201	\$247,389	\$182,499

Earnings per share is presented for the years ended December 31, 2018, 2017, 2016, 2015 and 2014. See Note 10

(1) “Equity” to our consolidated financial statements included in Part II, Item 8 of this Annual Report of this Form 10-K for calculation of earnings per share.

(2) Gross margin is home sales revenues less cost of sales.

(3) Calculated as a percentage of home sales revenues.

Adjusted gross margin is a non-GAAP financial measure used by management as a supplemental measure in evaluating operating performance. We define adjusted gross margin as gross margin less capitalized interest and adjustments resulting from the application of purchase accounting included in the cost of sales. Our management believes this information is useful because it isolates the impact that capitalized interest and purchase accounting adjustments have on gross margin. However, because adjusted gross margin information excludes capitalized

(4) interest and purchase accounting adjustments, which have real economic effects and could impact our results, the utility of adjusted gross margin information as a measure of our operating performance may be limited. In addition, other companies may not calculate adjusted gross margin information in the same manner that we do. Accordingly, adjusted gross margin information should be considered only as a supplement to gross margin information as a measure of our performance. Please see “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Non-GAAP Measures” for a reconciliation of adjusted gross margin to gross margin, which is the GAAP financial measure that our management believes to be most directly comparable.

(5) EBITDA and Adjusted EBITDA are non-GAAP financial measures used by management as supplemental measures in evaluating operating performance. We define EBITDA as net income before (i) interest expense, (ii) income taxes, (iii) depreciation and amortization and (iv) capitalized interest charged to the cost of sales. We define adjusted EBITDA as net income before (i) interest expense, (ii) income taxes, (iii) depreciation and amortization, (iv) capitalized interest charged to the cost of sales, (v) loss on extinguishment of debt, (vi) other income, net and (vii) adjustments resulting from the application of purchase accounting. Our management believes that the presentation of EBITDA and adjusted EBITDA provides useful information to investors regarding our results of operations because it assists both investors and management in analyzing and benchmarking the performance and value of our business. EBITDA and adjusted EBITDA provide indicators of general economic performance that are not affected by fluctuations in interest rates or effective tax rates, levels of depreciation or amortization and items considered to be unusual or non-recurring. Accordingly, our management believes that these measures are useful for comparing general operating performance from period to period. Other companies may define these measures differently and, as a result, our measures of EBITDA and adjusted EBITDA may not be directly comparable to the measures of other companies. Although we use EBITDA and adjusted EBITDA as financial measures to assess the performance of our business, the use of these measures is limited because they do not include certain material costs, such as interest and taxes, necessary to operate our business. EBITDA and Adjusted EBITDA should be considered in addition to, and not as a substitute for, net income in accordance with GAAP as a measure of performance. Our presentation of EBITDA and adjusted EBITDA should not be construed as an indication that our future results will be unaffected by unusual or non-recurring items. Our use of EBITDA and adjusted EBITDA is limited as an analytical tool, and you should not consider these measures in isolation or as substitutes for analysis of our results as reported under GAAP. Please see “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Non-GAAP Measures—Adjusted EBITDA” for reconciliations of

EBITDA and adjusted EBITDA to net income, which is the GAAP financial measure that our management believes to be most directly comparable.

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

For purposes of this Management's Discussion and Analysis of Financial Condition and Results of Operation, references to "we," "our," "us" or similar terms when used in a historical context refer to LGI Homes, Inc. and its subsidiaries.

Key Results

Key financial results as of and for the year ended December 31, 2018, as compared to the year ended December 31, 2017, were as follows:

• Home sales revenues increased 19.6% to \$1.5 billion from \$1.3 billion.

• Homes closed increased 11.4% to 6,512 homes from 5,845 homes.

• Average sales price of our homes increased \$15,800 to \$231,020 from \$215,220.

• Gross margin as a percentage of home sales revenues decreased to 25.3% from 25.5%.

• Adjusted gross margin (non-GAAP) as a percentage of home sales revenues increased to 27.0% from 26.9%.

• Net income before income taxes increased 16.2% to \$199.1 million from \$171.4 million.

• Net income increased 37.1% to \$155.3 million from \$113.3 million.

• EBITDA (non-GAAP) as a percentage of home sales revenues decreased to 14.9% from 15.1%.

• Adjusted EBITDA (non-GAAP) as a percentage of home sales revenues increased to 15.1% from 15.0%.

• Active communities at the end of 2018 increased to 88 from 78.

• Total owned and controlled lots increased 29.5% to 51,442 lots at December 31, 2018 from 39,709 lots at December 31, 2017.

For reconciliations of the non-GAAP financial measures of adjusted gross margin, EBITDA and adjusted EBITDA to the most directly comparable GAAP financial measures, please see "—Non-GAAP Measures."

Recent Developments

During November 2018, we announced that our Board of Directors (the "Board") authorized a stock repurchase program, pursuant to which we may purchase up to \$50.0 million of shares of our common stock through open market transactions, privately negotiated transactions or otherwise in accordance with applicable laws. For the year ended December 31, 2018, we repurchased 39,000 shares of our common stock for \$1.5 million to be held as treasury stock. During January 2019, the Board increased the authorized number of directors on the Board from six directors to seven directors and appointed Laura M. Miller to fill the newly created directorship.

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Results of Operations

The following table sets forth our results of operations for the periods indicated:

	Year Ended December 31,		
	2018	2017	2016
	(dollars in thousands, except per share data and average home sales price)		
Statement of Income Data:			
Home sales revenues	\$ 1,504,400	\$ 1,257,960	\$ 838,320
Expenses:			
Cost of sales	1,124,484	937,540	616,707
Selling expenses	109,460	94,957	66,984
General and administrative	70,345	55,662	43,158
Operating income	200,111	169,801	111,471
Loss on extinguishment of debt	3,599	—	—
Other income, net	(2,586)	(1,601)	(2,201)
Net income before income taxes	199,098	171,402	113,672
Income tax provision	43,812	58,096	38,641
Net income	\$ 155,286	\$ 113,306	\$ 75,031
Basic earnings per share	\$ 6.89	\$ 5.24	\$ 3.61
Diluted earnings per share	\$ 6.24	\$ 4.73	\$ 3.41
Other Financial and Operating Data:			
Active communities at end of year	88	78	63
Home closings	6,512	5,845	4,163
Average sales price of homes closed	\$ 231,020	\$ 215,220	\$ 201,374
Gross margin ⁽¹⁾	\$ 379,916	\$ 320,420	\$ 221,613
Gross margin % ⁽²⁾	25.3	% 25.5	% 26.4
Adjusted gross margin ⁽³⁾	\$ 405,635	\$ 338,066	\$ 232,778
Adjusted gross margin % ⁽²⁾⁽³⁾	27.0	% 26.9	% 27.8
EBITDA ⁽⁴⁾	\$ 224,120	\$ 189,593	\$ 125,441
EBITDA margin % ⁽²⁾⁽⁴⁾	14.9	% 15.1	% 15.0
Adjusted EBITDA ⁽⁴⁾	\$ 226,541	\$ 188,238	\$ 123,725
Adjusted EBITDA margin % ⁽²⁾⁽⁴⁾	15.1	% 15.0	% 14.8

(1) Gross margin is home sales revenues less cost of sales.

(2) Calculated as a percentage of home sales revenues.

Adjusted gross margin is a non-GAAP financial measure used by management as a supplemental measure in evaluating operating performance. We define adjusted gross margin as gross margin less capitalized interest and adjustments resulting from the application of purchase accounting included in the cost of sales. Our management believes this information is useful because it isolates the impact that capitalized interest and purchase accounting adjustments have on gross margin. However, because adjusted gross margin information excludes capitalized interest and purchase accounting adjustments, which have real economic effects and could impact our results, the utility of adjusted gross margin information as a measure of our operating performance may be limited. In addition, other companies may not calculate adjusted gross margin information in the same manner that we do. Accordingly, adjusted gross margin information should be considered only as a supplement to gross margin information as a measure of our performance. Please see “—Non-GAAP Measures” for a reconciliation of adjusted gross margin to gross margin, which is the GAAP financial measure that our management believes to be most directly comparable.

(4) EBITDA and adjusted EBITDA are non-GAAP financial measures used by management as supplemental measures in evaluating operating performance. We define EBITDA as net income before (i) interest expense, (ii) income taxes, (iii) depreciation and amortization and (iv) capitalized interest charged to the cost of sales. We define

adjusted EBITDA as net income before (i) interest expense, (ii) income taxes, (iii) depreciation and amortization, (iv) capitalized interest charged to the cost of sales, (v) loss on extinguishment of debt, (vi) other income, net and (vii) adjustments resulting from the application of purchase accounting. Our management believes that the presentation of EBITDA and adjusted EBITDA provides useful information to investors regarding our results of operations because it assists both investors and management in analyzing and benchmarking the performance and value of our business. EBITDA and adjusted EBITDA provide indicators of general economic performance that are not affected by fluctuations in interest rates or effective tax rates, levels of depreciation or amortization and items considered to be unusual or non-recurring. Accordingly, our management believes that

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these measures are useful for comparing general operating performance from period to period. Other companies may define these measures differently and, as a result, our measures of EBITDA and adjusted EBITDA may not be directly comparable to the measures of other companies. Although we use EBITDA and adjusted EBITDA as financial measures to assess the performance of our business, the use of these measures is limited because they do not include certain material costs, such as interest and taxes, necessary to operate our business. EBITDA and adjusted EBITDA should be considered in addition to, and not as a substitute for, net income in accordance with GAAP as a measure of performance. Our presentation of EBITDA and adjusted EBITDA should not be construed as an indication that our future results will be unaffected by unusual or non-recurring items. Our use of EBITDA and adjusted EBITDA is limited as an analytical tool, and you should not consider these measures in isolation or as substitutes for analysis of our results as reported under GAAP. Please see “—Non-GAAP Measures” for reconciliations of EBITDA and adjusted EBITDA to net income, which is the GAAP financial measure that our management believes to be most directly comparable.

Year Ended December 31, 2018 Compared to Year Ended December 31, 2017

Homes Sales. Our home sales revenues, home closings, average sales price (ASP), and ending community count by reportable segment for the years ended December 31, 2018 and 2017 were as follows (Revenues in thousands):

Year Ended December 31, 2018

	Revenues	Home Closings	ASP	Average Community Count	Average Monthly Absorption Rate
Central	\$623,751	2,937	\$212,377	30.7	8.0
Northwest	277,567	760	365,220	10.3	6.1
Southeast	271,073	1,324	204,738	18.7	5.9
Florida	180,950	864	209,433	11.6	6.2
West	151,059	627	240,923	9.3	5.6
Total	\$1,504,400	6,512	\$231,020	80.6	6.7

Year Ended December 31, 2017

	Revenues	Home Closings	ASP	Average Community Count	Average Monthly Absorption Rate
Central	\$533,254	2,616	\$203,843	26.2	8.3
Northwest	215,421	629	342,482	10.3	5.1
Southeast	183,422	973	188,512	15.0	5.4
Florida	199,733	1,014	196,975	11.5	7.3
West	126,130	613	205,759	10.1	5.1
Total	\$1,257,960	5,845	\$215,220	73.1	6.7

At
December
31,

Community count	2018	2017
Central	32	29
Northwest	11	11
Southeast	21	17
Florida	14	11
West	10	10
Total community count	88	78

Home sales revenues for the year ended December 31, 2018 were \$1,504.4 million, an increase of \$246.4 million, or 19.6%, from \$1,258.0 million for the year ended December 31, 2017. The increase in home sales revenues is primarily due to a 11.4% increase in homes closed and an increase in the average selling price per home during the year ended December 31, 2018 as compared to the year ended December 31, 2017. We closed 6,512 homes during 2018, as compared to 5,845 homes closed during 2017. This increase in home closings was largely due to the increase in the number of active communities in 2018. The average

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selling price per home closed during the year ended December 31, 2018 was \$231,020, an increase of \$15,800, or 7.3%, from the average selling price per home of \$215,220 for the year ended December 31, 2017. This increase in the average selling price per home was primarily due to changes in product mix, higher price points in certain new markets and a favorable pricing environment.

We continued to diversify our operations outside of our Central division during 2018. We increased our home sales revenues in our divisions other than our Central division by \$155.9 million during the year ended December 31, 2018 as compared to the year ended December 31, 2017 representing a 10.7% increase in the number of homes closed in these divisions during 2018 as compared to 2017. Our active selling communities at December 31, 2018 increased to 88 from 78 at December 31, 2017. Seven of the ten active selling communities added during 2018 were outside of our Central division, contributing to the further geographic diversification of our business.

Cost of Sales and Gross Margin (home sales revenues less cost of sales). Cost of sales increased for the year ended December 31, 2018 to \$1,124.5 million, an increase of \$186.9 million, or 19.9%, from \$937.5 million for the year ended December 31, 2017. This increase is primarily due to a 11.4% increase in homes closed during 2018 as compared to 2017 and, to a lesser degree, product mix. The increase in average cost of sales per home is primarily due to changes in construction costs associated with product mix and lot costs. Gross margin for the year ended December 31, 2018 was \$379.9 million, an increase of \$59.5 million, or 18.6%, from \$320.4 million for the year ended December 31, 2017. Gross margin as a percentage of home sales revenues was 25.3% for the year ended December 31, 2018 and 25.5% for the year ended December 31, 2017. This decrease in gross margin as a percentage of home sales revenues is primarily due to a combination of higher construction costs and lot costs partially offset by higher average home sales price for the year ended December 31, 2018 as compared to the year ended December 31, 2017 and, to a lesser extent, to 466 wholesale home closings during 2018, compared to 201 wholesale home closings during 2017.

Selling Expenses. Selling expenses for the year ended December 31, 2018 were \$109.5 million, an increase of \$14.5 million, or 15.3%, from \$95.0 million for the year ended December 31, 2017. Sales commissions increased to \$57.3 million for the year ended December 31, 2018 from \$50.2 million during 2017 largely due to a 19.6% increase in home sales revenues during 2018 as compared to 2017. Selling expenses as a percentage of home sales revenues were 7.3% and 7.5% for the years ended December 31, 2018 and 2017, respectively, and generally reflect operating leverage realized relating to advertising costs.

General and Administrative. General and administrative expenses for the year ended December 31, 2018 were \$70.3 million, an increase of \$14.7 million, or 26.4%, from \$55.7 million for the year ended December 31, 2017. The increase in the amount of general and administrative expenses is primarily due to additional general and administrative compensation costs associated with an increase of active communities and home closings during 2018 as compared to 2017. General and administrative expenses as a percentage of home sales revenues were 4.7% and 4.4% for the years ended December 31, 2018 and 2017, respectively. The increase in general and administrative expenses as a percentage of home sales revenues reflects additional costs realized from the increase in community count and one-time acquisition related transaction expenses associated with the Wynn Homes acquisition during the year ended December 31, 2018 as compared to the year ended December 31, 2017.

Loss on extinguishment of debt. Loss on extinguishment of debt for the year ended December 31, 2018 was \$3.6 million, due to debt issuance costs previously capitalized that were associated with the Credit Agreement. There was no loss on extinguishment of debt for the year ended December 31, 2017.

Operating Income, Net Income before Income Taxes, and Net Income. Operating income for the year ended December 31, 2018 was \$200.1 million, an increase of \$30.3 million, or 17.9%, from \$169.8 million for the year ended December 31, 2017. Net income before income taxes for the year ended December 31, 2018 was \$199.1 million, an increase of \$27.7 million, or 16.2%, over the year ended December 31, 2017. Our reportable segments contributed the following amounts and percentages of net income before income taxes during 2018: Central - \$104.6 million or 52.5%; Northwest - \$40.9 million or 20.5%; Florida - \$21.3 million or 10.7%; Southeast - \$29.1 million or 14.6%; and West - \$13.6 million or 6.8%. Net income for the year ended December 31, 2018 was \$155.3 million, an increase of \$42.0 million, or 37.1%, from \$113.3 million for the year ended December 31, 2017. The increases are primarily attributed to a 11.4% increase in homes closed, a higher average sales price per home, and a decrease in the

effective tax rate realized during 2018 as compared to 2017.

Year Ended December 31, 2017 Compared to the Year Ended December 31, 2016

Homes Sales. Our home sales revenues, home closings, average sales price (ASP), and ending community count by reportable segment for the years ended December 31, 2017 and 2016 were as follows (Revenues in thousands):

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Year Ended December 31, 2017

	Revenues	Home Closings	ASP	Average Community Count	Average Monthly Absorption Rate
Central	\$533,254	2,616	\$203,843	26.2	8.3
Northwest	215,421	629	342,482	10.3	5.1
Southeast	183,422	973	188,512	15.0	5.4
Florida	199,733	1,014	196,975	11.5	7.3
West	126,130	613	205,759	10.1	5.1
Total	\$1,257,960	5,845	\$215,220	73.1	6.7

Year Ended December 31, 2016

	Revenues	Home Closings	ASP	Average Community Count	Average Monthly Absorption Rate
Central	\$429,505	2,143	\$200,422	22.9	7.8
Northwest	86,496	270	320,356	6.3	3.6
Southeast	111,651	635	175,828	10.3	5.2
Florida	115,276	595	193,741	9.4	5.3
West	95,392	520	183,446	9.0	4.8
Total	\$838,320	4,163	\$201,374	57.9	6.0

At
December
31,

Community count	2017	2016
Central	29	24
Northwest	11	9
Southeast	17	11
Florida	11	10
West	10	9
Total community count	78	63

Home sales revenues for the year ended December 31, 2017 were \$1,258.0 million, an increase of \$419.6 million, or 50.1%, from \$838.3 million for the year ended December 31, 2016. The increase in home sales revenues is primarily due to a 40.4% increase in homes closed and an increase in the average selling price per home during the year ended December 31, 2017 as compared to the year ended December 31, 2016. We closed 5,845 homes during 2017, as compared to 4,163 homes closed during 2016. This increase in home closings was largely due to the increase in the number of active communities in 2017. The average selling price per home closed during the year ended December 31, 2017 was \$215,220, an increase of \$13,846, or 6.9%, from the average selling price per home of \$201,374 for the year ended December 31, 2016. This increase in the average selling price per home was primarily due to changes in product mix, higher price points in certain new markets and a favorable pricing environment. We continued to diversify our operations outside of our Central division during 2017. We increased our home sales revenues in our divisions other than our Central division by \$315.9 million during the year ended December 31, 2017 as compared to the year ended December 31, 2016 representing a 59.9% increase in the number of homes closed in these divisions during 2017 as compared to 2016. Our active selling communities at December 31, 2017 increased to 78 from 63 at December 31, 2016. Ten of the fifteen active selling communities added during 2017 were outside of our Central division, contributing to the further geographic diversification of our business.

Cost of Sales and Gross Margin (home sales revenues less cost of sales). Cost of sales increased for the year ended December 31, 2017 to \$937.5 million, an increase of \$320.8 million, or 52.0%, from \$616.7 million for the year ended

December 31, 2016. This increase is primarily due to a 40.4% increase in homes closed during 2017 as compared to 2016 and, to a lesser degree, product mix. The increase in average cost of sales per home is primarily due to changes in construction costs associated with product mix and lot costs. Gross margin for the year ended December 31, 2017 was \$320.4 million, an increase of \$98.8 million, or 44.6%, from \$221.6 million for the year ended December 31, 2016. Gross margin as a percentage of home sales revenues was

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25.5% for the year ended December 31, 2017 and 26.4% for the year ended December 31, 2016. This decrease in gross margin as a percentage of home sales revenues is primarily due to a combination of higher construction costs and lot costs partially offset by higher average home sales price for the year ended December 31, 2017 as compared to the year ended December 31, 2016 and, to a lesser extent, to 201 wholesale home closings during 2017 compared to no wholesale home closings during 2016.

Selling Expenses. Selling expenses for the year ended December 31, 2017 were \$95.0 million, an increase of \$28.0 million, or 41.8%, from \$67.0 million for the year ended December 31, 2016. Sales commissions increased to \$50.2 million for the year ended December 31, 2017 from \$31.1 million during 2016 largely due to a 50.1% increase in home sales revenues during 2017 as compared to 2016. Selling expenses as a percentage of home sales revenues were 7.5% and 8.0% for the years ended December 31, 2017 and 2016, respectively, and generally reflect operating leverage realized relating to advertising costs.

General and Administrative. General and administrative expenses for the year ended December 31, 2017 were \$55.7 million, an increase of \$12.5 million, or 29.0%, from \$43.2 million for the year ended December 31, 2016. The increase in the amount of general and administrative expenses is primarily due to additional general and administrative compensation costs associated with an increase of active communities and home closings during 2017 as compared to 2016. General and administrative expenses as a percentage of home sales revenues were 4.4% and 5.1% for the years ended December 31, 2017 and 2016, respectively. The decrease in general and administrative expenses as a percentage of home sales revenues reflects leverage realized from the increase in home sales revenues during 2017 as compared to 2016.

Operating Income, Net Income before Income Taxes, and Net Income. Operating income for the year ended December 31, 2017 was \$169.8 million, an increase of \$58.3 million, or 52.3%, from \$111.5 million for the year ended December 31, 2016. Net income before income taxes for the year ended December 31, 2017 was \$171.4 million, an increase of \$57.7 million, or 50.8%, over the year ended December 31, 2016. Our reportable segments contributed the following amounts and percentages of net income before income taxes during 2017: Central - \$89.1 million or 52.0%; Northwest - \$34.2 million or 20.0%; Florida - \$25.7 million or 15.0%; Southeast - \$20.0 million or 11.6%; and West - \$5.9 million or 3.4%. Net income for the year ended December 31, 2017 was \$113.3 million, an increase of \$38.3 million, or 51.0%, from \$75.0 million for the year ended December 31, 2016. The increases are primarily attributed to a 40.4% increase in homes closed, a higher average sales price and improved leverage realized during 2017 as compared to 2016.

Non-GAAP Measures

In addition to the results reported in accordance with U.S. GAAP, we have provided information in this Annual Report on Form 10-K relating to adjusted gross margin, EBITDA and adjusted EBITDA.

Adjusted gross margin is a non-GAAP financial measure used by management as a supplemental measure in evaluating operating performance. We define adjusted gross margin as gross margin less capitalized interest and adjustments resulting from the application of purchase accounting included in the cost of sales. Our management believes this information is useful because it isolates the impact that capitalized interest and purchase accounting adjustments have on gross margin. However, because adjusted gross margin information excludes capitalized interest and purchase accounting adjustments, which have real economic effects and could impact our results, the utility of adjusted gross margin information as a measure of our operating performance may be limited. In addition, other companies may not calculate adjusted gross margin information in the same manner that we do. Accordingly, adjusted gross margin information should be considered only as a supplement to gross margin information as a measure of our performance.

The following table reconciles adjusted gross margin to gross margin, which is the GAAP financial measure that our management believes to be most directly comparable (dollars in thousands):

	Year Ended December 31,		
	2018	2017	2016
Home sales revenues	\$1,504,400	\$1,257,960	\$838,320
Cost of sales	1,124,484	937,540	616,707

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Gross margin	379,916	320,420	221,613	
Capitalized interest charged to cost of sales	24,311	17,400	10,680	
Purchase accounting adjustments ^(a)	1,408	246	485	
Adjusted gross margin	\$405,635	\$338,066	\$232,778	
Gross margin % ^(b)	25.3	% 25.5	% 26.4	%
Adjusted gross margin % ^(b)	27.0	% 26.9	% 27.8	%

(a) Adjustments result from the application of purchase accounting for acquisitions and represent the amount of the fair value step-up adjustments included in cost of sales for real estate inventory sold after the acquisition dates.

(b) Calculated as a percentage of home sales revenues.

EBITDA and Adjusted EBITDA

EBITDA and adjusted EBITDA are non-GAAP financial measures used by management as supplemental measures in evaluating operating performance. We define EBITDA as net income before (i) interest expense, (ii) income taxes, (iii) depreciation and amortization and (iv) capitalized interest charged to the cost of sales. We define adjusted EBITDA as net income before (i) interest expense, (ii) income taxes, (iii) depreciation and amortization, (iv) capitalized interest charged to the cost of sales, (v) loss on extinguishment of debt, (vi) other income, net and (vii) adjustments resulting from the application of purchase accounting included in the cost of sales. Our management believes that the presentation of EBITDA and adjusted EBITDA provides useful information to investors regarding our results of operations because it assists both investors and management in analyzing and benchmarking the performance and value of our business. EBITDA and adjusted EBITDA provide indicators of general economic

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performance that are not affected by fluctuations in interest rates or effective tax rates, levels of depreciation or amortization and items considered to be unusual or non-recurring. Accordingly, our management believes that these measures are useful for comparing general operating performance from period to period. Other companies may define these measures differently and, as a result, our measures of EBITDA and adjusted EBITDA may not be directly comparable to the measures of other companies. Although we use EBITDA and adjusted EBITDA as financial measures to assess the performance of our business, the use of these measures is limited because they do not include certain material costs, such as interest and taxes, necessary to operate our business. EBITDA and adjusted EBITDA should be considered in addition to, and not as a substitute for, net income in accordance with GAAP as a measure of performance. Our presentation of EBITDA and adjusted EBITDA should not be construed as an indication that our future results will be unaffected by unusual or non-recurring items. Our use of EBITDA and adjusted EBITDA is limited as an analytical tool, and you should not consider these measures in isolation or as substitutes for analysis of our results as reported under GAAP. Some of these limitations are:

- (i) they do not reflect every cash expenditure, future requirements for capital expenditures or contractual commitments, including for purchase of land;
- (ii) they do not reflect the interest expense or the cash requirements necessary to service interest or principal payments on our debt;
- (iii) although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will often have to be replaced or require improvements in the future, and EBITDA and adjusted EBITDA do not reflect any cash requirements for such replacements or improvements;
- (iv) they are not adjusted for all non-cash income or expense items that are reflected in our statements of cash flows;
- (v) they do not reflect the impact of earnings or charges resulting from matters we consider not to be indicative of our ongoing operations; and
- (vi) other companies in our industry may calculate them differently than we do, limiting their usefulness as a comparative measure.

Because of these limitations, our EBITDA and adjusted EBITDA should not be considered as measures of discretionary cash available to us to invest in the growth of our business or as measures of cash that will be available to us to meet our obligations. We compensate for these limitations by using our EBITDA and adjusted EBITDA along with other comparative tools, together with GAAP measures, to assist in the evaluation of operating performance. These GAAP measures include operating income, net income and cash flow data. We have significant uses of cash flows, including capital expenditures, interest payments and other non-recurring charges, which are not reflected in our EBITDA or adjusted EBITDA. EBITDA and adjusted EBITDA are not intended as alternatives to net income as indicators of our operating performance, as alternatives to any other measure of performance in conformity with GAAP or as alternatives to cash flows as a measure of liquidity. You should therefore not place undue reliance on our EBITDA or adjusted EBITDA calculated using these measures.

The following table reconciles EBITDA and adjusted EBITDA to net income, which is the GAAP measure that our management believes to be most directly comparable (dollars in thousands):

	Year Ended December 31,			
	2018	2017	2016	
Net income	\$155,286	\$113,306	\$75,031	
Income taxes	43,812	58,096	38,641	
Depreciation and amortization	711	791	1,089	
Capitalized interest charged to cost of sales	24,311	17,400	10,680	
EBITDA	224,120	189,593	125,441	
Purchase accounting adjustments ⁽¹⁾	1,408	246	485	
Loss on extinguishment of debt	3,599	—	—	
Other income, net	(2,586)	(1,601)	(2,201)	
Adjusted EBITDA	\$226,541	\$188,238	\$123,725	
EBITDA margin % ⁽²⁾	14.9	% 15.1	% 15.0	%
Adjusted EBITDA margin % ⁽²⁾	15.1	% 15.0	% 14.8	%

- (1) Adjustments result from the application of purchase accounting related to prior acquisitions and represent the amount of the fair value step-up adjustments for real estate inventory included in cost of sales.
- (2) Calculated as a percentage of home sales revenues.

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Backlog

We sell our homes under standard purchase contracts, which generally require a homebuyer to pay a deposit at the time of signing the purchase contract. The amount of the required deposit is minimal (generally \$1,000 or less). The deposits are refundable if the retail homebuyer is unable to obtain mortgage financing. We permit our retail homebuyers to cancel the purchase contract and obtain a refund of their deposit in the event mortgage financing cannot be obtained within a certain period of time, as specified in their purchase contract. Typically, our retail homebuyers provide documentation regarding their ability to obtain mortgage financing within 14 days after the purchase contract is signed. If we determine that the homebuyer is not qualified to obtain mortgage financing or is not otherwise financially able to purchase the home, we will terminate the purchase contract. If a purchase contract has not been cancelled or terminated within 14 days after the purchase contract has been signed, then the homebuyer has met the preliminary criteria to obtain mortgage financing. Only purchase contracts that are signed by homebuyers who have met the preliminary criteria to obtain mortgage financing are included in new (gross) orders.

Our “backlog” consists of homes that are under a purchase contract that has been signed by homebuyers who have met the preliminary criteria to obtain mortgage financing but have not yet closed and wholesale contracts for which the required deposit has been made. Since our business model is generally based on building move-in ready homes before a purchase contract is signed, the majority of our homes in backlog are currently under construction or complete. Ending backlog represents the number of homes in backlog from the previous period plus the number of net orders (new orders for homes less cancellations) generated during the current period minus the number of homes closed during the current period. Our backlog at any given time will be affected by cancellations, the number of our active communities and the timing of home closings. Homes in backlog are generally closed within one to two months, although we may experience cancellations of purchase contracts at any time prior to closing. It is important to note that net orders, backlog and cancellation metrics are operational, rather than accounting data, and should be used only as a general gauge to evaluate performance. Backlog may be impacted by customer cancellations for various reasons that are beyond our control, and in light of our minimal required deposit, there is little negative impact to the potential homebuyer from the cancellation of the purchase contract.

As of the dates set forth below, our net orders, cancellation rate, and ending backlog homes and value were as follows (dollars in thousands):

Backlog Data	Year Ended December 31,			
	2018 ⁽⁴⁾	2017 ⁽⁵⁾	2016 ⁽⁶⁾	
Net orders ⁽¹⁾	6,320	6,215	4,086	
Cancellation rate ⁽²⁾	24.2	% 25.4	% 24.5	%
Ending backlog - homes ⁽³⁾	624	816	446	
Ending backlog - value ⁽³⁾	\$156,109	\$191,831	\$96,940	

(1) Net orders are new (gross) orders for the purchase of homes during the period, less cancellations of existing purchase contracts during the period.

(2) Cancellation rate for a period is the total number of purchase contracts cancelled during the period divided by the total new (gross) orders for the purchase of homes during the period.

(3) Ending backlog consists of homes at the end of the period that are under a purchase contract that has been signed by homebuyers who have met our preliminary financing criteria but have not yet closed and wholesale contracts for which the required deposit has been made. Ending backlog is valued at the contract amount.

(4) 92 units and values related to bulk sales agreements are not included in the table above.

(5) 106 units and values related to bulk sales agreements are not included in the table above.

(6) 156 units and values related to a bulk sales agreement are not included in the table above.

Land Acquisition Policies and Development

See discussion included in “Business—Land Acquisition Policies and Development.”

Homes in Inventory

See discussion included in “Business—Homes in Inventory.”

Raw Materials

See discussion included in “Business—Raw Materials and Labor.”

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Seasonality

In all of our divisions, we have historically experienced similar variability in our results of operations and in capital requirements from quarter to quarter due to the seasonal nature of the homebuilding industry. We generally close more homes in our second, third and fourth quarters. Thus, our revenue may fluctuate on a quarterly basis and we may have higher capital requirements in our second, third and fourth quarters in order to maintain our inventory levels. Our revenue and capital requirements are generally similar across our second, third and fourth quarters.

As a result of seasonal activity, our quarterly results of operations and financial position at the end of a particular quarter, especially the first quarter, are not necessarily representative of the results we expect at year end. We expect this seasonal pattern to continue in the long term.

Liquidity and Capital Resources

Overview

As of December 31, 2018, we had \$46.6 million of cash and cash equivalents. Cash flows for each of our active communities depend on the status of the development cycle and can differ substantially from reported earnings. Early stages of development or expansion require significant cash outlays for land acquisitions, land development, plats, vertical development, construction of information centers, general landscaping and other amenities. Because these costs are a component of our inventory and are not recognized in our statement of operations until a home closes, we incur significant cash outflows prior to recognition of home sales revenues. In the later stages of an active community, cash inflows may exceed home sales revenues reported for financial statement purposes, as the costs associated with home and land construction were previously incurred.

Our principal uses of capital are operating expenses, land and lot purchases, lot development, home construction, interest costs on our indebtedness and the payment of various liabilities. In addition, we may purchase land, lots, homes under construction or other assets as part of a business combination.

We generally rely on our ability to finance our operations by generating operating cash flows, borrowing under the Credit Facility or the issuance and sale of shares of our common stock. As needed, we will consider accessing the debt and equity capital markets as part of our ongoing financing strategy. We also rely on our ability to obtain performance, payment and completion surety bonds as well as letters of credit to finance our projects.

On August 24, 2018, we and certain of our subsidiaries filed an automatic shelf registration statement on Form S-3 (Registration No. 333-227012), registering the offering and sale of an indeterminate amount of debt securities, guarantees of debt securities, preferred stock, common stock, warrants, depositary shares, purchase contracts and units that include any of these securities. Under the shelf registration statement, we have the ability to access the debt and equity capital markets as needed as part of our ongoing financing strategy.

We believe that we will be able to fund our current and foreseeable liquidity needs for at least the next twelve months with our cash on hand, cash generated from operations, and cash expected to be available from the Credit Facility or through accessing debt or equity capital, as needed.

Revolving Credit Facility

On May 25, 2018, we entered into that certain Third Amended and Restated Credit Agreement with several financial institutions, and Wells Fargo Bank, National Association, as administrative agent, which was amended as of June 19, 2018 by that certain First Amendment thereto (the “First Amendment”; such credit agreement, as amended by the First Amendment, the “Credit Agreement”). The Credit Agreement has substantially similar terms and provisions to our second amended and restated credit agreement entered into in May 2017 with several financial institutions, and Wells Fargo Bank, National Association, as administrative agent (the “2017 Credit Agreement”) but, among other things, provided for, a revolving credit facility of \$450.0 million, which could be increased at our request by up to \$50.0 million if the lenders make additional commitments, subject to the terms and conditions of the Credit Agreement (which was requested and approved in October 2018). On October 18, 2018, we entered into a Lender Acknowledgement Agreement with certain lenders and Wells Fargo Bank, National Association, as administrative agent, whereby the aggregate revolving commitments under the Credit Agreement increased by \$50.0 million from \$450.0 million to \$500.0 million in accordance with the relevant provisions of the Credit Agreement.

The Credit Agreement matures on May 31, 2021. Before each anniversary of the closing of the Credit Agreement, we may request a one-year extension of the maturity date. The Credit Agreement is guaranteed by each of our subsidiaries

that have gross assets equal to or greater than \$0.5 million. The revolving credit facility is currently unsecured, but we have agreed to provide collateral if we fail to meet certain financial conditions in the future. As of December 31, 2018, the borrowing base under the Credit Agreement was \$695.2 million, of which borrowings, including the Convertible Notes (as defined below) and the Senior Notes (as defined below), of \$663.8 million were outstanding, \$5.1 million of letters of credit were outstanding and \$26.3 million was available to borrow under the Credit Agreement.

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The Credit Agreement requires us to maintain (i) a tangible net worth of not less than \$400.0 million plus 75% of the net proceeds of all equity issuances plus 50% of the amount of our positive net income in any fiscal quarter after December 31, 2017, (ii) a leverage ratio of not greater than 64.0%, (iii) liquidity of at least \$50.0 million and (iv) a ratio of EBITDA to interest expense for the most recent four quarters of at least 2.50 to 1.00. The Credit Agreement contains various covenants that, among other restrictions, limit the amount of our additional debt and our ability to make certain investments. At December 31, 2018, we were in compliance with all of the covenants contained in the Credit Agreement.

In connection with the issuance of our 6.875% Senior Notes due 2026 (the “Senior Notes”) in July 2018, we reduced the revolving commitment under the Credit Agreement from \$750.0 million to \$450.0 million pursuant to the First Amendment. During the year ended December 31, 2018, we recognized on our consolidated statements of operations \$3.4 million in debt extinguishment costs related to the Credit Agreement.

Senior Notes Offering

On July 6, 2018, we issued \$300.0 million aggregate principal amount of the Senior Notes in an offering to persons reasonably believed to be qualified institutional buyers in the United States pursuant to Rule 144A under the Securities Act of 1933, as amended (the “Securities Act”), and to certain non-U.S. persons in transactions outside the United States pursuant to Regulation S under the Securities Act. Interest on the Senior Notes accrues at a rate of 6.875% per annum, payable semi-annually in arrears on January 15 and July 15 of each year, commencing on January 15, 2019, and the Senior Notes mature on July 15, 2026. Terms of the Senior Notes are governed by an indenture and supplemental indenture, each dated as of July 6, 2018, among us, our subsidiaries that guarantee our obligations under the Credit Agreement (the “Subsidiary Guarantors”) and Wilmington Trust, National Association, as trustee.

We received net proceeds from the offering of the Senior Notes of approximately \$296.2 million, after deducting the initial purchasers’ discounts and commissions and offering expenses. The net proceeds from the offering were used to repay a portion of the borrowings under the Credit Agreement.

Convertible Notes

In November 2014, we issued \$85.0 million aggregate principal amount of our 4.25% Convertible Notes due 2019 (the “Convertible Notes”) pursuant to an exemption from the registration requirements afforded by Section 4(a)(2) of the Securities Act. The Convertible Notes mature on November 15, 2019 and bear interest at a rate of 4.25%, payable semi-annually in arrears on May 15 and November 15 of each year.

Prior to May 15, 2019, the Convertible Notes are convertible only upon satisfaction of any of the specified conversion events. On or after May 15, 2019 until the close of business on November 14, 2019 (the business day immediately preceding the stated maturity date of the Convertible Notes), the holders of Convertible Notes can convert their Convertible Notes at any time at their option. Upon the election of a holder of Convertible Notes to convert their Convertible Notes, we may settle the conversion of the Convertible Notes using any combination of cash and shares of our common stock. It is our intent, and belief that we have the ability, to settle in cash the conversion of any Convertible Notes that the holders elect to convert. The initial conversion rate of the Convertible Notes is 46.4792 shares of our common stock for each \$1,000 principal amount of Convertible Notes, which represents an initial conversion price of approximately \$21.52 per share of our common stock. The conversion rate is subject to adjustments upon the occurrence of certain specified events.

During the fourth quarter of 2017, we received notice from holders of \$15.0 million principal amount of the Convertible Notes to convert their Convertible Notes. The conversion of such Convertible Notes was settled in the first quarter of 2018, resulting in the issuance of 486,679 shares of our common stock, a \$0.6 million reduction to debt discount and additional paid in capital, a \$0.2 million loss on the extinguishment of debt and a cash payment of \$15.0 million for the principal amount of such Convertible Notes. As of December 31, 2018, we have \$70.0 million aggregate principal amount of Convertible Notes outstanding.

During the fourth quarter of 2018, the Convertible Notes were convertible because the closing sale price of our common stock was greater than 130% of the \$21.52 conversion price on at least 20 trading days during the 30 trading day period ending on September 30, 2018. As a result, the holders of the Convertible Notes could elect to convert some or all of their Convertible Notes in accordance with the terms and provisions of the indenture governing the Convertible Notes during the conversion period of October 1, 2018 through December 31, 2018 (inclusive). The

Convertible Notes continue to be convertible during the first quarter of 2019. As of the date of the filing of this Annual Report on Form 10-K, no other conversion notices have been received by us.

On July 6, 2018, concurrently with the offering of the Senior Notes, we entered into that certain First Supplemental Indenture, dated as of July 6, 2018, among us, the Subsidiary Guarantors and Wilmington Trust, National Association, as trustee, which supplements the indenture governing the Convertible Notes, pursuant to which (i) the subordination provisions in the indenture governing the Convertible Notes were eliminated, (ii) each Subsidiary Guarantor agreed (A) to, concurrently with the issuance of the Senior Notes, fully and unconditionally guarantee the Convertible Notes to the same extent that such Subsidiary Guarantor is

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guaranteeing the Senior Notes and (B) that such Subsidiary Guarantor's guarantee of the Convertible Notes ranks equally with such Subsidiary Guarantor's guarantee of the Senior Notes and (iii) the Company agreed to not, directly or indirectly, incur any indebtedness in the form of, or otherwise become liable in respect of, any notes or other debt securities issued pursuant to an indenture or note purchase agreement (including the Senior Notes) unless such indebtedness is equal with or contractually subordinated to the Convertible Notes in right of payment.

Letters of Credit, Surety Bonds and Financial Guarantees

We are often required to provide letters of credit and surety bonds to secure our performance under construction contracts, development agreements and other arrangements. The amount of such obligations outstanding at any time varies in accordance with our pending development activities. In the event any such bonds or letters of credit are drawn upon, we would be obligated to reimburse the issuer of such bonds or letters of credit.

Under these letters of credit, surety bonds and financial guarantees, we are committed to perform certain development and construction activities and provide certain guarantees in the normal course of business. Outstanding letters of credit, surety bonds and financial guarantees under these arrangements, totaled \$77.5 million as of December 31, 2018. Although significant development and construction activities have been completed related to the improvements at these sites, the letters of credit and surety bonds are not generally released until all development and construction activities are completed. We do not believe that it is probable that any outstanding letters of credit, surety bonds or financial guarantees as of December 31, 2018 will be drawn upon.

Cash Flows

Year Ended December 31, 2018 compared to Year Ended December 31, 2017

Net cash used in operating activities during the year ended December 31, 2018 was \$116.7 million as compared to \$68.5 million during the year ended December 31, 2017. The \$48.3 million increase in net cash used in operating activities was primarily attributable to cash outlays for the \$34.1 million increase in the net change in real estate inventory year-over-year, which was primarily related to our increased community count, additional homes under construction and land acquisitions, and to the \$88.9 million decrease in accounts payable, accrued expenses, and other liabilities, and the payment of income taxes. Year-over-year change in net cash provided by working capital items included a \$29.5 million decrease in accounts receivable and a \$7.2 million decrease in other assets, offset by a \$10.6 million increase in cash paid for pre-acquisition costs and deposits year-over-year. The increase in cash used in operating activities reflects our continued growth and, to a lesser extent, the timing of home sales and homebuilding activities.

Net cash used in investing activities during the year ended December 31, 2018 was \$74.9 million as compared to \$0.5 million during the year ended December 31, 2017. The \$74.4 million increase in net cash used in investing activities is primarily due to the business acquisition of Wynn Homes.

Net cash provided by financing activities during the year ended December 31, 2018 was \$170.7 million as compared to \$87.0 million during the year ended December 31, 2017. The \$83.7 million increase in net cash provided by financing activities consists primarily of the \$297.7 million increase in net borrowings from the issuance of the Senior Notes, including the related \$2.3 million discount and from the \$196.2 million decrease in net borrowings associated with the Credit Facility, offset by the related \$2.4 million in loan issuance costs, the \$14.4 million decrease in net proceeds realized from the issuance and sale of shares of our common stock, and \$1.5 million of common stock repurchases under our common stock repurchase program.

Year Ended December 31, 2017 compared to Year Ended December 31, 2016

Net cash used in operating activities during the year ended December 31, 2017 was \$68.5 million as compared to \$108.2 million during the year ended December 31, 2016. The \$39.7 million decrease in net cash used in operating activities was primarily attributable to a \$63.7 million increase in accounts payable, accrued expenses, and other liabilities, offset by cash outlays for the \$16.7 million increase in the net change in real estate inventory year-over-year, which is primarily related to our increased community count, additional homes under construction and land acquisitions combined with year-over-year change in net cash provided by working capital items (\$27.9 million increase in accounts receivable, \$14.1 million increase in other assets and \$4.6 million increase in cash paid for pre-acquisition costs and deposits).

Net cash used in investing activities during the year ended December 31, 2017 was \$0.5 million as compared to \$0.7 million during the year ended December 31, 2016 and reflects the purchase of property and equipment.

Net cash provided by financing activities totaled \$87.0 million during the year ended December 31, 2017 as compared to \$120.9 million during the year ended December 31, 2016. The \$33.8 million decrease in net cash provided by financing activities is primarily due to the \$20.0 million decrease in net borrowings under the Credit Facility, the \$12.3 million decrease in net proceeds realized from the issuance and sale of shares of our common stock, and the \$1.7 million increase in loan issuance costs associated with the Credit Agreement.

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Off-Balance Sheet Arrangements

In the ordinary course of business, we enter into land purchase contracts in order to procure land and lots for the construction of our homes. We are subject to customary obligations associated with entering into contracts for the purchase of land and improved lots. These contracts typically require cash deposits and the purchase of properties under these contracts is generally contingent upon satisfaction of certain requirements by the sellers, which may include obtaining applicable property and development entitlements or the completion of development activities and the delivery of finished lots. We also utilize contracts with land sellers as a method of acquiring lots and land in staged takedowns, which helps us manage the financial and market risk associated with land holdings and minimize the use of funds from our corporate financing sources. Such contracts generally require a non-refundable deposit for the right to acquire land or lots over a specified period of time at pre-determined prices. We generally have the right at our discretion to terminate our obligations under purchase contracts during the initial feasibility period and receive a refund of our deposit, or we may terminate the contracts after the end of the feasibility period by forfeiting our cash deposit with no further financial obligations to the land seller. In addition, our deposit may also be refundable if the land seller does not satisfy all conditions precedent in the respective contract. As of December 31, 2018, we had \$40.0 million of cash deposits pertaining to land purchase contracts for 22,820 lots with an aggregate purchase price of \$776.2 million. Approximately \$25.2 million of the cash deposits as of December 31, 2018 are secured by third-party guarantees or indemnity mortgages on the related property.

Our utilization of land purchase contracts is dependent on, among other things, the availability of land sellers willing to enter into contracts at acceptable terms, which may include option takedown arrangements, the availability of capital to financial intermediaries to finance the development of optioned lots, general housing conditions, and local market dynamics. Land purchase contracts may be more difficult to procure from land sellers in strong housing markets and are more prevalent in certain markets.

Inflation

Our business can be adversely impacted by inflation, primarily from higher land, financing, labor, material, and construction costs. In addition, inflation can lead to higher mortgage rates, which can significantly affect the affordability of mortgage financing to homebuyers.

Contractual Obligations

The following is a summary of our contractual obligations as of December 31, 2018 and the effect such obligations are expected to have on our liquidity and cash flows in future periods.

Contractual Obligations	Payments due by period (in thousands)				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Borrowings:					
Credit Facility ^(a)	\$293,800	\$—	\$293,800	\$—	\$—
Senior Notes ^(b)	300,000	—	—	—	300,000
Convertible Notes ^(c)	69,962	69,962	—	—	—
Inventory related obligations ^(d)	7,041	205	444	495	5,897
Interest and fees ^(e)	231,042	50,878	82,012	41,981	56,171
Operating leases	6,620	827	1,528	1,428	2,837
Total	\$908,465	\$121,872	\$377,784	\$43,904	\$364,905

Represents borrowings under our \$500.0 million revolving credit facility which matures on May 31, 2021. See (a) Note 8 “Notes Payable” to our consolidated financial statements included in Part II, Item 8 of this Annual Report on Form 10-K for additional information regarding our long-term debt.

Represents \$300.0 million aggregate principal amount of our 6.875% Senior Notes due 2026. The Senior Notes (b) mature on July 15, 2026. See Note 8 “Notes Payable” to our consolidated financial statements included in Part II, Item 8 of this Annual Report on Form 10-K for additional information regarding our long-term debt.

(c) Represents \$70.0 million aggregate principal amount of our 4.25% Convertible Notes due 2019. The Convertible Notes mature on November 15, 2019. See Note 8 “Notes Payable” to our consolidated financial statements included

in Part II, Item 8 of this Annual Report on Form 10-K for additional information regarding our long-term debt.

The Company owns lots in certain communities that have Community Development Districts or similar utility and (d) infrastructure development special assessment programs that allocate a fixed amount of debt service associated with development activities to each lot. Such obligations represent a non-cash cost of the lots.

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All of the outstanding borrowings under the Credit Facility are at variable rates based on LIBOR, or subject to an interest rate floor. The interest rate for our variable rate indebtedness as of December 31, 2018 was LIBOR plus 2.90%. Fees on the Credit Facility are approximately \$0.1 million per year. Interest on the Senior Notes accrues at a rate of 6.875% per annum, payable semi-annually in arrears on January 15 and July 15 of each year. Interest on the Convertible Notes accrues at a rate of 4.25% per year and is payable semi-annually in arrears on May 15 and November 15 of each year. Inventory related obligations for infrastructure development attached to the land are subject to a fixed interest rate generally ranging from 1.28% to 7.12%, typically payable over a 30 year period, and are ultimately assumed by the homebuyer when home sales are closed.

Critical Accounting Policies

Discussed below are accounting policies that we believe are critical because of the significance of the activity to which they relate or because they require the use of significant judgment in their application.

Revenue Recognition

Effective January 1, 2018, we adopted the Financial Accounting Standards Board Accounting Standards Update No. 2014-09, “Revenue from Contracts with Customers (Topic 606)” (“Topic 606”), which provides guidance for revenue recognition. Topic 606 affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets and supersedes the revenue recognition requirements in Topic 605, “Revenue Recognition” (“Topic 605”) and most industry-specific guidance. Topic 606 also supersedes certain cost guidance included in Subtopic 605-35, “Revenue Recognition—Construction-Type and Production-Type Contracts.” Topic 606’s core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which a company expects to be entitled in exchange for those goods or services. We adopted Topic 606 using the modified retrospective transition method only with respect to contracts not completed at the date of adoption. We have developed the additional expanded disclosures required; however, the adoption of Topic 606 did not have a material effect on our consolidated statements of operations, balance sheets or cash flows.

We recognize revenue upon the transfer of promised goods to our customers in an amount that reflects the consideration to which we expect to be entitled by applying the following five-step process specified in Topic 606.

- 1 Identify the contract(s) with a customer
- 2 Identify the performance obligations
- 3 Determine the transaction price
- 4 Allocate the transaction price
- 5 Recognize revenue when the performance obligations are met

Our contracts with customers include a single performance obligation to transfer a completed home to the customer. We generally determine selling price per home on the expected cost plus margin. Our contracts contain no significant financing terms as customers who finance do so through a third party. Performance obligations are satisfied at a moment in time when the home is complete and control of the asset is transferred to the customer at closing. Home sales proceeds are generally received from the title company within a few business days after closing.

Sales and broker commissions are incremental costs incurred to obtain a contract with a customer that would not have been incurred if the contract had not been obtained. Sales and broker commissions are expensed upon fulfillment of a home closing. Advertising costs are costs to obtain a contract that would have been incurred regardless of whether the contract was obtained and are recognized as an expense when incurred. Sales and broker commissions and advertising costs are recorded within sales and marketing expense presented in our consolidated statements of operations as selling expenses.

Real Estate Inventory and Cost of Home Sales

Inventory consists of land, land under development, finished lots, information centers, homes in progress and completed homes. Inventory is stated at cost unless the carrying amount is determined not to be recoverable, in which case inventory is written down to fair value.

Pre-acquisition costs, land, development and other project costs, including interest and property taxes, incurred during development and home construction, and net of expected reimbursements of development costs, are capitalized to real estate inventory. Pre-acquisition costs, land development and other common costs that benefit the entire community,

including field construction supervision and related direct overhead, are allocated to individual lots or homes, as appropriate, on a pro rata basis which we believe approximates the costs that would be determined using an allocation method based on relative sales values since the individual lots or homes within a community are similar in value. Changes to estimated total development costs subsequent to initial home closings in a community are allocated to the remaining unsold homes in the community on a prospective basis. Home construction costs and related carrying charges are allocated to the cost of individual homes using the specific identification method and are capitalized as they are incurred. Capitalized

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interest, property taxes, and other carrying costs are generally capitalized to real estate inventory from the point development begins to the point construction is completed. Costs associated with homes closed are charged to cost of sales simultaneously with revenue recognition.

Impairment of Real Estate Inventories.

In accordance with Accounting Standards Codification Topic 360, Property, Plant, and Equipment, real estate inventory is evaluated for indicators of impairment by each community during each reporting period. In conducting our review for indicators of impairment on a community level, we evaluate, among other things, the margins on homes that have been closed, communities with slow moving inventory, projected margins on future home sales over the life of the community, and the estimated fair value of the land. We pay particular attention to communities in which inventory is moving at a slower than anticipated absorption pace and communities whose average sales prices and/or margins are trending downward and are anticipated to continue to trend downward. Due largely to the relatively short development and construction periods for our communities and our growth, we have not experienced circumstances during 2018, 2017 or 2016 that are indicators of impairment. Our future sales and margins may be impacted by our inability to realize continued growth, increased cost associated with holding and developing land, local economic factors, pressure on home sales prices, increased carrying costs, and insufficient access to labor and materials at reasonable costs. For individual communities with indicators of impairment, we perform additional analysis to estimate the community's undiscounted future cash flows. If the estimated undiscounted future cash flows are greater than the carrying value of the asset, no impairment adjustment is required. If the undiscounted cash flows are less than the asset's carrying value, the asset is impaired and is written down to its fair value. We estimate the fair value of communities using a discounted cash flow model; changes to the expected cash flows may lead to changes in the outcome of our impairment analysis.

The life cycle of a community generally ranges from two to five years, commencing with the acquisition of land, continuing through the land development phase, and concluding with the construction, sale, and delivery of homes. A constructed home is used as the community information center during the life of the community and then sold. Actual individual community lives will vary based on the size of the community, the sales absorption rate, whether we purchased the property as raw land or finished lots, and the timing and phasing of development on larger projects.

Impairment of land and land under development.

For raw land, land under development and completed lots that our management anticipates will be utilized for future homebuilding activities or to be sold as finished lots to individuals, the recoverability of assets is measured by comparing the carrying amount of the assets to future undiscounted cash flows expected to be generated by the assets based on home or lot sales, consistent with the evaluation of operating communities discussed above. As of December 31, 2018, we had not identified any raw land, land under development or completed lots that management intends to market for sale in bulk to a third-party.

Pre-acquisition costs and controlled lots not owned.

We enter into land purchase agreements in the ordinary course of business in order to secure land for the construction of homes in the future. Pursuant to these agreements, we typically provide a deposit to the seller as consideration for the right to purchase land at different times in the future, usually at predetermined prices. We do not have title to the property and our obligations with respect to the contracts are generally limited to the forfeiture of the related nonrefundable cash deposits.

To the extent that any deposits are nonrefundable and the associated land acquisition process is terminated or no longer determined probable, the deposit and any related pre-acquisition costs (e.g. due diligence costs) are charged to other income, net. We review the likelihood of the acquisition of contracted lots in conjunction with our periodic real estate impairment analysis.

Warranty Reserves

We typically provide homebuyers with a one-year warranty on the house and a ten-year limited warranty for major defects in structural elements. Estimated future direct warranty costs are accrued and charged to cost of sales in connection with our home sales.

Our warranty liability is based upon historical warranty cost experience on a per house basis established based on (i) trends in historical warranty payment levels, (ii) the historical range of amounts paid per house, (iii) any warranty

expenditures not considered to be normal and recurring, and is adjusted as appropriate to reflect qualitative risks associated with the types of homes built, the geographic areas in which they are built, and potential impacts of our expansion. Our analysis also considers improvements in quality control and construction techniques expected to impact future warranty expenditures and the expertise of our personnel. Our warranty reserves are reviewed quarterly to assess the reasonableness and adequacy and we make adjustments to the balance of the pre-existing reserves, as needed, to reflect changes in trends and historical data as information becomes available.

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Goodwill

We record goodwill associated with our acquisitions of businesses when the consideration paid exceeds the fair value of the net tangible and identifiable intangible assets acquired. We evaluate our goodwill balances for potential impairment on an annual basis. In applying the goodwill impairment test, we have the option to perform a qualitative test (also known as “Step 0”) or a two-step quantitative test (consisting of “Step 1” and “Step 2”). Under the Step 0 test, we first assess qualitative factors to determine whether it is more likely than not that the fair value of the reporting units is less than their carrying value. Qualitative factors may include, but are not limited to economic conditions, industry and market considerations, cost factors, overall financial performance of the reporting unit and other entity and reporting unit specific events. If after assessing these qualitative factors, the Company determines it is “more-likely-than-not” that the fair value of the reporting unit is less than the carrying value, then performing the two-step quantitative test is necessary. During 2018 and 2017, we performed a Step 0 analysis and determined that it is not “more likely than not” that the fair values of the reporting units were less than their carrying amounts. During 2016, we performed the two-step quantitative impairment test.

Taxes

We utilize the liability method of accounting for income taxes. Under the liability method, deferred tax assets and liabilities are recognized using enacted tax rates for the effect of temporary differences between the book and tax bases of recorded assets and liabilities, changes in tax rate are recognized in the year of enactment. Deferred tax assets are reduced by a valuation allowance if it is more likely than not that some portion or all of the net deferred tax assets will not be realized. Our ability to realize deferred tax assets is assessed throughout the year and a valuation allowance is established, if required. We recognize the impact of a tax position only if it is more likely than not to be sustained upon examination based on the technical merits of the position. We recognize potential interest and penalties related to uncertain tax positions in income tax expense, as applicable.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our operations are interest rate sensitive. As overall housing demand is adversely affected by increases in interest rates, a significant increase in mortgage interest rates may negatively affect the ability of homebuyers to secure adequate financing. Higher interest rates could adversely affect our revenues, gross margin, and net income. We do not enter into, or intend to enter into, derivative financial instruments for trading or speculative purposes.

Quantitative and Qualitative Disclosures About Interest Rate Risk

We utilize both fixed-rate debt (\$70.0 million aggregate principal amount of the Convertible Notes, \$300.0 million aggregate principal amount of the Senior Notes and certain inventory related obligations) and variable-rate debt (our \$500.0 million revolving credit facility) as part of financing our operations. Upon the election of a holder of Convertible Notes to convert their Convertible Notes, we may settle the conversion of the Convertible Notes using any combination of cash and shares of our common stock. Other than as a result of an election of a holder of Convertible Notes to convert their Convertible Notes, we do not have the obligation to prepay the Convertible Notes, the Senior Notes or our fixed-rate inventory related obligations prior to maturity, and, as a result, interest rate risk and changes in fair market value should not have a significant impact on our fixed-rate debt. The Convertible Notes mature on November 15, 2019.

We are exposed to market risks related to fluctuations in interest rates on our outstanding variable rate indebtedness. We did not utilize swaps, forward or option contracts on interest rates or commodities, or other types of derivative financial instruments as of or during the year ended December 31, 2018. We have not entered into and currently do not hold derivatives for trading or speculative purposes, but we may do so in the future. Many of the statements contained in this section are forward looking and should be read in conjunction with our disclosures under the heading “Cautionary Statement about Forward-Looking Statements” in Item 1A. Risk Factors.

As of December 31, 2018, we had \$293.8 million of variable rate indebtedness outstanding under the Credit Agreement. All of the outstanding borrowings under the Credit Agreement are at variable rates based on LIBOR. The interest rate for our variable rate indebtedness as of December 31, 2018 was LIBOR plus 2.90%. At December 31, 2018, LIBOR was 2.46%. A hypothetical 100 basis point increase in the average interest rate on our variable rate indebtedness would increase our annual interest cost by approximately \$2.9 million.

Based on the current interest rate management policies we have in place with respect to our outstanding indebtedness, we do not believe that the future interest rate risks related to our existing indebtedness will have a material adverse impact on our financial position, results of operations, or liquidity.

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ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholders and the Board of Directors of LGI Homes, Inc.

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of LGI Homes, Inc. (the Company) as of December 31, 2018 and 2017, the related consolidated statements of operations, equity, and cash flows for each of the three years in the period ended December 31, 2018, and the related notes (collectively referred to as the “consolidated financial statements”). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company at December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 Framework), and our report dated February 26, 2019 expressed an unqualified opinion thereon.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB. We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Ernst & Young LLP

We have served as the Company's auditor since 2013.

Houston, Texas

February 26, 2019

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LGI HOMES, INC.
 CONSOLIDATED BALANCE SHEETS
 (In thousands, except share data)

	December 31,	
	2018	2017
ASSETS		
Cash and cash equivalents	\$46,624	\$67,571
Accounts receivable	42,836	44,706
Real estate inventory	1,228,256	918,933
Pre-acquisition costs and deposits	45,752	18,866
Property and equipment, net	1,432	1,674
Other assets	15,765	14,196
Deferred tax assets, net	2,790	1,928
Goodwill	12,018	12,018
Total assets	\$1,395,473	\$1,079,892
LIABILITIES AND EQUITY		
Accounts payable	\$9,241	\$12,020
Accrued expenses and other liabilities	76,555	102,831
Notes payable	653,734	475,195
Total liabilities	739,530	590,046
COMMITMENTS AND CONTINGENCIES		
EQUITY		
Common stock, par value \$0.01, 250,000,000 shares authorized, 23,746,385 shares issued and 22,707,385 shares outstanding as of December 31, 2018 and 22,845,580 shares issued and 21,845,580 shares outstanding as of December 31, 2017	237	228
Additional paid-in capital	241,988	229,680
Retained earnings	431,774	276,488
Treasury stock, at cost 1,039,000 shares and 1,000,000 shares, respectively	(18,056)	(16,550)
Total equity	655,943	489,846
Total liabilities and equity	\$1,395,473	\$1,079,892

See accompanying notes to the consolidated financial statements.

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LGI HOMES, INC.
 CONSOLIDATED STATEMENTS OF OPERATIONS
 (In thousands, except share and per share data)

	For the Year Ended December 31,		
	2018	2017	2016
Home sales revenues	\$ 1,504,400	\$ 1,257,960	\$ 838,320
Cost of sales	1,124,484	937,540	616,707
Selling expenses	109,460	94,957	66,984
General and administrative	70,345	55,662	43,158
Operating income	200,111	169,801	111,471
Loss on extinguishment of debt	3,599	—	—
Other income, net	(2,586)	(1,601)	(2,201)
Net income before income taxes	199,098	171,402	113,672
Income tax provision	43,812	58,096	38,641
Net income	\$ 155,286	\$ 113,306	\$ 75,031
Earnings per share:			
Basic	\$6.89	\$5.24	\$3.61
Diluted	\$6.24	\$4.73	\$3.41
Weighted average shares outstanding:			
Basic	22,551,762	21,604,932	20,798,333
Diluted	24,892,274	23,933,122	22,024,091

See accompanying notes to the consolidated financial statements.

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LGI HOMES, INC.
CONSOLIDATED STATEMENTS OF EQUITY
(In thousands, except share data)

	Common Stock		Additional	Retained	Treasury	Total
	Shares	Amount	Paid-In Capital	Earnings	Stock	Equity
BALANCE—December 31, 2015	21,270,389	\$ 213	\$ 175,575	\$ 88,151	\$(16,550)	\$ 247,389
Net income	—	—	—	75,031	—	75,031
Issuance of shares, net of offering costs	993,554	10	28,467	—	—	28,477
Issuance of restricted stock units in settlement of accrued bonuses	—	—	138	—	—	138
Compensation expense for equity awards	—	—	3,396	—	—	3,396
Stock issued under employee incentive plans	47,367	—	770	—	—	770
BALANCE—December 31, 2016	22,311,310	\$ 223	\$ 208,346	\$ 163,182	\$(16,550)	\$ 355,201
Net income	—	—	—	113,306	—	113,306
Issuance of shares, net of offering costs	354,620	3	15,339	—	—	15,342
Issuance of restricted stock units in settlement of accrued bonuses	—	—	167	—	—	167
Compensation expense for equity awards	—	—	4,188	—	—	4,188
Stock issued under employee incentive plans	179,650	2	1,640	—	—	1,642
BALANCE—December 31, 2017	22,845,580	\$ 228	\$ 229,680	\$ 276,488	\$(16,550)	\$ 489,846
Net income	—	—	—	155,286	—	155,286
Issuance of shares in settlement of Convertible Notes	486,679	5	(482)	—	—	(477)
Issuance of shares, Wynn Homes Acquisition	70,746	1	3,999	—	—	4,000
Repurchase of shares	—	—	—	—	(1,506)	(1,506)
Issuance of restricted stock units in settlement of accrued bonuses	—	—	181	—	—	181
Compensation expense for equity awards	—	—	5,923	—	—	5,923
Stock issued under employee incentive plans	343,380	3	2,687	—	—	2,690
BALANCE—December 31, 2018	23,746,385	\$ 237	\$ 241,988	\$ 431,774	\$(18,056)	\$ 655,943

See accompanying notes to the consolidated financial statements.

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LGI HOMES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	For the Year Ended December 31,		
	2018	2017	2016
Cash flows from operating activities:			
Net income	\$155,286	\$113,306	\$75,031
Adjustments to reconcile net income to net cash used in operating activities:			
Depreciation and amortization	711	791	1,089
Loss on extinguishment of debt	3,588	—	—
Loss on disposal of assets	6	13	1
Excess tax benefits from stock based compensation	—	—	(138)
Compensation expense for equity awards	5,937	4,188	3,396
Deferred income taxes	(724)	(2,092)	(2,562)
Changes in assets and liabilities:			
Accounts receivable	1,870	(27,651)	270
Real estate inventory	(234,664)	(200,609)	(183,884)
Pre-acquisition costs and deposits	(18,853)	(8,215)	(3,650)
Other assets	(1,398)	(8,643)	5,472
Accounts payable	(2,779)	(257)	(11,747)
Accrued expenses and other liabilities	(25,703)	60,702	8,539
Net cash used in operating activities	(116,723)	(68,467)	(108,183)
Cash flows from investing activities:			
Purchases of property and equipment	(475)	(518)	(722)
Payment for business acquisition	(74,463)	—	—
Net cash used in investing activities	(74,938)	(518)	(722)
Cash flows from financing activities:			
Proceeds from notes payable	612,717	100,000	140,000
Payments on notes payable	(436,238)	(25,000)	(45,000)
Loan issuance costs	(6,741)	(4,375)	(2,684)
Proceeds from sale of stock, net of offering expenses	2,690	17,130	29,448
Stock repurchase	(1,506)	—	—
Payment for offering costs	(76)	(69)	(204)
Payment for earnout obligation	(132)	(648)	(843)
Excess tax benefits from equity awards	—	—	138
Net cash provided by financing activities	170,714	87,038	120,855
Net increase (decrease) in cash and cash equivalents	(20,947)	18,053	11,950
Cash and cash equivalents, beginning of year	67,571	49,518	37,568
Cash and cash equivalents, end of year	\$46,624	\$67,571	\$49,518

See accompanying notes to the consolidated financial statements.

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LGI HOMES, INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION AND BUSINESS

Organization and Description of the Business

LGI Homes, Inc., a Delaware corporation (the “Company”, “us,” “we,” or “our”), was organized on July 9, 2013 as a holding company for the purposes of facilitating the initial public offering (the “IPO”) of its common stock in November 2013. Headquartered in the Woodlands, Texas, we engage in the design, construction and sale of new homes in Texas, Arizona, Florida, Georgia, New Mexico, Colorado, North Carolina, South Carolina, Washington, Tennessee, Minnesota, Oklahoma, Alabama, California, Oregon, and Nevada.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The consolidated financial statements have been prepared in accordance with U.S. Generally Accepted Accounting Principles (“GAAP”) and include the accounts of the Company and its subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates, and these differences could have a significant impact on the financial statements. The significant accounting estimates include real estate inventory and cost of sales, impairment of real estate inventory and property and equipment, goodwill, warranty reserves, the fair value of the convertible debt, loss contingencies, incentive compensation expense, and income taxes.

Cash and Cash Equivalents and Concentration of Credit Risk

Cash and cash equivalents are defined as cash on hand, demand deposits with financial institutions, and short-term liquid investments with an initial maturity date of less than three months. Our cash in demand deposit accounts may exceed federally insured limits and could be negatively impacted if the underlying financial institutions fail or are subject to other adverse conditions in the financial markets. To date, we have experienced no loss or diminished access to cash in our demand deposit accounts.

Accounts Receivable

Accounts receivable consist primarily of proceeds due from title companies for sales closed prior to period end and are generally collected within a few days from closing.

Real Estate Inventory

Inventory consists of land, land under development, finished lots, information centers, homes in progress, and completed homes. Inventory is stated at cost unless the carrying amount is determined not to be recoverable, in which case the affected inventory is written down to fair value.

Land, development and other project costs, including interest and property taxes incurred during development and home construction and net of expected reimbursements of development costs, are capitalized to real estate inventory. Land development and other common costs that benefit the entire community, including field construction supervision and related direct overhead, are allocated to individual lots or homes, as appropriate. The costs of lots are transferred to homes in progress when home construction begins. Home construction costs and related carrying charges are allocated to the cost of individual homes using the specific identification method. Costs that are not specifically identifiable to a home are allocated on a pro rata basis, which we believe approximates the costs that would be determined using an allocation method based on relative sales values since the individual lots or homes within a community are similar in value. Inventory costs for completed homes are expensed to cost of sales as homes are closed. Changes to estimated total development costs subsequent to initial home closings in a community are generally allocated to the remaining unsold lots and homes in the community on a pro rata basis.

The life cycle of a community generally ranges from two to five years, commencing with the acquisition of land, continuing through the land development phase, and concluding with the construction and sale of homes. A constructed home is used as the community information center during the life of the community and then sold. Actual

individual community lives will vary based on the size of the community, the sales absorption rate, and whether the property was purchased as raw land or finished lots.

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In accordance with the Accounting Standards Codification (“ASC”) Topic 360, Property, Plant, and Equipment, real estate inventory is evaluated for indicators of impairment by each community during each reporting period. In conducting its review for indicators of impairment on a community level, management evaluates, among other things, the margins on homes that have been closed, communities with slow moving inventory, projected margins on future home sales over the life of the community, and the estimated fair value of the land. For individual communities with indicators of impairment, additional analysis is performed to estimate the community’s undiscounted future cash flows. If the estimated undiscounted future cash flows are greater than the carrying value of the community group of assets, no impairment adjustment is required. If the undiscounted cash flows are less than the community’s carrying value, the asset group is impaired and is written down to its fair value. We estimate the fair value of communities using a discounted cash flow model. As of December 31, 2018 and 2017, the real estate inventory is stated at cost; there were no inventory impairment charges recorded during the years ended December 31, 2018, 2017 and 2016.

Capitalized Interest

Interest and other financing costs are capitalized as cost of inventory during community development and home construction activities, in accordance with ASC Topic 835, Interest and expensed in cost of sales as homes in the community are closed. To the extent the debt exceeds qualified assets, a portion of the interest incurred is expensed.

Pre-Acquisition Costs and Deposits

Amounts paid for land options, deposits on land purchase contracts, and other pre-acquisition costs are capitalized and classified as deposits to purchase. Upon execution of the purchase, these deposits are applied to the acquisition price of the land and recorded as a cost component of the land in real estate inventory. To the extent that any deposits are nonrefundable and the associated land acquisition process is terminated or no longer determined probable, the deposit and related pre-acquisition costs are charged to other income, net. Management reviews the likelihood of the acquisition of contracted lots in conjunction with its periodic real estate impairment analysis.

Under ASC Topic 810, Consolidation (“ASC 810”), a nonrefundable deposit paid to an entity is deemed to be a variable interest that will absorb some or all of the entity’s expected losses if they occur. Non-refundable land purchase and lot option deposits generally represent our maximum exposure if we elect not to purchase the optioned property. In some instances, we may also expend funds for due diligence, development and construction activities with respect to optioned land prior to close. Such costs are classified as preacquisition costs, which we would have to absorb should the option not be exercised. Therefore, whenever we enter into a land option or purchase contract with an entity and make a nonrefundable deposit, we may have a variable interest in a variable interest entity (“VIE”). In accordance with ASC 810, we perform ongoing reassessments of whether we are the primary beneficiary of a VIE and would consolidate the VIE if we are deemed to be the primary beneficiary. As of December 31, 2018 and 2017, we were not deemed to be the primary beneficiary for any VIEs associated with non-refundable land deposits.

Deferred Loan Costs

Deferred loan costs represent debt issuance costs related to a recognized debt liability and are presented in the balance sheet as a direct deduction from the carrying amount of that debt liability.

Other Assets

Other assets consist primarily of prepaid insurance, security deposits, and prepaid expenses. Our prepaid expenses were \$8.5 million and \$7.5 million as of December 31, 2018 and 2017, respectively.

Property and Equipment

Property, equipment and leasehold improvements are stated at cost, less accumulated depreciation. Depreciation expense is recorded in general and administrative expenses. Upon sale or retirement, the costs and related accumulated depreciation are eliminated from the respective accounts and any resulting gain or loss is included in other income, net. Depreciation is generally computed using the straight-line method over the estimated useful lives of the assets, ranging from two to five years for property and equipment. Leasehold improvements are depreciated over the shorter of the asset life or the term of the lease. Maintenance and repair costs are expensed as incurred.

Impairments of long-lived assets are determined periodically when indicators of impairment are present. If such indicators are present, the determination of the amount of impairment is based on judgments as to the future undiscounted operating cash flows to be generated from these assets throughout the remaining estimated useful lives. If these undiscounted cash flows are less than the carrying amount of the related asset, impairment is recognized for

the excess of the carrying value over its fair value. There were no impairments of property, equipment and leasehold improvements recorded during the years ended December 31, 2018, 2017 and 2016.

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Goodwill and Intangible Assets

The excess of the purchase price of a business acquisition over the net fair value of assets acquired and liabilities assumed is capitalized as goodwill in accordance with ASC Topic 805, Business Combinations. Goodwill and intangible assets that do not have finite lives are not amortized, but are assessed for impairment at least annually or more frequently if certain impairment indicators are present. The \$12.0 million of goodwill is related to the reorganization transactions completed in connection with the initial public offering of our common stock in November 2013. In applying the goodwill impairment test, we have the option to perform a qualitative test (also known as “Step 0”) or a two-step quantitative test (consisting of “Step 1” and “Step 2”). Under the Step 0 test, we first assess qualitative factors to determine whether it is more likely than not that the fair value of the reporting units is less than their carrying value. Qualitative factors may include, but are not limited to, economic conditions, industry and market considerations, cost factors, overall financial performance of the reporting unit and other entity and reporting unit specific events. If after assessing these qualitative factors, we determine it is “more-likely-than-not” that the fair value of the reporting unit is less than the carrying value, then performing the two-step quantitative test is necessary. During 2018 and 2017, we performed a Step 0 analysis and determined that it is not “more likely than not” that the fair values of the reporting units were less than their carrying amounts. During 2016, we performed the two-step quantitative impairment test. No goodwill impairment charges were recorded in 2018, 2017 and 2016.

Warranty Reserves

Future direct warranty costs are accrued and charged to cost of sales in the period when the related home is closed. Our warranty liability is based upon historical warranty cost experience and is adjusted as appropriate to reflect qualitative risks associated with the types of homes built, the geographic areas in which they are built, and potential impacts of our continued expansion.

Warranty reserves are reviewed quarterly to assess the reasonableness and adequacy and adjusted, as needed, to reflect changes in trends and historical data as information becomes available.

Customer Deposits

Customer deposits are received upon signing a purchase contract and are generally \$1,000 or less. Deposits are generally refundable if the customer is unable to obtain financing. Forfeited buyer deposits related to home sales are recognized in other income in the period in which it is determined that the buyer will not complete the purchase of the property and the deposit is nonrefundable to the buyer.

Home Sales

Revenues from home sales are recorded at the time each home sale is closed, title and possession are transferred to the buyer, and we have no significant continuing involvement with the home. Home sales proceeds are generally received from the title company within a few days after closing. Home sales are reported net of sales discounts and incentives granted to home buyers, which are primarily seller-paid closing costs.

Cost of Sales

As discussed under Real Estate Inventory above, cost of sales for homes closed include the construction costs of each home and allocable land acquisition and land development costs, capitalized interest, and other related common costs (both incurred and estimated to be incurred).

Selling and Commission Costs

Sales commissions are paid and expensed based on homes closed. Other selling costs are expensed in the period incurred.

Advertising Costs

Advertising and direct mail costs are expensed as incurred. Advertising and direct mail costs were \$17.6 million, \$15.2 million and \$11.3 million for the years ended December 31, 2018, 2017, and 2016, respectively.

Income Taxes

We are a taxable entity subject to federal and state taxes. We utilize the liability method of accounting for income taxes. Under the liability method, deferred tax assets and liabilities are recognized using enacted tax rates for the effect of temporary differences between the book and tax bases of recorded assets and liabilities. Changes in tax rate are recognized in the year of enactment. Deferred tax assets are reduced by a valuation allowance if it is more likely than not that some portion or all of the net deferred tax assets will not be realized. Our ability to realize deferred tax assets

is assessed throughout the year and a valuation allowance is established, if required. We recognize the impact of a tax position only if it is more likely than not to be sustained

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upon examination based on the technical merits of the position. We recognize potential interest and penalties related to uncertain tax positions in income tax expense.

Earnings Per Share

Basic earnings per share is based on the weighted average number of shares of common stock outstanding. Diluted earnings per share is based on the weighted average number of shares of common stock and dilutive securities outstanding. In accordance with ASC 260-10, Earnings Per Share, we calculated the dilutive effect of the Convertible Notes using the treasury stock method, since we have the intent and ability to settle the principal amount of the outstanding Convertible Notes in cash. Under the treasury stock method, the Convertible Notes have a dilutive impact on diluted earnings per share to the extent that the average market price of our common stock for a reporting period exceeds the conversion price of \$21.52 per share. Diluted earnings per share excludes all dilutive potential shares of common stock if their effect is antidilutive.

Stock-Based Compensation

Compensation costs for non-performance-based restricted stock awards are measured using the closing price of our common stock on the date of grant and are expensed on a straight-line basis over the requisite service period of the award. Compensation costs for performance-based restricted stock awards also contain a market condition. These costs are measured using the derived grant date fair value, based on a third party valuation analysis, and are expensed in accordance with ASC 718-10-25-20, Compensation - Stock Compensation, which requires an assessment of probability of attainment of the performance target. Once the performance target outcome is determined to be probable, the cumulative expense is adjusted, as needed, to recognize compensation expense on a straight-line basis over the award's requisite service period.

Recently Adopted Accounting Standards

Effective January 1, 2018, we adopted the Financial Accounting Standards Board (the "FASB") Accounting Standards Update ("ASU") No. 2016-15, "Statement of Cash Flows - Classification of Certain Cash Receipts and Cash Payments" ("ASU 2016-15"), which addresses specific classification issues and is intended to reduce diversity in current practice regarding the manner in which certain cash receipts and cash payments are presented and classified in the consolidated statements of cash flows. The adoption of ASU 2016-15 did not have a material effect on our consolidated statements of cash flows or disclosures.

Effective January 1, 2018, we adopted the FASB ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)" ("Topic 606"), which provides guidance for revenue recognition. Topic 606 affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets and supersedes the revenue recognition requirements in Topic 605, "Revenue Recognition" ("Topic 605") and most industry-specific guidance. Topic 606 also supersedes certain cost guidance included in Subtopic 605-35, "Revenue Recognition—Construction-Type and Production-Type Contracts." Topic 606's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which a company expects to be entitled in exchange for those goods or services. We adopted Topic 606 using the modified retrospective transition method only with respect to contracts not completed at the date of adoption. We have developed the additional expanded disclosures required; however, the adoption of Topic 606 did not have a material effect on our consolidated statements of operations, balance sheets or cash flows. See [Note 4](#) for further details.

Effective January 1 2018, we adopted the FASB ASU No. 2017-01, "Business Combinations - Clarifying the Definition of a Business" ("ASU 2017-01"). ASU 2017-01 provides additional guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The adoption of ASU 2017-01 was applied prospectively and had no effect on our consolidated financial statements.

Recently Issued Accounting Pronouncements

In August 2018, the FASB issued ASU No. 2018-13, "Fair Value Measurement (Topic 820) Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement" ("ASU 2018-13"), which modifies the disclosure requirements of fair value measurements. ASU 2018-13 is effective for us beginning January 1, 2020. Certain disclosures are required to be applied on a retrospective basis and others on a prospective basis. We are currently evaluating the impact that adoption of this guidance will have on our financial statement disclosures.

In January 2017, the FASB issued ASU No. 2017-04, “Intangibles - Goodwill and Other (Topic 350): Simplifying the Accounting for Goodwill Impairment.” (“ASU 2017-04”), which removes the requirement to perform a hypothetical purchase price allocation to measure goodwill impairment. A goodwill impairment will now be the amount by which a reporting unit’s carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. ASU 2017-04 is effective for us beginning January 1, 2020, with early adoption permitted, and applied prospectively. We do not expect ASU 2017-04 to have a material impact on our financial statements.

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In February 2016, the FASB issued ASU No. 2016-02, “Leases (Topic 842)” (“ASU 2016-02”), which amends the existing accounting standards for lease accounting, including requiring lessees to recognize most leases on their balance sheets. Under ASU 2016-02, a lessee will be required to recognize assets and liabilities for leases with lease terms of more than twelve months. Lessor accounting remains substantially similar to current GAAP. In addition, disclosures of leasing activities will be expanded to include qualitative and specific quantitative information. ASU 2016-02 will be effective for annual reporting periods beginning after December 15, 2018, and early adoption is permitted. We expect to adopt the new standard in the quarter ending March 31, 2019. ASU 2016-02 requires a modified retrospective transition approach. We believe the recognition of new right-of-use (“ROU”) assets and lease liabilities will be the most significant change for us under ASU 2016-02. ASU 2016-02 includes several practical expedients, which we anticipate we will elect upon adoption, including to not reassess the lease classification for any expired or existing leases. Management is continuing to assess the values of the ROU assets and lease liabilities that will be included on the balance sheet as of January 1, 2019. Management does not expect the adoption of ASU 2016-02 to have a material impact on our results of operations or cash flows.

3. ACQUISITION

On August 2, 2018, we acquired certain homebuilding assets owned by Crosswind Properties, LLC, Wynn Construction, Inc., Crosswind Development, Inc., Crosswind Investments, Inc. and First Continental Communities, Inc. (collectively, “Wynn Homes”), and assumed certain related liabilities. As a result of the Wynn Homes acquisition, we expanded our North Carolina presence in the Raleigh market, as well as established an immediate presence in the Wilmington market. We acquired approximately 200 homes under construction and more than 4,000 owned and controlled lots. The total purchase price for the Wynn Homes acquisition was approximately \$78.5 million, consisting of approximately \$74.5 million in cash and \$4.0 million in shares of our common stock.

The acquisition was accounted for in accordance with ASC Topic 805, Business Combinations (“ASC 805”). Our purchase accounting for Wynn Homes as of December 31, 2018 was complete concerning the working capital adjustment and valuation of the tangible assets, intangible assets and liabilities assumed as of the acquisition date. At December 31, 2018, the acquired assets and assumed liabilities have been recorded at their estimated fair values at the acquisition date as noted below (amounts in thousands):

Purchase Consideration:	Total
Cash paid for net assets	\$74,463
Common Stock	4,000
Total consideration	78,463
Assets acquired and liabilities assumed:	
Real estate inventory	75,927
Pre-acquisition costs, deposits and other assets	8,143
Total assets	84,070
Accounts payable and accrued liabilities	(5,607)
Total liabilities	(5,607)
Net assets acquired	\$78,463

Pre-acquisition costs, which approximate fair value, deposits and other assets, accounts payable and accrued liabilities, are stated at historical carrying values given the short-term nature of these assets and liabilities. Real estate inventory was adjusted to reflect fair value.

We determined the estimated fair values of the real estate inventory with the assistance of appraisals performed by independent third-party specialists and estimates by management.

Significant assumptions included in our estimates of the fair value of the assets acquired include market comparisons, gross margin comparisons, future development costs and the timing of the completion of development activities, absorption rates, and mix of products sold in each community. Based on the estimated purchase consideration, management believes that the purchase price for the Wynn Homes acquisition was at market value and there was no excess of purchase price over the net fair value of assets acquired and liabilities assumed.

We expensed approximately \$0.8 million of acquisition related costs for legal and due diligence services; these costs are included in the general and administrative expenses in the accompanying consolidated statements of operations.

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4. REVENUES

Adoption of Topic 606, “Revenue from Contracts with Customers”

On January 1, 2018, we adopted Topic 606 using the modified retrospective method. Results for reporting periods beginning after January 1, 2018 are presented under Topic 606, while prior period amounts were not adjusted and continue to be reported in accordance with our historic accounting under Topic 605. We did not record any adjustments or net reductions to opening retained earnings as of January 1, 2018 in relation to the adoption of Topic 606.

Revenue Recognition

Revenues from home sales are recognized when control of the promised goods or services is transferred to our customers, in an amount that reflects the consideration we expect to be entitled to in exchange for those goods or services. Revenues from home sales are recorded at the time each home sale is closed, title and possession are transferred to the customer and we have no significant continuing involvement with the home. Proceeds from home sales are generally received from the title company within a few business days after closing. Home sales discounts and incentives granted to customers, which are related to the customers’ closing costs that we pay on the customers’ behalf, are recorded as a reduction of revenue in our consolidated financial statements of operations.

The following table presents our home sales revenues disaggregated by revenue stream (in thousands):

	For the Year Ended December 31,		
	2018	2017	2016
Retail home sales revenues	\$1,394,475	\$1,217,191	\$838,320
Other	109,925	40,769	—
Total home sales revenues	\$1,504,400	\$1,257,960	\$838,320

The following table presents our home sales revenues disaggregated by geography, based on our determined operating segments in Note 16 (in thousands):

	For the Year Ended December 31,		
	2018	2017	2016
Central	\$623,751	\$533,254	\$429,505
Northwest	277,567	215,421	86,496
Southeast	271,073	183,422	111,651
Florida	180,950	199,733	115,276
West	151,059	126,130	95,392
Home sales revenues	\$1,504,400	\$1,257,960	\$838,320

Home Sales Revenues

We generate revenues primarily by delivering move-in ready spec homes with our entry-level and move-up homes sold under our LGI Homes brand and our luxury series homes sold under our Terrata Homes brand.

Retail homes sold under both our LGI Homes brand and Terrata Homes brand focus on providing move-in ready homes with standardized features within favorable markets that meet certain demographic and economic conditions.

Our LGI Homes brand primarily markets to entry-level or first-time homebuyers, while our Terrata Homes brand primarily markets to move-up homebuyers.

Our other revenues are composed of our wholesale home sales under our LGI Homes brand and Terrata Homes brand in existing markets. Wholesale homes are primarily sold under a bulk sales agreement and focus on providing move-in ready homes with standardized features to real estate investors that will ultimately use the single-family homes as rental properties.

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Performance Obligations

Our contracts with customers include a single performance obligation to transfer a completed home to the customer. We generally determine selling price per home on the expected cost plus margin. Our contracts contain no significant financing terms as customers who finance do so through a third party. Performance obligations are satisfied at a moment in time when the home is complete and control of the asset is transferred to the customer at closing. Home sales proceeds are generally received from the title company within a few business days after closing.

Sales and broker commissions are incremental costs incurred to obtain a contract with a customer that would not have been incurred if the contract had not been obtained. Sales and broker commissions are expensed upon fulfillment of a home closing. Advertising costs are costs to obtain a contract that would have been incurred regardless of whether the contract was obtained and are recognized as an expense when incurred. Sales and broker commissions and advertising costs are recorded within sales and marketing expense presented in our consolidated statements of operations as selling expenses.

5. REAL ESTATE INVENTORY

Our real estate inventory consists of the following (in thousands):

	December 31,	
	2018	2017
Land, land under development, and finished lots	\$736,402	\$494,552
Information centers	21,179	18,327
Homes in progress	149,506	191,659
Completed homes	321,169	214,395
Total real estate inventory	\$1,228,256	\$918,933

See "Real Estate Inventory" under Note 2 for more information.

Interest and financing costs incurred under our debt obligations, as more fully discussed in Note 8, are capitalized to qualifying real estate projects under development and homes under construction.

6. PROPERTY AND EQUIPMENT

Property and equipment consist of the following (in thousands):

	December 31,		
	Asset Life	2018	2017
	(years)		
Computer equipment	2-5	\$1,342	\$1,483
Machinery and equipment	5	102	112
Furniture and fixtures	2-5	3,183	2,987
Leasehold improvements	5	267	240
Total property and equipment		4,894	4,822
Less: Accumulated depreciation		(3,462)	(3,148)
Property and equipment, net		\$1,432	\$1,674

Depreciation expense incurred for the years ended December 31, 2018, 2017 and 2016 was \$0.7 million, \$0.8 million and \$0.9 million, respectively.

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7. ACCRUED EXPENSES AND OTHER LIABILITIES

Accrued and other liabilities consist of the following (in thousands):

	December 31,	
	2018	2017
Inventory related obligations	\$7,041	\$12,906
Taxes payable	10,773	48,733
Retentions and development payable	18,899	12,025
Accrued compensation, bonuses and benefits	13,913	14,462
Accrued interest	12,339	2,096
Warranty reserve	2,950	2,450
Other	10,640	10,159
Total accrued expenses and other liabilities	\$76,555	\$102,831

Inventory Related Obligations

We own lots in certain communities in Arizona, California, Florida, and Texas that have Community Development Districts (“CDD”) or similar utility and infrastructure development special assessment programs that allocate a fixed amount of debt service associated with development activities to each lot. This obligation for infrastructure development is attached to the land, is typically payable over a 30-year period, and is ultimately assumed by the homebuyer when home sales are closed. Such obligations represent a non-cash cost of the lots. At December 31, 2018 and 2017, we had CDD and other utility development obligations of approximately \$7.0 million and \$12.9 million, respectively.

Estimated Warranty Reserve

We typically provide homebuyers with a one-year warranty on the house and a ten-year limited warranty for major defects in structural elements such as framing components and foundation systems.

Changes to our warranty accrual are as follows (in thousands):

	December 31,		
	2018	2017	2016
Warranty reserves, beginning of period	\$2,450	\$1,600	\$1,325
Warranty provision	4,438	4,999	3,084
Warranty expenditures	(3,938)	(4,149)	(2,809)
Warranty reserves, end of period	\$2,950	\$2,450	\$1,600

8. NOTES PAYABLE

Revolving Credit Agreement

On May 25, 2018, we entered into that certain Third Amended and Restated Credit Agreement with several financial institutions, and Wells Fargo Bank, National Association, as administrative agent, which was amended as of June 19, 2018 by that certain First Amendment thereto (the “First Amendment”; such credit agreement, as amended by the First Amendment, the “Credit Agreement”). The Credit Agreement has substantially similar terms and provisions to our second amended and restated credit agreement entered into in May 2017 with several financial institutions, and Wells Fargo Bank, National Association, as administrative agent (the “2017 Credit Agreement”) but, among other things, provided for, a revolving credit facility of \$450.0 million, which could be increased at our request by up to \$50.0 million if the lenders make additional commitments, subject to the terms and conditions of the Credit Agreement (which was requested and approved in October 2018). On October 18, 2018, we entered into a Lender Acknowledgement Agreement with certain lenders and Wells Fargo Bank, National Association, as administrative agent, whereby the aggregate revolving commitments under the Credit Agreement increased by \$50.0 million from \$450.0 million to \$500.0 million in accordance with the relevant provisions of the Credit Agreement.

The Credit Agreement matures on May 31, 2021. Before each anniversary of the Credit Agreement, we may request a one-year extension of the maturity date. The Credit Agreement is guaranteed by each of our subsidiaries that have gross assets equal to or greater than \$0.5 million. The revolving credit facility is currently unsecured, but we have agreed to provide collateral if we fail to meet certain financial conditions in the future. As of December 31, 2018, the borrowing base under the Credit Agreement was \$695.2 million, of which borrowings, including the Convertible

Notes (as defined below) and the Senior Notes (as defined

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below), of \$663.8 million were outstanding, \$5.1 million of letters of credit were outstanding and \$26.3 million was available to borrow under the Credit Agreement.

Interest is paid monthly on borrowings under the Credit Agreement at LIBOR plus 2.90%. The Credit Agreement applicable margin for LIBOR loans ranges from 2.65% to 3.25% based on our leverage ratio. At December 31, 2018, LIBOR was 2.46%.

The Credit Agreement contains various financial covenants, including a minimum tangible net worth, a leverage ratio, a minimum liquidity amount and an EBITDA to interest expense ratio. The Credit Agreement contains various covenants that, among other restrictions, limit the amount of our additional debt and our ability to make certain investments. At December 31, 2018, we were in compliance with all of the covenants contained in the Credit Agreement.

In connection with the issuance of our 6.875% Senior Notes due 2026 (the “Senior Notes”) in July 2018, we reduced the revolving commitment under the Credit Agreement from \$750.0 million to \$450.0 million pursuant to the First Amendment. During the year ended December 31, 2018, we recognized on our consolidated statements of operations \$3.4 million in debt extinguishment costs related to the Credit Agreement.

Convertible Notes

We issued \$85.0 million aggregate principal amount of our 4.25% Convertible Notes due 2019 (the “Convertible Notes”) in November 2014 pursuant to an exemption from the registration requirements afforded by Section 4(a)(2) of the Securities Act of 1933, as amended (the “Securities Act”). The Convertible Notes mature on November 15, 2019. Interest on the Convertible Notes is payable semi-annually in arrears on May 15 and November 15 of each year at a rate of 4.25%. When the Convertible Notes were issued, the fair value of \$76.5 million was recorded to notes payable. \$5.5 million of the remaining proceeds was recorded to additional paid in capital to reflect the equity component and the remaining \$3.0 million was recorded as a deferred tax liability. The carrying amount of the Convertible Notes is being accreted to face value over the term to maturity.

Prior to May 15, 2019, the Convertible Notes are convertible only upon satisfaction of any of the specified conversion events. On or after May 15, 2019 until the close of business on November 14, 2019 (the business day immediately preceding the stated maturity date of the Convertible Notes), the holders of the Convertible Notes can convert their Convertible Notes at any time at their option. Upon the election of a holder of Convertible Notes to convert their Convertible Notes, we may settle the conversion of the Convertible Notes using any combination of cash and shares of our common stock. It is our intent, and belief that we have the ability, to settle in cash the conversion of any Convertible Notes that the holders elect to convert. The initial conversion rate of the Convertible Notes is 46.4792 shares of our common stock for each \$1,000 principal amount of Convertible Notes, which represents an initial conversion price of approximately \$21.52 per share of our common stock. The conversion rate is subject to adjustments upon the occurrence of certain specified events.

During the fourth quarter of 2017, we received notice from holders of \$15.0 million principal amount of the Convertible Notes to convert their Convertible Notes. The conversion of such Convertible Notes was settled in the first quarter of 2018, resulting in the issuance of 486,679 shares of our common stock, a \$0.6 million reduction to debt discount and additional paid in capital, a \$0.2 million loss on the extinguishment of debt and a cash payment of \$15.0 million for the principal amount of such Convertible Notes. As of December 31, 2018, we have \$70.0 million aggregate principal amount of Convertible Notes outstanding.

During the fourth quarter of 2018, the Convertible Notes were convertible because the closing sale price of our common stock was greater than 130% of the \$21.52 conversion price on at least 20 trading days during the 30 trading day period ending on September 30, 2018. As a result, the holders of the Convertible Notes could elect to convert some or all of their Convertible Notes in accordance with the terms and provisions of the indenture governing the Convertible Notes during the conversion period of October 1, 2018 through December 31, 2018 (inclusive). The Convertible Notes continue to be convertible during the first quarter of 2019. As of the date of the filing of this Annual Report on Form 10-K, no other conversion notices have been received by us.

On July 6, 2018, concurrently with the offering of the Senior Notes, we entered into that certain First Supplemental Indenture, dated as of July 6, 2018, among us, our subsidiaries that guarantee our obligations under the Credit Agreement (the “Subsidiary Guarantors”) and Wilmington Trust, National Association, as trustee, which supplements

the indenture governing the Convertible Notes, pursuant to which (i) the subordination provisions in the indenture governing the Convertible Notes were eliminated, (ii) each Subsidiary Guarantor agreed (A) to, concurrently with the issuance of the Senior Notes, fully and unconditionally guarantee the Convertible Notes to the same extent that such Subsidiary Guarantor is guaranteeing the Senior Notes and (B) that such Subsidiary Guarantor's guarantee of the Convertible Notes ranks equally with such Subsidiary Guarantor's guarantee of the Senior Notes and (iii) the Company agreed to not, directly or indirectly, incur any indebtedness in the form of, or otherwise become liable in respect of, any notes or other debt securities issued pursuant to an indenture or note purchase agreement (including the Senior Notes) unless such indebtedness is equal with or contractually subordinated to the Convertible Notes in right of payment.

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Senior Notes Offering

On July 6, 2018, we issued \$300.0 million aggregate principal amount of the Senior Notes in an offering to persons reasonably believed to be qualified institutional buyers in the United States pursuant to Rule 144A under the Securities Act and to certain non-U.S. persons in transactions outside the United States pursuant to Regulation S under the Securities Act. Interest on the Senior Notes accrues at a rate of 6.875% per annum, payable semi-annually in arrears on January 15 and July 15 of each year, commencing on January 15, 2019, and the Senior Notes mature on July 15, 2026. Terms of the Senior Notes are governed by an indenture and supplemental indenture, each dated as of July 6, 2018, among us, the Subsidiary Guarantors and Wilmington Trust, National Association, as trustee.

We received net proceeds from the offering of the Senior Notes of approximately \$296.2 million, after deducting the initial purchasers' discounts of \$2.3 million and commissions and offering expenses of \$1.5 million. The net proceeds from the offering were used to repay a portion of the borrowings under the Credit Agreement.

Notes payable consist of the following (in thousands):

	December 31,	
	2018	2017
Notes payable under the Credit Agreement (\$500.0 million revolving credit facility at December 31, 2018) maturing on May 31, 2021; interest paid monthly at LIBOR plus 2.90%; net of debt issuance costs of approximately \$3.7 million and \$5.3 million at December 31, 2018 and December 31, 2017, respectively	\$290,131	\$394,714
4.25% Convertible Notes due November 15, 2019; interest paid semi-annually at 4.25%; net of debt issuance costs of approximately \$0.4 million and \$1.0 million at December 31, 2018 and December 31, 2017, respectively; and approximately \$1.3 million and \$3.5 million in unamortized discount at December 31, 2018 and December 31, 2017, respectively	68,251	80,481
Senior Notes due July 15, 2026; interest paid semi-annually at 6.875%; net of debt issuance costs of approximately \$2.5 million at December 31, 2018 and approximately \$2.1 million in unamortized discount at December 31, 2018	295,352	—
Total Notes Payable	\$653,734	\$475,195

As of December 31, 2018, the annual aggregate maturities of notes payable during each of the next five fiscal years are as follows (in thousands):

	Amount
2019	\$69,962
2020	—
2021	293,800
2022	—
2023	—
Thereafter	300,000
Total notes payable	663,762
Less: Debt discount	(3,447)
Less: Debt issuance costs	(6,581)
Net notes payable	\$653,734

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Capitalized Interest

Interest activity, including other financing costs, for notes payable for the periods presented is as follows (in thousands):

	Year Ended December 31,		
	2018	2017	2016
Interest incurred	\$38,216	\$24,275	\$18,457
Less: Amounts capitalized	(38,216)	(24,275)	(18,457)
Interest expense	\$—	\$—	\$—

Cash paid for interest \$23,376 \$19,704 \$14,339

Included in interest incurred was amortization of deferred financing costs for notes payable and amortization of the Convertible Notes and the Senior Notes discounts of \$4.6 million, \$4.1 million, and \$3.6 million for the years ended December 31, 2018, 2017, and 2016, respectively.

9. INCOME TAXES

All Company operations are domestic. The provision for income taxes consisted of the following (in thousands):

	Year ended December 31,		
	2018	2017	2016
Current:			
Federal	\$39,053	\$55,218	\$37,751
State	5,483	4,970	3,452
Current tax provision	44,536	60,188	41,203
Deferred:			
Federal	(663)	(1,918)	(2,451)
State	(61)	(174)	(111)
Deferred tax provision (benefit)	(724)	(2,092)	(2,562)
Total income tax provision	\$43,812	\$58,096	\$38,641

Income taxes paid were \$83.3 million, \$16.8 million and \$42.4 million for the years ended December 31, 2018, 2017 and 2016, respectively.

A reconciliation of the provision for income taxes and the amount computed by applying the statutory federal income tax rate to income before provision for income taxes for the years ended December 31, 2018, 2017 and 2016 (in thousands):

	Year Ended December 31,					
	2018		2017		2016	
Tax at federal statutory rate ⁽¹⁾	\$41,816	21.0 %	\$60,008	35.0 %	\$39,791	35.0 %
State income taxes (net of federal benefit)	4,263	2.1	3,060	1.8	2,143	1.9
Domestic production activity deduction	—	—	(5,461)	(3.2)	(3,727)	(3.3)
Non deductible expenses and other	(2,257)	(1.1)	(657)	(0.4)	435	0.4
Change in tax rates - deferred taxes	(10)	—	1,146	0.7	(1)	—
Tax at effective rate	\$43,812	22.0 %	\$58,096	33.9 %	\$38,641	34.0 %

(1) The Tax Act (as defined below) reduced the U.S. federal statutory rate from 35% to 21% beginning in 2018.

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Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes.

The components of net deferred tax assets and liabilities at December 31, 2018 and 2017 are as follows (in thousands):

	December 31	
	2018	2017
Deferred tax assets:		
Accruals and reserves	\$2,642	\$2,756
Inventory	755	475
Stock-based compensation	1,918	1,048
Other	297	38
Debt extinguishment	531	—
Total deferred tax assets	6,143	4,317
Deferred tax liabilities:		
Discount on Convertible Notes	(307)	(801)
Prepays	(2,370)	(1,035)
Tax depreciation in excess of book depreciation	(183)	(177)
Goodwill and other assets amortized for tax	(493)	(376)
Total deferred tax liabilities	(3,353)	(2,389)
Total net deferred tax assets (liabilities)	\$2,790	\$1,928

The Company has not recorded any accruals related to uncertain tax positions as of December 31, 2018 and 2017, respectively. We file U.S. and state income tax returns in jurisdictions with varying statutes of limitations. The statute of limitations with regards to our federal income tax filings is three years. The statute of limitations for our state tax jurisdictions is three to four years depending on the jurisdiction. In the normal course of business, we are subject to tax audits in various jurisdictions, and such jurisdictions may assess additional income taxes. We do not expect the outcome of any examination to have a material effect on our consolidated financial statements; however, audit outcomes and the timing of audit adjustments are subject to significant uncertainty.

On December 22, 2017, the President signed into law the U.S. federal income tax legislation commonly referred to as the “Tax Cuts and Jobs Act” (the “Tax Act”), reducing the U.S. federal corporate income tax rate for tax years beginning after December 31, 2017, among other changes. Under ASC 740, Income Taxes (“ASC 740”), the effects of the Tax Act are recognized in the period that includes the date of enactment. The effect of this change impacts our effective tax rate. The estimated impact on 2017 was to reduce the value of our deferred tax assets by approximately \$1.1 million and has been reflected in our effective tax rate reconciliation. The disclosed impact was our most reasonable estimate at that time based on our understanding of the Tax Act as it applied to our business. At December 31, 2018, we have completed our accounting for the income tax effects of the Tax Act on our deferred tax assets in accordance with the Securities and Exchange Commission Staff Accounting Bulletin No. 118 and ASC 740, and no material adjustments were required.

10. EQUITY

We are authorized to issue 250,000,000 shares of common stock, par value \$0.01 per share, and 5,000,000 shares of preferred stock, par value \$0.01 per share. As of December 31, 2018 and 2017, no shares of preferred stock were issued or outstanding.

At December 31, 2018, we had 23,746,385 shares of common stock issued and 22,707,385 shares of common stock outstanding, including 1,039,000 treasury shares of our common stock. On November 19, 2018, we purchased 39,000 shares of our common stock at \$38.58 per share to be held as treasury stock, in addition to the 1,000,000 treasury shares of our common stock previously purchased by us on November 21, 2014 at \$16.55 per share. At December 31, 2017, we had 22,845,580 shares of common stock issued and 21,845,580 shares of common stock outstanding, including the 1,000,000 treasury shares of our common stock purchased by us on November 21, 2014.

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On August 24, 2018, we and certain of our subsidiaries filed an automatic shelf registration statement on Form S-3 (Registration No. 333-227012), registering the offering and sale of an indeterminate amount of debt securities, guarantees of debt securities, preferred stock, common stock, warrants, depositary shares, purchase contracts and units that include any of these securities. Under our prior shelf registration statement, we established an at the market common stock offering program in September 2015 (the “2015 ATM Program”) and September 2016 (the “2016 ATM Program”) with Deutsche Bank Securities Inc., J.P. Morgan Securities LLC, JMP Securities LLC and Builder Advisor Group, LLC, as sales agents to sell up to \$30.0 million and \$25.0 million, respectively, of our common stock. We issued and sold 743,554 shares of our common stock under the 2015 ATM Program, and received net proceeds of approximately \$19.8 million, during 2016. We issued and sold 354,620 and 250,000 shares of our common stock under the 2016 ATM Program, and received net proceeds of approximately \$15.5 million and \$9.0 million, during 2017 and 2016, respectively.

Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share for the years ended December 31, 2018, 2017, and 2016.

	For the Year Ended December 31,		
	2018	2017	2016
Numerator (in thousands):			
Net income	\$ 155,286	\$ 113,306	\$ 75,031
Denominator:			
Basic weighted average shares outstanding	22,551,762	21,604,932	20,798,333
Effect of dilutive securities:			
Convertible Notes - treasury stock method	2,030,023	1,975,648	1,044,519
Stock-based compensation units	310,489	352,542	181,239
Diluted weighted average shares outstanding	24,892,274	23,933,122	22,024,091
Basic earnings per share	\$ 6.89	\$ 5.24	\$ 3.61
Diluted earnings per share	\$ 6.24	\$ 4.73	\$ 3.41
Antidilutive non-vested restricted stock units excluded from calculation of diluted earnings per share	20,462	16,473	13,613

In accordance with ASC 260-10, Earnings Per Share, we calculated the dilutive effect of the Convertible Notes using the treasury stock method, since we have the intent and ability to settle the principal amount of the outstanding Convertible Notes in cash. Under the treasury stock method, the Convertible Notes have a dilutive impact on diluted earnings per share to the extent that the average market price of our common stock for a reporting period exceeds the conversion price of \$21.52 per share.

During the years ended December 31, 2018, 2017, and 2016, the average market price of our common stock exceeded the conversion price of \$21.52 per share, therefore the calculation of diluted earnings per share for all years presented includes the effect of our common stock related to the conversion spread of the Convertible Notes.

11. STOCK-BASED COMPENSATION**Non-performance Based Restricted Stock Units**

A total of 3,000,000 shares of our common stock have been reserved for issuance under the LGI Homes, Inc. Amended and Restated 2013 Equity Incentive Plan (the “2013 Incentive Plan”). The 2013 Incentive Plan was approved by our stockholders at our 2017 Annual Meeting of Stockholders in May 2017. There were 171,055 restricted stock units (“RSUs”) outstanding at December 31, 2018, issued at a \$0.00 exercise price.

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The following table summarizes the activity of our time-vested RSUs:

	Shares	Weighted Average Grant Date Fair Value
Balance at December 31, 2015	107,814	\$ 16.48
Granted	62,453	\$ 23.66
Vested	(29,010)	\$ 14.73
Forfeited	(7,404)	\$ 17.97
Balance at December 31, 2016	133,853	\$ 20.13
Granted	76,586	\$ 36.83
Vested	(25,803)	\$ 18.45
Forfeited	(9,536)	\$ 20.48
Balance at December 31, 2017	175,100	\$ 27.66
Granted	54,874	\$ 57.60
Vested	(51,694)	\$ 20.79
Forfeited	(7,225)	\$ 34.77
Balance at December 31, 2018	171,055	\$ 39.04

In 2018, we issued 15,867 RSUs to senior management for the time-based portion of our 2018 long-term incentive compensation program and 11,780 RSUs for 2017 bonuses to managers under the Annual Bonus Plan, which generally cliff vest on the third anniversary of the grant date. In 2017, we issued 27,764 RSUs to senior management for the time-based portion of our 2017 long-term incentive compensation program and 18,366 RSUs for 2016 bonuses to managers under the Annual Bonus Plan, which generally cliff vest on the third anniversary of the grant date. In 2016, we issued 21,905 RSUs to senior management for the time-based portion of our 2016 long-term incentive compensation program and 22,059 RSUs for 2015 bonuses to certain officers and managers under the Annual Bonus Plan, which vest over three years. In addition, during the years ended December 31, 2018, 2017 and 2016, we issued 27,227, 30,456 and 18,489 RSUs, respectively, to certain employees, executives and non-employee directors, which vest over periods ranging from one to three years. Under the terms of the grant award agreements, all of the RSUs may only be settled in shares of our common stock.

We recognized \$2.0 million, \$1.3 million, and \$0.8 million of stock-based compensation expense related to outstanding RSUs grants for the years ended December 31, 2018, 2017 and 2016, respectively. At December 31, 2018, we had unrecognized compensation cost of \$3.6 million related to unvested RSUs, which is expected to be recognized over a weighted average period of 2.1 years.

Performance Based Restricted Stock Units

The Compensation Committee of our Board of Directors has granted awards of performance-based RSUs (“PSUs”) under the 2013 Incentive Plan to certain members of senior management based on three-year performance cycles. At December 31, 2018, there were 253,821 PSUs outstanding that have been granted to certain members of management at a \$0.00 exercise price. The PSUs provide for shares of our common stock to be issued based on the attainment of certain performance metrics over the applicable three-year periods. The number of shares of our common stock that may be issued to the recipients for the PSUs range from 0% to 200% of the target amount depending on actual results as compared to the target performance metrics. The terms of the PSUs provide that the payouts will be capped at 100% of the target number of PSUs granted if absolute total stockholder return is negative during the performance period, regardless of EPS performance; this market condition applies for amounts recorded above target. The compensation expense associated with the grants of PSU is determined using the derived grant date fair value, based on a third-party valuation analysis, and expensed over the applicable period. The PSUs vest upon the determination date for the actual results at the end of the three-year period and require that the recipients continue to be employed by us through the determination date. The PSUs can only be settled in shares of our common stock.

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Period Granted	Performance Period	Target PSUs Outstanding at December 31, 2017	Target PSUs Granted	Target PSUs Vested	Target PSUs Forfeited	Target PSUs Outstanding at December 31, 2018	Weighted Average Grant Date Fair Value
2015	2015 - 2017	120,971	—	(120,971)	—	—	\$ 13.34
2016	2016 - 2018	87,605	—	—	(3,929)	83,676	\$ 21.79
2017	2017 - 2019	111,035	—	—	(2,788)	108,247	\$ 31.64
2018	2018 - 2020	—	61,898	—	—	61,898	\$ 64.60
Total		319,611	61,898	(120,971)	(6,717)	253,821	

At December 31, 2018, management estimates that the recipients will receive approximately 100%, 200%, and 200%, of the 2018, 2017, and 2016 target number of PSUs, respectively, at the end of the applicable three-year performance cycle based on projected performance compared to the target performance metrics. The 2015 - 2017 performance period grants vested on March 15, 2018 at 200% of the target number. We recognized \$4.0 million, \$2.9 million, and \$2.6 million of total stock-based compensation expense related to outstanding PSUs grants for the years ended December 31, 2018, 2017 and 2016, respectively. At December 31, 2018, we had unrecognized compensation cost of \$5.3 million, based on the probable amount, related to unvested PSUs, which is expected to be recognized over a weighted average period of 1.8 years.

Employee Stock Purchase Plan

In 2016, we adopted the LGI Homes, Inc. Employee Stock Purchase Plan (the “ESPP”). The ESPP provides for employees to make quarterly elections for payroll withholdings to purchase shares of our common stock at a 15% discount from the closing price of our common stock on the purchase date, which is the last business day of each calendar quarter. During the years ended December 31, 2018, 2017 and 2016, we issued 49,744, 33,887, and 19,398 shares of our common stock to the ESPP participants. We received net proceeds of approximately \$2.7 million, \$1.6 million and \$0.6 million related to the ESPP for 2018, 2017, and 2016, respectively. We recognized \$0.4 million, \$0.2 million, and \$0.1 million in stock compensation expense related to the ESPP for 2018, 2017, and 2016, respectively. The ESPP contributions are not refundable (other than in the case of termination of employment) and, therefore, the shares purchasable with the amounts withheld are included in weighted-average shares outstanding for both basic and diluted earnings per share. The maximum aggregate number of shares of our common stock which may be issued pursuant to the ESPP is 500,000 shares, and as of December 31, 2018, 396,971 shares of our common stock remain available for issuance under the ESPP.

12. FAIR VALUE DISCLOSURES

ASC Topic 820, Fair Value Measurements (“ASC 820”), defines fair value as “the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date” within an entity’s principal market, if any. The principal market is the market in which the reporting entity would sell the asset or transfer the liability with the greatest volume and level of activity, regardless of whether it is the market in which the entity will ultimately transact for a particular asset or liability or if a different market is potentially more advantageous. Accordingly, this exit price concept may result in a fair value that differs from the transaction price or market price of the asset or liability.

ASC 820 provides a framework for measuring fair value under GAAP, expands disclosures about fair value measurements, and establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The three levels of the fair value hierarchy are summarized as follows:

Level 1 - Fair value is based on quoted prices in active markets for identical assets or liabilities.

Level 2 - Fair value is determined using significant observable inputs, generally either quoted prices in active markets for

similar assets or liabilities, or quoted prices in markets that are not active.

Level 3 - Fair value is determined using one or more significant inputs that are unobservable in active markets at the measurement date, such as a pricing model, discounted cash flow, or similar technique.

We utilize fair value measurements to account for certain items and account balances within our consolidated financial statements. Fair value measurements may also be utilized on a nonrecurring basis, such as for the impairment of long-lived assets. The fair value of financial instruments, including cash and cash equivalents, accounts receivable and accounts payable, approximate their carrying amounts due to the short-term nature of these instruments. As of December 31, 2018, the Credit Facility's carrying value approximates market value since it has a floating interest rate, which increases or decreases with market interest rates and our leverage ratio.

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In order to determine the fair value of the Convertible Notes and the Senior Notes listed below, the future contractual cash flows are discounted at our estimate of current market rates of interest, which were determined based upon the average interest rates of similar convertible notes and senior notes within the homebuilding industry (Level 2 measurement).

The following table below shows the level and measurement of liabilities at December 31, 2018 and 2017 (in thousands):

	Fair Value Hierarchy	December 31, 2018		December 31, 2017	
		Carrying Value	Estimated Fair Value ⁽¹⁾	Carrying Value	Estimated Fair Value ⁽¹⁾
Convertible Notes	Level 2	\$68,251	\$67,787	\$80,481	\$81,523
Senior Notes	Level 2	\$295,352	\$296,905	\$—	\$—

(1) Excludes the fair value of the equity component of the Convertible Notes. See the “Convertible Notes” section within Note 8 for further details.

13. RELATED PARTY TRANSACTIONS

Land Purchases from Affiliates

As of December 31, 2018, we have two land purchase contracts to purchase a total of 198 finished lots in Pasco County and Manatee County, Florida from affiliates of one of our directors for a total base purchase price of approximately \$6.9 million. The lots will be purchased in takedowns, subject to annual price escalation ranging from 3% to 6% per annum, and may provide for additional payments to the seller at the time of sale to the homebuyer. We have a \$0.7 million non-refundable deposit at December 31, 2018 related to these land purchase contracts. We anticipate closing on these contracts in the first half of 2019.

In April 2018, we completed our commitments under a land purchase contract to purchase 106 finished lots in Montgomery County, Texas from an affiliate of a family member of our chief executive officer for a total base purchase price of approximately \$8.0 million. The lots were purchased in takedowns of at least 21 lots during successive six-month periods, subject to 5% annual price escalation and certain price protection terms. During 2018, we purchased the final takedown of 22 lots under this land purchase contract for \$1.8 million and a \$100,000 non-refundable deposit related to this land purchase contract was applied to this takedown. We purchased 42 lots under this land purchase contract during 2017 and 2016 for \$3.4 million (escalated price) and \$3.2 million, respectively.

Consulting Fees

We had a three-year consulting agreement with a family member of our chief executive officer for \$100,000 per year payable on a monthly basis, which was terminated in June 2016 by mutual agreement of the parties. Consulting fees were \$83,333 for the year ended December 31, 2016.

Home Sales to Affiliates

In 2018, we had no home closings to affiliates. In 2017, we sold three homes to an affiliate of one of our directors for approximately \$0.7 million. In 2016, we sold two homes to an affiliate of one of our directors for approximately \$0.5 million.

14. RETIREMENT BENEFITS

Our employees are eligible to participate in a 401(k) savings plan. Employees are eligible to participate after completing 90 days of service and having attained the age of 21. Salary deferrals are allowed in amounts up to 100% of an eligible employee’s salary, not to exceed the maximum allowed by law. A discretionary match may be made by us of up to 100% of the first 4% of an eligible employee’s deferral, not to exceed the maximum allowed by law. For each of the years ended December 31, 2018, 2017 and 2016, our matching contributions were \$2.6 million, \$1.8 million and \$0.8 million, respectively.

15. COMMITMENTS AND CONTINGENCIES

Contingencies

In the ordinary course of doing business, we are subject to claims or proceedings from time to time relating to the purchase, development, and sale of real estate and homes and other aspects of our homebuilding operations. Management believes that these claims include usual obligations incurred by real estate developers and residential home builders in the normal course of business. In the opinion of management, these matters will not have a material effect on our consolidated financial position, results of operations or cash flows.

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We have provided unsecured environmental indemnities to certain lenders and other counterparties. In each case, we have performed due diligence on the potential environmental risks including obtaining an independent environmental review from outside environmental consultants. These indemnities obligate us to reimburse the guaranteed parties for damages related to environmental matters. There is no term or damage limitation on these indemnities; however, if an environmental matter arises, we may have recourse against other previous owners. In the ordinary course of doing business, we are subject to regulatory proceedings from time to time related to environmental and other matters. In the opinion of management, these matters will not have a material effect on our consolidated financial position, results of operations, or cash flows.

Land Deposits

We have land purchase contracts, generally through cash deposits, for the right to purchase land or lots at a future point in time with predetermined terms. We do not have title to the property, and obligations with respect to the land purchase contracts are generally limited to the forfeiture of the related nonrefundable cash deposits. The following is a summary of our land purchase deposits included in pre-acquisition costs and deposits (in thousands, except for lot count):

	December 31,	
	2018	2017
Land deposits and option payments	\$40,015	\$17,761
Commitments under the land purchase contracts if the purchases are consummated	\$776,224	\$460,714
Lots under land purchase contracts	22,820	18,758

As of December 31, 2018 and 2017, approximately \$25.2 million and \$8.4 million, respectively, of the land deposits are related to purchase contracts to deliver finished lots that are refundable under certain circumstances and secured by mortgages or letters of credit, or guaranteed by the seller or its affiliates.

Leasing Arrangements

We lease office facilities and certain equipment under non-cancellable operating lease agreements. Rent escalation provisions are accounted for using the straight-line method. Rent expense includes common area maintenance costs. Rent expense totaled \$1.0 million, \$1.0 million and \$0.8 million for the years ended December 31, 2018, 2017 and 2016, respectively.

Future minimum lease payments under non-cancellable operating lease agreements are as follows at December 31, 2018 (in thousands):

2019	\$827
2020	760
2021	768
2022	706
2023	722
Thereafter	2,837
Total	\$6,620

Bonding and Letters of Credit

We have outstanding letters of credit and performance and surety bonds totaling \$77.5 million (including \$5.1 million of letters of credit issued under the Credit Agreement) and \$49.7 million at December 31, 2018 and 2017, respectively, related to our obligations for site improvements at various projects. Management does not believe that draws upon the letters of credit, surety bonds, or financial guarantees if any, will have a material effect on our consolidated financial position, results of operations, or cash flows.

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16. SEGMENT INFORMATION

Beginning in the fourth quarter of 2018, we changed our reportable segments to Central, Northwest, Southeast, Florida, and West. These segments reflect the way the Company evaluates its business performance and manages its operations. Prior year information has been restated for corresponding items of our segment information.

We operate one principal homebuilding business that is organized and reports by division. We have seven operating segments that we aggregate into five reportable segments at December 31, 2018: our Central, Northwest, Southeast, Florida, and West divisions. The Central division is our largest division and comprised approximately 41.5%, 42.4% and 51.2% of total home sales revenues for the years ended December 31, 2018, 2017 and 2016, respectively.

In accordance with ASC Topic 280, Segment Reporting, operating segments are defined as components of an enterprise for which separate financial information is available that is evaluated regularly by the chief operating decision-makers (“CODMs”) in deciding how to allocate resources and in assessing performance. The CODMs primarily evaluate performance based on the number of homes closed, gross margin and average sales price.

The seven operating segments qualify as our five reporting segments. In determining the most appropriate reportable segments, we consider operating segments’ economic and other characteristics, including home floor plans, average selling prices, gross margin percentage, geographical proximity, production construction processes, suppliers, subcontractors, regulatory environments, customer type, and underlying demand and supply. Each operating segment follows the same accounting policies and is managed by our management team. We have no inter-segment sales, as all sales are to external customers. Operating results for each segment may not be indicative of the results for such segment had it been an independent, stand-alone entity for the periods presented. Financial information relating to our reportable segments was as follows (in thousands):

	For the Year Ended December 31,		
	2018	2017	2016
Revenues:			
Central	\$623,751	\$533,254	\$429,505
Northwest	277,567	215,421	86,496
Southeast	271,073	183,422	111,651
Florida	180,950	199,733	115,276
West	151,059	126,130	95,392
Total home sales revenues	\$1,504,400	\$1,257,960	\$838,320
Net income (loss) before income taxes:			
Central	\$104,625	\$89,133	\$73,026
Northwest	40,906	34,206	6,612
Southeast	29,078	19,959	11,996
Florida	21,341	25,687	14,471
West	13,595	5,890	10,108
Corporate ⁽¹⁾	(10,447)	(3,473)	(2,541)
Total net income (loss) before income taxes	\$199,098	\$171,402	\$113,672

(1) The Corporate balance consists primarily of general and administration unallocated costs for various shared service functions, as well as our warranty reserve and loss on extinguishment of debt. Actual warranty expenses are reflected within the reportable segments.

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	December 31,	
Assets:	2018	2017
Central	\$569,409	\$454,899
Northwest	200,443	159,489
Southeast	300,758	155,928
Florida	106,398	119,257
West	161,514	96,647
Corporate ⁽¹⁾	56,951	93,672
Total assets	\$1,395,473	\$1,079,892

(1) As of December 31, 2018, the Corporate balance consists primarily of cash, prepaid insurance and prepaid expenses. As of December 31, 2017, the Corporate balance consists primarily of cash, deposits and pre-acquisition costs, prepaid insurance and prepaid expenses. As of December 31, 2017, \$18.9 million of deposits and pre-acquisition costs were reported at Corporate and balances as of December 31, 2018 were allocated to the five reportable segments.

17. SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)

Quarterly results are as follows (in thousands, except per share data):

	First Quarter 2018	Second Quarter 2018	Third Quarter 2018	Fourth Quarter 2018
Total home sales revenues	\$279,024	\$419,847	\$380,369	\$425,160
Gross margin	69,259	109,765	97,334	103,558
Income before income taxes	31,227	62,671	48,991	56,209
Net income	27,302	47,608	37,723	42,653
Basic earnings per share	1.23	2.11	1.66	1.89
Diluted earnings per share	1.10	1.90	1.52	1.72

	First Quarter 2017	Second Quarter 2017	Third Quarter 2017	Fourth Quarter 2017
Total home sales revenues	\$162,911	\$324,178	\$365,896	\$404,975
Gross margin	43,499	86,348	91,896	98,677
Income before income taxes	16,842	48,642	50,877	55,041
Net income	11,780	32,199	33,687	35,640
Basic earnings per share	0.55	1.49	1.55	1.65
Diluted earnings per share	0.52	1.39	1.40	1.43

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ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

Under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, management has evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) or 15d-15(e) of the Securities Exchange Act of 1934) as of December 31, 2018. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, our disclosure controls and procedures are effective to ensure information is recorded, processed, summarized and reported within the periods specified in the Securities and Exchange Commission's rules and forms and is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Management's Report on Internal Control Over Financial Reporting

Management of LGI Homes, Inc. (the "Company") is responsible for establishing and maintaining effective internal control over financial reporting and for the assessment of the effectiveness of internal control over financial reporting. The Company's internal control over financial reporting is a process designed, as defined in Rule 13a-15(f) under the Exchange Act, to provide reasonable assurance to the Company's management and board of directors regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with generally accepted accounting principles in the United States.

In connection with respect to the preparation of the Company's annual consolidated financial statements, and the processes under which they were prepared, management of the Company has undertaken an assessment of the effectiveness of the Company's internal control over financial reporting based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the 2013 COSO framework). Management's assessment included an evaluation of the design of the Company's internal control over financial reporting and testing of the operational effectiveness of the Company's internal control over financial reporting. Based on this assessment, management has concluded that the Company's internal control over financial reporting was effective as of December 31, 2018.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Ernst & Young LLP, the independent registered public accounting firm that audited the Company's consolidated financial statements included in this Annual Report on Form 10-K, has issued an attestation report on the effectiveness of the Company's internal control over financial reporting which appears below.

Changes in Internal Controls

No change in our internal control over financial reporting as such term is defined in Exchange Act Rule 13a-15(f) occurred during the year ended December 31, 2018 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholders and the Board of Directors of LGI Homes, Inc.

Opinion on Internal Control over Financial Reporting

We have audited LGI Homes, Inc.'s internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 Framework), (the COSO criteria). In our opinion, LGI Homes, Inc. (the Company) maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated balance sheets of the Company as of December 31, 2018 and 2017, the related consolidated statements of operations, equity and cash flows for each of the three years in the period ended December 31, 2018, and the related notes and our report dated February 26, 2019 expressed an unqualified opinion thereon.

Basis for Opinion

The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying "Management's Report on Internal Control Over Financial Reporting". Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB. We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects.

Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control Over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Ernst & Young LLP

Houston, Texas

February 26, 2019

ITEM 9B. OTHER INFORMATION

None.

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PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information called for by Item 10, to the extent not set forth in “Business—Executive Officers” in Item 1, will be set forth in the definitive proxy statement relating to the 2019 annual meeting of stockholders of LGI Homes, Inc. pursuant to SEC Regulation 14A. Such definitive proxy statement relates to a meeting of stockholders involving the election of directors and the portions thereof called for by Item 10 are incorporated herein by reference pursuant to Instruction G to Form 10-K.

ITEM 11. EXECUTIVE COMPENSATION

The information called for by Item 11 will be set forth in the definitive proxy statement relating to the 2019 annual meeting of stockholders of LGI Homes, Inc. pursuant to SEC Regulation 14A. Such definitive proxy statement relates to a meeting of stockholders involving the election of directors and the portions thereof called for by Item 11 are incorporated herein by reference pursuant to Instruction G to Form 10-K.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information called for by Item 12 will be set forth in the definitive proxy statement relating to the 2019 annual meeting of stockholders of LGI Homes, Inc. pursuant to SEC Regulation 14A. Such definitive proxy statement relates to a meeting of stockholders involving the election of directors and the portions thereof called for by Item 12 are incorporated herein by reference pursuant to Instruction G to Form 10-K.

ITEM 13. CERTAIN RELATIONSHIPS, RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE

The information called for by Item 13 will be set forth in the definitive proxy statement relating to the 2019 annual meeting of stockholders of LGI Homes, Inc. pursuant to SEC Regulation 14A. Such definitive proxy statement relates to a meeting of stockholders involving the election of directors and the portions thereof called for by Item 13 are incorporated herein by reference pursuant to Instruction G to Form 10-K.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The information called for by Item 14 will be set forth in the definitive proxy statement relating to the 2019 annual meeting of stockholders of LGI Homes, Inc. pursuant to SEC Regulation 14A. Such definitive proxy statement relates to a meeting of stockholders involving the election of directors and the portions thereof called for by Item 14 are incorporated herein by reference pursuant to Instruction G to Form 10-K.

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PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENTS SCHEDULES

(1) The following Consolidated Financial Statements as set forth in Item 8 of this report are filed herein.

Consolidated Financial Statements

Report of Independent Registered Public Accounting Firm

Consolidated Balance Sheets as of December 31, 2018 and 2017

Consolidated Statements of Operations for the years ended December 31, 2018, 2017 and 2016

Consolidated Statements of Equity from December 31, 2015 to December 31, 2018

Consolidated Statements of Cash Flows for the years ended December 31, 2018, 2017 and 2016

Notes to the Consolidated Financial Statements for the years ended December 31, 2018, 2017 and 2016

(2) Financial Statement Schedules

All schedules are omitted because the required information is not present, in amounts sufficient to require submission of the schedule, or because the required information is included in the financial statements and related notes thereto.

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(3) Exhibits

The exhibits filed or furnished as part of this annual report on Form 10-K are listed in the Index to Exhibits, which Index includes the management contracts or compensatory plans or arrangements required to be filed as exhibits to this Annual Report on Form 10-K by Item 601(b)(10)(iii) of Regulation S-K, and is incorporated in this Item by reference.

Exhibit No.	Description
3.1	<u>Certificate of Incorporation of LGI Homes, Inc. (incorporated herein by reference to Exhibit 3.1 to the Registration Statement on Form S-1 (Registration No. 333-190853) of LGI Homes, Inc. filed with the SEC on August 28, 2013).</u>
3.2	<u>Bylaws of LGI Homes, Inc. (incorporated herein by reference to Exhibit 3.2 to the Registration Statement on Form S-1 (Registration No. 333-190853) of LGI Homes, Inc. filed with the SEC on August 28, 2013).</u>
4.1	<u>Indenture dated as of November 21, 2014, by and between LGI Homes, Inc. and Wilmington Trust, National Association, as trustee, governing LGI Homes, Inc.'s 4.25% Convertible Notes due 2019, including a form of note (incorporated herein by reference to Exhibit 4.01 to the Current Report on Form 8-K (File No. 001-36126) of LGI Homes, Inc. filed with the SEC on November 26, 2014).</u>
4.2	<u>First Supplemental Indenture, dated as of July 6, 2018, among LGI Homes, Inc., the subsidiary guarantors listed therein and Wilmington Trust, National Association, as trustee, governing LGI Homes, Inc.'s 4.25% Convertible Notes due 2019 (incorporated herein by reference to Exhibit 4.3 to the Current Report on Form 8-K (File No. 001-36126) of LGI Homes, Inc. filed with the SEC on July 6, 2018).</u>
4.3	<u>Indenture, dated as of July 6, 2018, among LGI Homes, Inc., the potential subsidiary guarantors listed therein and Wilmington Trust, National Association, as trustee (incorporated herein by reference to Exhibit 4.1 to the Current Report on Form 8-K (File No. 001-36126) of LGI Homes, Inc. filed with the SEC on July 6, 2018).</u>
4.4	<u>First Supplemental Indenture, dated as of July 6, 2018, among LGI Homes, Inc., the subsidiary guarantors listed therein and Wilmington Trust, National Association, as trustee, governing LGI Homes, Inc.'s 6.875% Senior Notes due 2026, including the form of the senior notes (incorporated herein by reference to Exhibit 4.2 to the Current Report on Form 8-K (File No. 001-36126) of LGI Homes, Inc. filed with the SEC on July 6, 2018).</u>
10.1+	<u>Employment Agreement, dated as of November 13, 2018, between the Company and Eric Lipar, the Company's Chief Executive Officer and Chairman of the Board (incorporated herein by reference to Exhibit 10.1 to the Current Report on Form 8-K (File No. 001-36126) of LGI Homes, Inc. filed with the SEC on November 16, 2018).</u>
10.2+	<u>LGI Homes, Inc. Amended and Restated 2013 Equity Incentive Plan (incorporated herein by reference to Exhibit 10.1 to Amendment No. 1 to the Registration Statement on Form S-1 (Registration No. 333-190853) of LGI Homes, Inc. filed with the SEC on May 9, 2017).</u>
10.3+	<u>LGI Homes, Inc. 2016 Employee Stock Purchase Plan (incorporated herein by reference to Exhibit 10.1 to the Registration Statement on Form S-8 (Registration No. 333-211843) of LGI Homes, Inc. filed with the SEC on June 3, 2016).</u>
10.4	<u>Third Amended and Restated Credit Agreement, dated as of May 25, 2018, by and among LGI Homes, Inc., each of the financial institutions initially a signatory thereto, and Wells Fargo Bank, National Association, as administrative agent, with Wells Fargo Securities, LLC, as sole Lead Arranger and sole Bookrunner, and Fifth Third Bank and U.S. Bank, National Association, as Documentation Agents (incorporated herein by reference to Exhibit 10.1 to the Current Report on Form 8-K (File No. 001-36126) of LGI Homes, Inc. filed with the SEC on May 29, 2018).</u>
10.5	<u>First Amendment to the Third Amended and Restated Credit Agreement, dated as of June 19, 2018, by and among LGI Homes, Inc., the lenders party thereto and Wells Fargo Bank, National Association, as</u>

administrative agent (incorporated herein by reference to Exhibit 10.1 to the Current Report on Form 8-K (File No. 001-36126) of LGI Homes, Inc. filed with the SEC on June 21, 2018).

- 10.6 Lender Acknowledgement Agreement dated as of October 18, 2018 by and among LGI Homes, Inc., Wells Fargo Bank, National Association, as an Increasing Lender and as administrative agent, Fifth Third Bank, U.S. Bank National Association d/b/a Housing Capital Company, Bank of America, N.A., BMO Harris Bank N.A., Compass Bank, Flagstar Bank, FSB, Deutsche Bank AG New York Branch, ZB, N.A. dba Amegy Bank, Associated Bank, National Association, Academy Bank, N.A., and Sunflower Bank, N.A. (incorporated herein by reference to Exhibit 10.1 to the Form 8-K of LGI Homes, Inc. (File No. 001-36126) filed with the SEC on October 23, 2018).
- 21.1* List of Subsidiaries of LGI Homes, Inc.
- 23.1* Consent of Independent Registered Public Accounting Firm
- 31.1* CEO Certification, Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2* CFO Certification, Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1* Certification Pursuant to 18 U.S.C. Section 1350, as adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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32.2* Certification Pursuant to 18 U.S.C. Section 1350, as adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

101.INS† XBRL Instance Document.

101.SCH†XBRL Taxonomy Extension Schema Document.

101.CAL†XBRL Taxonomy Extension Calculation Linkbase Document.

101.DEF†XBRL Taxonomy Extension Definition Linkbase Document.

101.LAB†XBRL Taxonomy Extension Label Linkbase Document.

101.PRE† XBRL Taxonomy Extension Presentation Linkbase Document.

* Filed herewith.

+ Management contract or compensatory plan or arrangement required to be filed as an exhibit to this Form 10-K.

XBRL information is deemed not filed or a part of a registration statement or Annual Report for purposes of Sections ¶1 and 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under such sections.

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ITEM 16. FORM 10-K SUMMARY

None.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

LGI Homes, Inc.

Date: February 26, 2019 /s/ Eric Lipar
Eric Lipar
Chief Executive Officer and Chairman of the Board

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

Signature	Title	Date
/s/ Eric Lipar Eric T. Lipar	Chief Executive Officer and Chairman of the Board (Principal Executive Officer)	February 26, 2019
/s/ Charles Merdian Charles Merdian	Chief Financial Officer and Treasurer (Principal Financial and Accounting Officer)	February 26, 2019
/s/ Ryan Edone Ryan Edone	Director	February 26, 2019
/s/ Duncan Gage Duncan Gage	Director	February 26, 2019
/s/ Laura Miller Laura Miller	Director	February 26, 2019
/s/ Bryan Sansbury Bryan Sansbury	Director	February 26, 2019
/s/ Steven Smith Steven Smith	Director	February 26, 2019
/s/ Robert Vaharadian Robert Vaharadian	Director	February 26, 2019