NVR INC
Form 10-Q
April 29, 2016

United States

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2016

OR

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

For the transition period from ____ to ____

Commission File Number: 1-12378

NVR, Inc.

(Exact name of registrant as specified in its charter)

Virginia	54-1394360
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

11700 Plaza America Drive, Suite 500

Reston, Virginia 20190

(703) 956-4000

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

(Not Applicable)

(Former name, former address, and former fiscal year if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

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

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

As of April 27, 2016 there were 3,896,889 total shares of common stock outstanding.

NVR, Inc.

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PART I. FINANCIAL INFORMATION

Item 1.Financial Statements

NVR, Inc.

Condensed Consolidated Balance Sheets

(in thousands, except share and per share data)

(unaudited)

	March 31, 2016	December 31, 2015
ASSETS		
Homebuilding:		
Cash and cash equivalents	$302,945	$397,522
Receivables	13,829	11,482
Inventory:		
Lots and housing units, covered under sales agreements with customers	915,352	785,982
Unsold lots and housing units	168,945	147,832
Land under development	163,826	60,611
Building materials and other	13,012	12,101
	1,261,135	1,006,526
Assets related to consolidated variable interest entity	1,731	1,749
Contract land deposits, net	346,951	343,295
Property, plant and equipment, net	44,933	44,651
Reorganization value in excess of amounts allocable to identifiable assets, net	41,580	41,580
Goodwill and finite-lived intangible assets, net	3,636	3,982
Other assets	289,800	281,381
	2,306,540	2,132,168
Mortgage Banking:		
Cash and cash equivalents	15,042	26,804
Mortgage loans held for sale, net	189,191	319,553
Property and equipment, net	5,093	5,313
Reorganization value in excess of amounts allocable to identifiable assets, net	7,347	7,347
Other assets	18,438	20,533
	235,111	379,550
Total assets	$2,541,651	$2,511,718
LIABILITIES AND SHAREHOLDERS' EQUITY		
Homebuilding:		
Accounts payable	$232,221	$227,437
Accrued expenses and other liabilities	298,045	304,922
Liabilities related to consolidated variable interest entity	1,230	1,091

Customer deposits	126,552	110,965
Senior notes	595,999	595,847
	1,254,047	1,240,262
Mortgage Banking:		
Accounts payable and other liabilities	31,141	32,291
	31,141	32,291
Total liabilities	1,285,188	1,272,553
Commitments and contingencies		
Shareholders' equity:		
Common stock, $0.01 par value; 60,000,000 shares authorized; 20,555,330 shares issued as of both March 31, 2016 and December 31, 2015	206	206
Additional paid-in capital	1,467,000	1,447,795
Deferred compensation trust – 108,621 and 108,614 shares of NVR, Inc. common stock as of March 31, 2016 and December 31, 2015	(17,343)	(17,333)
Deferred compensation liability	17,343	17,333
Retained earnings	5,335,417	5,270,114
Less treasury stock at cost – 16,660,526 and 16,664,342 shares as of March 31, 2016 and December 31, 2015, respectively	(5,546,160)	(5,478,950)
Total shareholders' equity	1,256,463	1,239,165
Total liabilities and shareholders' equity	$2,541,651	$2,511,718

See notes to condensed consolidated financial statements.

NVR, Inc.

Condensed Consolidated Statements of Income

(in thousands, except per share data)

(unaudited)

	Three Months Ended March 31,	
	2016	2015
Homebuilding:		
Revenues	$1,121,504	$941,538
Other income	767	725
Cost of sales	(925,760)	(781,668)
Selling, general and administrative	(98,015)	(98,229)
Operating income	98,496	62,366
Interest expense	(4,842)	(5,782)
Homebuilding income	93,654	56,584
Mortgage Banking:		
Mortgage banking fees	22,522	16,211
Interest income	1,674	1,078
Other income	258	105
General and administrative	(14,550)	(11,479)
Interest expense	(246)	(136)
Mortgage banking income	9,658	5,779
Income before taxes	103,312	62,363
Income tax expense	(38,009)	(23,305)
Net income	$65,303	$39,058
Basic earnings per share	$16.81	$9.63
Diluted earnings per share	$15.79	$9.22
Basic weighted average shares outstanding	3,884	4,057
Diluted weighted average shares outstanding	4,135	4,235

See notes to condensed consolidated financial statements.

NVR, Inc.

Condensed Consolidated Statements of Cash Flows

(in thousands)

(unaudited)

	Three Months Ended March 31, 2016	2015
Cash flows from operating activities:		
Net income	$65,303	$39,058
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	5,447	5,281
Excess income tax benefit from equity-based compensation	(6,284)	(7,998)
Equity-based compensation expense	10,549	13,399
Contract land deposit (recoveries) impairments, net	(1,303)	33
Gain on sale of loans, net	(17,022)	(11,238)
Mortgage loans closed	(688,361)	(545,325)
Mortgage loans sold and principal payments on mortgage loans held for sale	839,297	606,932
Distribution of earnings from unconsolidated joint ventures	3,521	5,846
Net change in assets and liabilities:		
Increase in inventory	(254,639)	(84,212)
Increase in contract land deposits	(2,353)	(478)
(Increase) decrease in receivables	(4,022)	223
Decrease in accounts payable and accrued expenses	(1,382)	(31,982)
Increase in customer deposits	15,587	19,210
Other, net	(10,615)	(10,352)
Net cash used in operating activities	(46,277)	(1,603)
Cash flows from investing activities:		
Investments in and advances to unconsolidated joint ventures	(138)	(863)
Distribution of capital from unconsolidated joint ventures	4,017	6,154
Purchase of property, plant and equipment	(5,431)	(4,893)
Proceeds from the sale of property, plant and equipment	199	138
Net cash (used in) provided by investing activities	(1,353)	536
Cash flows from financing activities:		
Purchase of treasury stock	(87,101)	(63,099)
Repayments under non-recourse debt related to consolidated variable interest entity and note payable	—	(64)
Distributions to partner in consolidated variable interest entity	(150)	(300)
Excess income tax benefit from equity-based compensation	6,284	7,998
Proceeds from the exercise of stock options	22,263	43,626

Net cash used in financing activities	(58,704)	(11,839)
Net decrease in cash and cash equivalents	(106,334)	(12,906)
Cash and cash equivalents, beginning of the period	425,316	545,419
Cash and cash equivalents, end of the period	$318,982	$532,513
Supplemental disclosures of cash flow information:		
Interest paid during the period, net of interest capitalized	$10,837	$12,039
Income taxes paid during the period, net of refunds	$16,516	$14,458

See notes to condensed consolidated financial statements.

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NVR, Inc.

Notes to Condensed Consolidated Financial Statements

(dollars and shares in thousands)

(unaudited)

1. Basis of Presentation

The accompanying unaudited, condensed consolidated financial statements include the accounts of NVR, Inc. (“NVR” or the “Company”) and its subsidiaries and certain other entities in which the Company is deemed to be the primary beneficiary (see Notes 2 and 3 to the accompanying condensed consolidated financial statements). Intercompany accounts and transactions have been eliminated in consolidation. The statements have been prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. Because the accompanying condensed consolidated financial statements do not include all of the information and footnotes required by GAAP, they should be read in conjunction with the financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2015. In the opinion of management, all adjustments (consisting only of normal recurring accruals except as otherwise noted herein) considered necessary for a fair presentation have been included. Operating results for the three months ended March 31, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

In 2016, the Company adopted Accounting Standards Update (“ASU”) 2015-03, Interest – Imputation of Interest, which requires that debt issuance costs be presented on the balance sheet as a direct deduction from the carrying amount of the related debt liability. The adoption of this standard resulted in the reclassification of the unamortized debt issuance costs related to the Company’s 3.95% Senior Notes due 2022 (the “Senior Notes”) from the homebuilding “Other assets” line item to the homebuilding “Senior notes” line item in the accompanying condensed consolidated balance sheets. See Note 12 for further discussion of the Company’s Senior Notes and the related unamortized debt issuance costs.

For the three months ended March 31, 2016 and 2015, comprehensive income equaled net income; therefore, a separate statement of comprehensive income is not included in the accompanying condensed consolidated financial statements.

2. Variable Interest Entities

Fixed Price Finished Lot Purchase Agreements (“Lot Purchase Agreements”)

NVR generally does not engage in the land development business. Instead, the Company typically acquires finished building lots at market prices from various development entities under Lot Purchase Agreements. The Lot Purchase Agreements require deposits that may be forfeited if NVR fails to perform under the Lot Purchase Agreements. The deposits required under the Lot Purchase Agreements are in the form of cash or letters of credit in varying amounts, and typically range up to 10% of the aggregate purchase price of the finished lots.

NVR believes this lot acquisition strategy reduces the financial requirements and risks associated with direct land ownership and land development. NVR may, at its option, choose for any reason and at any time not to perform under these Lot Purchase Agreements by delivering notice of its intent not to acquire the finished lots under contract. NVR's sole legal obligation and economic loss for failure to perform under these Lot Purchase Agreements is limited to the amount of the deposit pursuant to the liquidated damage provisions contained within the Lot Purchase Agreements. In other words, if NVR does not perform under a Lot Purchase Agreement, NVR loses only its deposit. None of the creditors of any of the development entities with which NVR enters Lot Purchase Agreements have recourse to the general credit of NVR. NVR generally does not have any specific performance obligations to purchase a certain number or any of the lots, nor does NVR guarantee completion of the development by the developer or guarantee any of the developers' financial or other liabilities.

NVR is not involved in the design or creation of any of the development entities from which the Company purchases lots under Lot Purchase Agreements. The developer's equity holders have the power to direct 100% of the operating activities of the development entity. NVR has no voting rights in any of the development entities. The sole purpose of

NVR, Inc.

Notes to Condensed Consolidated Financial Statements

(dollars and shares in thousands)

(unaudited)

the development entity's activities is to generate positive cash flow returns for the equity holders. Further, NVR does not share in any of the profit or loss generated by the project's development. The profits and losses are passed directly to the developer's equity holders.

The deposit placed by NVR pursuant to the Lot Purchase Agreement is deemed to be a variable interest in the respective development entities. Those development entities are deemed to be variable interest entities ("VIE"). Therefore, the development entities with which NVR enters into Lot Purchase Agreements, including the joint venture limited liability corporations discussed below, are evaluated for possible consolidation by NVR. An enterprise must consolidate a VIE when that enterprise has a controlling financial interest in the VIE. An enterprise is deemed to have a controlling financial interest if it has i) the power to direct the activities of a VIE that most significantly impact the entity's economic performance, and ii) the obligation to absorb losses of the VIE that could be significant to the VIE or the rights to receive benefits from the VIE that could be significant to the VIE.

NVR believes the activities that most significantly impact a development entity's economic performance are the operating activities of the entity. Unless and until a development entity completes finished building lots through the development process to be able to sell, the process of which the development entity's equity investors bear the full risk, the entity does not earn any revenues. The operating development activities are managed solely by the development entity's equity investors.

The development entities with which NVR contracts to buy finished lots typically select the respective projects, obtain the necessary zoning approvals, obtain the financing required with no support or guarantees from NVR, select who will purchase the finished lots and at what price, and manage the completion of the infrastructure improvements, all for the purpose of generating a cash flow return to the development entity's equity holders and all independent of NVR. The Company possesses no more than limited protective legal rights through the Lot Purchase Agreement in the specific finished lots that it is purchasing, and NVR possesses no participative rights in the development entities. Accordingly, NVR does not have the power to direct the activities of a developer that most significantly impact the developer's economic performance. For this reason, NVR has concluded that it is not the primary beneficiary of the development entities with which the Company enters into Lot Purchase Agreements, and therefore, NVR does not consolidate any of these VIEs.

As of March 31, 2016, NVR controlled approximately 69,100 lots under Lot Purchase Agreements with third parties through deposits in cash and letters of credit totaling approximately $380,500 and $3,500, respectively. As noted above, NVR's sole legal obligation and economic loss for failure to perform under these Lot Purchase Agreements is limited to the amount of the deposit pursuant to the liquidated damage provisions contained in the Lot Purchase Agreements and, in very limited circumstances, specific performance obligations.

In addition, NVR has certain properties under contract with land owners that are expected to yield approximately 9,300 lots, which are not included in the number of total lots controlled. Some of these properties may require rezoning or other approvals to achieve the expected yield. These properties are controlled with deposits and letters of credit totaling approximately $7,400 and $350, respectively, as of March 31, 2016, of which approximately $3,800 is refundable if NVR does not perform under the contract. NVR generally expects to assign the raw land contracts to a land developer and simultaneously enter into a Lot Purchase Agreement with the assignee if the project is determined to be feasible.

NVR’s total risk of loss related to contract land deposits as of March 31, 2016 and December 31, 2015 was as follows:

	March 31, 2016	December 31, 2015
Contract land deposits	$387,861	$385,534
Loss reserve on contract land deposits	(40,910)	(42,239)
Contract land deposits, net	346,951	343,295
Contingent obligations in the form of letters of credit	3,889	3,302
Contingent specific performance obligations (1)	1,505	1,505
Total risk of loss	$352,345	$348,102

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Notes to Condensed Consolidated Financial Statements

(dollars and shares in thousands)

(unaudited)

(1) As of both March 31, 2016 and December 31, 2015, the Company was committed to purchase 10 finished lots under specific performance obligations.

3. Joint Ventures

On a limited basis, NVR obtains finished lots using joint venture limited liability corporations (“JVs”). The JVs are typically structured such that NVR is a non-controlling member and is at risk only for the amount the Company has invested, or has committed to invest, in addition to any deposits placed under Lot Purchase Agreements with the joint venture. NVR is not a borrower, guarantor or obligor on any debt of the JVs, as applicable. The Company enters into Lot Purchase Agreements to purchase lots from these JVs, and as a result has a variable interest in these JVs.

At March 31, 2016, the Company had an aggregate investment totaling approximately $55,700 in six JVs that are expected to produce approximately 7,900 finished lots, of which approximately 4,600 lots were under contract with the Company and the remaining approximately 3,300 lots were either under contract with unrelated parties or not currently under contract. In addition, NVR had additional funding commitments totaling approximately $6,700 in the aggregate to three of the JVs at March 31, 2016. The Company has determined that it is not the primary beneficiary of five of the JVs because either NVR and the other JV partner share power or the other JV partner has the controlling financial interest. The aggregate investment in unconsolidated JVs was approximately $55,200 and $59,800 at March 31, 2016 and December 31, 2015, respectively, and is reported in the “Other assets” line item on the accompanying condensed consolidated balance sheets. For the remaining JV, NVR has concluded that it is the primary beneficiary because the Company has the controlling financial interest in the JV. The condensed balance sheets as of March 31, 2016 and December 31, 2015 of the consolidated JV were as follows:

	March 31, 2016	December 31, 2015
Assets:		
Cash	$995	$ 990
Other assets	326	379
Land under development	410	380
Total assets	$1,731	$ 1,749
Liabilities and equity:		
Accrued expenses	$858	$ 567
Equity	873	1,182

Total liabilities and equity	$1,731	$ 1,749

The Company recognizes income from the JVs as a reduction to the lot cost of the lots purchased from the respective JVs when the homes are settled and is based on the expected total profitability and the total number of lots expected to be produced by the respective JVs. Distributions received from the unconsolidated JVs are allocated between return of capital and distributions of earnings based on the ratio of capital contributed by NVR to the total expected returns for the respective JVs, and are classified within the accompanying condensed consolidated statements of cash flows as cash flows from investing activities and operating activities, respectively.

4. Land Under Development

On a limited basis, NVR directly acquires raw parcels of land already zoned for its intended use to develop into finished lots. Land under development includes the land acquisition costs, direct improvement costs, capitalized interest where applicable, and real estate taxes.

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(dollars and shares in thousands)

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During February 2016, the Company purchased a land parcel which included both land under development and finished lots for approximately $150,000. The parcel is expected to produce approximately 1,000 lots, of which approximately 160 lots were under contract with unrelated parties at the date of purchase. As of March 31, 2016, the carrying values of the land under development, unsold finished lot inventory and sold finished lot inventory related to this purchase were approximately $108,000, $26,000 and $13,000, respectively. During the first quarter, the Company sold 34 lots under contract with unrelated parties for approximately $10,500.

As of March 31, 2016, NVR directly owned a total of five separate raw parcels of land with a carrying value of $163,826 that are expected to produce approximately 1,700 finished lots, of which approximately 130 lots were under contract with unrelated parties. The Company also has additional funding commitments of approximately $17,500 under a joint development agreement related to one parcel, a portion of which the Company expects will be offset by development credits of approximately $9,300.

None of the raw parcels had any indicators of impairment as of March 31, 2016. Based on market conditions, NVR may on a limited basis continue to directly acquire additional raw parcels to develop into finished lots.

5. Capitalized Interest

The Company capitalizes interest costs to land under development during the active development of finished lots. In addition, the Company capitalizes interest costs to its joint venture investments while the investments are considered qualified assets pursuant to ASC 835-20, Interest. Capitalized interest is transferred to sold or unsold inventory as the development of finished lots is completed, then charged to cost of sales upon the Company's settlement of homes and the respective lots. Interest incurred in excess of the interest capitalizable based on the level of qualified assets is expensed in the period incurred. NVR's interest costs incurred, capitalized, expensed and charged to cost of sales during the three months ended March 31, 2016 and 2015 was as follows:

	Three Months Ended March 31,	
	2016	2015
Interest capitalized, beginning of period	$4,434	$4,072
Interest incurred	6,388	6,263
Interest charged to interest expense	(5,088)	(5,918)
Interest charged to cost of sales	(376)	(146)
Interest capitalized, end of period	$5,358	$4,271

6. Earnings per Share

The following weighted average shares and share equivalents were used to calculate basic and diluted earnings per share for the three months ended March 31, 2016 and 2015:

	Three Months Ended March 31,	
	2016	2015
Weighted average number of shares outstanding used to calculate basic EPS	3,884	4,057
Dilutive securities:		
Stock options and restricted share units	251	178
Weighted average number of shares and share equivalents outstanding used to calculate diluted EPS	4,135	4,235

The following stock options and restricte