

Howard Hughes Corp  
Form 10-Q  
August 08, 2016  
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2016

or

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

Commission file number 001-34856

THE HOWARD HUGHES CORPORATION

(Exact name of registrant as specified in its charter)

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





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THE HOWARD HUGHES CORPORATION

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## THE HOWARD HUGHES CORPORATION

## CONDENSED CONSOLIDATED BALANCE SHEETS

## UNAUDITED

| (In thousands, except share amounts)   | June 30,<br>2016 | December 31,<br>2015 |
|--|------------------|----------------------|
| Assets:  |                  |                      |
| Investment in real estate:   |                  |                      |
| Master Planned Community assets  | \$ 1,652,056     | \$ 1,642,842         |
| Land   | 315,617          | 322,462              |
| Buildings and equipment  | 1,910,016        | 1,772,401            |
| Less: accumulated depreciation   | (271,451)        | (232,969)            |
| Developments   | 915,157          | 1,036,927            |
| Net property and equipment   | 4,521,395        | 4,541,663            |
| Investment in Real Estate and Other Affiliates   | 65,834           | 57,811               |
| Net investment in real estate  | 4,587,229        | 4,599,474            |
| Cash and cash equivalents  | 670,800          | 445,301              |
| Accounts receivable, net   | 40,152           | 32,203               |
| Municipal Utility District receivables, net  | 163,639          | 139,946              |
| Notes receivable, net  | 69               | 1,664                |
| Deferred expenses, net   | 63,099           | 61,804               |
| Prepaid expenses and other assets, net   | 692,631          | 441,190              |
| Total assets   | \$ 6,217,619     | \$ 5,721,582         |
| Liabilities:   |                  |                      |
| Mortgages, notes and loans payable   | \$ 2,651,805     | \$ 2,443,962         |
| Deferred tax liabilities   | 158,177          | 89,221               |
| Warrant liabilities  | 322,090          | 307,760              |
| Uncertain tax position liability   | 9,588            | 1,396                |
| Accounts payable and accrued expenses  | 572,772          | 515,354              |
| Total liabilities  | 3,714,432        | 3,357,693            |
| Commitments and Contingencies (see Note 15)  |                  |                      |
| Equity:  |                  |                      |
| Preferred stock: \$.01 par value; 50,000,000 shares authorized, none issued  | —                | —                    |
| Common stock: \$.01 par value; 150,000,000 shares authorized, 39,846,036 shares issued and 39,833,975 outstanding as of June 30, 2016 and 39,714,838 shares issued and outstanding as of December 31, 2015 | 398              | 398                  |
| Additional paid-in capital   | 2,853,880        | 2,847,823            |

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|   |              |              |
|---|--------------|--------------|
| Accumulated deficit   | (329,480)    | (480,215)    |
| Accumulated other comprehensive loss  | (24,152)     | (7,889)      |
| Treasury stock, at cost, 12,061 shares as of June 30, 2016 and 0 shares as of December 31, 2015 | (1,231)      | —            |
| Total stockholders' equity  | 2,499,415    | 2,360,117    |
| Noncontrolling interests  | 3,772        | 3,772        |
| Total equity  | 2,503,187    | 2,363,889    |
| Total liabilities and equity  | \$ 6,217,619 | \$ 5,721,582 |

See Notes to Condensed Consolidated Financial Statements.

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## THE HOWARD HUGHES CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

## UNAUDITED

| (In thousands, except per share amounts)                 | Three Months Ended June 30, |           | Six Months Ended June 30, |            |
|--|-----------------------------|-----------|---------------------------|------------|
|  | 2016                        | 2015      | 2016                      | 2015       |
| <b>Revenues:</b>   |                             |           |                           |            |
| Condominium rights and unit sales                        | \$ 125,112                  | \$ 86,513 | \$ 247,206                | \$ 121,370 |
| Master Planned Community land sales                      | 61,098                      | 45,433    | 103,040                   | 93,514     |
| Minimum rents  | 42,036                      | 36,989    | 83,345                    | 72,183     |
| Builder price participation                              | 6,501                       | 7,907     | 11,148                    | 13,605     |
| Tenant recoveries  | 10,923                      | 10,701    | 21,451                    | 20,368     |
| Hospitality revenues                                     | 19,129                      | 11,481    | 32,038                    | 23,484     |
| Other land revenues                                      | 2,759                       | 3,145     | 5,792                     | 6,438      |
| Other rental and property revenues                       | 4,593                       | 6,994     | 7,797                     | 13,291     |
| Total revenues   | 272,151                     | 209,163   | 511,817                   | 364,253    |
| <b>Expenses and other income:</b>                        |                             |           |                           |            |
| Condominium rights and unit cost of sales                | 79,726                      | 56,765    | 154,541                   | 79,174     |
| Master Planned Community cost of sales                   | 29,008                      | 24,236    | 44,696                    | 48,132     |
| Master Planned Community operations                      | 7,806                       | 11,963    | 17,400                    | 21,946     |
| Other property operating costs                           | 15,236                      | 19,634    | 30,978                    | 37,779     |
| Rental property real estate taxes                        | 7,329                       | 6,568     | 14,077                    | 12,768     |
| Rental property maintenance costs                        | 2,753                       | 2,900     | 5,885                     | 5,644      |
| Hospitality costs  | 14,242                      | 8,893     | 24,717                    | 17,971     |
| Provision for doubtful accounts                          | (352)                       | 1,266     | 2,689                     | 2,075      |
| Demolition costs   | 490                         | 1,496     | 962                       | 1,613      |
| Development-related marketing costs                      | 6,339                       | 5,594     | 10,870                    | 11,837     |
| General and administrative                               | 20,053                      | 19,606    | 40,377                    | 38,569     |
| Other income, net  | (9,067)                     | (399)     | (9,426)                   | (1,863)    |
| Gain on sale of 80 South Street Assemblage               | —                           | —         | (140,479)                 | —          |
| Depreciation and amortization                            | 24,952                      | 25,069    | 47,924                    | 46,579     |
| Total expenses, net of other income                      | 198,515                     | 183,591   | 245,211                   | 322,224    |
| Operating income   | 73,636                      | 25,572    | 266,606                   | 42,029     |
| Interest income  | 435                         | 271       | 704                       | 407        |
| Interest expense   | (16,533)                    | (14,685)  | (32,526)                  | (27,931)   |
| Warrant liability (loss) gain                            | (44,150)                    | 42,620    | (14,330)                  | (66,190)   |
| Equity in earnings from Real Estate and Other Affiliates | 20,275                      | 1,081     | 22,207                    | 2,869      |
| Income (loss) before taxes                               | 33,663                      | 54,859    | 242,661                   | (48,816)   |

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|   |          |           |            |             |
|---|----------|-----------|------------|-------------|
| Provision for income taxes                            | 26,693   | 4,274     | 91,926     | 6,558       |
| Net income (loss)                                     | 6,970    | 50,585    | 150,735    | (55,374)    |
| Net income attributable to noncontrolling interests   | —        | (12)      | —          | (12)        |
| Net income (loss) attributable to common stockholders | \$ 6,970 | \$ 50,573 | \$ 150,735 | \$ (55,386) |
| Basic income (loss) per share:                        | \$ 0.18  | \$ 1.28   | \$ 3.82    | \$ (1.40)   |
| Diluted income (loss) per share:                      | \$ 0.16  | \$ 0.18   | \$ 3.53    | \$ (1.40)   |

See Notes to Condensed Consolidated Financial Statements.

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## THE HOWARD HUGHES CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

## UNAUDITED

| (In thousands)  | Three Months Ended June 30, |           | Six Months Ended June 30, |             |
|---|-----------------------------|-----------|---------------------------|-------------|
|   | 2016                        | 2015      | 2016                      | 2015        |
| Net income (loss)   | \$ 6,970                    | \$ 50,585 | \$ 150,735                | \$ (55,374) |
| Other comprehensive income (loss):                              |                             |           |                           |             |
| Interest rate swaps (a)   | (5,565)                     | 196       | (15,373)                  | 708         |
| Capitalized swap interest expense (b)                           | (254)                       | (53)      | (317)                     | (112)       |
| Pension adjustment (c)  | (573)                       | —         | (573)                     | —           |
| Other comprehensive income (loss)                               | (6,392)                     | 143       | (16,263)                  | 596         |
| Comprehensive income (loss)                                     | 578                         | 50,728    | 134,472                   | (54,778)    |
| Comprehensive income attributable to noncontrolling interests   | —                           | (12)      | —                         | (12)        |
| Comprehensive income (loss) attributable to common stockholders | \$ 578                      | \$ 50,716 | \$ 134,472                | \$ (54,790) |

- (a) Amounts are shown net of deferred tax benefit of \$3.0 million and deferred tax benefit of \$8.3 million for the three and six months ended June 30, 2016, respectively. For the three and six months ended June 30, 2015, amounts are shown net of deferred tax expense of \$0.1 million and \$0.6 million, respectively.
- (b) Net of deferred tax benefit of \$0 and \$0.1 million for the three and six months ended June 30, 2016, respectively. For the three and six months ended June 30, 2015, amounts shown net of deferred tax benefit of both \$0.1 million, respectively.
- (c) Net of deferred tax benefit of \$0.4 million for both the three and six months ended June 30, 2016, respectively. For both the three and six months ended June 30, 2015, amounts shown net of deferred tax benefit of \$0, respectively.

See Notes to Condensed Consolidated Financial Statements.



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## THE HOWARD HUGHES CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF EQUITY

## UNAUDITED

| (In thousands,<br>except share<br>amounts)                             | Common stock |        | Additional<br>paid-in | Accumulated  | Accumulated<br>other<br>comprehensive | Treasury stock |        | Noncontrol |
|--|--------------|--------|-----------------------|--------------|---------------------------------------|----------------|--------|------------|
|  | Shares       | Amount | capital               | deficit      | income<br>(loss)                      | Shares         | Amount | interests  |
| Balance,<br>December 31,<br>2014                                       | 39,638,094   | \$ 396 | \$ 2,838,013          | \$ (606,934) | \$ (7,712)                            | —              | \$ —   | \$ 3,743   |
| Net loss   |              | —      | —                     | (55,386)     | —                                     | —              | —      | 12         |
| Preferred<br>dividend<br>payment on<br>behalf of<br>REIT<br>subsidiary |              | —      | —                     | —            | —                                     | —              | —      | 29         |
| Interest rate<br>swaps, net of<br>tax of \$555                         |              | —      | —                     | —            | 708                                   | —              | —      | —          |
| Capitalized<br>swap interest,<br>net of tax<br>benefit of \$41         |              | —      | —                     | —            | (112)                                 | —              | —      | —          |
| Stock plan<br>activity   | 76,911       | 2      | 4,253                 | —            | —                                     | —              | —      | —          |
| Issuances of<br>treasury stock   | —            | —      | —                     | —            | —                                     | —              | —      | —          |
| Balance,<br>June 30, 2015  | 39,715,005   | \$ 398 | \$ 2,842,266          | \$ (662,320) | \$ (7,116)                            | —              | \$ —   | \$ 3,784   |
| Balance,<br>December 31,<br>2015                                       | 39,714,838   | \$ 398 | \$ 2,847,823          | \$ (480,215) | \$ (7,889)                            | —              | \$ —   | \$ 3,772   |
| Net income   |              | —      | —                     | 150,735      | —                                     | —              | —      | —          |
| Interest rate<br>swaps, net of<br>tax of \$8,245                       |              | —      | —                     | —            | (15,373)                              | —              | —      | —          |

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|   |            |        |              |              |             |          |            |          |
|---|------------|--------|--------------|--------------|-------------|----------|------------|----------|
| Pension adjustment, net of tax of \$350               |            | —      | —            | —            | (573)       | —        | —          | —        |
| Capitalized swap interest, net of tax benefit of \$61 |            | —      | —            | —            | (317)       | —        | —          | —        |
| Stock plan activity                                   | 131,198    | 0      | 6,057        | —            | —           | —        | —          | —        |
| Treasury stock activity                               | —          | —      | —            | —            | —           | (12,061) | (1,231)    | —        |
| Balance, June 30, 2016                                | 39,846,036 | \$ 398 | \$ 2,853,880 | \$ (329,480) | \$ (24,152) | (12,061) | \$ (1,231) | \$ 3,772 |

See Notes to Condensed Consolidated Financial Statements.

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## THE HOWARD HUGHES CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

## UNAUDITED

| (In thousands)  | Six Months Ended June 30, |             |
|---|---------------------------|-------------|
|   | 2016                      | 2015        |
| Cash Flows from Operating Activities:   |                           |             |
| Net income (loss)   | \$ 150,735                | \$ (55,374) |
| Adjustments to reconcile net income (loss) to cash used in operating activities:            |                           |             |
| Depreciation  | 41,126                    | 37,155      |
| Amortization  | 6,798                     | 9,424       |
| Amortization of deferred financing costs  | 3,747                     | 3,192       |
| Amortization of intangibles other than in-place leases                                      | (710)                     | 472         |
| Straight-line rent amortization   | (5,187)                   | (2,727)     |
| Deferred income taxes   | 85,927                    | 6,135       |
| Restricted stock and stock option amortization  | 4,670                     | 3,232       |
| Gain on disposition of 80 South Street Assemblage   | (140,479)                 | —           |
| Warrant liability loss  | 14,330                    | 66,190      |
| Equity in earnings from Real Estate and Other Affiliates, net of distributions              | (8,212)                   | 1,437       |
| Provision for doubtful accounts   | 2,689                     | 2,075       |
| Master Planned Community land acquisitions  | (69)                      | (1,928)     |
| Master Planned Community development expenditures   | (70,678)                  | (83,868)    |
| Master Planned Community cost of sales  | 41,310                    | 44,792      |
| Condominium development expenditures  | (155,222)                 | (79,500)    |
| Condominium rights and unit cost of sales   | 154,541                   | 75,991      |
| Percentage of completion revenue recognition from sale of condominium rights and unit sales | (247,206)                 | (121,370)   |
| Net changes:  |                           |             |
| Accounts and notes receivable   | (3,230)                   | (1,115)     |
| Prepaid expenses and other assets   | 2,616                     | 15,520      |
| Condominium deposits received   | 51,573                    | 18,423      |
| Deferred expenses   | (1,659)                   | 240         |
| Accounts payable and accrued expenses   | (24,798)                  | (11,030)    |
| Condominium deposits held in escrow   | (51,573)                  | (18,423)    |
| Condominium deposits released from escrow   | 15,661                    | 90,425      |
| Other, net  | (3,535)                   | (325)       |
| Cash used in operating activities   | (136,835)                 | (957)       |
| Cash Flows from Investing Activities:   |                           |             |
| Property and equipment expenditures   | (7,339)                   | (3,863)     |

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|  |            |            |
|--|------------|------------|
| Operating property improvements                              | (5,712)    | (4,401)    |
| Property developments and redevelopments                     | (214,276)  | (364,044)  |
| Proceeds from grant to reimburse development costs           | 2,915      | —          |
| Proceeds from disposition of 80 South Street Assemblage, net | 378,257    | —          |
| Proceeds from insurance claims                               | 3,107      | —          |
| Investment in KR Holdings, LLC                               | —          | 9,121      |
| Distributions from Real Estate and Other Affiliates          | 12,002     | —          |
| Note issued to Real Estate Affiliate                         | (25,000)   | —          |
| Proceeds from repayment of note to Real Estate Affiliate     | 25,000     | —          |
| Investments in Real Estate and Other Affiliates, net         | (11,813)   | (501)      |
| Change in restricted cash                                    | 4,658      | (1,485)    |
| Cash provided by (used in) investing activities              | 161,799    | (365,173)  |
| Cash Flows from Financing Activities:                        |            |            |
| Proceeds from mortgages, notes and loans payable             | 207,561    | 310,822    |
| Principal payments on mortgages, notes and loans payable     | (4,492)    | (14,900)   |
| Deferred financing costs                                     | (1,303)    | (1,614)    |
| Taxes paid on vested restricted stock                        | (1,231)    | —          |
| Cash provided by financing activities                        | 200,535    | 294,308    |
| Net change in cash and cash equivalents                      | 225,499    | (71,822)   |
| Cash and cash equivalents at beginning of period             | 445,301    | 560,451    |
| Cash and cash equivalents at end of period                   | \$ 670,800 | \$ 488,629 |



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## THE HOWARD HUGHES CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

## UNAUDITED

| (In thousands)   | Six Months Ended June 30, |           |
|--|---------------------------|-----------|
|  | 2016                      | 2015      |
| <b>Supplemental Disclosure of Cash Flow Information:</b>               |                           |           |
| Interest paid  | \$ 57,335                 | \$ 48,460 |
| Interest capitalized   | 28,681                    | 23,074    |
| Income taxes paid  | 3,067                     | 2,067     |
| <b>Non-Cash Transactions:</b>  |                           |           |
| Special Improvement District bond transfers associated with land sales | 3,386                     | 3,340     |
| Property developments and redevelopments                               | —                         | (4,534)   |
| Accrued interest on construction loan borrowing                        | 3,005                     | 1,359     |
| MPC Land contributed to Real Estate Affiliates                         | —                         | 15,234    |
| Special Improvement District bond transfer to Real Estate Affiliate    | —                         | (1,518)   |
| Capitalized stock compensation   | 1,387                     | 1,262     |

See Notes to Condensed Consolidated Financial Statements.

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THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

NOTE 1 BASIS OF PRESENTATION AND ORGANIZATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”), with intercompany transactions between consolidated subsidiaries eliminated for interim financial statements. In accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X as issued by the Securities and Exchange Commission (the “SEC”), these condensed consolidated financial statements do not include all of the information and disclosures required by GAAP for complete financial statements. Readers of this Quarterly Report on Form 10-Q (“Quarterly Report”) should refer to The Howard Hughes Corporation’s (“HHC” or the “Company”) audited Consolidated Financial Statements which are included in the Company’s Annual Report on Form 10-K (the “Annual Report”) for the fiscal year ended December 31, 2015, filed on February 29, 2016 with the SEC. Certain amounts in 2015 have been reclassified to conform to 2016 presentation. In the opinion of management, all normal recurring adjustments necessary for a fair presentation of the financial position, results of operations, comprehensive income (loss), cash flows and equity for the interim periods have been included. The results for the three and six months ended June 30, 2016 are not necessarily indicative of the results that may be expected for the year ended December 31, 2016.

Management has evaluated for disclosure or recognition all material events occurring subsequent to the date of the condensed consolidated financial statements up to the date and time this Quarterly Report was filed.

NOTE 2 RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In June 2016, the FASB issued ASU 2016-13, “Financial Instruments—Credit Losses.” The standard modifies the impairment model for most financial assets, including trade accounts receivables and loans, and will require the use of an “expected loss” model for instruments measured at amortized cost. Under this model, entities will be required to estimate the lifetime expected credit loss on such instruments and record an allowance to offset the amortized cost basis of the financial asset, resulting in a net presentation of the amount expected to be collected on the financial asset. The effective date of the standard is for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2019 for public companies. We are currently evaluating the impact of adopting ASU 2016-13 on our consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, “Improvements to Employee Share-Based Payment Accounting.” The standard amends several aspects of accounting for share-based payment transactions, including the accounting for income taxes, forfeitures and statutory tax withholding requirements, as well as classification in the statement of cash flows. The new guidance will require entities to recognize all income tax effects of awards in the income statement when the awards vest or are settled. It also will allow an employer to repurchase more of an employee’s shares for tax withholding purposes without triggering liability accounting and to make a policy election to account for forfeitures as they occur. ASU 2016-09 will be effective as of January 1, 2017. Early adoption is permitted. We are currently evaluating the impact of adopting ASU 2016-09 on our consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, "Leases." ASU 2016-02, codified in Accounting Standards Codification ("ASC") 842, amends the existing accounting standards for lease accounting, including requiring lessees to recognize most leases on their balance sheets and making targeted changes to lessor accounting. ASU 2016-02 will be effective beginning in the first quarter of 2019. Early adoption of ASU 2016-02 is permitted. The new Leases standard requires a modified retrospective transition approach for all leases existing at, or entered into after, the date of initial application. We are currently evaluating the impact of adopting ASU 2016-02 on our consolidated financial statements.

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THE HOWARD HUGHES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

In February 2015, the FASB issued ASU 2015-02, “Consolidation (Topic 810) - Amendments to the Consolidation Analysis.” The standard modifies whether: (1) fees paid to a decision maker or service provider represent a variable interest; (2) a limited partnership or similar entity has the characteristics of a variable interest entity (“VIE”) per consolidation guidance in ASC 810-10-65; and (3) a reporting entity is the primary beneficiary of a VIE. The effective date of the standard is for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015 for public companies. We adopted the standard as of January 1, 2016, and there was no impact on our consolidated financial statements.

In May 2014, the FASB and International Accounting Standards Board (“IASB”) issued ASU 2014-09 “Revenues from Contracts with Customers (Topic 606).” The standard’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 the company expects to be entitled in exchange for those goods or services. In doing so, companies will need to use more judgment and make more estimates than under current guidance. These may include identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. The effective date of this standard is for fiscal years, and interim periods within those years, beginning after December 15, 2017. Early adoption is permitted after December 15, 2016. Entities have the option of using either a full retrospective or a modified approach. Preliminary assessments of our revenue streams indicate that after adoption we will not be able to recognize revenue for condominium projects on a percentage of completion basis and generally revenue will be recognized when the units close and the title has transferred to the buyer. We are continuing to evaluate the new guidance to determine the impact on our consolidated financial statements.

In August 2014, the FASB issued ASU 2014-15, “Presentation of Financial Statements — Going Concern: Disclosure of Uncertainties about an Entity’s Ability to Continue as a Going Concern.” This ASU requires management to assess an entity’s ability to continue as a going concern. This ASU is effective for the annual and interim periods ending after December 15, 2016 and for annual and interim periods thereafter. We do not expect the adoption of this ASU to have an impact on our consolidated financial statements.

NOTE 3 SPONSOR AND MANAGEMENT WARRANTS

On November 9, 2010, we issued warrants to purchase shares of our common stock to certain of our sponsors (the “Sponsor Warrants”). The exercise price for the warrants of \$50.00 per share and the number of shares of common stock underlying each warrant are subject to adjustment for future stock dividends, splits or reverse splits of our common stock or certain other events. The 1,916,667 of Sponsor Warrants outstanding are exercisable at any time and expire on November 9, 2017.

In November 2010 and February 2011, we entered into certain agreements (the “Management Warrants”) with David R. Weinreb, our Chief Executive Officer, Grant Herlitz, our President, and Andrew C. Richardson, our Chief Financial Officer, in each case prior to his appointment to such position to purchase shares of our common stock. The

Management Warrants represent 2,862,687 underlying shares, which may be adjusted pursuant to a net settlement option, were issued pursuant to such agreements at fair value in exchange for a combined total of approximately \$19.0 million in cash from such executives at the commencement of their respective employment. Mr. Weinreb and Mr. Herlitz's warrants have exercise prices of \$42.23 per share and Mr. Richardson's warrants have an exercise price of \$54.50 per share. Generally, the Management Warrants become exercisable in November 2016 and expire in February 2018.

As of June 30, 2016, the estimated \$124.1 million fair value for the Sponsor Warrants representing warrants to purchase 1,916,667 shares and the estimated \$198.0 million fair value for the Management Warrants representing warrants to purchase 2,862,687 shares have been recorded as liabilities because the holders of these warrants could require us to settle such warrants in cash upon a change of control. The estimated fair values for the outstanding Sponsor Warrants and Management Warrants were \$123.1 million and \$184.7 million, respectively, as of December 31, 2015. The fair values

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## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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were estimated using an option pricing model and Level 3 inputs due to the unavailability of comparable market data, as further discussed in Note 7 – Fair Value of Financial Instruments. Decreases and increases in the fair value of the Sponsor Warrants and the Management Warrants are recognized as either warrant liability gains or losses, respectively, in the condensed consolidated statements of operations.

## NOTE 4 EARNINGS PER SHARE

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

Information related to our EPS calculations is summarized as follows:

| (In thousands, except per share amounts)              | Three Months Ended June 30, |           | Six Months Ended June 30, |             |
|---|-----------------------------|-----------|---------------------------|-------------|
|   | 2016                        | 2015      | 2016                      | 2015        |
| Basic EPS:  |                             |           |                           |             |
| Numerator:  |                             |           |                           |             |
| Net income (loss)                                     | \$ 6,970                    | \$ 50,585 | \$ 150,735                | \$ (55,374) |
| Net income attributable to noncontrolling interests   | —                           | (12)      | —                         | (12)        |
| Net income (loss) attributable to common stockholders | \$ 6,970                    | \$ 50,573 | \$ 150,735                | \$ (55,386) |
| Denominator:  |                             |           |                           |             |
| Weighted average basic common shares outstanding      | 39,492                      | 39,468    | 39,483                    | 39,467      |
| Diluted EPS:  |                             |           |                           |             |
| Numerator:  |                             |           |                           |             |

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|  |          |           |            |             |
|--|----------|-----------|------------|-------------|
| Net income (loss) attributable to common stockholders          | \$ 6,970 | \$ 50,573 | \$ 150,735 | \$ (55,386) |
| Less: Warrant liability gain                                   | —        | (42,620)  | —          | —           |
| Adjusted net income (loss) attributable to common stockholders | \$ 6,970 | \$ 7,953  | \$ 150,735 | \$ (55,386) |
| Denominator:   |          |           |            |             |
| Weighted average basic common shares outstanding               | 39,492   | 39,468    | 39,483     | 39,467      |
| Restricted stock and stock options                             | 337      | 438       | 324        | —           |
| Warrants   | 2,835    | 3,291     | 2,835      | —           |
| Weighted average diluted common shares outstanding             | 42,664   | 43,197    | 42,642     | 39,467      |
| Basic income (loss) per share:                                 | \$ 0.18  | \$ 1.28   | \$ 3.82    | \$ (1.40)   |
| Diluted income (loss) per share:                               | \$ 0.16  | \$ 0.18   | \$ 3.53    | \$ (1.40)   |

The diluted EPS computation for the three and six months ended June 30, 2016 excludes 363,000 stock options and 402,500 stock options, respectively, because their inclusion would have been anti-dilutive. The diluted EPS computation for the

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three and six months ended June 30, 2016 excludes 8,729 shares of restricted stock and 9,254 shares of restricted stock, respectively, because performance conditions have not been met.

The diluted EPS computation for the three months ended June 30, 2015 excludes 125,769 stock options. The diluted EPS computation for the six months ended June 30, 2015 excludes 1,048,750 stock options, 242,055 shares of restricted stock, 1,916,667 shares of common stock underlying the Sponsors Warrants and 2,862,687 shares of common stock underlying the Management Warrants because their inclusion would have been anti-dilutive.

NOTE 5 RECENT TRANSACTIONS

On March 16, 2016, we sold the 80 South Street Assemblage (“80 South Street”) for net cash proceeds of \$378.3 million, resulting in a pre-tax gain of \$140.5 million. 80 South Street was comprised of a 42,694 square foot lot with certain air rights, providing total residential and commercial development rights of 817,784 square feet that had been acquired over the course of 2014 and 2015.

NOTE 6 IMPAIRMENT

We review our real estate assets for potential impairment indicators whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. GAAP related to the impairment or disposal of long lived assets requires that if impairment indicators exist and expected undiscounted cash flows generated by the asset are less than its carrying amount, an impairment provision should be recorded to write down the carrying amount of the asset to its fair value. The impairment analysis does not consider the timing of future cash flows and whether the asset is expected to earn an above or below market rate of return.

Each investment in Real Estate and Other Affiliates as discussed in Note 8 – Real Estate and Other Affiliates is evaluated periodically for recoverability and valuation declines that are other-than-temporary. If the decrease in value of our investment in a Real Estate and Other Affiliate is deemed to be other-than-temporary, our investment in such Real Estate and Other Affiliate is reduced to its estimated fair value.

No impairment charges were recorded during the six months ended June 30, 2016 or June 30, 2015. We continually evaluate our strategic alternatives with respect to each of our properties and may revise our strategy from time to time,



including our intent to hold the asset on a long-term basis or the timing of potential asset dispositions. For example, we may decide to sell property that is held for use, and the sale price may be less than the carrying amount. As a result, these changes in strategy could result in impairment charges in future periods.

#### NOTE 7 FAIR VALUE OF FINANCIAL INSTRUMENTS

ASC 820, Fair Value Measurement, emphasizes that fair value is a market-based measurement that should be determined on the assumptions market participants would use in pricing an asset or liability. The standard establishes a hierarchal disclosure framework which prioritizes and ranks the level of market price observability used in measuring assets or liabilities at fair value. Market price observability is impacted by a number of factors, including the type of investment and the characteristics specific to the asset or liability. Assets or liabilities with readily available active quoted prices or for which fair value can be measured from actively quoted prices generally will have a higher degree of market price observability and a lesser degree of judgment used in measuring fair value.

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The following table presents the fair value measurement hierarchy levels required under ASC 820 for each of our assets and liabilities that are measured at fair value on a recurring basis:

| (In thousands)             | June 30, 2016 |  |   |  | December 31, 2015 |  |   |  |
|----------------------------|---------------|--|---|--|-------------------|--|---|--|
|                            | Total         | Quoted Prices<br>in Active<br>Markets for<br>Identical Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Total             | Quoted Prices<br>in Active<br>Markets for<br>Identical Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
| Assets:                    |               |  |   |  |                   |  |   |  |
| Cash equivalents           | \$ 378,535    | \$ 378,535   | \$ —  | \$ —   | \$ 18             | \$ 18  | \$ —  | \$ —   |
| Liabilities:               |               |  |   |  |                   |  |   |  |
| Warrants                   | 322,090       | —  | —   | 322,090  | 307,760           | —  | —   | 307,760  |
| Interest Rate Swaps & Caps | 27,729        | —  | 27,729  | —  | 4,217             | —  | 4,217   | —  |

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

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

The valuation of warrants is based on an option pricing model, utilizing inputs which are classified as Level 3 due to the unavailability of comparable market data. The following table presents a rollforward of the valuation of our Sponsor and Management warrants:

| (In thousands)             | 2016       | 2015       |
|----------------------------|------------|------------|
| Balance as of January 1    | \$ 307,760 | \$ 366,080 |
| Warrant liability loss (a) | 14,330     | 66,190     |
| Balance as of June 30      | \$ 322,090 | \$ 432,270 |

(a) All losses during 2016 and 2015 were unrealized. Changes in the fair value of the Sponsor and Management Warrants are recognized in net income as a warrant liability gain or loss.

The inputs to the valuation model include the fair value of stock related to the warrants, exercise price and term of the warrants, expected volatility, risk-free interest rate and dividend yield and, with respect to the Management Warrants, a discount for lack of marketability. Generally, an increase in expected volatility would increase the fair value of the liability, while a decrease in expected volatility would decrease the fair value of the liability, but the impact of the volatility on fair value diminishes as the market value of the stock increases above the strike price. As the period of restriction lapses, the marketability discount reduces to zero and increases the fair value of the warrants.

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The significant unobservable inputs used in the fair value measurement of our warrants as of June 30, 2016 and December 31, 2015 are as follows:

|                   | Unobservable Inputs     |                            |
|-------------------|-------------------------|----------------------------|
|                   | Expected Volatility (a) | Marketability Discount (b) |
| June 30, 2016     | 30.9%                   | 5.0% - 7.0%                |
| December 31, 2015 | 27.4%                   | 10.0% - 12.0%              |

(a) Based on our implied equity volatility.

(b) Represents the discount rate for lack of marketability of the Management Warrants.

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

| (In thousands)            | Fair Value Hierarchy | June 30, 2016   |                      | December 31, 2015 |                      |
|---------------------------|----------------------|-----------------|----------------------|-------------------|----------------------|
|                           |                      | Carrying Amount | Estimated Fair Value | Carrying Amount   | Estimated Fair Value |
| <b>Assets:</b>            |                      |                 |                      |                   |                      |
| Cash                      | Level 1              | \$ 292,265      | \$ 292,265           | \$ 445,283        | \$ 445,283           |
| Notes receivable, net (a) | Level 3              | 69              | 69                   | 1,664             | 1,664                |
| <b>Liabilities:</b>       |                      |                 |                      |                   |                      |
| Fixed-rate debt           | Level 2              | \$ 1,108,453    | \$ 1,122,964         | \$ 1,141,381      | \$ 1,137,166         |
| Variable-rate debt        | Level 2              | 1,553,786       | 1,553,786            | 1,314,973         | 1,314,973            |

(a) Notes receivable is shown net of an allowance of \$0.6 million as of June 30, 2016 and \$0.2 million as of December 31, 2015.

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

The fair value of fixed-rate debt in the table above, not including our Senior Notes (please refer to Note 9 – Mortgages, Notes and Loans Payable), was estimated based on a discounted future cash payment model, which includes risk premiums and a risk free rate derived from the current London Interbank Offered Rate (“LIBOR”) or U.S. Treasury obligation interest rates. The discount rates reflect our judgment as to what the approximate current lending rates for loans or groups of loans with similar maturities and credit quality would be if credit markets were operating efficiently and assuming that the debt is outstanding through maturity. The fair values of our Senior Notes, included in fixed-rate debt in the table above, are based upon the last trade price closest to the end of the period presented.

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

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

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NOTE 8 REAL ESTATE AND OTHER AFFILIATES

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

In accordance with ASC 810, we assess our joint ventures at inception to determine if any meet the qualifications of a VIE. We consider a partnership or joint venture a VIE if: (a) the total equity investment is not sufficient to permit the entity to finance its activities without additional subordinated financial support; (b) characteristics of a controlling financial interest are missing (either the ability to make decisions through voting or other rights, the obligation to absorb the expected losses of the entity or the right to receive the expected residual returns of the entity); or (c) the voting rights of the equity holders are not proportional to their obligations to absorb the expected losses of the entity and/or their rights to receive the expected residual returns of the entity, and substantially all of the entity’s activities either involve or are conducted on behalf of an investor that has disproportionately few voting rights. Upon the occurrence of certain events outlined in ASC 810, we reassess our initial determination of whether the partnership or joint venture is a VIE.

We perform a qualitative assessment of each VIE to determine if we are the primary beneficiary, as required by ASC 810. A company has a controlling financial interest and must consolidate the VIE if it has both (1) the power to direct the activities of the VIE that most significantly impact the VIE’s performance, and (2) “benefits,” defined as the obligation to absorb the losses of the VIE that potentially could be significant to the VIE or the right to receive benefits from the VIE that potentially could be significant to the VIE. The variable interest model requires a reporting entity to reevaluate whether an entity is a VIE upon the occurrence of certain significant events as listed in ASC 810-10-35-4, including any event that changes the design of the entity and calls into question the entity’s sufficiency of equity at risk or characteristics of a controlling financial interest (i.e. amendments to legal governing documents, returns or additions of equity, curtailments or modifications to activities in a way that impacts the equity at risk, etc.).

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



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Our investment in Real Estate and Other Affiliates that are reported on the equity and cost methods are as follows:

|   | Economic/Legal Ownership |                      | Carrying Value   |                      | Share of Earnings/Dividends       |       |                              |         |
|---|--------------------------|----------------------|------------------|----------------------|-----------------------------------|-------|------------------------------|---------|
|   | June 30,<br>2016         | December 31,<br>2015 | June 30,<br>2016 | December 31,<br>2015 | Three Months<br>Ended<br>June 30, |       | Six Months Ended<br>June 30, |         |
| (\$ in<br>Thousands)  |                          |                      |                  |                      | 2016                              | 2015  | 2016                         | 2015    |
| Equity Method<br>Investments<br>Master Planned<br>Communities:<br>The Summit (a)                | —                        | (a) —                | (a) \$ 20,926    | \$ 12,052            | \$ 8,874                          | \$ —  | \$ 8,874                     | \$ —    |
| Operating<br>Assets:<br>Grandview<br>SHG, LLC (a)   | 35.00                    | % —                  | % 8,179          | —                    | 22                                | —     | 41                           | —       |
| Millennium<br>Woodlands<br>Phase II, LLC<br>(b) (c)   | 81.43                    | % 81.43              | % —              | —                    | 22                                | (489) | 35                           | (1,150) |
| Stewart Title<br>Clark County<br>Las Vegas<br>Stadium, LLC<br>(c)                               | 50.00                    | % 50.00              | % 3,521          | 3,715                | 154                               | 302   | 256                          | 496     |
| The<br>Metropolitan<br>Downtown<br>Columbia (d)   | 50.00                    | % 50.00              | % 11,345         | 11,050               | 454                               | 401   | 295                          | 284     |
| Woodlands<br>Sarofim<br>Strategic<br>Developments:<br>Circle T Ranch<br>and Power<br>Center (a) | 50.00                    | % 50.00              | % 3,961          | 4,872                | 205                               | (89)  | (512)                        | (408)   |
| HHMK<br>Development<br>(c)  | 20.00                    | % 20.00              | % 2,673          | 2,588                | 42                                | 35    | 95                           | 75      |
|   | 50.00                    | % 50.00              | % 4,956          | 9,128                | 10,498                            | —     | 10,498                       | —       |
|   | 50.00                    | % 50.00              | % 10             | 10                   | —                                 | 10    | —                            | 549     |



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|  |       |   |       |   |           |           |           |          |           |          |
|--|-------|---|-------|---|-----------|-----------|-----------|----------|-----------|----------|
| KR Holdings<br>(c)<br>m.flats<br>(formerly<br>Parcel C) (a)<br>(c)<br>Constellation<br>(a) (c) | 50.00 | % | 50.00 | % | 758       | 689       | 4         | 911      | 9         | 1,276    |
| Cost method<br>investments<br>Investment in<br>Real Estate and<br>Other Affiliates             | 50.00 | % | 50.00 | % | 2,473     | 7,070     | —         | —        | —         | —        |
|  | 50.00 | % | 50.00 | % | 2,685     | 2,685     | —         | —        | —         | —        |
|  |       |   |       |   | 61,487    | 53,859    | 20,275    | 1,081    | 19,591    | 1,122    |
|  |       |   |       |   | 4,347     | 3,952     | —         | —        | 2,616     | 1,747    |
|  |       |   |       |   | \$ 65,834 | \$ 57,811 | \$ 20,275 | \$ 1,081 | \$ 22,207 | \$ 2,869 |

- (a) Please refer to the discussion below for a description of the joint venture ownership structure.
- (b) Millennium Woodlands Phase II, LLC was placed into service in the third quarter 2014. The investment balance is in a deficit position, which is reported in Accounts payable and accrued expenses. As of July 20, 2016, we acquired our joint venture partner's interest in this property, as discussed in Note 5 – Recent Transactions.
- (c) Equity method variable interest entity (“VIE”). As of first quarter 2016, m.flats was no longer a VIE.
- (d) The Metropolitan Downtown Columbia was placed into service in the first quarter 2015.

We are not the primary beneficiary of any of the VIEs listed above because we do not have the power to direct activities that most significantly impact the economic performance of such joint ventures and therefore we report our interests using the equity method. Our maximum exposure to loss as a result of these investments is limited to the aggregate carrying value of the investment as we have not provided any guarantees or otherwise made firm commitments to fund amounts on behalf of these VIEs. The aggregate carrying value of the unconsolidated VIEs was \$13.3 million and \$21.5 million as of June 30, 2016 and December 31, 2015, and was classified as Investment in Real Estate and Other Affiliates in the condensed consolidated balance sheets.

As of June 30, 2016 approximately \$134.6 million of indebtedness was secured by the properties owned by our Real Estate and Other Affiliates of which our share was approximately \$74.6 million based upon our economic ownership. All of this indebtedness is without recourse to us.

We are the primary beneficiary of one VIE which is consolidated in the financial statements. The creditors of the consolidated VIE do not have recourse to us. As of June 30, 2016, the carrying values of the assets and liabilities associated with the operations of the consolidated VIE were \$21.5 million and \$1.2 million, respectively. As of December 31, 2015, the carrying values of the assets and liabilities associated with the operations of the consolidated VIE were \$21.5 million and \$1.1 million, respectively. The assets of the VIE are restricted for use only by the particular VIE and are not available for our general operations.

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

The Summit

During the first quarter 2015, we formed DLV/HHPI Summerlin, LLC (“The Summit”) a joint venture with Discovery Land Company (“Discovery”). At formation, we contributed land with a book basis of \$13.4 million and transferred Special Improvement District (“SID”) bonds related to such land with a carrying value of \$1.3 million to the joint venture at an agreed upon capital contribution value of \$125.4 million, or \$226,000 per acre. Discovery is required to fund up to a maximum of \$30.0 million cash as its capital contribution, and we have no further capital obligations. The gain on the contributed land will be recognized in Equity in earnings from Real Estate and Other Affiliates as the joint venture sells lots.

After receipt of our capital contribution and a 5.0% preferred return, Discovery is entitled to a 5.0% return on its capital contributions, if any, plus cash distributions by the joint venture until it has received two times its equity contribution. Any further cash distributions are shared 50/50. Discovery is the manager of the project, and development began in the second quarter 2015. As of July 15, 2016, the project has contracted for approximately \$122.3 million in land sales, of which \$48.2 million in lot closings were completed in the second quarter 2016, resulting in Equity in earnings to us of \$8.9 million. Given the nature of the venture’s capital structure, our share of the venture’s income producing activities is recognized based on the Hypothetical Liquidation Book Value (“HLBV”) method, which is an amount equal to the change in our underlying share of the hypothetical distribution assuming all of the venture’s net assets were liquidated at book value.

Grandview SHG, LLC

In January 2016, we entered into a joint venture with Grandview SHG, LLC (“Grandview”) which purchased a hotel located at 33 Peck Slip in the Seaport District of New York. We advanced a bridge loan of \$25.0 million at a 5.0% interest rate to the joint venture at closing to expedite the acquisition, which was repaid in full in June 2016. In the second quarter 2016, upon completion of a refinancing of the property with a \$36.0 million redevelopment loan, we made an additional capital contribution of \$2.3 million. Our total investment in the joint venture is \$8.2 million as of June 30, 2016. We and our partner are in the process of evaluating potential development plans for the property.

Millennium Woodlands Phase II

On July 20, 2016, we purchased our joint venture partner’s 18.57% interest in Millennium Woodlands Phase II for \$4.0 million and distributed excess cash of approximately \$0.5 million to the partners. The venture developed, owns and operates a 314 unit multi-family property in The Woodlands. Simultaneously with the buyout, we replaced the joint venture’s existing \$37.7 million loan and secured a \$42.5 million fixed-rate loan at 3.39% maturing August 1, 2028.

Circle T Ranch and Power Center

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On June 1, 2016, the Circle T Ranch joint venture sold approximately 74 acres. As a result of the land sale, in the three and six months ended June 30, 2016 we recognized \$10.5 million as our share of the joint venture earnings in Equity in earnings from Real Estate and Other Affiliates.

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m.flats

On October 4, 2013, we entered into a joint venture agreement with a local developer, Kettler, Inc. (“Kettler”), to construct an apartment complex with ground floor retail in Downtown Columbia, Maryland. We contributed approximately five acres of land having a book value of \$4.0 million to the joint venture and subsequently incurred an additional \$3.1 million in capitalized development costs for a total book value contribution of \$7.1 million. Our land was valued at \$23.4 million, or \$53,500 per constructed unit. In January 2016, the venture closed on an \$88.0 million construction loan which is non-recourse to us and bears interest at one-month LIBOR plus 2.40% with an initial maturity date of February 2020, with three, one-year extension options. At loan closing, Kettler contributed \$16.1 million in cash, of which \$7.3 million was distributed to us. This transaction was accounted for as a partial sale of the land for which we recognized a net profit of \$0.2 million in the three months ended March 30, 2016. We contributed \$2.4 million in the three months ended June 30, 2016, and we are required to fund an additional \$3.9 million into this joint venture.

Constellation

On January 24, 2014, we entered into a joint venture with a national multi-family real estate developer, The Calida Group (“Calida”), to construct, own and operate a 124-unit gated luxury apartment development in downtown Summerlin. We own 50% of the venture and unanimous consent of the partners is required for all major decisions. This project represents the first residential development in Summerlin’s 400-acre downtown. In the first quarter 2015, we contributed a 4.5-acre parcel of land with an agreed value of \$3.2 million in exchange for a 50% interest in the venture. Our partner contributed \$3.2 million of cash for their 50% interest, is the development manager, funded all pre-development activities, obtained construction financing in the first quarter 2015 and provided guarantees required by the lender. The project is financed by a \$15.8 million construction loan which is non-recourse to us, of which \$9.3 million is outstanding as of June 30, 2016. In the fourth quarter 2015, we contributed an additional \$1.0 million to the joint venture to fund development costs. Upon a sale of the property, we are entitled to 50% of the proceeds up to, and 100% of the proceeds in excess of, an amount determined by applying a 7.0% capitalization rate to net operating income. The venture commenced construction in February 2015 and will complete the project in phases. The first units are currently available for rent, and we expect new tenants to take occupancy in the third quarter 2016.

NOTE 9 MORTGAGES, NOTES AND LOANS PAYABLE

Mortgages, notes and loans payable are summarized as follows:

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| (In thousands)   | June 30,<br>2016 | December 31,<br>2015 |
|--|------------------|----------------------|
| Fixed-rate debt:   |                  |                      |
| Collateralized mortgages, notes and loans payable  | \$ 1,059,210     | \$ 1,087,642         |
| Special Improvement District bonds   | 49,243           | 53,739               |
| Variable-rate debt:  |                  |                      |
| Collateralized mortgages, notes and loans payable (a)  | 1,553,786        | 1,314,973            |
| Deferred Financing Costs, net of accumulated amortization of \$14.7 million and \$12.7 million, respectively | (10,434)         | (12,392)             |
| Total mortgages, notes and loans payable   | \$ 2,651,805     | \$ 2,443,962         |

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(a) As more fully described below, \$207.6 million and \$209.5 million of variable rate debt has been swapped to a fixed-rate for the term of the related debt as of June 30, 2016 and December 31, 2015, respectively.

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

| (\$ In thousands)                    | Maturity (a)  | Interest Rate |          | Maximum         | Carrying Value |                   |
|--------------------------------------|---------------|---------------|----------|-----------------|----------------|-------------------|
|                                      |               |               |          | Facility Amount | June 30, 2016  | December 31, 2015 |
| <b>Master Planned Communities</b>    |               |               |          |                 |                |                   |
| Bridgeland Credit Facility           | November 2022 | 4.60          | %        | \$ 65,000       | \$ 59,349      | \$ 40,072         |
| Summerlin South SID Bonds - S124     | December 2019 | 5.95          | %        |                 | 141            | 159               |
| Summerlin South SID Bonds - S128     | December 2020 | 6.05          | %        |                 | 487            | 534               |
| Summerlin South SID Bonds - S128C    | December 2030 | 6.05          | %        |                 | 4,728          | 4,856             |
| Summerlin South SID Bonds - S132     | December 2020 | 6.00          | %        |                 | 1,494          | 1,676             |
| Summerlin South SID Bonds - S151     | June 2025     | 6.00          | %        |                 | 4,349          | 4,534             |
| Summerlin South SID Bonds - S159     | June 2035     | 6.00          | %        |                 | 6,614          | 9,020             |
| Summerlin West SID Bonds - S808/S810 | April 2031    | 6.00          | %        |                 | —              | 1,047             |
| Summerlin West SID Bonds - S812      | October 2035  | 6.00          | %        |                 | 27,844         | 28,328            |
| The Woodlands Master Credit Facility | August 2018   | 3.20          | % (b)    | 200,000         | 192,662        | 192,663           |
| Master Planned Communities Total     |               |               |          |                 | 297,668        | 282,889           |
| <b>Operating Assets</b>              |               |               |          |                 |                |                   |
| 10-60 Columbia Corporate Centers     | May 2022      | 2.81          | % (b)(c) |                 | 80,000         | 80,000            |
| 70 Columbia Corporate Center         | July 2019     | 2.70          | % (b)    |                 | 20,000         | 20,000            |
| Columbia Regional Building           | March 2018    | 2.45          | % (b)    | 23,008          | 22,188         | 22,188            |
| Downtown Summerlin                   | July 2019     | 2.70          | % (b)    | 311,800         | 293,732        | 289,804           |
| Downtown Summerlin SID Bonds - S108  | December 2016 | 5.95          | %        |                 | 235            | 235               |
| Downtown Summerlin SID Bonds - S128  | December 2030 | 6.05          | %        |                 | 3,350          | 3,350             |

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|  |               |      |          |         |           |           |
|--|---------------|------|----------|---------|-----------|-----------|
| Embassy Suites at Hughes Landing         | October 2020  | 2.95 | % (b)    | 37,100  | 28,829    | 20,064    |
|  | December      |      |          |         |           |           |
| One Hughes Landing                       | 2029          | 4.30 | %        |         | 52,000    | 52,000    |
|  | December      |      |          |         |           |           |
| Two Hughes Landing                       | 2030          | 4.20 | %        |         | 48,000    | 48,000    |
| 1725-35 Hughes Landing Boulevard         | June 2019     | 2.10 | % (b)    | 143,000 | 103,968   | 89,677    |
|  | December      |      |          |         |           |           |
| Hughes Landing Retail                    | 2018          | 2.40 | % (b)    | 36,575  | 32,465    | 28,726    |
| 1701 Lake Robbins                        | April 2017    | 5.81 | %        |         | 4,600     | 4,600     |
| Millennium Waterway Apartments           | June 2022     | 3.75 | %        |         | 55,584    | 55,584    |
| 110 N. Wacker                            | October 2019  | 5.21 | % (d)    |         | 24,593    | 26,481    |
|  | December      |      |          |         |           |           |
| 9303 New Trails                          | 2023          | 4.88 | %        |         | 12,558    | 12,734    |
|  | November      |      |          |         |           |           |
| One Lakes Edge                           | 2016          | 2.70 | % (b)    | 73,525  | 69,646    | 67,517    |
| Outlet Collection at Riverwalk           | October 2018  | 3.20 | % (b)    | 64,400  | 56,100    | 56,100    |
| 3831 Technology Forest Drive             | March 2026    | 4.50 | %        |         | 22,573    | 22,759    |
| The Westin at The Woodlands              | August 2019   | 3.10 | % (b)    | 69,300  | 49,788    | 33,361    |
| The Woodlands Resort & Conference Center | December      |      |          |         |           |           |
|  | 2020          | 3.20 | % (b)    |         | 85,000    | 85,000    |
|  | September     |      |          |         |           |           |
| Ward Village                             | 2016          | 3.46 | % (b)(e) | 250,000 | 238,716   | 238,716   |
| 20/25 Waterway Avenue                    | May 2022      | 4.79 | %        |         | 14,000    | 14,112    |
| 3 Waterway Square                        | August 2028   | 3.94 | %        |         | 52,000    | 52,000    |
|  | December      |      |          |         |           |           |
| 4 Waterway Square                        | 2023          | 4.88 | %        |         | 36,777    | 37,293    |
| Capital lease obligations                | various       | 3.60 | %        |         | 28        | 52        |
| Operating Assets Total                   |               |      |          |         | 1,406,730 | 1,360,353 |
| Strategic Developments                   |               |      |          |         |           |           |
| HHC 242 Self Storage Facility            | October 2021  | 3.05 | % (b)    | 6,658   | 866       | —         |
| HHC 2978 Self Storage Facility           | January 2022  | 3.05 | % (b)    | 6,368   | —         | —         |
| Lakeland Village Center                  | May 2020      | 2.80 | % (b)    | 14,000  | 8,514     | —         |
| Merriweather Post Pavilion               | October 2021  | 2.45 | % (b)    | 9,500   | 158       | —         |
| One Merriweather                         | February 2020 | 2.60 | % (b)    | 49,900  | 3,988     | —         |
|  | December      |      |          |         |           |           |
| Three Hughes Landing                     | 2017          | 2.80 | % (b)    | 65,455  | 33,200    | 23,268    |
| Waiea and Anaha                          | November      |      |          |         |           |           |
| Condominiums                             | 2019          | 7.20 | % (b)    | 600,000 | 150,025   | 27,817    |
| Strategic Developments Total             |               |      |          |         | 196,751   | 51,085    |
| Other Corporate Financing                |               |      |          |         |           |           |
| Arrangements                             | June 2018     | 3.00 | %        |         | 17,372    | 18,794    |
| Senior Notes                             | October 2021  | 6.88 | %        |         | 750,000   | 750,000   |
| Unamortized underwriting fees            |               |      |          |         | (6,282)   | (6,767)   |
| Deferred Financing Costs, net            |               |      |          |         | (10,434)  | (12,392)  |

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|   |              |              |
|---|--------------|--------------|
| Total mortgages, notes, and loans payable | \$ 2,651,805 | \$ 2,443,962 |
|---|--------------|--------------|

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- (a) Maturity date includes any extension periods that can be exercised at our option at the initial maturity date, subject to customary extension terms that based on current property performance projections, we expect to meet. Such terms may include but are not limited to minimum debt service coverage, minimum occupancy levels and other performance criteria.
- (b) The interest rate presented is based on the one month LIBOR rate, which was 0.45% at June 30, 2016.



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- (c) \$40.0 million of the outstanding principal balance is swapped to a 3.41% fixed-rate through maturity.
- (d) The \$24.6 million outstanding principal balance is swapped to a 5.21% fixed-rate through maturity.
- (e) \$143.0 million of the outstanding principal balance is swapped to a 3.81% fixed-rate through maturity. As of June 30, 2016 there is no undrawn availability on this facility. Management expects to refinance this note in the third quarter 2016.

The weighted average interest rate on our mortgages, notes and loans payable, excluding interest rate hedges, was 4.56% and 4.44% as of June 30, 2016 and December 31, 2015, respectively.

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

- (i) \$750.0 million of Senior Notes;
- (ii) \$311.8 million financing for the Downtown Summerlin development which has an initial maximum recourse of 35% of the outstanding balance, which will reduce to 15.0% upon completion of the project and achievement of a 1.15:1.0 debt service coverage ratio. The recourse further reduces to 10% upon achievement of a 1.25:1.0 debt service coverage ratio, a 90% occupancy level, and average tenant sales of at least \$500.00 per net rentable square foot. As of June 30, 2016, 35% of the outstanding loan balance remains recourse to HHC;
- (iii) \$64.4 million of construction financing for the Outlet Collection at Riverwalk with an initial maximum recourse of 50% of the outstanding balance, which will be reduced to 25.0% upon completion of the project and the achievement of an 11.0% debt yield and a minimum level of tenant sales per square foot for twelve months. As of June 30, 2016, 50% of the outstanding loan balance remains recourse to HHC;
- (iv) \$17.4 million of Other Corporate Financing Arrangements; and
- (v) \$7.0 million of the 110 N. Wacker mortgage.

Certain of our loans contain provisions which grant the lender a security interest in the operating cash flow of the property that represents the collateral for the loan. Certain mortgage notes may be prepaid, but may be subject to a prepayment penalty equal to a yield maintenance premium, defeasance, or a percentage of the loan balance. As of June 30, 2016, land, buildings and equipment and developments with a cost basis of \$2.4 billion have been pledged as collateral for our mortgages, notes and loans payable.

As of June 30, 2016, we were in compliance with all of the financial covenants related to our debt agreements.

Master Planned Communities

On November 9, 2015, we refinanced \$15.2 million of existing debt in connection with closing on a modification which increased the Bridgeland Credit Facility to \$65.0 million. The facility bears interest at three-month LIBOR plus 3.15%, with a 4.60% floor, and has an initial maturity date of November 2020 with two, one-year extension options. The proceeds are intended to provide working capital at Bridgeland for development efforts necessary to meet the demand of homebuilders for finished lots in the community.

The Woodlands Master Credit Facility was amended and restated on July 31, 2015 to a \$200.0 million maximum facility amount consisting of a \$100.0 million term loan and a \$100.0 million revolver (together, the "TWL Facility"). The TWL Facility bears interest at one-month LIBOR plus 2.75% and has an August 2016 initial maturity date with two, one-year extension options. In July, we exercised our first one-year extension option, which requires a reduction of the total commitment to \$175.0 million and semi-annual principal payments of \$25.0 million beginning on December 31, 2016 and continuing through a second, optional one-year extension period. The TWL Facility and The Woodlands Resort & Conference Center loans are recourse to the entities that directly own The Woodlands operations. The TWL Facility also contains certain covenants that, among other things, require the maintenance of specified financial ratios, limit the incurrence of additional recourse indebtedness at The Woodlands, and limit distributions from The Woodlands to us based

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on a loan to value test. The amendment also modified certain covenants to allow for more construction loan guarantees by the entities that directly own The Woodlands than would otherwise have been permitted by the prior facility.

The Summerlin MPC uses SID bonds to finance certain common infrastructure improvements. These bonds are issued by the municipalities and are secured by the assessments on the land. The majority of proceeds from each bond issued is held in a construction escrow and disbursed to us as infrastructure projects are completed, inspected by the municipalities and approved for reimbursement. Accordingly, the SID bonds have been classified as debt, and the Summerlin MPC pays the debt service on the bonds semi-annually. As Summerlin sells land, the buyers assume a proportionate share of the bond obligation at closing, and the residential sales contracts provide for the reimbursement of the principal amounts that we previously paid with respect to such proportionate share of the bond. In 2016, no new SID bonds have been issued and \$3.4 million in obligations were assumed by buyers.

Operating Assets

Our \$250.0 million first mortgage financing secured by the Ward Centers bears interest at LIBOR plus 2.50% and matures on September 29, 2016. There was no undrawn availability on the \$238.7 million balance as of June 30, 2016, and a refinance of the facility is currently underway and expected to close in the third quarter 2016.

Strategic Developments

On February 25, 2016, we closed on a \$49.9 million non-recourse construction loan for One Merriweather. The loan bears interest at one-month LIBOR plus 2.15% with an initial maturity date of February 25, 2020, with a one-year extension option. \$0.2 million was drawn on this loan as of June 30, 2016.

On January 27, 2016, we closed on a \$6.4 million non-recourse construction loan for the HHC 2978 Self-Storage Facility, bearing interest at one-month LIBOR plus 2.60% with an initial maturity date of January 2020, with two, one-year extension options. No amounts were drawn on this loan as of June 30, 2016.

Corporate

On October 2, 2013, we issued \$750.0 million in aggregate principal amount of 6.875% Senior Notes due 2021 (the "Senior Notes"). Interest is payable semiannually, on April 1 and October 1 of each year. At any time prior to October 1, 2016, we may redeem up to 35% of the Senior Notes at a price equal to 106.875% using the proceeds from equity offerings. We may redeem all or part of the Senior Notes at any time with a declining call premium thereafter to maturity. The Senior Notes contain customary terms and covenants for non-investment grade senior notes and have no maintenance covenants.

NOTE 10 DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

We are exposed to interest rate risk related to our variable interest rate debt, and we manage this risk by utilizing interest rate derivatives. Our objective in using interest rate derivatives is to add stability to interest costs by reducing our exposure to interest rate movements. To accomplish this objective, we use interest rate swaps, forward-starting swaps, and caps as part of our interest rate risk management strategy. As of June 30, 2016, we had interest rate swaps with gross notional amounts of \$207.6 million and a \$100.0 million interest rate cap, both of which were designated as effective cash flow hedges of interest rate risk. We also have \$250.0 million in gross notional amounts of forward-starting interest rate swaps that become effective December 31, 2017 to hedge a portion of anticipated future fixed-rate debt issuance.

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Interest rate swaps designated as cash flow hedges involve the receipt of variable amounts from a counterparty in exchange for the Company's fixed rate payments over the life of the agreements without exchange of the underlying notional amount. The three forward-starting interest rate swaps are designated as cash flow hedges of the variability of the anticipated interest rate of our long-term financing needs at our Downtown Summerlin property. Interest rate caps designated as cash flow hedges involve the receipt of variable amounts from a counterparty if interest rates rise above the strike rate on the contract in exchange for an up front premium.

The effective portion of changes in the fair value of derivatives designated and that qualify as cash flow hedges is recorded in Accumulated Other Comprehensive Income ("AOCI") and is subsequently reclassified into earnings in the period that the hedged forecasted transaction affects earnings. The ineffective portion of the change in fair value of the derivatives is recognized directly in earnings. During the six months ended June 30, 2016 and June 30, 2015, the ineffective portion recorded in earnings was insignificant.

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

Amounts reported in AOCI related to derivatives will be reclassified to interest expense as interest payments are made on our variable rate debt. Over the next 12 months, we estimate that an additional \$1.3 million will be reclassified to interest expense.

The table below presents the fair value of our derivative financial instruments, which are included in accounts payable and accrued liabilities in the condensed consolidated balance sheets:

|                            | June 30,<br>2016 | December<br>31,<br>2015 |
|----------------------------|------------------|-------------------------|
| (In thousands)             |                  |                         |
| Interest Rate Swaps & Caps | \$ 3,037         | \$ 2,292                |
| Forward-Starting Swaps     | 24,692           | 1,925                   |

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|   |           |          |
|---|-----------|----------|
| Total derivatives designated as hedging instruments | \$ 27,729 | \$ 4,217 |
|---|-----------|----------|

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The tables below present the effect of our derivative financial instruments on the condensed consolidated statements of operations for the three and six months ended June 30, 2016 and 2015:

| (In thousands)                | Three Months Ended June 30,           |                                       | Location of Loss<br>Reclassified<br>from AOCI into<br>Earnings | Three Months Ended<br>June 30,                              |   |
|-------------------------------|---------------------------------------|---------------------------------------|--|---|---|
|                               | 2016                                  | 2015                                  |  | 2016  | 2015  |
|                               | Amount of (Loss)<br>Recognized in OCI | Amount of (Loss)<br>Recognized in OCI |  | Amount of (Loss)<br>Reclassified from<br>AOCI into Earnings | Amount of (Loss)<br>Reclassified from<br>AOCI into Earnings |
| Cash Flow Hedges              |                                       |                                       |  |   |   |
| Interest Rate Swaps &<br>Caps | \$ (328)                              | \$ (240)                              | Interest Expense   | \$ (367)  | \$ (436)  |
| Forward-Starting Swaps        | (5,629)                               | —                                     | Interest Expense   | —   | —   |
|                               | \$ (5,957)                            | \$ (240)                              |  | \$ (367)  | \$ (436)  |

| (In thousands)                | Six Months Ended June 30,             |                                       | Location of Loss<br>Reclassified<br>from AOCI into<br>Earnings | Six Months Ended June 30,                                   |   |
|-------------------------------|---------------------------------------|---------------------------------------|--|---|---|
|                               | 2016                                  | 2015                                  |  | 2016  | 2015  |
|                               | Amount of (Loss)<br>Recognized in OCI | Amount of (Loss)<br>Recognized in OCI |  | Amount of (Loss)<br>Reclassified from<br>AOCI into Earnings | Amount of (Loss)<br>Reclassified from<br>AOCI into Earnings |
| Cash Flow Hedges              |                                       |                                       |  |   |   |
| Interest Rate Swaps &<br>Caps | \$ (1,206)                            | \$ (103)                              | Interest Expense   | \$ (743)  | \$ (811)  |
| Forward-Starting Swaps        | (14,910)                              | —                                     | Interest Expense   | —   | —   |
|                               | \$ (16,116)                           | \$ (103)                              |  | \$ (743)  | \$ (811)  |

## NOTE 11 INCOME TAXES

Unrecognized tax benefits pursuant to uncertain tax positions were \$36.5 million as of June 30, 2016 and December 31, 2015, respectively, none of which would impact our effective tax rate.

We have significant permanent differences, primarily from warrant liability gains and losses and changes in valuation allowances that cause our effective tax rate to deviate from statutory rates. The effective tax rates, based upon actual operating results, were 79.3% and 37.9% for the three and six months ended June 30, 2016 compared to 7.8% and (13.4)% for the three and six months ended June 30, 2015. The changes in the tax rates were primarily attributable to changes in the warrant liability, valuation allowance related to our deferred tax assets, as well as other items which are permanent differences for tax purposes.

The increase in deferred tax liabilities between December 31, 2015 and June 30, 2016 is due primarily to the utilization of federal tax assets used to offset the tax gain on the sale of the 80 South Street Assemblage.



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NOTE 12 STOCK BASED PLANS

Our stock based plans are described and informational disclosures are provided in the Notes to the Consolidated Financial Statements included in our Form 10-K for the year ended December 31, 2015.

Stock Options

The following table summarizes our stock option plan:

|  | Stock<br>Options | Weighted<br>Average<br>Exercise Price |
|--|------------------|---------------------------------------|
| Stock Options outstanding at December 31, 2015 | 1,086,040        | \$ 77.11                              |
| Granted  | 136,500          | 108.64                                |
| Forfeited                                      | (33,000)         | 118.23                                |
| Stock Options outstanding at June 30, 2016     | 1,189,540        | 79.55                                 |

Compensation costs related to stock options were \$0.5 million and \$2.3 million for the three and six months ended June 30, 2016, respectively, of which \$0.2 million and \$0.8 million were capitalized to development projects during the same periods. Stock option costs were \$1.2 million and \$1.8 million for the three and six months ended June 30, 2015, respectively, of which \$0.6 million and \$1.1 million were capitalized to development projects during the same periods.

Restricted Stock

The following table summarizes restricted stock activity:

| Restricted<br>Stock | Weighted<br>Average Grant<br>Date Fair Value |
|---------------------|--|
|---------------------|--|

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|   |          |           |
|---|----------|-----------|
| Restricted stock outstanding at December 31, 2015 | 242,556  | \$ 100.15 |
| Granted   | 131,198  | 65.79     |
| Vested  | (37,670) | 83.47     |
| Forfeited   | (4,985)  | 86.48     |
| Restricted Stock outstanding at June 30, 2016     | 331,099  | 88.64     |

Compensation expense related to restricted stock awards was \$1.8 million and \$3.4 million for the three and six months ended June 30, 2016, respectively, of which \$0.3 million and \$0.6 million were capitalized to development projects during the same periods. Compensation expense related to restricted stock awards was \$1.4 million and \$2.5 million for the three and six months ended June 30, 2015, respectively, of which \$0.3 million and \$0.5 million were capitalized to development projects during the same periods.

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## NOTE 13 OTHER ASSETS AND LIABILITIES

## Prepaid Expenses and Other Assets

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

| (In thousands)  | June 30,<br>2016 | December 31,<br>2015 |
|---|------------------|----------------------|
| Condominium receivables (a)   | \$ 423,906       | \$ 191,037           |
| Condominium deposits  | 91,661           | 55,749               |
| Special Improvement District receivable   | 72,594           | 72,558               |
| In-place leases   | 17,033           | 22,139               |
| Below-market ground leases  | 19,155           | 19,325               |
| Above-market tenant leases  | 2,714            | 3,581                |
| Equipment, net of accumulated depreciation of \$4.7 million and \$3.9 million, respectively | 18,182           | 18,772               |
| Security and escrow deposits  | 9,855            | 17,599               |
| Tenant incentives and other receivables   | 9,873            | 10,480               |
| Prepaid expenses  | 8,205            | 8,474                |
| Federal income tax receivable   | 12,106           | 11,972               |
| Intangibles   | 4,124            | 4,045                |
| Uncertain tax position asset  | 143              | 112                  |
| Other   | 3,080            | 5,347                |
|   | \$ 692,631       | \$ 441,190           |

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(a) Of the total Condominium receivables, \$329.7 million are expected to be collected in 2016 and \$94.2 million are expected to be collected in 2017, consistent with anticipated closings of the respective condominium projects.

The \$251.4 million net increase primarily relates to the following increases: a \$232.9 million increase in condominium receivables, which represents revenue recognized in excess of buyer deposits received for our Ward Village Condominium projects, an increase in condominium deposits of \$35.9 million due to deposits for sales of units and \$0.2 million in other increases.

These increases were partially offset by the following decreases: a net \$7.7 million decrease in security and escrow deposits mostly attributable to our January 2016 investment in the Grandview SHG, LLC joint venture; a decrease of \$5.1 million relating primarily to the amortization of in-place leases; a net decrease in other prepaids of \$2.3 million which was primarily due to the reimbursement from a tenant in the three months ended June 30, 2016; and a \$2.5 million decrease in other small net changes.

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## Accounts Payable and Accrued Expenses

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

| (In thousands)                                 | June 30,<br>2016 | December 31,<br>2015 |
|--|------------------|----------------------|
| Construction payables                          | \$ 193,847       | \$ 185,731           |
| Deferred income                                | 114,634          | 117,700              |
| Condominium deposit liabilities                | 87,428           | 50,192               |
| Accounts payable and accrued expenses          | 37,687           | 33,928               |
| Tenant and other deposits                      | 32,896           | 31,193               |
| Accrued interest                               | 16,627           | 16,504               |
| Accrued payroll and other employee liabilities | 20,142           | 31,271               |
| Accrued real estate taxes                      | 12,935           | 15,134               |
| Interest rate swaps                            | 27,729           | 4,217                |
| Above-market ground leases                     | 2,034            | 2,113                |
| Other  | 26,813           | 27,371               |
|  | \$ 572,772       | \$ 515,354           |

Total accounts payable and accrued expenses increased by \$57.4 million. This net increase primarily includes the following increases: a \$37.2 million increase in condominium deposits liability; an increase of \$3.8 million in accounts payable and accrued expenses; an increase of \$8.1 million in construction payables; an increase of \$23.5 million in interest rate swaps liability primarily due to a decrease in fair value of the forward-starting swaps; and \$1.8 million in other immaterial increases.

These increases are partially offset by the following decreases: decrease of \$11.1 million in accrued payroll and other employee liabilities due to payment in the first quarter 2016 of the 2015 annual incentive bonus; a decrease of \$2.2 million in accrued real estate taxes related to timing of payments; a decrease of \$3.1 million in deferred income; and \$0.6 million in other immaterial decreases.



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NOTE 14 ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS) (“AOCI”)

The following table summarizes AOCI for the period indicated:

|  | For the Three<br>Months Ended<br>June 30, 2016  | For the Three<br>Months<br>Ended<br>June 30, 2015 |
|--|---|---|
| Balance as of March 31   | \$ (17,760)                                     | \$ (7,259)  |
| Other comprehensive loss before reclassifications                                | (6,759)   | (293)   |
| Loss reclassified from accumulated other comprehensive loss to net income (loss) | 367   | 436   |
| Net current-period other comprehensive income (loss)                             | (6,392)   | 143   |
| Balance as of June 30  | \$ (24,152)                                     | \$ (7,116)  |
|  | For the Six<br>Months<br>Ended<br>June 30, 2016 | For the Six<br>Months<br>Ended<br>June 30, 2015   |
| Balance as of December 31  | \$ (7,889)                                      | \$ (7,712)  |
| Other comprehensive loss before reclassifications                                | (17,006)  | (215)   |
| Loss reclassified from accumulated other comprehensive loss to net income (loss) | 743   | 811   |
| Net current-period other comprehensive loss                                      | (16,263)  | 596   |
| Balance as of June 30  | \$ (24,152)                                     | \$ (7,116)  |

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

| Accumulated Other Comprehensive Income (Loss) Components | Amounts reclassified from Accumulated Other<br>Income (Loss) | For the Three Months Ended<br>June 30, 2016 | For the Six Months Ended<br>June 30, 2016 | For the Three Months Ended<br>June 30, 2015 | For the Six Months Ended<br>June 30, 2015 | Item in the<br>Statement of Operations |
|--|--|---|---|---|---|--|
| Losses on cash flow hedges                               | \$ 588   | \$ 1,193                                    | \$ 588                                    | \$ 588                                      | \$ 588                                    | Interest expense                       |

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|  |               |               |   |
|--|---------------|---------------|---|
| Interest rate swap contracts                             | (221)         | (450)         | Provision for income taxes                  |
| Total reclassifications for the period                   | \$ 367        | \$ 743        | Net of tax                                  |
|  |               |               | Amounts reclassified from Accumulated Other |
|  |               |               | Income (Loss)                               |
|  |               |               | For the Three Months Ended                  |
| Accumulated Other Comprehensive Income (Loss) Components | June 30, 2016 | June 30, 2015 | Item in the                                 |
| Losses on cash flow hedges                               | \$ 705        | \$ 1,301      | Statement of Operations                     |
| Interest rate swap contracts                             | (269)         | (490)         | Interest expense                            |
| Total reclassifications for the period                   | \$ 436        | \$ 811        | Provision for income taxes                  |
|  |               |               | Net of tax                                  |

NOTE 15 COMMITMENTS AND CONTINGENCIES

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

We had outstanding letters of credit and surety bonds totaling \$98.4 million and \$86.1 million as of June 30, 2016 and December 31, 2015, respectively. These letters of credit and bonds were issued primarily in connection with insurance requirements, special real estate assessments and construction obligations.



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On June 27, 2013, the City of New York executed the amended and restated ground lease for South Street Seaport. The restated lease terms provide for annual fixed base rent of \$1.2 million starting July 1, 2013 with an expiration of December 30, 2072, including our options to extend. The rent escalates at 3.0% compounded annually. On July 1, 2048 the base rent will be adjusted to the higher of the fair market value or the then base rent. In addition to the annual base rent, we are required to make annual payments of \$210,000 as additional rent through the term of the lease. The additional rent escalates annually at the Consumer Price Index. Simultaneously with the execution of the lease, we executed a completion guaranty for the redevelopment of Pier 17 by 2017.

In the fourth quarter 2012, the historic area of South Street Seaport suffered damage due to flooding as a result of Superstorm Sandy. Reconstruction efforts are ongoing and the property has only partially operated over the last three years. We have received \$54.1 million in insurance proceeds, and we recognized Other income of \$6.2 million and \$0.3 million for the six months ended June 30, 2016 and June 30, 2015, respectively, for the receipt of insurance proceeds related to our claim. This matter is currently being litigated with an insurance carrier, and there can be no assurance that we will collect additional insurance proceeds.

NOTE 16 SEGMENTS

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

- Master Planned Communities ("MPCs") – includes the development and sale of land, in large scale, long term community development projects in and around Las Vegas, Nevada; Houston, Texas; and Columbia, Maryland.
- Operating Assets – includes retail, office, hospitality and multi-family properties along with other real estate investments. These assets are currently generating revenues, and are comprised of commercial real estate properties developed or acquired by us, and properties where we believe there is an opportunity to redevelop, reposition, or sell to improve segment performance or to recycle capital.

- Strategic Developments – includes our residential condominium and commercial property projects currently under development and all other properties held for development which have no substantial operations.

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## THE HOWARD HUGHES CORPORATION

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## UNAUDITED

The assets included in each segment as of June 30, 2016, are contained in the following chart:

| Master Planned Communities | Operating Assets   |   | Strategic Developments   |
|----------------------------|--|---|--|
|                            | Retail   | Office  | Under Construction   |
| • Bridgeland               | Columbia Regional Building   | 10-70 Columbia Corporate Center   | Ae'o   |
| • Maryland                 | Cottonwood Square  | Columbia Office Properties  | Anaha  |
| • Summerlin                | Creekside Village Green (b)  | 1725-35 Hughes Landing Boulevard (b)  | Constellation (a)  |
| • The Woodlands            | Downtown Summerlin   | One Hughes Landing  | HHC 242 Self-Storage   |
| • The Woodlands Hills      | Hughes Landing Retail (b)  | Two Hughes Landing  | HHC 2978 Self-Storage  |
|                            | 1701 Lake Robbins Landmark Mall  | 2201 Lake Woodlands Drive<br>9303 New Trails  | Lakeland Village Center m.flats (formerly Parcel C)<br>(a)   |
| Other                      | Outlet Collection at Riverwalk   | 110 N. Wacker   | One Merriweather   |
| • The Summit (a)           | Park West<br>South Street Seaport<br><br>(under construction)<br>Ward Village<br>20/25 Waterway Avenue<br>Waterway Garage Retail   | ONE Summerlin (b)<br>3831 Technology Forest Drive<br>3 Waterway Square<br>4 Waterway Square<br>1400 Woodloch Forest   | Three Hughes Landing<br>Waiea  |
|                            | Multi-family<br>Millennium Waterway Apartments<br>Millennium Woodlands Phase II (a)<br>One Lakes Edge (b)<br>85 South Street<br>The Metropolitan<br>Downtown<br>Columbia (a) (b) | Other<br>Clark County Las Vegas Stadium (a)<br>Kewalo Basin Harbor<br>Merriweather Post Pavilion<br>Stewart Title of Montgomery County, TX (a)<br>Summerlin Hospital Medical Center (a)<br>The Woodlands Parking<br>Garages<br>Woodlands Sarofim #1 (a) | Other<br>Alameda Plaza<br>AllenTowne<br>Bridges at Mint Hill<br>Century Plaza Mall<br>Circle T Ranch and<br><br>Power Center (a)<br>Cottonwood Mall<br>80% Interest in Fashion Show Air Rights<br>Gateway Towers<br><br>Ke Kilohana<br>Kendall Town Center<br><br>Lakemoor (Volo) Land |
|                            | Hospitality  |   |  |

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Embassy Suites at Hughes  
Landing (b)  
Grandview SHG, LLC (a)

The Woodlands Resort &  
Conference Center  
The Westin at The  
Woodlands (c)

Maui Ranch Land

The Outlet Collection at  
Elk Grove  
Two Merriweather  
West Windsor

- 
- (a) A non-consolidated investment. Refer to Note 8 – Real Estate and Other Affiliates.
  - (b) Asset was placed in service and moved from the Strategic Developments segment to the Operating Assets segment during 2015.
  - (c) Asset was placed in service and moved from the Strategic Developments segment to the Operating Assets segment during 2016.

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

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

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Segment operating results are as follows:

| (In thousands)  | Three Months Ended June 30, |           | Six Months Ended June 30, |           |
|---|-----------------------------|-----------|---------------------------|-----------|
|   | 2016                        | 2015      | 2016                      | 2015      |
| <b>Master Planned Communities</b>                         |                             |           |                           |           |
| Land sales  | \$ 61,098                   | \$ 45,433 | \$ 103,040                | \$ 93,514 |
| Builder price participation                               | 6,501                       | 7,907     | 11,148                    | 13,606    |
| Minimum rents   | 142                         | 215       | 282                       | 429       |
| Other land revenues                                       | 2,749                       | 3,140     | 5,772                     | 6,426     |
| Other rental and property revenues                        | 17                          | 9         | 20                        | 7         |
| Total revenues  | 70,507                      | 56,704    | 120,262                   | 113,982   |
| Cost of sales – land                                      | 29,008                      | 24,236    | 44,696                    | 48,132    |
| Land sales operations                                     | 5,506                       | 9,721     | 12,806                    | 17,300    |
| Land sales real estate and business taxes                 | 2,300                       | 2,242     | 4,594                     | 4,646     |
| Depreciation and amortization                             | 81                          | 95        | 164                       | 190       |
| Interest income   | (5)                         | (15)      | (21)                      | (31)      |
| Interest expense (*)                                      | (5,004)                     | (4,684)   | (10,343)                  | (9,446)   |
| Equity in earnings in Real Estate and Other<br>Affiliates | (8,874)                     | —         | (8,874)                   | —         |
| Total expenses, net of other income                       | 23,012                      | 31,595    | 43,022                    | 60,791    |
| MPC EBT   | 47,495                      | 25,109    | 77,240                    | 53,191    |
| <b>Operating Assets</b>                                   |                             |           |                           |           |
| Minimum rents   | 41,811                      | 36,697    | 82,929                    | 71,009    |
| Tenant recoveries   | 10,914                      | 10,693    | 21,437                    | 20,266    |
| Hospitality revenues                                      | 19,129                      | 11,481    | 32,038                    | 23,484    |
| Other rental and property revenues                        | 4,416                       | 6,971     | 7,499                     | 13,245    |
| Total revenues  | 76,270                      | 65,842    | 143,903                   | 128,004   |
| Other property operating costs                            | 13,830                      | 18,350    | 27,948                    | 35,836    |
| Real estate taxes   | 6,709                       | 5,990     | 12,851                    | 11,510    |
| Rental property maintenance costs                         | 2,645                       | 2,785     | 5,646                     | 5,412     |
| Hospitality costs   | 14,242                      | 8,893     | 24,717                    | 17,971    |
| Provision for doubtful accounts                           | (353)                       | 1,266     | 2,626                     | 2,075     |
| Demolition costs  | 6                           | 1,496     | 478                       | 1,613     |
| Development-related marketing costs                       | 1,988                       | 2,748     | 3,088                     | 5,014     |
| Depreciation and amortization                             | 22,613                      | 22,887    | 43,814                    | 41,649    |
| Other income, net   | (2,750)                     | —         | (3,113)                   | —         |
| Interest income   | (8)                         | (9)       | (16)                      | (19)      |

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|  |            |           |            |           |
|--|------------|-----------|------------|-----------|
| Interest expense   | 10,116     | 7,629     | 19,269     | 14,123    |
| Equity in earnings from Real Estate and Other Affiliates | (899)      | (160)     | (2,826)    | (1,044)   |
| Total expenses, net of other income                      | 68,139     | 71,875    | 134,482    | 134,140   |
| Operating Assets EBT                                     | 8,131      | (6,033)   | 9,421      | (6,136)   |
| Strategic Developments                                   |            |           |            |           |
| Minimum rents  | 83         | 77        | 134        | 744       |
| Tenant recoveries  | 9          | 8         | 14         | 102       |
| Condominium rights and unit sales                        | 125,112    | 86,513    | 247,206    | 121,370   |
| Other land revenues                                      | 10         | 5         | 20         | 12        |
| Other rental and property revenues                       | 160        | 14        | 278        | 39        |
| Total revenues   | 125,374    | 86,617    | 247,652    | 122,267   |
| Condominium rights and unit cost of sales                | 79,726     | 56,765    | 154,541    | 79,174    |
| Other property operating costs                           | 1,406      | 1,284     | 3,030      | 1,943     |
| Real estate taxes  | 620        | 578       | 1,226      | 1,258     |
| Rental property maintenance costs                        | 108        | 115       | 239        | 232       |
| Provision for doubtful accounts                          | 1          | —         | 63         | —         |
| Demolition costs   | 484        | —         | 484        | —         |
| Development-related marketing costs                      | 4,351      | 2,846     | 7,782      | 6,823     |
| Depreciation and amortization                            | 660        | 601       | 1,319      | 1,617     |
| Other income, net  | —          | —         | (244)      | (334)     |
| Interest income  | (125)      | (166)     | (131)      | (166)     |
| Interest expense (*)                                     | (1,899)    | (1,580)   | (3,033)    | (3,385)   |
| Equity in earnings from Real Estate and Other Affiliates | (10,502)   | (921)     | (10,507)   | (1,825)   |
| Gain on sale of 80 South Street Assemblage               | —          | —         | (140,479)  | —         |
| Total expenses, net of other income                      | 74,830     | 59,522    | 14,290     | 85,337    |
| Strategic Developments EBT                               | 50,544     | 27,095    | 233,362    | 36,930    |
| REP EBT  | \$ 106,170 | \$ 46,171 | \$ 320,023 | \$ 83,985 |

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

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

## Reconciliation of REP EBT to GAAP income

| (loss) before taxes<br>(In thousands)   | Three Months Ended June 30, |           | Six Months Ended June 30, |             |
|---|-----------------------------|-----------|---------------------------|-------------|
|   | 2016                        | 2015      | 2016                      | 2015        |
| REP EBT                                 | \$ 106,170                  | \$ 46,171 | \$ 320,023                | \$ 83,985   |
| General and administrative              | (20,053)                    | (19,606)  | (40,377)                  | (38,569)    |
| Corporate interest expense, net         | (13,023)                    | (13,235)  | (26,097)                  | (26,447)    |
| Warrant liability gain (loss)           | (44,150)                    | 42,620    | (14,330)                  | (66,190)    |
| Corporate other income, net             | 6,317                       | 396       | 6,069                     | 1,529       |
| Corporate depreciation and amortization | (1,598)                     | (1,487)   | (2,627)                   | (3,124)     |
| Income (loss) before taxes              | \$ 33,663                   | \$ 54,859 | \$ 242,661                | \$ (48,816) |

The following reconciles segment revenues to GAAP consolidated revenues:

## Reconciliation of Segment Basis Revenues

| to GAAP Revenues<br>(In thousands) | Three Months Ended June 30, |            | Six Months Ended June 30, |            |
|------------------------------------|-----------------------------|------------|---------------------------|------------|
|                                    | 2016                        | 2015       | 2016                      | 2015       |
| Master Planned Communities         | \$ 70,507                   | \$ 56,704  | \$ 120,262                | \$ 113,982 |
| Operating Assets                   | 76,270                      | 65,842     | 143,903                   | 128,004    |
| Strategic Developments             | 125,374                     | 86,617     | 247,652                   | 122,267    |
| Total revenues                     | \$ 272,151                  | \$ 209,163 | \$ 511,817                | \$ 364,253 |

The assets by segment and the reconciliation of total segment assets to the total assets in the condensed consolidated balance sheets are summarized as follows:

| (In thousands)             | June 30,<br>2016 | December 31,<br>2015 |
|----------------------------|------------------|----------------------|
| Master Planned Communities | \$ 2,006,094     | \$ 2,022,524         |
| Operating Assets           | 2,496,917        | 2,365,724            |
| Strategic Developments     | 1,525,312        | 1,138,695            |
| Total segment assets       | 6,028,323        | 5,526,943            |

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|                     |              |              |
|---------------------|--------------|--------------|
| Corporate and other | 189,296      | 194,639      |
| Total assets        | \$ 6,217,619 | \$ 5,721,582 |

The \$386.6 million increase in the Strategic Developments segment asset balance as of June 30, 2016 compared to December 31, 2015 is primarily due to the net change resulting from receipt of sale proceeds in excess of our cost basis relating to the 80 South Street Assemblage transaction and increased development expenditures primarily at Waiea, Anaha, Ae'o and One Merriweather. These increases were partially offset by sales recognized and deposits utilized for construction at Waiea and Anaha, and placing The Westin at The Woodlands in service in the Operating Assets segment.

The increase in the Operating Assets segment asset balance as of June 30, 2016 of \$131.2 million compared to December 31, 2015 is primarily due to placing The Westin at The Woodlands in service and additional development expenditures at South Street Seaport.

The decrease in the MPC segment assets primarily relates to distributions of cash from the MPC segment to the corporate parent.



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

The following discussion and analysis should be read in conjunction with the Consolidated Financial Statements and Notes included in this Quarterly Report and in the Company's Form 10-K for the year ended December 31, 2015. All references to numbered Notes are to specific notes to our Condensed Consolidated Financial Statements included in this Quarterly Report.

Forward-looking information

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

Forward-looking statements include:

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

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

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

Forward-looking statements give our current expectations relating to our financial condition, results of operations, plans, objectives, future performance and business. You can identify forward-looking statements by the fact that they do not relate strictly to current or historical facts. These statements may include words such as "anticipate," "believe," "estimate," "expect," "forecast," "intend," "likely," "may," "plan," "project," "realize," "should," "transform," "would," and other similar expression. Forward-looking statements should not be relied upon. They give our expectations about the future

and are not guarantees.

There are several factors, many beyond our control, which could cause results to differ materially from our expectations. These risk factors are described in our Annual Report on Form 10-K for the year ended December 31, 2015 (the “Annual Report”) and are incorporated herein by reference. Any factor could, by itself, or together with one or more other factors, adversely affect our business, results of operations or financial condition. There may be other factors that we have not described in this Quarterly Report or in our Annual Report that could cause results to differ from our expectations. These forward-looking statements present our estimates and assumptions as of the date of this Quarterly Report. Except as may be required by law, we undertake no obligation to modify or revise any forward-looking statements to reflect events or circumstances occurring after the date of this Quarterly Report.

### Real Estate Property Earnings Before Taxes

We use a number of operating measures for assessing operating performance of properties within our segments, some of which may not be common among all three of our segments. We believe that investors may find some operating measures more useful than others when separately evaluating each segment. One common operating measure used to assess operating results for our business segments is Real Estate Property Earnings Before Taxes (“REP EBT”). We believe REP EBT provides useful information about the operating performance of our properties because it excludes certain non-

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recurring and non-cash items which we believe are not indicative of our core business. REP EBT may be calculated differently by other companies in our industry, limiting its usefulness as a comparative measure.

REP EBT, as it relates to our business, is defined as net income (loss) excluding general and administrative expenses, corporate other income, corporate interest income, corporate interest and depreciation expense, provision for income taxes, and warrant liability gain (loss). We present REP EBT because we use this measure, among others, internally to assess the core operating performance of our assets. We also present this measure because we believe certain investors use it as a measure of a company's historical operating performance and its ability to service and incur debt. We believe that the inclusion of certain adjustments to net income (loss) to calculate REP EBT is appropriate to provide additional information to investors. A reconciliation of REP EBT to consolidated net income (loss) as computed in accordance with GAAP has been presented in Note 16 – Segments. We also provide a measure of Adjusted Operating Assets REP EBT, which excludes depreciation and amortization, demolition costs and development-related marketing costs. A reconciliation of Adjusted Operating Assets EBT to Operating Assets EBT is included in the Operating Assets discussion.

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

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

## Operating Assets Net Operating Income

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

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

Results of Operations

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

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The following table reflects our results of operations for the three and six months ended June 30, 2016 and 2015, respectively:

| (In thousands, except per share amounts)                     | Three Months Ended<br>June 30, |                   |                    | Six Months Ended<br>June 30, |                    |                   |
|--|--------------------------------|-------------------|--------------------|------------------------------|--------------------|-------------------|
|  | 2016                           | 2015              | Change             | 2016                         | 2015               | Change            |
| <b>Revenues</b>  |                                |                   |                    |                              |                    |                   |
| MPC segment revenues   | \$ 70,507                      | \$ 56,704         | \$ 13,803          | \$ 120,262                   | \$ 113,982         | \$ 6,280          |
| Operating Assets segment revenues                            | 76,270                         | 65,842            | 10,428             | 143,903                      | 128,004            | 15,899            |
| Strategic Developments segment revenues                      | 125,374                        | 86,617            | 38,757             | 247,652                      | 122,267            | 125,385           |
| <b>Total revenues</b>  | <b>\$ 272,151</b>              | <b>\$ 209,163</b> | <b>\$ 62,988</b>   | <b>\$ 511,817</b>            | <b>\$ 364,253</b>  | <b>\$ 147,564</b> |
| <b>MPC segment REP EBT</b>                                   | <b>\$ 47,495</b>               | <b>\$ 25,109</b>  | <b>\$ 22,386</b>   | <b>\$ 77,240</b>             | <b>\$ 53,191</b>   | <b>\$ 24,049</b>  |
| Operating Assets segment REP EBT                             | 8,131                          | (6,033)           | 14,164             | 9,421                        | (6,136)            | 15,557            |
| Strategic Developments segment REP EBT                       | 50,544                         | 27,095            | 23,449             | 233,362                      | 36,930             | 196,432           |
| <b>Total segment REP EBT (a)</b>                             | <b>106,170</b>                 | <b>46,171</b>     | <b>59,999</b>      | <b>320,023</b>               | <b>83,985</b>      | <b>236,038</b>    |
| General and administrative                                   | (20,053)                       | (19,606)          | (447)              | (40,377)                     | (38,569)           | (1,808)           |
| Corporate interest expense, net                              | (13,023)                       | (13,235)          | 212                | (26,097)                     | (26,447)           | 350               |
| Warrant liability (loss) gain                                | (44,150)                       | 42,620            | (86,770)           | (14,330)                     | (66,190)           | 51,860            |
| Corporate other income, net                                  | 6,317                          | 396               | 5,921              | 6,069                        | 1,529              | 4,540             |
| Corporate depreciation and amortization                      | (1,598)                        | (1,487)           | (111)              | (2,627)                      | (3,124)            | 497               |
| Provision for income taxes                                   | (26,693)                       | (4,274)           | (22,419)           | (91,926)                     | (6,558)            | (85,368)          |
| <b>Net income (loss)</b>                                     | <b>6,970</b>                   | <b>50,585</b>     | <b>(43,615)</b>    | <b>150,735</b>               | <b>(55,374)</b>    | <b>206,109</b>    |
| Net income attributable to noncontrolling interests          | —                              | (12)              | 12                 | —                            | (12)               | 12                |
| <b>Net income (loss) attributable to common stockholders</b> | <b>\$ 6,970</b>                | <b>\$ 50,573</b>  | <b>\$ (43,603)</b> | <b>\$ 150,735</b>            | <b>\$ (55,386)</b> | <b>\$ 206,121</b> |
| <b>Diluted income (loss) per share</b>                       | <b>\$ 0.16</b>                 | <b>\$ 0.18</b>    | <b>\$ (0.02)</b>   | <b>\$ 3.53</b>               | <b>\$ (1.40)</b>   | <b>\$ 4.94</b>    |

(a) Total segment REP EBT includes depreciation and amortization expense. Non-cash total segment depreciation and amortization, primarily relating to Operating Assets recently placed into service, is currently offsetting the net operating income generated from these properties because they typically will not stabilize for 12 – 36 months after they are placed into service, but the full amount of their annual depreciation and amortization begins when they are placed into service. The following table shows the amounts included in segment REP EBT related to non-cash depreciation and amortization:

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| (In thousands)                              | Three Months Ended |           |          | Six Months Ended |           |          |
|---|--------------------|-----------|----------|------------------|-----------|----------|
|   | June 30,<br>2016   | 2015      | Change   | June 30,<br>2016 | 2015      | Change   |
| Total segment depreciation and amortization | \$ 23,354          | \$ 23,583 | \$ (229) | \$ 45,297        | \$ 43,456 | \$ 1,841 |

Total revenues for the three and six months ended June 30, 2016 increased compared to the same period in 2015 due to higher revenues in our MPC, Operating Assets and Strategic Developments segments. The MPC segment revenues increase is due to higher residential land sales in our MPCs for the three and six months ended June 30, 2016 as compared to the same periods in 2015. Strategic Developments segment revenue increased due to higher revenue related to sales at our Waiea and Anaha condominium projects, which are currently reported on the percentage of completion method. Operating Assets segment revenue increased primarily due to assets placed in service in 2016 and 2015, including 1725-1735 Hughes Landing Boulevard, The Westin at The Woodlands, Embassy Suites at Hughes Landing, Hughes Landing Retail, One Lakes Edge and ONE Summerlin, and the ongoing stabilization of Downtown Summerlin.

General and administrative expenses for the three and six months ended June 30, 2016 increased compared to the same periods in 2015. For the three months ended June 30, 2016, the increase is primarily due to \$0.8 million of higher compensation costs related to headcount, offset by \$0.6 million of decreased travel costs compared to the same period in the prior year. For the six months ended June 30, 2016, the increase is primarily due to \$1.2 million of higher compensation costs related to headcount compared to the same period in the prior year.

Provision for income taxes increased for the three and six months ended June 30, 2016 due to increases in pre-tax earnings, as noted on the Condensed Consolidated Statement of Operations, adjusted to exclude the non-taxable warrant gain (loss) which has no impact on our tax provision.

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We have significant permanent differences, primarily due to warrant liability gains and losses and changes in valuation allowances that cause our effective tax rate to deviate greatly from statutory rates. The effective tax rates, based upon actual operating results were 79.3% and 37.9% for the three and six months ended June 30, 2016 compared to 7.8% and (13.4)% for the three and six months ended June 30, 2015. The changes in the tax rate were primarily attributable to changes in the warrant liability, valuation allowance related to our deferred tax asset, as well as other items which are permanent differences for tax purposes. If changes in the warrant liability, valuation allowance, unrecognized tax benefits, and other material discrete adjustments to deferred tax liabilities were excluded from the effective tax rate computation, the adjusted effective tax rates would have been 36.7% and 37.0% for the three and six months ended June 30, 2016, respectively, compared to 34.9% and 34.7% for three and six months ended June 30, 2015.

The decrease in Net income attributable to common stockholders for the three months ended June 30, 2016 compared to the same period in 2015 is primarily due to a higher warrant liability loss, offset by increased REP EBT in our MPC, Operating Assets and Strategic Developments segments. The increase in Net income (loss) attributable to common stockholders for the six months ended June 30, 2016 compared to the same period in 2015 is primarily due to a gain on the sale of the 80 South Street Assemblage included in Strategic Developments segment REP EBT, significant growth in earnings from condominium rights and unit sales in Strategic Developments segment revenues, a lower warrant liability loss and moderately increased REP EBT in our MPC and Operating Assets segments. These increases were partially offset by an increased provision for income taxes.

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

Segment Operations

Please refer to Note 16 - Segments for additional information including reconciliations of our segment basis results to generally accepted accounting principles (“GAAP”) basis results.

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## Master Planned Communities Revenues and Expenses(\*)

For the three months ended June 30, 2016 and 2015

(In thousands, except %)

| (In thousands)                            | Bridgeland |          | Maryland Communities |       | Summerlin |           | The Woodlands |          | The Wood Hills |
|---|------------|----------|----------------------|-------|-----------|-----------|---------------|----------|----------------|
|   | 2016       | 2015     | 2016                 | 2015  | 2016      | 2015      | 2016          | 2015     | 2016           |
| Land sales (e)                            | \$ 4,500   | \$ 1,495 | \$ —                 | \$ —  | \$ 55,212 | \$ 34,832 | \$ 1,386      | \$ 9,106 | \$ —           |
| Builder price participation               | 180        | 398      | —                    | —     | 5,425     | 6,280     | 896           | 1,229    | —              |
| Minimum rents                             | —          | —        | —                    | —     | 142       | 215       | —             | —        | —              |
| Other land sale revenues                  | 34         | 65       | 2                    | 1     | 2,604     | 1,676     | 104           | 1,398    | 5              |
| Other rental and property revenues        | —          | —        | —                    | —     | 13        | 9         | —             | —        | 4              |
| Total revenues                            | 4,714      | 1,958    | 2                    | 1     | 63,396    | 43,012    | 2,386         | 11,733   | 9              |
| Cost of sales - land                      | 1,532      | 532      | —                    | —     | 26,904    | 20,592    | 572           | 3,112    | —              |
| Land sales operations                     | 1,259      | 942      | 39                   | 99    | 1,811     | 3,671     | 2,350         | 5,006    | 47             |
| Land sales real estate and business taxes | 251        | 73       | 158                  | 162   | 613       | 919       | 1,255         | 1,060    | 23             |
| Depreciation and amortization             | 23         | 29       | 5                    | 6     | 23        | 30        | 30            | 30       | —              |
| Total expenses                            | 3,065      | 1,576    | 202                  | 267   | 29,351    | 25,212    | 4,207         | 9,208    | 70             |
| Operating income                          | 1,649      | 382      | (200)                | (266) | 34,045    | 17,800    | (1,821)       | 2,525    | (61)           |
| Interest expense, net (a)                 | (2,220)    | (2,320)  | 2                    | (7)   | (4,090)   | (3,537)   | 1,443         | 1,296    | (144)          |
|   | —          | —        | —                    | —     | (8,874)   | —         | —             | —        | —              |



|  |          |          |             |             |           |           |               |          |       |
|--|----------|----------|-------------|-------------|-----------|-----------|---------------|----------|-------|
| Equity in earnings in Real Estate and Other Affiliates MPC REP EBT | \$ 3,869 | \$ 2,702 | \$ (202)(c) | \$ (259)(c) | \$ 47,009 | \$ 21,337 | \$ (3,264)(d) | \$ 1,229 | \$ 83 |
| Gross Margin %   |          |          |             |             |           |           |               |          |       |
| (b)  | 66.0 %   | 64.4 %   | NM          | NM          | 51.3 %    | 40.9 %    | 58.7 %        | 65.8 %   | NM    |

(\*) For a reconciliation of MPC REP EBT to consolidated income (loss) before taxes, refer to Note 16 – Segments.

- (a) Negative interest expense amounts relate to interest capitalized on debt assigned to our Operating Assets segment and corporate debt.
- (b) Gross Margin % is the ratio of Land sales less Cost of sales-land, divided by Land sales.
- (c) The negative MPC REP EBT in Maryland is due to no land sales in 2016 or 2015; however, certain costs such as real estate taxes and administrative expenses continue to be incurred.
- (d) The number of residential lots sold decreased from 43 to nine for the three months ended June 30, 2016 compared to the same period in 2015, resulting in negative MPC REP EBT at The Woodlands.
- (e) Land sales includes deferred revenue from land sales closed in a previous period which met criteria for recognition in the current period.

NM – Not meaningful

Interest expense, net reflects the amount of interest that is capitalized at the project level.

Although our business does not involve the sale or resale of homes, we believe that net new home sales are an important indicator of future demand for our superpad sites and lots; therefore, we use this statistic where relevant in the discussion of our MPC operating results. Net new home sales reflect home sales made by homebuilders, less cancelations. Cancelations occur when a home buyer signs a contract to purchase a home, but later fails to qualify for a home mortgage or is unable to provide an adequate down payment to complete the home sale.

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## Master Planned Communities Revenues and Expenses(\*)

For the six months ended June 30, 2016 and 2015

(In thousands, except %)

| (In thousands)                            | Bridgeland |          | Maryland Communities |       | Summerlin |           | The Woodlands |           | The Wood Hills |
|---|------------|----------|----------------------|-------|-----------|-----------|---------------|-----------|----------------|
|   | 2016       | 2015     | 2016                 | 2015  | 2016      | 2015      | 2016          | 2015      | 2016           |
| Land sales (e)                            | \$ 8,782   | \$ 6,073 | \$ —                 | \$ —  | \$ 80,004 | \$ 71,120 | \$ 14,254     | \$ 16,321 | \$ —           |
| Builder price participation               | 435        | 522      | —                    | —     | 9,314     | 10,542    | 1,399         | 2,542     | —              |
| Minimum rents                             | —          | —        | —                    | —     | 282       | 429       | —             | —         | —              |
| Other land sale revenues                  | 109        | 201      | 3                    | 53    | 5,421     | 3,455     | 234           | 2,717     | 5              |
| Other rental and property revenues        | —          | —        | —                    | —     | 16        | 7         | —             | —         | 4              |
| Total revenues                            | 9,326      | 6,796    | 3                    | 53    | 95,037    | 85,553    | 15,887        | 21,580    | 9              |
| Cost of sales - land                      | 2,979      | 2,203    | —                    | —     | 36,045    | 40,387    | 5,672         | 5,542     | —              |
| Land sales operations                     | 2,262      | 1,930    | 120                  | 202   | 4,317     | 6,363     | 6,008         | 8,802     | 99             |
| Land sales real estate and business taxes | 487        | 147      | 323                  | 328   | 1,155     | 1,855     | 2,583         | 2,288     | 46             |
| Depreciation and amortization             | 47         | 59       | 10                   | 10    | 47        | 61        | 60            | 60        | —              |
| Total expenses                            | 5,775      | 4,339    | 453                  | 540   | 41,564    | 48,666    | 14,323        | 16,692    | 145            |
| Operating income                          | 3,551      | 2,457    | (450)                | (487) | 53,473    | 36,887    | 1,564         | 4,888     | (136)          |
| Interest expense, net (a)                 | (4,686)    | (4,597)  | (7)                  | (17)  | (8,456)   | (7,056)   | 3,066         | 2,517     | (281)          |
| Equity in earnings in Real Estate         | —          | —        | —                    | —     | (8,874)   | —         | —             | —         | —              |

|                                    |          |          |             |             |           |           |               |          |        |  |  |  |  |  |  |
|------------------------------------|----------|----------|-------------|-------------|-----------|-----------|---------------|----------|--------|--|--|--|--|--|--|
| and Other<br>Affiliates<br>MPC REP |          |          |             |             |           |           |               |          |        |  |  |  |  |  |  |
| EBT                                | \$ 8,237 | \$ 7,054 | \$ (443)(c) | \$ (470)(c) | \$ 70,803 | \$ 43,943 | \$ (1,502)(d) | \$ 2,371 | \$ 145 |  |  |  |  |  |  |
| Gross<br>Margin %                  |          |          |             |             |           |           |               |          |        |  |  |  |  |  |  |
| (b)                                | 66.1 %   | 63.7 %   | NM          | NM          | 54.9 %    | 43.2 %    | 60.2 %        | 66.0 %   | NM     |  |  |  |  |  |  |

(\*) For a reconciliation of MPC REP EBT to consolidated income (loss) before taxes, refer to Note 16 – Segments.

- (a) Negative interest expense amounts relate to interest capitalized on debt assigned to our Operating Assets segment and corporate debt.
- (b) Gross margin % is the ratio of Land sales less Cost of sales-land, divided by Land sales.
- (c) The negative MPC REP EBT in Maryland is due to no land sales in 2016 or 2015; however, certain costs such as real estate taxes and administrative expenses continue to be incurred.
- (d) The number of residential lots sold decreased from 89 to 26 for the six months ended June 30, 2016 compared to the same period in 2015, resulting in negative MPC REP EBT at The Woodlands.
- (e) Land sales includes deferred revenue from land sales closed in a previous period which met criteria for recognition in the current period.

NM – Not meaningful

MPC revenues vary between periods based on economic conditions and several factors such as, but not limited to, location, availability of land for sale, development density and residential or commercial use. Gross margin for each MPC may vary from period to period based on the locations of the land sold and the related costs associated with developing the land sold. Reported results may differ significantly from actual cash flows generated principally because cost of sales for GAAP purposes is derived from margins calculated using carrying values, projected future improvements and other capitalized project costs in relation to projected future land sale revenues. Carrying values, generally, represent acquisition and development costs reduced by any previous impairment charges. Development expenditures are capitalized and generally not reflected in the condensed consolidated statements of operations in the current period.

Builder price participation revenue is based on an agreed-upon percentage of the estimated sales price of the home relative to the base lot price.

Cost of sales – land includes both actual and estimated future costs allocated based upon relative sales value to the lots or land parcels in each of the villages and neighborhoods in our MPCs.

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## Summary of MPC Land Sales Closed in the Three Months Ended June 30,

| (\$ In thousands)                    | Land Sales |           | Acres Sold |      | Number of Lots/Units |      | Price per acre |        | Price per lot |       |
|--------------------------------------|------------|-----------|------------|------|----------------------|------|----------------|--------|---------------|-------|
|                                      | 2016       | 2015      | 2016       | 2015 | 2016                 | 2015 | 2016           | 2015   | 2016          | 2015  |
| Bridgeland Residential               |            |           |            |      |                      |      |                |        |               |       |
| Single family - detached             | \$ 4,656   | \$ 1,495  | 12.9       | 3.7  | 68                   | 19   | \$ 361         | \$ 404 | \$ 68         | \$ 79 |
| Total                                | 4,656      | 1,495     | 12.9       | 3.7  | 68                   | 19   | 361            | 404    | 68            | 79    |
| \$ Change                            | 3,161      |           | 9.2        |      | 49                   |      | (43)           |        | (11)          |       |
| % Change                             | 211.4%     |           | 248.6%     |      | 257.9%               |      | (10.6%)        |        | (13.9%)       |       |
| Maryland Communities                 |            |           |            |      |                      |      |                |        |               |       |
| No land sales                        |            |           |            |      |                      |      |                |        |               |       |
| Summerlin Residential                |            |           |            |      |                      |      |                |        |               |       |
| Superpad sites                       | 26,987     | 29,256    | 53.4       | 52.0 | 316                  | 155  | 505            | 563    | 85            | 189   |
| Custom lots                          | 505        | 3,775     | 0.3        | 2.5  | 1                    | 6    | 1,683          | 1,510  | 505           | 629   |
| Commercial                           |            |           |            |      |                      |      |                |        |               |       |
| Not-for-profit                       | 348        | —         | 10.0       | —    | —                    | —    | 35             | —      | —             | —     |
| Other                                | —          | 3,136     | —          | 3.6  | —                    | —    | —              | 871    | —             | —     |
| Total                                | 27,840     | 36,167    | 63.7       | 58.1 | 317                  | 161  | 437            | 622    | 87            | 205   |
| \$ Change                            | (8,327)    |           | 5.6        |      | 156                  |      | (185)          |        | (118)         |       |
| % Change                             | (23.0%)    |           | 9.6%       |      | 96.9%                |      | (29.7%)        |        | (57.6%)       |       |
| The Woodlands Residential            |            |           |            |      |                      |      |                |        |               |       |
| Single family - detached             | 1,386      | 7,052     | 2.3        | 12.2 | 9                    | 43   | 603            | 578    | 154           | 164   |
| Commercial                           |            |           |            |      |                      |      |                |        |               |       |
| Not-for-profit                       | —          | 733       | —          | 5.0  | —                    | —    | —              | 147    | —             | —     |
| Other                                | —          | 1,321     | —          | 0.9  | —                    | —    | —              | 1,468  | —             | —     |
| Total                                | 1,386      | 9,106     | 2.3        | 18.1 | 9                    | 43   | 603            | 503    | 154           | 164   |
| \$ Change                            | (7,720)    |           | (15.8)     |      | (34)                 |      | 100            |        | (10)          |       |
| % Change                             | (84.8%)    |           | (87.3%)    |      | (79.1%)              |      | 19.9%          |        | (6.1%)        |       |
| Total acreage sales closed in period |            |           |            |      |                      |      |                |        |               |       |
|                                      | \$ 33,882  | \$ 46,768 | 78.9       | 79.9 | 394                  | 223  |                |        |               |       |
| Net recognized (deferred) revenue    |            |           |            |      |                      |      |                |        |               |       |
| Bridgeland                           | \$ (156)   | \$ —      |            |      |                      |      |                |        |               |       |
| Summerlin                            | 23,671     | (2,500)   |            |      |                      |      |                |        |               |       |
|                                      | 23,515     | (2,500)   |            |      |                      |      |                |        |               |       |

|  |           |           |
|--|-----------|-----------|
| Total net<br>recognized<br>(deferred)<br>revenue (a)   |           |           |
| Special  | 3,701     | 1,165     |
| Improvement<br>District revenue                        |           |           |
| Total segment<br>land sales<br>revenue - GAAP<br>basis | \$ 61,098 | \$ 45,433 |

(a) Represents additional revenues recognized currently on sales closed in prior periods where revenue was deferred, net of amounts deferred on sales closed in the current period.

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## Summary of MPC Land Sales Closed in the Six Months Ended June 30,

| (\$ In thousands)                    | Land Sales |           | Acres Sold |       | Number of Lots/Units |      | Price per acre |        | Price per lot |        |
|--------------------------------------|------------|-----------|------------|-------|----------------------|------|----------------|--------|---------------|--------|
|                                      | 2016       | 2015      | 2016       | 2015  | 2016                 | 2015 | 2016           | 2015   | 2016          | 2015   |
| Bridgeland Residential               |            |           |            |       |                      |      |                |        |               |        |
| Single family - detached             | \$ 8,870   | \$ 6,073  | 24.0       | 15.5  | 132                  | 60   | \$ 370         | \$ 392 | \$ 67         | \$ 101 |
| Total                                | 8,870      | 6,073     | 24.0       | 15.5  | 132                  | 60   | 370            | 392    | 67            | 101    |
| \$ Change                            | 2,797      |           | 8.5        |       | 72                   |      | (22)           |        | (34)          |        |
| % Change                             | 46.1%      |           | 54.8%      |       | 120.0%               |      | (5.6%)         |        | (33.7%)       |        |
| Maryland Communities                 |            |           |            |       |                      |      |                |        |               |        |
| No land sales                        |            |           |            |       |                      |      |                |        |               |        |
| Summerlin Residential                |            |           |            |       |                      |      |                |        |               |        |
| Superpad sites                       | 66,987     | 46,030    | 170.2      | 81.2  | 868                  | 233  | 394 (a)        | 567    | 77            | 198    |
| Single family - detached             | —          | 13,650    | —          | 14.9  | —                    | 75   | —              | 916    | —             | 182    |
| Custom lots                          | 2,645      | 6,320     | 1.6        | 4.5   | 5                    | 11   | 1,653          | 1,404  | 529           | 575    |
| Commercial                           |            |           |            |       |                      |      |                |        |               |        |
| Not-for-profit                       | 348        | —         | 10.0       | —     | —                    | —    | 35             | —      | —             | —      |
| Other                                | —          | 3,136     | —          | 3.6   | —                    | —    | —              | 871    | —             | —      |
| Total                                | 69,980     | 69,136    | 181.8      | 104.2 | 873                  | 319  | 385            | 663    | 80            | 207    |
| \$ Change                            | 844        |           | 77.6       |       | 554                  |      | (278)          |        | (127)         |        |
| % Change                             | 1.2%       |           | 74.5%      |       | 173.7%               |      | (41.9%)        |        | (61.4%)       |        |
| The Woodlands Residential            |            |           |            |       |                      |      |                |        |               |        |
| Single family - detached             | 3,850      | 13,859    | 6.4        | 22.0  | 26                   | 80   | 602            | 630    | 148           | 173    |
| Single family - attached             | —          | 408       | —          | 0.8   | —                    | 9    | —              | 510    | —             | 45     |
| Commercial                           |            |           |            |       |                      |      |                |        |               |        |
| Not-for-profit                       | —          | 733       | —          | 5.0   | —                    | —    | —              | 147    | —             | —      |
| Medical                              | 10,405     | —         | 4.3        | —     | —                    | —    | 2,420          | —      | —             | —      |
| Other                                | —          | 1,321     | —          | 0.9   | —                    | —    | —              | 1,468  | —             | —      |
| Total                                | 14,255     | 16,321    | 10.7       | 28.7  | 26                   | 89   | 1,332          | 569    | 148           | 160    |
| \$ Change                            | (2,066)    |           | (18.0)     |       | (63)                 |      | 763            |        | (12)          |        |
| % Change                             | (12.7%)    |           | (62.7%)    |       | (70.8%)              |      | 134.1%         |        | (7.5%)        |        |
| Total acreage sales closed in period |            |           |            |       |                      |      |                |        |               |        |
|                                      | \$ 93,105  | \$ 91,530 | 216.5      | 148.4 | 1,031                | 468  |                |        |               |        |

|  |            |           |
|--|------------|-----------|
| Net recognized<br>(deferred)<br>revenue                |            |           |
| Bridgeland   | \$ (88)    | \$ —      |
| Summerlin  | 6,291      | (2,107)   |
| Total net<br>recognized<br>(deferred)<br>revenue (b)   | 6,203      | (2,107)   |
| Special<br>Improvement<br>District revenue             | 3,732      | 4,091     |
| Total segment<br>land sales<br>revenue - GAAP<br>basis | \$ 103,040 | \$ 93,514 |

(a) Please see discussion below.

(b) Represents additional revenues recognized currently on sales closed in prior periods where revenue was deferred, net of amounts deferred on sales closed in the current period.

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Houston MPCs

Bridgeland

Bridgeland's land sales for the three and six months ended June 30, 2016 were substantially higher compared to the same periods in 2015 due to increased demand from homebuilders. While the greater Houston market remains impacted by the ongoing economic stagnancy caused by low oil prices, the Bridgeland submarket has shown improvement in the mid-range of the residential market. For the three and six months ended June 30, 2016, Bridgeland sold 12.9 and 24.0 residential acres, respectively, compared to 3.7 and 15.5 acres for the same periods in 2015. The average price per residential acre for single-family – detached product decreased for the three and six months ended June 30, 2016 compared to 2015, by 10.6% and 5.6%, respectively. The decrease is attributable to a slight reduction in our lot pricing to respond to the Bridgeland submarket demand for more moderately priced lots and to the mix of lot sizes that were sold in the respective periods. For the three and six months ended June 30, 2016, there were a larger percentage of smaller, lower priced lots sold than in the same periods in 2015. Additionally, we experienced a slight increase to gross margins for the three and six months ended June 30, 2016, resulting primarily from lower cost estimates for lots sold during the period.

There were 100 and 170 new home sales at Bridgeland for the three and six months ended June 30, 2016, representing an increase of 63.9% and 57.4%, respectively, compared to the same periods in 2015. For the three months ended June 30, 2016, the median price of new homes sold in Bridgeland was \$316,000, a 23.9% decrease compared to \$415,000 for the same period in 2015. The median price of new homes sold in the six months ended June 30, 2016 decreased 20.3% to \$329,000 compared to \$413,000 for the same period in 2015. These decreases in median home pricing are due to the mix of homes sold and reflect increased sales of more affordable homes. Land and home absorption rates at Bridgeland in 2016 have benefited from the wide variety of products being offered at highly competitive prices. In addition, the Grand Parkway toll road, which opened in February 2016, provides greater connectivity between Bridgeland and major employment centers in Houston.

The Woodlands

The Woodlands total residential land sales for the three and six months ended June 30, 2016 decreased to 2.3 and 6.4 acres, respectively, compared to 12.2 and 22.8 acres for the same periods in 2015. The decrease in acreage sold for the three and six months ended June 30, 2016 compared to the same periods in 2015 is attributable to homebuilder caution on expanding their land inventory given the continued slow absorption of higher priced lots and homes, reduced demand for new homes and increased builder lot inventory. The economic uncertainty in The Woodlands submarket is driven by continued low oil prices and declining job growth. As of June 30, 2016, homebuilders had 491 lots in inventory, which is approximately two years of supply based on current home sales pace. The average price per residential acre for single-family – detached product increased 4.3% for the three months ended June 30, 2016 and decreased 4.4% for the six months ended June 30, 2016 compared to the same periods in 2015, respectively, primarily due to the mix of lots sold.

There were 61 and 117 new home sales in The Woodlands for the three and six months ended June 30, 2016, respectively, representing a 26.5% and 29.9% decrease compared to the 83 and 167 new home sales for the same periods in 2015. For the three months ended June 30, 2016, the median price of new homes sold in The Woodlands



decreased 4.1% to \$559,000 compared to \$583,000 for the same period in 2015. The median price of new homes sold in the six months ended June 30, 2016 increased 0.5% to \$553,000 compared to \$550,000 for the same period in 2015.

#### The Woodlands Hills

On June 30, 2016, we received approval of our development plan for The Woodlands Hills from the City of Conroe. As a result of this approval, we can now begin submitting plats to the City of Conroe for their review and approval of the first sections scheduled for development. We currently expect to start water, sewer and drainage construction in the fourth quarter 2016 and sales to begin in the fourth quarter 2017. We believe that The Woodlands Hills is well-positioned to generate demand. It has a projected lower price point for all product types compared to The Woodlands, with more moderate pricing such as that at Bridgeland. Furthermore, it benefits from The Woodlands' brand reputation and has a favorable location to major employment centers, such as the medical and office centers at The Woodlands and the ExxonMobil campus located just south of The Woodlands.

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Maryland

Our Columbia, Gateway, Emerson and Fairwood communities contain approximately 108 commercial acres remaining to be sold, but there were no commercial land sales for the three or six month periods ended June 30, 2016 or 2015. All of the residential inventory was sold out in prior years.

In December 2015, approximately 35 acres of the Columbia commercial acreage was transferred to our Strategic Developments segment as we began development of office space in the Downtown Columbia Town Center Redevelopment District (“DCRD”). The entitlements, which do not expire under Maryland law, are enabling us to redevelop Downtown Columbia, a portion of DCRD and further support the approximate 112,000 residents.

Summerlin

Land sales revenue of \$61.1 million and \$103.0 million recognized for the three and six months ended June 30, 2016, includes \$23.7 million and \$6.3 million, respectively, in revenue from land sales closed in prior periods which were previously deferred and met criteria for recognition in the current periods.

Summerlin’s land sales for the three months ended June 30, 2016 were lower compared to the same period in 2015 because second quarter 2015 included the sale of a high-end superpad in The Ridges, Summerlin’s exclusive gated community. The average price per superpad acre sold for the three months ended June 30, 2016 was \$505,000 compared to \$563,000 for the same period in 2015, a reduction of 10.3% primarily due to this superpad sale. Summerlin’s land sales for the six months ended June 30, 2016 were higher compared to the same period in 2015 primarily due to a \$40 million bulk sale to a homebuilder for a large parcel in the first quarter 2016. This sale was unique as the homebuilder will be responsible for installing roads, utilities and drainage facilities to the village, and Summerlin is not obligated to incur any development costs within the boundaries of the parcel. Accordingly, the average price per superpad acre for the six months ended June 30, 2016 of \$394,000 is not comparable to the average price per acre of \$567,000 for the same period in 2015, given the nature of this bulk sale transaction. If the price was adjusted to include the development costs that would typically be incurred by us and paid for through an increased sales price, we estimate that the price per superpad acre for the six months ended June 30, 2016 would have been approximately \$563,000. Gross margin increased for the six months ended June 30, 2016 compared to 2015 due to this sale of undeveloped land for which we incurred much lower development costs. In addition, as part of the transaction we negotiated a favorable adjustment to the builder price participation on the land we sold to the same homebuilder in 2006.

The Summerlin market remains strong. Summerlin had 201 and 350 new home sales for the three and six months ended June 30, 2016, respectively, representing a 9.8% and 7.0% increase compared to 183 and 327 new home sales for the three and six months ended June 30, 2015, respectively. For the three months ended June 30, 2016, the median price of new homes sold in Summerlin increased 0.2% to \$538,000 compared to \$537,000 for the same period in 2015. The median price of new homes sold in Summerlin increased 1.7% to \$544,000 for the six months ended June

30, 2016 compared to \$535,000 for the same period in 2015.

Land development began at The Summit, our joint venture with Discovery Land, in the second quarter 2015 and continues to progress on schedule based upon the initial plan. For the six months ended June 30, 2016, 17 custom residential lots were sold resulting in the recognition of \$8.9 million Equity in earnings in Real Estate and Other Affiliates. Discovery is the manager of the project, and development began in the second quarter 2015. As of July 15, 2016, the project has contracted for approximately \$122.3 million in land sales, of which \$48.2 million in lot closings were completed in the second quarter 2016. This revenue is being recognized as the development progresses under the percentage of completion method of accounting. Please refer to Note 8 – Real Estate and Other Affiliates for a description of the joint venture and our share of equity earnings in the period.

#### MPC Net Contribution

In addition to REP EBT for the MPCs, we believe that certain investors measure the value of the assets in this segment based on their contribution to liquidity and capital available for investment. MPC Net Contribution is defined as MPC REP EBT, plus MPC cost of sales, depreciation and amortization, and net collections from Special Improvement District (“SID”) bonds and Municipal Utility District (“MUD”) receivables, reduced by MPC development and land acquisition expenditures. Although MPC Net Contribution can be computed from GAAP elements of income and cash flows, it is not

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a GAAP-based operational metric and should not be used to measure operating performance of the MPC assets as a substitute for GAAP measures of such performance. A reconciliation of REP EBT to consolidated net income (loss) as computed in accordance with GAAP is presented in Note 16 - Segments.

The following table sets forth the MPC Net Contribution for the three and six months ended June 30, 2016 and 2015:

| (in thousands)                            | Three Months Ended<br>June 30, |           |           | Six Months Ended<br>June 30, |           |           |
|---|--------------------------------|-----------|-----------|------------------------------|-----------|-----------|
|   | 2016                           | 2015      | Change    | 2016                         | 2015      | Change    |
| MPC REP EBT (a)                           | \$ 47,495                      | \$ 25,109 | \$ 22,386 | \$ 77,240                    | \$ 53,191 | \$ 24,049 |
| Plus:                                     |                                |           |           |                              |           |           |
| Cost of sales - land                      | 29,008                         | 24,236    | 4,772     | 44,696                       | 48,132    | (3,436)   |
| Depreciation and amortization             | 81                             | 95        | (14)      | 164                          | 190       | (26)      |
| MUD and SID bonds collections, net<br>(b) | (3,040)                        | 834       | (3,874)   | (3,071)                      | (2,512)   | (559)     |
| Less:                                     |                                |           |           |                              |           |           |
| MPC development expenditures              | (36,210)                       | (46,525)  | 10,315    | (70,678)                     | (83,868)  | 13,190    |
| MPC land acquisitions                     | -                              | (827)     | 827       | (69)                         | (1,928)   | 1,859     |
| MPC Net Contribution                      | \$ 37,334                      | \$ 2,922  | \$ 34,412 | \$ 48,282                    | \$ 13,205 | \$ 35,077 |

(a) For a detailed breakdown of our Master Planned Communities segment EBT, refer to Note 16 – Segments.

(b) SID bond collections are shown net of SID bond assumptions by buyers in the respective periods.

While the land sales closed for the three months ended June 30, 2016 decreased as compared to the same period in 2015, \$23.5 million of revenue previously deferred due to future performance obligations met criteria for recognition in the current period. Accordingly, MPC Net Contribution increased for the three and six months ended June 30, 2016 compared to the three and six months ended June 30, 2015, primarily due to an increase in MPC REP EBT at the Bridgeland and Summerlin MPCs and the reduction in MPC development expenditures in 2016.

The following table sets forth MPC land inventory activity for the six months ended June 30, 2016:

| (In thousands)                  | Bridgeland | Maryland  | Summerlin  | The<br>Woodlands | The Woodlands<br>Hills | Total MPC    |
|---------------------------------|------------|-----------|------------|------------------|------------------------|--------------|
| Balance<br>December 31, 2015    | \$ 435,220 | \$ 22,143 | \$ 864,276 | \$ 220,099       | \$ 101,104             | \$ 1,642,842 |
| Acquisitions                    | —          | —         | —          | 69               | —                      | 69           |
| Development<br>expenditures (a) | 20,945     | 158       | 32,294     | 16,429           | 852                    | 70,678       |
| MPC Cost of Sales               | (2,979)    | —         | (36,045)   | (5,672)          | —                      | (44,696)     |
|                                 | (18,953)   | —         | —          | (3,024)          | —                      | (21,977)     |

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MUD reimbursable costs

|                       |            |           |            |            |            |              |
|-----------------------|------------|-----------|------------|------------|------------|--------------|
| (b)                   |            |           |            |            |            |              |
| Other                 | (4,113)    | 10        | 12,726     | (3,501)    | 18         | 5,140        |
| Balance June 30, 2016 | \$ 430,120 | \$ 22,311 | \$ 873,251 | \$ 224,400 | \$ 101,974 | \$ 1,652,056 |

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(a) Development expenditures are inclusive of capitalized interest and property taxes.

(b) MUD reimbursable costs represent land development expenditures transferred to MUD Receivables.

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## Operating Assets

Operating assets typically generate rental revenues sufficient to cover their operating costs except when a substantial portion, or all, of the property is being redeveloped, vacated for development or in its initial lease-up phase. Variances between years in NOI typically result from changes in rental rates, occupancy, tenant mix and operating expenses. We view NOI as an important measure of the operating performance of our Operating Assets segment.

Total revenues and expenses for the Operating Assets segment are summarized as follows:

| (In thousands)   | Three Months Ended |            |           | Six Months Ended |            |           |
|--|--------------------|------------|-----------|------------------|------------|-----------|
|  | June 30,<br>2016   | 2015       | Change    | June 30,<br>2016 | 2015       | Change    |
| Minimum rents  | \$ 41,811          | \$ 36,697  | \$ 5,114  | \$ 82,929        | \$ 71,009  | \$ 11,920 |
| Tenant recoveries  | 10,914             | 10,693     | 221       | 21,437           | 20,266     | 1,171     |
| Hospitality revenues                                     | 19,129             | 11,481     | 7,648     | 32,038           | 23,484     | 8,554     |
| Other rental and property revenues                       | 4,416              | 6,971      | (2,555)   | 7,499            | 13,245     | (5,746)   |
| Total revenues   | 76,270             | 65,842     | 10,428    | 143,903          | 128,004    | 15,899    |
| Other property operating costs                           | 13,830             | 18,350     | (4,520)   | 27,948           | 35,836     | (7,888)   |
| Rental property real estate taxes                        | 6,709              | 5,990      | 719       | 12,851           | 11,510     | 1,341     |
| Rental property maintenance costs                        | 2,645              | 2,785      | (140)     | 5,646            | 5,412      | 234       |
| Hospitality costs  | 14,242             | 8,893      | 5,349     | 24,717           | 17,971     | 6,746     |
| Provision for doubtful accounts                          | (353)              | 1,266      | (1,619)   | 2,626            | 2,075      | 551       |
| Other income, net  | (2,750)            | —          | (2,750)   | (3,113)          | —          | (3,113)   |
| Depreciation and amortization                            | 22,613             | 22,887     | (274)     | 43,814           | 41,649     | 2,165     |
| Interest income  | (8)                | (9)        | 1         | (16)             | (19)       | 3         |
| Interest expense   | 10,116             | 7,629      | 2,487     | 19,269           | 14,123     | 5,146     |
| Equity in earnings from Real Estate and Other Affiliates | (899)              | (160)      | (739)     | (2,826)          | (1,044)    | (1,782)   |
| Total operating expenses                                 | 66,145             | 67,631     | (1,486)   | 130,916          | 127,513    | 3,403     |
| Income before development expenses                       | 10,125             | (1,789)    | 11,914    | 12,987           | 491        | 12,496    |
| Demolition costs   | 6                  | 1,496      | (1,490)   | 478              | 1,613      | (1,135)   |
| Development-related marketing costs                      | 1,988              | 2,748      | (760)     | 3,088            | 5,014      | (1,926)   |
| Total development expenses                               | 1,994              | 4,244      | (2,250)   | 3,566            | 6,627      | (3,061)   |
| Operating Assets REP EBT                                 | \$ 8,131           | \$ (6,033) | \$ 14,164 | \$ 9,421         | \$ (6,136) | \$ 15,557 |

(\*)For a reconciliation of Operating Assets REP EBT to consolidated income (loss) before taxes, refer to Note 16 - Segments.

Minimum rents and tenant recoveries for the three and six months ended June 30, 2016 compared to the three and six months ended June 30, 2015 increased primarily due to increases of \$1.1 million and \$3.9 million, respectively, for our retail properties, \$2.9 million and \$6.3 million, respectively, for our office properties, and \$1.1 million and \$2.5 million, respectively, for our multi-family properties. The increase for our retail properties was primarily due to the 2015 opening of Hughes Landing Retail and increased leasing and the elimination of co-tenancy allowances for current tenants at Downtown Summerlin. The increase in our office properties was primarily due to the openings of 1725-1735 Hughes Landing Boulevard and ONE Summerlin in 2015 (“2015 Office Openings”), and increased leasing at Two Hughes Landing. The increase in our multi-family properties was primarily due to the opening of One Lakes Edge in 2015.

Hospitality revenues increased for the three and six months ended June 30, 2016 due to the opening of the Embassy Suites at Hughes Landing in December 2015 and The Westin at The Woodlands in 2016, partially offset by a decrease at The Woodlands Resort and Conference Center due to a decline in revenues from group business.

Other rental and property revenue for the three and six months ended June 30, 2016 decreased primarily due to the sale of the Club at Carlton Woods in September 2015.

Other property operating costs and rental property maintenance costs for the three and six months ended June 30, 2016 compared to the same period 2015, respectively decreased due to the sale of the Club at Carlton Woods partially offset by an increase of \$1.1 million for our office properties for the six months ended June 30, 2016, primarily due to the opening of 1725-1735 Hughes Landing Boulevard.

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Rental property real estate taxes for the three months ended June 30, 2016 compared to the same period 2015 increased \$1.3 million primarily due to the opening of Hughes Landing Retail, 2015 Office Openings and the opening of One Lakes Edge, apartments offset by the sale of Carlton Woods.

Hospitality costs increased for the three and six months ended June 30, 2016 due to the opening of the Embassy Suites at Hughes Landing in late 2015 and The Westin at The Woodlands in early 2016 offset by a decrease in hospitality costs at the Woodlands Resort and Conference Center due to a decline in occupancy and conference center services.

Provision for doubtful accounts increased for the six months ended June 30, 2016 compared to the same period 2015 due primarily to the March 2016 bankruptcy filing of a tenant at Ward Village, resulting in the reserve of all rent and a tenant improvement reimbursement receivable. Provision for doubtful accounts decreased for the three months ended June 30, 2016 compared to the same period in 2015 due to a partial recovery of the provision for the same tenant at Ward Village as a result of an agreement reached in the second quarter to assume the bankrupt tenant's lease. Recoveries of the pre-petition receivables are recognized in accordance with the agreement.

Depreciation and amortization for the three and six months ended June 30, 2016 compared to the same period in 2015 increased \$2.4 million and \$3.6 million, respectively, for our office properties, decreased \$3.8 million and \$3.7 million, respectively, for our retail properties, increased \$1.1 million and \$1.7 million, respectively for our hospitality properties, and increased \$0.1 million and \$0.6 million, respectively, for our multi-family properties. The decrease for retail properties is due to the assets which have been fully depreciated in anticipation of redevelopment. The increase for office properties is primarily due to 2015 Office Openings. The increase for hospitality is due to the 2015 and 2016 openings of our two new hotels in The Woodlands. The increase for multi-family is due to the opening of One Lakes Edge in The Woodlands.

When a development property is placed into service, depreciation is calculated for the property ratably over the estimated useful lives of each of its components; however, most of our recently developed properties do not reach stabilization for 12 to 36 months after being placed into service due to the timing of tenants taking occupancy and subsequent leasing of remaining unoccupied space during that period. As a result, operating income, earnings before taxes (EBT) and net income will not reflect the ongoing earnings potential of newly-placed in service operating assets during this transition period to stabilization. Accordingly, we calculate Adjusted Operating Assets REP EBT, which excludes depreciation and amortization and development-related demolition and marketing costs, as they do not represent recurring costs for stabilized real estate properties. Adjusted Operating Assets REP EBT increased 55.2% and 34.8% for the three and six months ended June 30, 2016, respectively, as compared to the three and six months ended June 30, 2015, respectively, due to the 2015 Office Openings and the opening of Hughes Landing Retail.

The following table reconciles Adjusted Operating Assets REP EBT to Operating Assets REP EBT:

| Reconciliation of Adjusted Operating Assets REP EBT to Operating Assets REP EBT (in thousands) | Three Months Ended June 30 |            | Six Months Ended June 30, |            |
|--|----------------------------|------------|---------------------------|------------|
|  | 2016                       | 2015       | 2016                      | 2015       |
| Adjusted Operating Assets REP EBT  | \$ 32,738                  | \$ 21,098  | \$ 56,801                 | \$ 42,140  |
| Depreciation and amortization  | (22,613)                   | (22,887)   | (43,814)                  | (41,649)   |
| Demolition costs   | (6)                        | (1,496)    | (478)                     | (1,613)    |
| Development-related marketing costs  | (1,988)                    | (2,748)    | (3,088)                   | (5,014)    |
| Operating Assets REP EBT   | \$ 8,131                   | \$ (6,033) | \$ 9,421                  | \$ (6,136) |

Interest expense increased primarily due to higher loan balances on properties acquired or placed into service. The increase for retail is primarily due to Downtown Summerlin and Hughes Landing Retail. The increase for office was



due primarily to 10-60 Columbia Corporate Center, Two Hughes Landing, and 1725-1735 Hughes Landing. Multifamily interest expense increased due to placing One Lakes Edge in service in 2015.

Equity in earnings from Real Estate and Other Affiliates increased for the three and six months ended June 30, 2016 compared to the same period for 2015 due primarily to a \$2.6 million distribution from our Summerlin Hospital investment as compared to \$1.7 million in 2015.

Demolition costs decreased for the three and six months ended June 30, 2016 compared to the same periods in 2015 due primarily to the completion of the interior demolition work for the Fulton Market Building at South Street Seaport.

Development-related marketing costs decreased for the three and six months ended June 30, 2016 compared to the same periods in 2015. The costs in both periods relate to special events at the Seaport District. We incurred higher costs in 2015 due to the opening and operations of our studio store for pre-leasing activities. The costs in 2016 relate to ongoing marketing initiatives as we continue leasing efforts in advance of the completion of our Pier 17 renovation project.

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## Operating Assets NOI and REP EBT

| (In thousands)                     | Three Months<br>Ended June 30, |        |        | Six Months<br>Ended June 30, |        |        |
|------------------------------------|--------------------------------|--------|--------|------------------------------|--------|--------|
|                                    | 2016                           | 2015   | Change | 2016                         | 2015   | Change |
| Retail                             |                                |        |        |                              |        |        |
| Columbia Regional                  | \$ 297                         | \$ 204 | \$ 93  | \$ 601                       | \$ 465 | \$ 136 |
| Cottonwood Square                  | 183                            | 146    | 37     | 360                          | 305    | 55     |
| Creekside Village Green (a)        | 425                            | 186    | 239    | 789                          | 225    | 564    |
| Downtown Summerlin (a)             | 4,028                          | 2,450  | 1,578  | 8,241                        | 4,194  | 4,047  |
| Hughes Landing Retail (a)          | 864                            | 328    | 536    | 1,523                        | 387    | 1,136  |
| 1701 Lake Robbins                  | 95                             | 15     | 80     | 183                          | 184    | (1)    |
| Landmark Mall (b)                  | (173)                          | (109)  | (64)   | (324)                        | (186)  | (138)  |
| Outlet Collection at Riverwalk (c) | 1,120                          | 1,966  | (846)  | 2,232                        | 3,119  | (887)  |
| Park West (d)                      | 437                            | 535    | (98)   | 936                          | 1,175  | (239)  |
| Ward Village (e)                   | 7,296                          | 6,700  | 596    | 11,891                       |        |        |