M I HOMES INC
Form 10-Q
April 30, 2013

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

FORM 10-Q

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

For the Quarterly Period Ended March 31, 2013

o	TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (D) OF THE SECURITIES ACT OF 1934

Commission File Number 1-12434

M/I HOMES, INC.
(Exact name of registrant as specified in it charter)

Ohio	31-1210837
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

3 Easton Oval, Suite 500, Columbus, Ohio 43219
(Address of principal executive offices) (Zip Code)
(614) 418-8000
(Registrant's telephone number, including area code)

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

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

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

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.
Common shares, par value $.01 per share: 24,173,111 shares outstanding as of April 26, 2013.

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M/I HOMES, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except par values)	March 31, 2013	December 31, 2012
ASSETS:		
Cash and cash equivalents	$263,057	$145,498
Restricted cash	9,494	8,680
Mortgage loans held for sale	57,721	71,121
Inventory	577,640	556,817
Property and equipment - net	9,994	10,439
Investment in Unconsolidated LLCs	22,275	11,732
Other assets	28,471	27,013
TOTAL ASSETS	$968,652	$831,300
LIABILITIES AND SHAREHOLDERS' EQUITY		
LIABILITIES:		
Accounts payable	$57,071	$47,690
Customer deposits	12,246	10,239
Other liabilities	47,760	49,972
Preferred shares subject to redemption	50,352	—
Community development district ("CDD") obligations	4,266	4,634
Obligation for consolidated inventory not owned	16,994	19,105
Notes payable bank - financial services operations	53,126	67,957
Notes payable - other	10,316	11,105
Convertible senior subordinated notes due 2017	57,500	57,500
Convertible senior subordinated notes due 2018	86,250	—
Senior notes	227,770	227,670
TOTAL LIABILITIES	623,651	495,872
Commitments and contingencies	—	—
SHAREHOLDERS' EQUITY:		
Preferred shares - $.01 par value; authorized 2,000,000 shares; 4,000 shares issued at March 31, 2013 and December 31, 2012; 2,000 and 4,000 shares outstanding as of March 31, 2013 and December 31, 2012, respectively	48,163	96,325
Common shares - $.01 par value; authorized 38,000,000 shares; issued 27,092,723 and 24,631,723 shares at March 31, 2013 and December 31, 2012, respectively	271	246
Additional paid-in capital	235,109	180,289
Retained earnings	119,445	117,048
Treasury shares - at cost - 2,919,612 and 2,944,470 shares at March 31, 2013 and December 31, 2012, respectively	(57,987)	(58,480)
TOTAL SHAREHOLDERS' EQUITY	345,001	335,428
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$968,652	$831,300

See Notes to Unaudited Condensed Consolidated Financial Statements.

M/I HOMES, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended March 31,	
(In thousands, except per share amounts)	2013	2012
Revenue	$190,727	$131,125
Costs and expenses:		
Land and housing	151,513	107,330
Impairment of inventory and investment in Unconsolidated LLCs	900	95
General and administrative	15,979	12,457
Selling	13,109	11,011
Interest	4,340	4,606
Total costs and expenses	185,841	135,499
Income (loss) before income taxes	4,886	(4,374)
Provision (benefit) for income taxes	299	(1,188)
Net income (loss)	$4,587	$(3,186)
Excess of fair value over book value of preferred shares subject to redemption	2,190	—
Net income (loss) to common shareholders	$2,397	$(3,186)
Earnings (loss) per common share:		
Basic	$0.11	$(0.17)
Diluted	$0.11	$(0.17)
Weighted average shares outstanding:		
Basic	22,273	18,772
Diluted	22,688	18,772

See Notes to Unaudited Condensed Consolidated Financial Statements.

M/I HOMES, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

	Three Months Ended March 31, 2013							
	Preferred Shares		Common Shares					
(Dollars in thousands)	Shares Outstanding	Amount	Shares Outstanding	Amount	Additional Paid-in Capital	Retained Earnings	Treasury Shares	Total Shareholders' Equity
Balance at December 31, 2012	4,000	$96,325	21,687,253	$ 246	$ 180,289	$ 117,048	$ (58,480)	$ 335,428
Net income	—	—	—	—	—	4,587	—	4,587
Fair value over carrying value of preferred shares subject to redemption	—	2,190	—	—	—	(2,190)	—	—
Common share issuance	—	—	2,461,000	25	54,592	—	—	54,617
Reclassification of preferred shares subject to redemption	(2,000)	(50,352)	—	—		—	—	(50,352)
Stock-based compensation expense	—	—	—	—	519	—	—	519
Deferral of executive and director compensation	—	—	—	—	202	—	—	202
Executive and director deferred compensation distributions	—	—	24,858	—	(493)	—	493	—
Balance at March 31, 2013	2,000	$48,163	24,173,111	$ 271	$ 235,109	$ 119,445	$ (57,987)	$ 345,001

See Notes to Unaudited Condensed Consolidated Financial Statements.

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M/I HOMES, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three Months Ended March 31,	
(Dollars in thousands)	2013	2012
OPERATING ACTIVITIES:		
Net income (loss)	$4,587	$(3,186)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Inventory valuation adjustments and abandoned land transaction write-offs	900	126
Mortgage loan originations	(121,244)	(97,255)
Proceeds from the sale of mortgage loans	135,568	108,587
Fair value adjustment of mortgage loans held for sale	(924)	598
Depreciation	1,317	1,355
Amortization of intangibles, debt discount and debt issue costs	821	587
Stock-based compensation expense	519	434
Deferred income tax expense (benefit)	1,788	(1,140)
Deferred tax asset valuation allowances	(1,788)	1,140
Net loss from property disposals	26	2
Change in assets and liabilities:		
Cash held in escrow	(193)	(139)
Inventory	(23,567)	(24,625)
Other assets	1,371	(1,366)
Accounts payable	9,380	(188)
Customer deposits	2,007	4,153
Accrued compensation	(5,959)	(1,500)
Other liabilities	3,949	4,742
Net cash provided by (used in) operating activities	8,558	(7,675)
INVESTING ACTIVITIES:		
Change in restricted cash	(621)	27,740
Purchase of property and equipment	(229)	(47)
Investment in Unconsolidated LLCs	(11,852)	(361)
Net cash (used in) provided by investing activities	(12,702)	27,332
FINANCING ACTIVITIES:		
Proceeds from issuance of convertible senior subordinated notes	86,250	—
Repayments of bank borrowings - net	(14,831)	(11,026)
(Principal repayments of) proceeds from notes payable-other and CDD bond obligations	(789)	80
Net proceeds from issuance of common shares	54,617	—
Debt issue costs	(3,544)	(1,893)
Proceeds from exercise of stock options	—	367
Net cash provided by (used in) financing activities	121,703	(12,472)
Net increase in cash and cash equivalents	117,559	7,185
Cash and cash equivalents balance at beginning of period	145,498	59,793
Cash and cash equivalents balance at end of period	$263,057	$66,978

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:
Cash paid during the year for:

Interest — net of amount capitalized	$(1,112)	$(981)
Income taxes	$73	$80
NON-CASH TRANSACTIONS DURING THE PERIOD:		
Consolidated inventory not owned	$(2,111)	$(357)
Reclassification of preferred shares subject to redemption	$50,352	$—
Distribution of single-family lots from unconsolidated LLC's	$1,303	$—

See Notes to Unaudited Condensed Consolidated Financial Statements.

M/I HOMES, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. Basis of Presentation

The accompanying Unaudited Condensed Consolidated Financial Statements (the "financial statements") of M/I Homes, Inc. and its subsidiaries (the "Company") and notes thereto have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission (the "SEC") for interim financial information. The financial statements include the accounts of M/I Homes, Inc. and its subsidiaries. All intercompany transactions have been eliminated. Results for the interim period are not necessarily indicative of results for a full year. In the opinion of management, the accompanying financial statements reflect all adjustments (all of which are normal and recurring in nature) necessary for a fair presentation of financial results for the interim periods presented. These financial statements should be read in conjunction with the Consolidated Financial Statements and Notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2012 (the "2012 Form 10-K").

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during that period. Actual results could differ from these estimates and have a significant impact on the financial condition and results of operations and cash flows. With regard to the Company, estimates and assumptions are inherent in calculations relating to valuation of inventory and investment in unconsolidated limited liability companies ("Unconsolidated LLCs"), property and equipment depreciation, valuation of derivative financial instruments, accounts payable on inventory, accruals for costs to complete inventory, accruals for warranty claims, accruals for self-insured general liability claims, litigation, accruals for health care and workers' compensation, accruals for guaranteed or indemnified loans, stock-based compensation expense, income taxes, and contingencies. Items that could have a significant impact on these estimates and assumptions include the risks and uncertainties listed in "Item 1A. Risk Factors" in Part I of our 2012 Form 10-K, as the same may be updated from time to time in our subsequent filings with the SEC.

Impact of New Accounting Standards

In January 2013, the FASB issued ASU No. 2013-01: Balance Sheet (Topic 210) - Disclosures about Offsetting Assets and Liabilities ("ASU 2013-01"). ASU 2013-01 amended ASU 2011-11 and will enhance disclosures required by U.S. GAAP by requiring additional information about financial and derivative instruments that are either (1) offset in accordance with Section 210-20-45 or Section 815-10-45 or (2) subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in accordance with Section 210-20-45 or Section 815-10-45. We are required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and for interim periods within those annual periods. The Company adopted this standard on January 1, 2013 and the adoption did not have a material impact on the Company's Unaudited Condensed Consolidated Financial Statements.

NOTE 2. Fair Value Measurements

There are three measurement input levels for determining fair value: Level 1, Level 2, and Level 3. Fair values determined by Level 1 inputs utilize quoted prices in active markets for identical assets or liabilities that the Company has the ability to access. Fair values determined by Level 2 inputs utilize inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals. Level 3 inputs are unobservable inputs for the asset or liability, and include situations where there is little, if any, market activity for the asset or liability.

Assets Measured on a Recurring Basis

The Company measures both mortgage loans held for sale and interest rate lock commitments ("IRLCs") at fair value. Fair value measurement results in a better presentation of the changes in fair values of the loans and the derivative instruments used to economically hedge them.

In the normal course of business, our financial services segment enters into contractual commitments to extend credit to buyers of single-family homes with fixed expiration dates. The commitments become effective when the borrowers "lock-in" a specified interest rate within established time frames. Market risk arises if interest rates move adversely between the time of the "lock-in" of rates by the borrower and the sale date of the loan to an investor. To mitigate the effect of the interest rate risk inherent in providing rate lock commitments to borrowers, the Company enters into optional or mandatory delivery forward sale contracts to sell whole loans and mortgage-backed securities to broker/dealers. The forward sale contracts lock in an interest rate and price for the sale of loans similar to the specific rate lock commitments. The Company does not engage in speculative or trading derivative activities. Both the rate lock commitments to borrowers and the forward sale contracts to broker/dealers or investors are undesignated derivatives, and accordingly, are marked to fair value through earnings. Changes in fair value measurements are included in earnings in the accompanying statements of operations.

The fair value of mortgage loans held for sale is estimated based primarily on published prices for mortgage-backed securities with similar characteristics. To calculate the effects of interest rate movements, the Company utilizes applicable published mortgage-backed security prices, and multiplies the price movement between the rate lock date and the balance sheet date by the notional loan commitment amount. The Company generally sells loans on a servicing released basis, and receives a servicing release premium upon sale. Thus, the value of the servicing rights included in the fair value measurement is based upon contractual terms with investors and depends on the loan type. The Company applies a fallout rate to IRLCs when measuring the fair value of rate lock commitments. Fallout is defined as locked loan commitments for which the Company does not close a mortgage loan and is based on management's judgment and company experience.

The fair value of the Company's forward sales contracts to broker/dealers solely considers the market price movement of the same type of security between the trade date and the balance sheet date. The market price changes are multiplied by the notional amount of the forward sales contracts to measure the fair value.

Interest Rate Lock Commitments. IRLCs are extended to certain home-buying customers who have applied for a mortgage loan and meet certain defined credit and underwriting criteria. Typically, the IRLCs will have a duration of less than six months; however, in certain markets, the duration could extend to twelve months.

Some IRLCs are committed to a specific third party investor through the use of best-efforts whole loan delivery commitments matching the exact terms of the IRLC loan. Uncommitted IRLCs are considered derivative instruments and are fair value adjusted, with the resulting gain or loss recorded in current earnings.

Forward Sales of Mortgage-Backed Securities. Forward sales of mortgage-backed securities ("FMBSs") are used to protect uncommitted IRLC loans against the risk of changes in interest rates between the lock date and the funding date. FMBSs related to uncommitted IRLCs are classified and accounted for as non-designated derivative instruments and are recorded at fair value, with gains and losses recorded in current earnings.

Mortgage Loans Held for Sale. Mortgage loans held for sale consists primarily of single-family residential loans collateralized by the underlying property. Generally, all of the mortgage loans and related servicing rights are sold to third-party investors shortly after origination. During the intervening period between when a loan is closed and when it is sold to an investor, the interest rate risk is covered through the use of a best-efforts contract or by FMBSs. The FMBSs are classified and accounted for as non-designated derivative instruments, with gains and losses recorded in current earnings.

The table below shows the notional amounts of our financial instruments at March 31, 2013 and December 31, 2012:

Description of financial instrument (in thousands)	March 31, 2013	December 31, 2012
Best efforts contracts and related committed IRLCs	$1,820	$1,184
Uncommitted IRLCs	36,407	25,854
FMBSs related to uncommitted IRLCs	38,000	26,000
Best efforts contracts and related mortgage loans held for sale	3,969	25,441

FMBSs related to mortgage loans held for sale	50,766	44,000
Mortgage loans held for sale covered by FMBSs	50,962	44,524

The table below shows the level and measurement of assets and liabilities measured on a recurring basis at March 31, 2013 and December 31, 2012:

Description of Financial Instrument (in thousands)	Fair Value Measurements March 31, 2013	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Mortgage loans held for sale	$57,721	$—	$57,721	$—
Forward sales of mortgage-backed securities	(77)	—	(77)	—
Interest rate lock commitments	194	—	194	—
Best-efforts contracts	(126)	—	(126)	—
Total	$57,712	$—	$57,712	$—

Description of Financial Instrument (in thousands)	Fair Value Measurements December 31, 2012	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Mortgage loans held for sale	$71,121	$—	$71,121	$—
Forward sales of mortgage-backed securities	253	—	253	—
Interest rate lock commitments	1	—	1	—
Best-efforts contracts	(3)	—	(3)	—
Total	$71,372	$—	$71,372	$—

The following table sets forth the amount of gain (loss) recognized, within our revenue in the Unaudited Condensed Consolidated Statements of Operations, on assets and liabilities measured on a recurring basis for the three months ended March 31, 2013 and 2012:

	Three Months Ended March 31,	
Description (in thousands)	2013	2012
Mortgage loans held for sale	$924	$(597)
Forward sales of mortgage-backed securities	(330)	765
Interest rate lock commitments	193	(47)
Best-efforts contracts	(123)	71
Total gain recognized	$664	$192

The following tables set forth the fair value of the Company's derivative instruments and their location within the Unaudited Condensed Consolidated Balance Sheets for the periods indicated (except for mortgage loans held for sale which is disclosed as a separate line item):

	Asset Derivatives March 31, 2013		Liability Derivatives March 31, 2013	
Description of Derivatives	Balance Sheet Location	Fair Value (in thousands)	Balance Sheet Location	Fair Value (in thousands)
Forward sales of mortgage-backed securities	Other assets	$—	Other liabilities	$77
Interest rate lock commitments	Other assets	194	Other liabilities	—
Best-efforts contracts	Other assets	—	Other liabilities	126
Total fair value measurements		$194		$203
	Asset Derivatives December 31, 2012		Liability Derivatives December 31, 2012	

Description of Derivatives	Balance Sheet Location	Fair Value (in thousands)	Balance Sheet Location	Fair Value (in thousands)
Forward sales of mortgage-backed securities	Other assets	$253	Other liabilities	$—
Interest rate lock commitments	Other assets	1	Other liabilities	—
Best-efforts contracts	Other assets	—	Other liabilities	3
Total fair value measurements		$254		$3

Assets Measured on a Non-Recurring Basis

The Company assesses inventory for recoverability on a quarterly basis if events or changes in local or national economic conditions indicate that the carrying amount of an asset may not be recoverable. In conducting our quarterly review for indicators of impairment on a community level, we evaluate, among other things, margins on sales contracts in backlog, the margins on homes that have been delivered, expected changes in margins with regard to future home sales over the life of the community, expected changes in margins with regard to future land sales, the value of the land itself as well as any results from third party appraisals. We pay particular attention to communities in which inventory is moving at a slower than anticipated absorption pace, and communities whose average sales price and/or margins are trending downward and are anticipated to continue to trend downward. We also evaluate communities where management intends to lower the sales price or offer incentives in order to improve absorptions even if the community's historical results do not indicate a potential for impairment. From the review of all of these factors, we identify communities whose carrying values may exceed their estimated undiscounted future cash flows and run a test for recoverability. For those communities whose carrying values exceed the estimated undiscounted future cash flows and which are deemed to be impaired, the impairment recognized is measured by the amount by which the carrying amount of the communities exceeds the estimated fair value. Due to the fact that the Company's cash flow models and estimates of fair values are based upon management estimates and assumptions, unexpected changes in market conditions and/or changes in management's intentions with respect to the inventory may lead the Company to incur additional impairment charges in the future.

Our determination of fair value is based on projections and estimates, which are Level 3 measurement inputs. Our analysis is completed at a phase level within each community; therefore, changes in local conditions may affect one or several of our communities. For all of the categories listed below, the key assumptions relating to the valuations are dependent on project-specific local market and/or community conditions and are inherently uncertain. Because each inventory asset is unique, there are numerous inputs and assumptions used in our valuation techniques. Market factors that may impact these assumptions include:

- historical project results such as average sales price and sales pace, if closings have occurred in the project;
- competitors' market and/or community presence and their competitive actions;
- project specific attributes such as location desirability and uniqueness of product offering;
- potential for alternative product offerings to respond to local market conditions; and
- current economic and demographic conditions and related trends and forecasts.

These and other market factors that may impact project assumptions are considered by personnel in our homebuilding divisions as they prepare or update the forecasts for each community. Quantitative and qualitative factors other than home sales prices could significantly impact the potential for future impairments. The sales objectives can differ between communities, even within a given sub-market. For example, facts and circumstances in a given community may lead us to price our homes with the objective of yielding a higher sales absorption pace, while facts and circumstances in another community may lead us to price our homes to minimize deterioration in our gross margins, although it may result in a slower sales absorption pace. Furthermore, the key assumptions included in our estimated future undiscounted cash flows may be interrelated. For example, a decrease in estimated base sales price or an increase in home sales incentives may result in a corresponding increase in sales absorption pace or a reduction in base house costs. Changes in our key assumptions, including estimated average selling price, construction and development costs, absorption pace, selling strategies, or discount rates, could materially impact future cash flow and fair value estimates.

As of March 31, 2013, our projections generally assume a gradual improvement in market conditions over time. If communities are not recoverable based on estimated future undiscounted cash flows, the impairment to be recognized is measured as the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets. The fair value of a community is estimated by discounting management's cash flow projections using an appropriate risk-adjusted interest rate. As of March 31, 2013, we utilized discount rates ranging from 13% to 16% in our valuations. The discount rate used in determining each asset's estimated fair value reflects the inherent risks associated with the related estimated cash flow stream, as well as current risk-free rates available in the market and estimated market risk premiums. For example, construction in progress inventory, which is closer to completion, will generally require a lower discount rate than land under development in communities consisting of multiple phases spanning several years of development.

Operating Communities. If an indicator for impairment exists for existing operating communities, the recoverability of assets is evaluated by comparing the carrying amount of the assets to estimated future undiscounted net cash flows expected to be generated by the assets based on home sales. These estimated cash flows are developed based primarily on management's assumptions relating to the specific community. The significant assumptions used to evaluate the recoverability of assets include: the timing of development and/or marketing phases; projected sales price and sales pace of each existing or planned community; the estimated land development, home construction, and selling costs of the community; overall market supply and demand; the local market; and competitive conditions. Management reviews these assumptions on a quarterly basis. While we consider available information to determine what we believe to be our best estimates as of the end of a reporting period, these estimates are subject to change in future reporting periods as facts and circumstances change. We believe the most critical assumptions in the Company's cash flow models are projected absorption pace for home sales, sales prices, and costs to build and deliver homes on a community by community basis.

In order to estimate the assumed absorption pace for home sales included in the Company's cash flow models, the Company analyzes the historical absorption pace in the community as well as other communities in the geographic area. In addition, the Company considers internal and external market studies and trends, which may include, but are not limited to, statistics on population demographics, unemployment rates, foreclosure sales, and availability of competing products in the geographic area where a community is located. When analyzing the Company's historical absorption pace for home sales and corresponding internal and external market studies, the Company places greater emphasis on more current metrics and trends such as the absorption pace realized in its most recent quarters and management's most current assessment of sales pace.

In order to estimate the sales prices included in its cash flow models, the Company considers the historical sales prices realized on homes it delivered in the community and other communities in the geographic area, as well as the sales prices included in its current backlog for such communities. In addition, the Company considers internal and external market studies and trends, which may include, but are not limited to, statistics on sales prices in neighboring communities, which include the impact of short sales, if any, and sales prices on similar products in non-neighboring communities in the geographic area where the community is located. When analyzing its historical sales prices and corresponding market studies, the Company places greater emphasis on more current metrics and trends such as the sales prices realized in its most recent quarters and the sales prices in current backlog. Based upon this analysis, the Company sets a sales price for each house type in the community which it believes will achieve an acceptable gross margin and sales pace in the community. This price becomes the price published to the sales force for use in its sales efforts. The Company then considers the average of these published sales prices when estimating the future sales prices in its cash flow models, assuming no increase in weighted average sales price in 2013 and a 2% increase in 2014 and beyond.

In order to arrive at the Company's assumed costs to build and deliver homes, the Company generally assumes a cost structure reflecting contracts currently in place with its vendors and subcontractors, adjusted for any anticipated cost reduction initiatives or increases in cost structure. With respect to overhead included in the cash flow models, the Company uses forecasted rates included in the Company's annual budget adjusted for actual experience that is materially different than budgeted rates. The Company anticipates no increase in assumed weighted average costs in 2013 and a 2% increase in 2014 and beyond.

Future communities. If an indicator of impairment exists for raw land, land under development, or lots that management anticipates will be utilized for future homebuilding activities, the recoverability of assets is evaluated by comparing the carrying amount of the assets to the estimated future undiscounted cash flows expected to be generated by the assets based on home sales, consistent with the evaluations performed for operating communities discussed above.

For raw land, land under development, or lots that management intends to market for sale to a third party, but that do not meet all of the criteria to be classified as land held for sale as discussed below, the estimated fair value of the assets is determined based on either the estimated net sales proceeds expected to be realized on the sale of the assets or the estimated fair value determined using cash flow valuation techniques.

If the Company has not yet determined whether raw land, land under development, or lots will be utilized for future homebuilding activities or marketed for sale to a third party, the Company assesses the recoverability of the inventory using a probability-weighted approach.

Land held for sale. Land held for sale includes land that meets all of the following six criteria: (1) management, having the authority to approve the action, commits to a plan to sell the asset; (2) the asset is available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets; (3) an active program to locate a buyer and other actions required to complete the plan to sell the asset have been initiated; (4) the sale of the asset is probable, and transfer of the asset is expected to qualify for recognition as a completed sale, within one year; (5) the asset is being actively marketed for sale at a price that is reasonable in relation to its current fair value; and (6) actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn. The Company records land held for sale at the lower of its carrying value or estimated fair value less costs to sell. In performing the impairment evaluation for land held for sale, management considers, among other things, prices for land in recent comparable sales transactions, market analysis and recent bona fide offers received from outside third parties, as well as actual contracts. If the estimated fair value less the costs to sell an asset is less than the asset's current carrying value, the asset is written down to its estimated fair value less costs to sell.

Our quarterly assessments reflect management's best estimates. Due to the inherent uncertainties in management's estimates and uncertainties related to our operations and our industry as a whole, we are unable to determine at this time if and to what extent continuing future impairments will occur. Additionally, due to the volume of possible outcomes that can be generated from changes in the various model inputs for each community, we do not believe it is possible to create a sensitivity analysis that can provide meaningful information for the users of our financial statements.

Variable Interest Entities. In order to minimize our investment and risk of land exposure in a single location, we have periodically partnered with other land developers or homebuilders to share in the land investment and development of a property through joint ownership and development agreements, joint ventures, and other similar arrangements. For such joint venture arrangements where a special purpose entity is established to own the property, we enter into limited liability company arrangements (“LLCs”) or other joint development agreements with the other partners. During the three month period ended March 31, 2013, we increased our investment in LLCs from December 31, 2012 by $10.5 million primarily due to a joint investment with another builder in a land development in our Southern region. The Company's ownership in these entities as of March 31, 2013 ranged from 50% to 61%. These entities typically engage in land development activities for the purpose of distributing or selling developed lots to the Company and its partners in the entity. With respect to our investments in these entities, we are required, under ASC 810-10, Consolidation (“ASC 810-10”), to evaluate whether or not such entities should be consolidated into our financial statements. We initially perform these evaluations when each new entity is created and upon any events that require reconsideration of the entity. In order to determine if we should consolidate an LLC, we determine if the LLC is a Variable Interest Entity (“VIE”) and if we are the primary beneficiary of the entity. Factors considered are whether we have the ability to control the activities of the VIE that most significantly impact its economic performance. Such activities include, but are not limited to, the ability to determine the budget and scope of land development work, if any; the ability to control financing decisions for the VIE; the ability to acquire additional land into the VIE or dispose of land in the VIE not under contract with M/I Homes; and the ability to change or amend the existing option contract with the VIE. If it is determined we are not able to control such activities, we are not considered the primary beneficiary of the VIE.

During the three month period ended March 31, 2013, we have determined that one of the LLCs in which we have an interest meets the requirements of a VIE due to a lack of equity at risk in the entity. However, we have determined that we do not have substantive control over any of these entities, including our VIE. As a result, none of these entities are required to be consolidated into our financial statements and the entities are instead recorded in Investment in Unconsolidated Limited Liability Companies on our Unaudited Condensed Consolidated Balance Sheets.

We enter into option or purchase agreements to acquire land or lots, for which we generally pay non-refundable deposits. We also analyze these agreements under ASC 810-10 to determine whether we are the primary beneficiary of the VIE, if applicable, using an analysis similar to that described above. If we are deemed to be the primary beneficiary of the VIE, we will consolidate the VIE in our consolidated financial statements. In cases where we are the primary beneficiary, even though we do not have title to such land, we are required to consolidate these purchase/option agreements and reflect such assets and liabilities as Consolidated Inventory not Owned in our Unaudited Condensed Consolidated Balance Sheets.

Investment In Unconsolidated Limited Liability Companies: We use the equity method of accounting for investments in unconsolidated entities over which we exercise significant influence but do not have a controlling interest. Under the equity method, our share of the unconsolidated entities' earnings or loss, if any, is included in our statement of operations. We evaluate our investments in unconsolidated entities for impairment at least quarterly as described below.

If the fair value of the investment is less than the investment's carrying value and the Company has determined that the decline in value is other than temporary, the Company would write down the value of the investment to fair value. The determination of whether an investment's fair value is less than the carrying value requires management to make certain assumptions regarding the amount and timing of future contributions to the Unconsolidated LLC, the timing of distribution of lots to the Company from the Unconsolidated LLC, the projected fair value of the lots at the time of distribution to the Company, and the estimated proceeds from, and timing of, the sale of land or lots to third parties. In determining the fair value of investments in Unconsolidated LLCs, the Company evaluates the projected cash flows associated with each Unconsolidated LLC. As of March 31, 2013, the Company used a discount rate of 16% in determining the fair value of investments in Unconsolidated LLCs. In addition to the assumptions management must make to determine if the investment's fair value is less than the carrying value, management must also use judgment in determining whether the impairment is other than temporary. The factors management considers are: (1) the length of time and the extent to which the market value has been less than cost; (2) the financial condition and near-term prospects of the company; and (3) the intent and ability of the Company to retain its investment in the Unconsolidated LLC for a period of time sufficient to allow for any anticipated recovery in market value. We believe that the Company's maximum exposure related to its investment in these entities as of March 31, 2013 is the amount invested of $22.3 million (in addition to a $2.5 million note due to the Company from one of the Unconsolidated LLCs), though we expect to invest further amounts in these LLCs as development of the properties progresses. Included in the Company's investment in Unconsolidated LLCs at March 31, 2013 and December 31, 2012 were $0.7 million and $0.8 million of capitalized interest and other costs, respectively.

Because of the high degree of judgment involved in developing these assumptions, it is possible that the Company may determine the investment is not impaired in the current period; however, due to the passage of time, change in market conditions, and/or changes in management's intentions with respect to the inventory, a change in assumptions could result and impairment could occur.

The tables below show the level and measurement of assets measured on a non-recurring basis for the three months ended March 31, 2013 and as of and for the year ended December 31, 2012:

Description of asset or liability (In thousands)	Fair Value Measurements March 31, 2013	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Losses For The Three Months Ended March 31, 2013
Inventory	$2,015	$—	$—	$ 2,015	$900
Investments in Unconsolidated LLCs	—	—	—	—	—
Total fair value measurements	$2,015	$—	$—	$ 2,015	$900

Description of asset or liability (In thousands)	Fair Value Measurements December 31, 2012	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Losses For The Year Ended December 31, 2012
Inventory	$5,608	$—	$—	$ 5,608	$3,112
Investments in Unconsolidated LLCs	1,050	—	—	1,050	390
Total fair value measurements	$6,658	$—	$—	$ 6,658	$3,502

Financial Instruments

Counterparty Credit Risk. To reduce the risk associated with accounting losses that would be recognized if counterparties failed to perform as contracted, the Company limits the entities with whom management can enter into commitments. This risk of accounting loss is the difference between the market rate at the time of non-performance by the counterparty and the rate to which the Company committed.

The following table presents the carrying amounts and fair values of the Company's financial instruments at March 31, 2013 and December 31, 2012. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (an exit price).

	March 31, 2013		December 31, 2012	
(In thousands)	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Assets:				
Cash, cash equivalents and restricted cash	$272,551	$272,551	$154,178	$154,178
Mortgage loans held for sale	57,721	57,721	71,121	71,121
Split dollar life insurance policies	725	700	710	678
Notes receivable	4,565	3,758	8,787	7,460
Commitments to extend real estate loans	194	194	1	1

Forward sales of mortgage-backed securities	—	—	253	253
Liabilities:				
Notes payable - banks	53,126	53,126	67,957	67,957
Notes payable - other	10,316	10,449	11,105	11,148
Convertible senior subordinated notes due 2017	57,500	72,234	57,500	74,175
Convertible senior subordinated notes due 2018	86,250	88,838	—	—
Senior notes due 2018	227,770	255,300	227,670	250,700
Best-efforts contracts for committed IRLCs and mortgage loans held for sale	126	126	3	3
Forward sales of mortgage-backed securities	77	77	—	—
Off-Balance Sheet Financial Instruments:				
Letters of credit	—	471	—	493

The following methods and assumptions were used by the Company in estimating its fair value disclosures of financial instruments at March 31, 2013 and December 31, 2012:

Cash, Cash Equivalents and Restricted Cash. The carrying amounts of these items approximate fair value because they are short-term by nature.

Mortgage Loans Held for Sale, Forward Sales of Mortgage-Backed Securities, Commitments to Extend Real Estate Loans, Best-Efforts Contracts for Committed IRLCs and Mortgage Loans Held for Sale, 2017 Convertible Senior Subordinated Notes, 2018 Convertible Senior Subordinated Notes and 2018 Senior Notes. The fair value of these financial instruments was determined based upon market quotes at March 31, 2013 and December 31, 2012. The market quotes used were quoted prices for similar assets or liabilities along with inputs taken from observable market data by correlation. The inputs were adjusted to account for the condition of the asset or liability.

Split Dollar Life Insurance Policies and Notes Receivable. The estimated fair value was determined by calculating the present value of the amounts based on the estimated timing of receipts using discount rates that incorporate management's estimate of risk associated with the corresponding note receivable.

Notes Payable - Banks. The interest rate available to the Company fluctuates with the Alternate Base Rate or the Eurodollar Rate (for the Company's $140 million secured revolving credit facility (the "Credit Facility")) or LIBOR (for M/I Financial Corp.'s $80 million secured mortgage warehousing agreement as amended and restated on March 29, 2013 (the "MIF Mortgage Warehousing Agreement") and for M/I Financial's mortgage repurchase agreement dated November 13, 2012, as amended (the "MIF Mortgage Repurchase Facility")), and thus their carrying value is a reasonable estimate of fair value.

Notes Payable - Other. The estimated fair value was determined by calculating the present value of the future cash flows using the Company's current incremental borrowing rate.

Letters of Credit. Letters of credit of $24.8 million and $25.7 million represent potential commitments at March 31, 2013 and December 31, 2012, respectively. The letters of credit generally expire within one or two years. The estimated fair value of letters of credit was determined using fees currently charged for similar agreements.

NOTE 3. Inventory

A summary of the Company's inventory as of March 31, 2013 and December 31, 2012 is as follows:

(In thousands)	March 31, 2013	December 31, 2012
Single-family lots, land and land development costs	$255,934	$257,397
Land held for sale	8,591	8,442
Homes under construction	245,074	221,432
Model homes and furnishings - at cost (less accumulated depreciation: March 31, 2013 - $5,341; December 31, 2012 - $4,883)	36,251	37,080
Community development district infrastructure	4,266	4,634
Land purchase deposits	10,530	8,727
Consolidated inventory not owned	16,994	19,105
Total inventory	$577,640	$556,817

Single-family lots, land and land development costs include raw land that the Company has purchased to develop into lots, costs incurred to develop the raw land into lots, and lots for which development has been completed, but which have not yet been used to start construction of a home.

Homes under construction include homes that are in various stages of construction. As of March 31, 2013 and December 31, 2012, we had 616 homes (with a carrying value of $76.1 million) and 649 homes (with a carrying value of $89.8 million), respectively, included in homes under construction that were not subject to a sales contract.

Model homes and furnishings include homes that are under construction or have been completed and are being used as sales models. The amount also includes the net book value of furnishings included in our model homes. Depreciation on model home furnishings is recorded using an accelerated method over the estimated useful life of the assets, typically three years.

The Company assesses inventory for recoverability on a quarterly basis. Refer to Note 2 of our Unaudited Condensed Consolidated Financial Statements for additional details relating to our procedures for evaluating our inventories for impairment.

Land purchase deposits include both refundable and non-refundable amounts paid to third party sellers relating to the purchase of land. On an ongoing basis, the Company evaluates the land option agreements relating to the land purchase deposits. In the period during which the Company makes the decision not to proceed with the purchase of land under an agreement, the Company writes off any deposits and accumulated pre-acquisition costs relating to such agreement.

NOTE 4. Valuation Adjustments and Write-offs

The Company assesses inventory for recoverability on a quarterly basis, by reviewing for impairment whenever events or changes in local or national economic conditions indicate that the carrying amount of an asset may not be recoverable.

A summary of the Company’s valuation adjustments and write-offs for the three months ended March 31, 2013 and 2012 is as follows:

	Three Months Ended March 31,	
(In thousands)	2013	2012
Impairment of operating communities:		
Midwest	$—	$—
Southern	—	—
Mid-Atlantic	—	—
Total impairment of operating communities (a)	$—	$—
Impairment of future communities:		
Midwest	$252	$—
Southern	—	—
Mid-Atlantic	—	—
Total impairment of future communities (a)	$252	$—
Impairment of land held for sale:		
Midwest	$648	$95
Southern	—	—
Mid-Atlantic	—	—
Total impairment of land held for sale (a)	$648	$95
Option deposits and pre-acquisition costs write-offs:		
Midwest	$—	$2
Southern	—	7
Mid-Atlantic	—	22
Total option deposits and pre-acquisition costs write-offs (b)	$—	$31
Impairment of investments in Unconsolidated LLCs:		
Midwest	$—	$—
Southern	—	—
Mid-Atlantic	—	—
Total impairment of investments in Unconsolidated LLCs (a)	$—	$—
Total impairments and write-offs of option deposits and pre-acquisition costs	$900	$126

(a) Amounts are recorded within Impairment of inventory and investment in Unconsolidated LLCs in the Company's Unaudited Condensed Consolidated Statements of Operations.

(b) Amounts are recorded within General and administrative expenses in the Company's Unaudited Condensed Consolidated Statements of Operations.

NOTE 5. Capitalized Interest

The Company capitalizes interest during land development and home construction. Capitalized interest is charged to cost of sales as the related inventory is delivered to a third party. The summary of capitalized interest for the three months ended March 31, 2013 and 2012 is as follows:

	Three Months Ended March 31,	
(In thousands)	2013	2012
Capitalized interest, beginning of period	$15,376	$18,869
Interest capitalized to inventory	2,777	1,866
Capitalized interest charged to cost of sales	(3,528)	(2,565)
Capitalized interest, end of period	$14,625	$18,170
Interest incurred	$7,117	$6,472

NOTE 6. Guarantees and Indemnifications

Warranty

Warranty reserves are recorded for warranties under our Home Builder’s Limited Warranty (“HBLW”) and our 30-year transferable structural warranty in Other liabilities on the Company's Unaudited Condensed Consolidated Balance Sheets.

The warranty reserves for the HBLW are established as a percentage of average sales price and adjusted based on historical payment patterns determined, generally, by geographic area and recent trends. Factors that are given consideration in determining the HBLW reserves include: (1) the historical range of amounts paid per average sales price on a home; (2) type and mix of amenity packages added to the home; (3) any warranty expenditures not considered to be normal and recurring; (4) timing of payments; (5) improvements in quality of construction expected to impact future warranty expenditures; and (6) conditions that may affect certain projects and require a different percentage of average sales price for those specific projects. Changes in estimates for warranties occur due to changes in the historical payment experience and differences between the actual payment pattern experienced during the period and the historical payment pattern used in our evaluation of the warranty reserve balance at the end of each quarter. Actual future warranty costs could differ from our current estimated amount.

Our warranty reserves for our transferable structural warranty programs are established on a per-unit basis. While the structural warranty reserve is recorded as each house closes, the sufficiency of the structural warranty per unit charge and total reserve is re-evaluated on an annual basis, with the assistance of an actuary, using our own historical data and trends, industry-wide historical data and trends, and other project specific factors. The reserves are also evaluated quarterly and adjusted if we encounter activity that is inconsistent with the historical experience used in the annual analysis. These reserves are subject to variability due to uncertainties regarding structural defect claims for products we build, the markets in which we build, claim settlement history, insurance and legal interpretations, among other factors.

While we believe that our warranty reserves are sufficient to cover our projected costs, there can be no assurances that historical data and trends will accurately predict our actual warranty costs.

A summary of warranty activity for the three months ended March 31, 2013 and 2012 is as follows:

	Three Months Ended March 31,	
(In thousands)	2013	2012
Warranty reserves, beginning of period	$10,438	$9,025
Warranty expense on homes delivered during the period	1,338	1,042
Changes in estimates for pre-existing warranties	—	(57)
Settlements made during the period	(1,376)	(1,462)
Warranty reserves, end of period	$10,400	$8,548

Guarantees

In the ordinary course of business, M/I Financial Corp. (“M/I Financial”), a 100%-owned subsidiary of M/I Homes, Inc., enters into agreements that guarantee certain purchasers of its mortgage loans that M/I Financial will repurchase a loan if certain conditions occur, primarily if the mortgagor does not meet those conditions of the loan within the first six months after the sale of the loan. Loans totaling approximately $6.0 million and $3.1 million were covered under the above guarantees as of March 31, 2013 and December 31, 2012, respectively. A portion of the revenue paid to M/I Financial for providing the guarantees on the above loans was deferred at March 31, 2013, and will be recognized in income as M/I Financial is released from its obligation under the guarantees. M/I Financial did not repurchase any loans under the above agreements during the three months ended March 31, 2013. The risk associated with the guarantees above is offset by the value of the underlying assets.

M/I Financial has received inquiries concerning underwriting matters from purchasers of its loans regarding certain loans totaling approximately $8.2 million and $7.9 million at March 31, 2013 and December 31, 2012, respectively. The risk associated with the guarantees above is offset by the value of the underlying assets.

M/I Financial has also guaranteed the collectability of certain loans to third party insurers (U.S. Department of Housing and Urban Development and U.S. Veterans Administration) of those loans for periods ranging from five to thirty years. As of both March 31, 2013 and December 31, 2012, the total of all loans indemnified to third party insurers relating to the above agreements was $1.0 million. The maximum potential amount of future payments is equal to the outstanding loan value less the value of the underlying asset plus administrative costs incurred related to foreclosure on the loans, should this event occur.

The Company has recorded a liability relating to the guarantees described above totaling $3.0 million and $2.6 million at March 31, 2013 and December 31, 2012, respectively, which is management's best estimate of the Company's liability.

At March 31, 2013, the Company had outstanding $230.0 million aggregate principal amount of 8.625% Senior Notes due 2018 (the “2018 Senior Notes”), $57.5 million aggregate principal amount of 3.25% Convertible Senior Subordinated Notes due 2017 (the "2017 Convertible Senior Subordinated Notes") and $86.3 million aggregate principal amount of 3.0% Convertible Senior Subordinated Notes due 2018 (the "2018 Convertible Senior Subordinated Notes"). The Company's obligations under the 2018

Senior Notes, the 2017 Convertible Senior Subordinated Notes and the 2018 Convertible Senior Subordinated Notes, and the Credit Facility are guaranteed jointly and severally by all of the Company's subsidiaries, with the exception of subsidiaries that are primarily engaged in the business of mortgage financing, title insurance or similar financial businesses relating to the homebuilding and home sales business, certain subsidiaries that are not 100%-owned by the Company or another subsidiary, and other subsidiaries designated by the Company as Non-Guarantor Subsidiaries, subject to limitations on the aggregate amount invested in such Non-Guarantor Subsidiaries.

NOTE 7. Commitments and Contingencies

At March 31, 2013, the Company had outstanding approximately $65.9 million of completion bonds and standby letters of credit, some of which were issued to various local governmental entities that expire at various times through February 2018. Included in this total are: (1) $37.6 million of performance and maintenance bonds and $13.9 million of performance letters of credit that serve as completion bonds for land development work in progress; (2) $10.9 million of financial letters of credit, of which $4.7 million represent deposits on land and lot purchase agreements; and (3) $3.4 million of financial bonds.

At March 31, 2013, the Company also had options and contingent purchase agreements to acquire land and developed lots with an aggregate purchase price of approximately $301.7 million. Purchase of properties under these agreements is contingent upon satisfaction of certain requirements by the Company and the sellers.

NOTE 8. Legal Liabilities

On March 5, 2009, a resident of Florida and an owner of one of our homes filed a complaint in the United States District Court for the Southern District of Ohio, on behalf of himself and other similarly situated owners and residents of homes in the United States or alternatively in Florida, against the Company and certain other identified and unidentified parties (the “Initial Action”). The plaintiff alleged that the Company built his home with defective drywall, manufactured and supplied by certain of the defendants, that contains sulfur or other organic compounds capable of harming the health of individuals and damaging property. The plaintiff alleged physical and economic damages and sought legal and equitable relief, medical monitoring and attorney's fees. The Company filed a responsive pleading on or about April 30, 2009. The Initial Action was consolidated with other similar actions not involving the Company and transferred to the Eastern District of Louisiana pursuant to an order from the United States Judicial Panel on Multidistrict Litigation for coordinated pre-trial proceedings (collectively, the “In Re: Chinese Manufactured Drywall Product Liability Litigation”). In connection with the administration of the In Re: Chinese Manufactured Drywall Product Liability Litigation, the same homeowner and nine other homeowners were named as plaintiffs in omnibus class action complaints filed in and after December 2009 against certain identified manufacturers of drywall and others (including the Company), including one homeowner named as a plaintiff in an omnibus class action complaint filed in March 2010 against various unidentified manufacturers of drywall and others (including the Company) (collectively, the “MDL Omnibus Actions”). As they relate to the Company, the Initial Action and the MDL Omnibus Actions address substantially the same claims and seek substantially the same relief. The Company has entered into agreements with several of the homeowners named as plaintiffs pursuant to which the Company agreed to make repairs to their homes consistent with repairs made to the homes of other homeowners. As a result of these agreements, the Initial Action has been resolved and dismissed, and seven of the nine other homeowners named as plaintiffs in omnibus class action complaints have dismissed their claims against the Company. One of the two remaining plaintiffs has also filed a complaint in Florida state court asserting essentially the same claims and seeking substantially the same relief as asserted in the MDL Omnibus Actions. The court in the MDL Omnibus Actions has entered an order and judgment certifying various settlement classes and granting final approval of various class settlements, including a global class action settlement, which is intended to resolve all Chinese drywall-related claims of and against those who participate in the settlement. The time to appeal that order and judgment lapsed without any appeals. The Company has elected to participate in the global settlement. Further, to our knowledge none of our homeowners elected to opt out of the class and, therefore, we believe the global settlement resolves all claims against the Company. Our total obligation as a defendant under the global settlement was not material and has been paid. We expect to receive proceeds under some of the settlements based on repairs we made to homes impacted by defective drywall. The Company also continues to pursue recovery against various manufacturers, suppliers, insurance companies and others for damages resulting from the defective drywall.

The Company and certain of its subsidiaries have been named as defendants in other claims, complaints and legal actions which are routine and incidental to our business. Certain of the liabilities resulting from these other matters are covered by insurance. While management currently believes that the ultimate resolution of these other matters, individually and in the aggregate, will not have a material effect on the Company's financial position, results of operations and cash flows, such matters are subject to inherent uncertainties. The Company has recorded a liability to provide for the anticipated costs, including legal defense costs, associated with the resolution of these other matters. However, there exists the possibility that the costs to resolve these other matters could differ from the recorded estimates and, therefore, have a material effect on the Company's net income for the periods in which the matters are resolved. At both March 31, 2013 and December 31, 2012, we had $0.3 million reserved for legal expenses.

NOTE 9. Debt

Notes Payable - Homebuilding

At March 31, 2013, borrowing availability under the Credit Facility was $62.2 million in accordance with the borrowing base calculation, and there were no borrowings outstanding and $15.9 million of letters of credit outstanding under the Credit Facility, leaving net remaining borrowing availability of $46.3 million. At March 31, 2013, the Company had pledged $154.9 million in aggregate book value of inventory to secure any borrowings and letters of credit outstanding under the Credit Facility. At March 31, 2013, the Company was in compliance with all financial covenants of the Credit Facility.

At March 31, 2013, the Company is party to three secured credit agreements for the issuance of letters of credit outside of the Credit Facility (collectively, the “Letter of Credit Facilities”).

At March 31, 2013, there was $9.0 million of outstanding letters of credit in aggregate under the Company's three Letter of Credit Facilities, which were collateralized with $9.1 million of the Company's cash.

Notes Payable — Financial Services

In March 2013, M/I Financial amended and restated the MIF Mortgage Warehousing Agreement, which, among other things, increased the maximum borrowing availability from $70.0 million to $80.0 million and provided for an optional increase of the maximum borrowing availability of up to an additional $20.0 million (subject to certain conditions), extended the expiration date to March 28, 2014, and increased the maximum principal amount permitted to be outstanding at any one time in aggregate under all warehouse credit lines from $100.0 million to $125.0 million. The interest rate was also adjusted to a per annum rate equal to the greater of (1) the floating LIBOR rate plus 275 basis points and (2) 3.50%. The rate had previously been a per annum rate equal to the greater of (1) the floating LIBOR rate plus 225 basis points and (2) 3.50%.

On November 13, 2012, we entered into the MIF Mortgage Repurchase Facility with a maximum borrowing availability of $15.0 million. At March 31, 2013, our total combined maximum borrowing availability under the two credit facilities is $95.0 million.

At March 31, 2013, M/I Financial had $53.1 million outstanding on a combined basis under its credit facilities and was in compliance with all financial covenants of those agreements.

Convertible Senior Subordinated Notes

In March 2013, the Company issued $86.3 million aggregate principal amount of 2018 Convertible Senior Subordinated Notes. The 2018 Convertible Senior Subordinated Notes bear interest at a rate of 3.0% per year, payable semiannually in arrears on March 1 and September 1 of each year beginning on September 1, 2013. The 2018 Convertible Senior Subordinated Notes mature on March 1, 2018. At any time prior to the close of business on the second scheduled trading day immediately preceding the maturity date, holders may convert their 2018 Convertible Senior Subordinated Notes into the Company's common shares. The conversion rate initially equals 30.9478 shares per $1,000 of principal amount. This corresponds to an initial conversion price of approximately $32.31 per common share, which equates to approximately 2.7 million common shares. The conversion rate is subject to adjustment upon the occurrence of certain events. The 2018 Convertible Senior Subordinated Notes are fully and unconditionally guaranteed on a senior subordinated unsecured basis by those subsidiaries of the Company that are guarantors under the Company's 2018 Senior Notes and 2017 Convertible Senior Subordinated Notes. The 2018 Convertible Senior Subordinated Notes are senior subordinated unsecured obligations of the Company and the subsidiary guarantors and are subordinated in right of payment to our existing and future senior indebtedness and are also effectively subordinated to our existing and future secured indebtedness. The indenture governing the 2018 Convertible Senior Subordinated Notes provides that the Company may not redeem the 2018 Convertible Senior Subordinated Notes prior to March 6, 2016, but also contains provisions requiring the Company to repurchase the notes (subject to certain exceptions), at a holder's option, upon the occurrence of a fundamental change (as defined in the indenture).

On or after March 6, 2016, the Company may redeem for cash any or all of the 2018 Convertible Senior Subordinated Notes (except for any 2018 Convertible Senior Subordinated Notes that the Company is required to repurchase in connection with a fundamental change), but only if the last reported sale price of the Company's common shares exceeds 130% of the applicable conversion price for the notes on each of at least 20 applicable trading days. The 20 trading days do not need to be consecutive, but must occur during a period of 30 consecutive trading days that ends within 10 trading days immediately prior to the date the Company provides the notice of redemption. The redemption price for the 2018 Convertible Senior Subordinated Notes to be redeemed will equal 100% of the principal amount, plus accrued and unpaid interest, if any.

In September 2012, the Company issued $57.5 million aggregate principal amount of 2017 Convertible Senior Subordinated Notes. The 2017 Convertible Senior Subordinated Notes bear interest at a rate of 3.25% per year, payable semiannually in arrears on March 15 and September 15 of each year beginning on March 15, 2013. The 2017 Convertible Senior Subordinated Notes mature on September 15, 2017. At any time prior to the close of business on the second scheduled trading day immediately preceding the maturity date, holders may convert their 2017 Convertible Senior Subordinated Notes into the Company's common shares. The conversion rate initially equals 42.0159 shares per $1,000 of their principal amount. This corresponds to an initial conversion price of approximately $23.80 per common share, which equates to approximately 2.4 million common shares. The conversion rate is subject to adjustment upon the occurrence of certain events. The 2017 Convertible Senior Subordinated Notes are fully and unconditionally guaranteed on a senior subordinated unsecured basis by those subsidiaries of the Company that are guarantors under the Company's 2018 Senior Notes and 2018 Convertible Senior Subordinated Notes. The 2017 Convertible Senior Subordinated Notes are senior subordinated unsecured obligations of the Company and the subsidiary guarantors and are subordinated in right of payment to our existing and future senior indebtedness and are also effectively subordinated to our existing and future secured indebtedness. The indenture governing the 2017 Convertible Senior Subordinated Notes provides that we may not redeem the notes prior to their stated maturity date, but also contains provisions requiring the Company to repurchase the 2017 Convertible Senior Subordinated Notes (subject to certain exceptions), at a holder's option, upon the occurrence of a fundamental change (as defined in the indenture).

Senior Notes

As of March 31, 2013, we had $230.0 million of our 2018 Senior Notes outstanding. The 2018 Senior Notes bear interest at a rate of 8.625% per year, payable semiannually in arrears on May 15 and November 15 of each year, and mature on November 15, 2018. The 2018 Senior Notes are general, unsecured senior obligations of the Company and the subsidiary guarantors and rank equally in right of payment with all our existing and future unsecured senior indebtedness. The 2018 Senior Notes are fully and unconditionally guaranteed on a senior unsecured basis by all of our subsidiaries, with the exception of subsidiaries that are primarily engaged in the business of mortgage financing, the origination of mortgages for resale, title insurance or similar financial businesses relating to the homebuilding and home sales business and certain subsidiaries that are not 100%-owned by the Company or another subsidiary, and certain subsidiaries that are otherwise designated by the Company as Unrestricted Subsidiaries in accordance with the terms of the indenture.

The indenture governing our 2018 Senior Notes limits our ability to pay dividends on, and repurchase, our common shares and our 9.75% Series A Preferred Shares (the “Series A Preferred Shares”) to the amount of the positive balance in our “restricted payments basket,” as defined in the indenture. The restricted payments basket was $95.7 million at March 31, 2013. We are permitted to pay dividends on, and repurchase, our common shares and Series A Preferred Shares to the extent of the positive balance in our restricted payments basket.

On March 11, 2013, we announced our intention to redeem 2,000 of our outstanding Series A Preferred Shares. Such shares were redeemed on April 10, 2013 for $50.4 million of cash, which will reduce the restricted payments basket with respect to our 2018 Senior Notes by that amount. In addition, although not yet declared, our board of directors has determined that we will pay the quarterly dividend on our Series A Preferred Shares for the second quarter of 2013 (with such dividend being payable on June 17, 2013 to holders of record on June 1, 2013). The determination to pay future dividends on, or make future repurchases of, our common shares or Series A Preferred Shares will be at the discretion of our board of directors and will depend upon our results of operations, financial condition, capital requirements and compliance with debt covenants and the terms of our Series A Preferred Shares, and other factors deemed relevant by our board of directors.

NOTE 10. Earnings (Loss) Per Share

The table below presents a reconciliation between basic and diluted weighted average shares outstanding, net income (loss) available to common shareholders and basic and diluted income (loss) per share for the three months ended March 31, 2013 and 2012:

	Three Months Ended March 31,	
(In thousands, except per share amounts)	2013	2012
NUMERATOR		
Net income (loss)	$4,587	$(3,186)
Excess of fair value over book value of preferred shares subject to redemption	(2,190)	—
Net income (loss) to common shareholders	2,397	(3,186)
DENOMINATOR		
Basic weighted average shares outstanding	22,273	18,772
Effect of dilutive securities:		
Stock option awards	296	—
Deferred compensation awards	119	—
Diluted weighted average shares outstanding - adjusted for assumed conversions	22,688	18,772
Earnings (loss) per common share		
Basic	$0.11	$(0.17)
Diluted	$0.11	$(0.17)
Anti-dilutive equity awards not included in the calculation of diluted earnings per common share	856	2,227

On March 11, 2013, the Company announced its intention to redeem 2,000 of its outstanding Series A Preferred Shares on April 10, 2013 and recognized a $2.2 million non-cash equity charge related to the excess of fair value over carrying value relating primarily to the original issuance costs that were paid in 2007, which reduced net income to common shareholders in the earnings per share calculation above for the quarter ended March 31, 2013. On April 10, 2013, the redemption was completed. Refer to Note 15 of our Unaudited Condensed Consolidated Financial Statements for additional details.

During the quarter ended March 31, 2013, the Company also issued 2.461 million common shares in a public offering at a price of $23.50 per share (for net proceeds of $54.6 million), which shares are included above in our total basic weighted average shares outstanding.

NOTE 11. Income Taxes

Deferred federal and state income tax assets primarily represent the deferred tax benefits arising from temporary differences between book and tax income which will be recognized in future years as an offset against future taxable income. These assets were largely generated as a result of inventory impairments that the Company incurred in 2006 through 2011. If, for some reason, the combination of future years' income (or loss), combined with the reversal of the timing differences, results in a loss, such losses can be carried back to prior years or carried forward to future years to recover the deferred tax assets.

In accordance with ASC 740-10, Income Taxes, we evaluate our deferred tax assets, including the benefit from net operating losses (“NOLs”), to determine if a valuation allowance is required. Companies must assess, using significant judgments, whether a valuation allowance should be established based on the consideration of all available evidence using a “more likely than not” standard with significant weight being given to evidence that can be objectively verified. This assessment considers, among other matters, the nature, frequency and severity of current and cumulative losses, forecasts of future profitability, the length of statutory carryforward periods, our experience with operating losses and our experience of utilizing tax credit carryforwards and tax planning alternatives. Based upon a review of all available evidence, we recorded a full valuation allowance against our deferred tax assets during 2008. We continue to maintain a full non-cash valuation allowance against the entire amount of our remaining net deferred tax assets at March 31, 2013 as we have determined that the weight of the negative evidence exceeds that of the positive evidence and it continues to be more likely than not that we will not be able to utilize all of our deferred tax assets and NOL carryovers.

For the three months ended March 31, 2013, the Company had a valuation allowance of $134.0 million against deferred tax assets which include the tax benefit from NOL and credit carryovers. At March 31, 2013, the Company had federal net operating loss carryforwards of approximately $82.3 million and federal credit carryforwards of $4.2 million and $16.1 million of state net operating loss carryforwards. Our future deferred tax asset realization depends on sufficient taxable income in the carryforward periods under existing tax laws. Our federal carryforward benefits will begin to expire in 2028. Our state net operating loss benefits began to expire in 2012, with $9.0 million expiring between 2012 and 2027 and $7.1 million expiring between 2028 and 2033.

We will continue to review on an ongoing basis all available evidence to determine if and when we expect to realize our deferred tax assets and NOL carryovers. Additionally, due to the considerable estimates utilized in establishing a valuation allowance and the potential for changes in facts and circumstances in future reporting periods, it is reasonably possible that we will be required to either increase or decrease our valuation allowance in future reporting periods.

During the three months ended March 31, 2013, the Company reduced its valuation allowance by $1.8 million, for a total valuation allowance recorded of $134.0 million, against its deferred tax assets. The accounting for deferred taxes is based upon an estimate of future results. Differences between the anticipated and actual outcomes of these future tax consequences could have a material impact on the Company's consolidated results of operations or financial position.

NOTE 12. Business Segments

The Company’s segment information is presented on the basis that the chief operating decision makers use in evaluating segment performance. The Company’s chief operating decision makers evaluate the Company’s performance in various ways, including: (1) the results of our 12 individual homebuilding operating segments and the results of our financial services operations; (2) the results of our three homebuilding regions; and (3) our consolidated financial results. We have determined our reportable segments as follows: Midwest homebuilding, Southern homebuilding, Mid-Atlantic homebuilding and financial services operations. The homebuilding operating segments that are included within each reportable segment have similar operations and exhibit similar long-term economic characteristics. Our homebuilding operations include the acquisition and development of land, the sale and construction of single-family attached and detached homes, and the occasional sale of lots to third parties. The homebuilding operating segments that comprise each of our reportable segments are as follows:

Midwest	Southern	Mid-Atlantic
Columbus, Ohio	Tampa, Florida	Washington, D.C.
Cincinnati, Ohio	Orlando, Florida	Charlotte, North Carolina
Indianapolis, Indiana	Houston, Texas	Raleigh, North Carolina
Chicago, Illinois	San Antonio, Texas	
	Austin, Texas	

Our financial services operations include the origination and sale of mortgage loans and title services primarily for purchasers of the Company's homes.

The following table shows, by segment, revenue, operating income (loss) and interest expense for the three months ended March 31, 2013 and 2012, as well as the Company's income (loss) before income taxes for such periods:

	Three Months Ended March 31,	
(In thousands)	2013	2012
Revenue:		
Midwest homebuilding	$60,702	$56,953
Southern homebuilding	50,961	29,072
Mid-Atlantic homebuilding	70,654	40,784
Financial services (b)	8,410	4,316
Total revenue	$190,727	$131,125
Operating income (loss):		
Midwest homebuilding (a)	$2,201	$1,111
Southern homebuilding (a)	3,091	885
Mid-Atlantic homebuilding (a)	4,345	461
Financial services (b)	5,455	2,436
Less: Corporate selling, general and administrative expense	(5,866)	(4,661)
Total operating income (loss)	$9,226	$232
Interest expense:		
Midwest homebuilding	$1,474	$1,726
Southern homebuilding	1,304	802
Mid-Atlantic homebuilding	1,244	1,710
Financial services (b)	318	368
Total interest expense	$4,340	$4,606
Income (loss) before income taxes	$4,886	$(4,374)

(a) For the three months ended March 31, 2013 and 2012, the impact of charges relating to the impairment of inventory and investment in Unconsolidated LLCs and the write-off of abandoned land transaction costs was $0.9 million and $0.1 million, respectively. These charges reduced operating income by $0.9 million and $0.1 million in the Midwest region for the three months ended March 31, 2013 and 2012, respectively, and less than $0.1 million in the Southern and Mid-Atlantic regions for the three months ended March 31, 2012, respectively. There were no charges in the Mid-Atlantic or Southern regions for the three months ended March 31, 2013.

(b) Our financial services operational results should be viewed in connection with our homebuilding business as its operations originate loans and provide title services primarily for our homebuying customers, with the exception of a small amount of mortgage re-financing.

The following tables show total assets by segment at March 31, 2013 and December 31, 2012:

	March 31, 2013				
(In thousands)	Midwest	Southern	Mid-Atlantic	Corporate, Financial Services and Unallocated	Total
Deposits on real estate under option or contract	$2,005	$5,358	$3,167	$—	$10,530
Inventory (a)	198,812	185,314	182,983	—	567,109
Investments in Unconsolidated LLCs	5,630	16,645	—	—	22,275

Other assets	5,807	10,204	8,187	344,540	368,738
Total assets	$212,254	$217,521	$194,337	$344,540	$968,652

	December 31, 2012				
(In thousands)	Midwest	Southern	Mid-Atlantic	Corporate, Financial Services and Unallocated	Total
Deposits on real estate under option or contract	$1,462	$4,612	$2,653	$—	$8,727
Inventory (a)	196,554	157,302	194,234	—	548,090
Investments in Unconsolidated LLCs	5,121	6,611	—	—	11,732
Other assets	4,421	8,436	7,759	242,135	262,751
Total assets	$207,558	$176,961	$204,646	$242,135	$831,300

(a) Inventory includes single-family lots, land and land development costs; land held for sale; homes under construction; model homes and furnishings; community development district infrastructure; and consolidated inventory not owned.

NOTE 13. Supplemental Guarantor Information

The Company's obligations under the 2018 Senior Notes, the 2017 Convertible Senior Subordinated Notes and the 2018 Convertible Senior Subordinated Notes are not guaranteed by all of the Company's subsidiaries and therefore, the Company has disclosed condensed consolidating financial information in accordance with SEC Regulation S-X Rule 3-10, Financial Statements of Guarantors and Issuers of Guaranteed Securities Registered or Being Registered. The subsidiary guarantors of the 2018 Senior Notes, the 2017 Convertible Senior Subordinated Notes and the 2018 Convertible Senior Subordinated Notes are the same.

The following condensed consolidating financial information includes balance sheets, statements of operations and cash flow information for the parent company, the guarantors for the 2018 Senior Notes, the 2017 Convertible Senior Subordinated Notes and the 2018 Convertible Senior Subordinated Notes (the “Guarantor Subsidiaries”), collectively, and for all other subsidiaries and joint ventures of the Company (the “Non-Guarantor Subsidiaries”), collectively. Each Guarantor Subsidiary is a direct or indirect 100%-owned subsidiary of M/I Homes, Inc. and has fully and unconditionally guaranteed the (a) 2018 Senior Notes, on a joint and several senior unsecured basis, (b) the 2017 Convertible Senior Subordinated Notes on a joint and several senior subordinated unsecured basis and (c) the 2018 Convertible Senior Subordinated Notes on a joint and several senior subordinated unsecured basis.

There are no significant restrictions on the parent company's ability to obtain funds from its Guarantor Subsidiaries in the form of a dividend, loan, or other means.

As of March 31, 2013, each of the Company's subsidiaries is a Guarantor Subsidiary, with the exception of subsidiaries that are primarily engaged in the business of mortgage financing, title insurance or similar financial businesses relating to the homebuilding and home sales business, certain subsidiaries that are not 100%-owned by the Company or another subsidiary, and other subsidiaries designated by the Company as Non-Guarantor Subsidiaries, subject to limitations on the aggregate amount invested in such Non-Guarantor Subsidiaries.

In the condensed financial tables presented below, the parent company presents all of its 100%-owned subsidiaries as if they were accounted for under the equity method. All applicable corporate expenses have been allocated appropriately among the Guarantor Subsidiaries and Non-Guarantor Subsidiaries.

CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS

	Three Months Ended March 31, 2013
(In thousands)	M/I Homes, Inc.